IVEY BUSINESS REVIEW

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THE IVEY HBA BUSINESS STRATEGY JOURNAL

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The Ivey Business Review is an undergraduate business strategy publication conceived, written, and managed exclusively by students at the Richard Ivey School of Business. The magazine aims to push the boundaries of student thought; foster the development of world-class business insights; and give the leaders of tomorrow a chance to voice their opinion on today's major business issues and strategies. Each article has been created specifically for the magazine and comes from several weeks of intense collaboration between the writers and members of the Editorial Board.

The Richard Ivey School of Business at The University of Western Ontario (www.ivey.ca) offers undergraduate (HBA) and graduate degree programs (MSc, MBA, Executive MBA and PhD) in addition to non-degree Executive Development programs. Ivey has campuses in London (Ontario), Toronto, and Hong Kong. Ivey recently redesigned its curriculum to focus on Cross-Enterprise Leadership – a holistic issues-based approach to management education that meets the demands of today's complex global business world.

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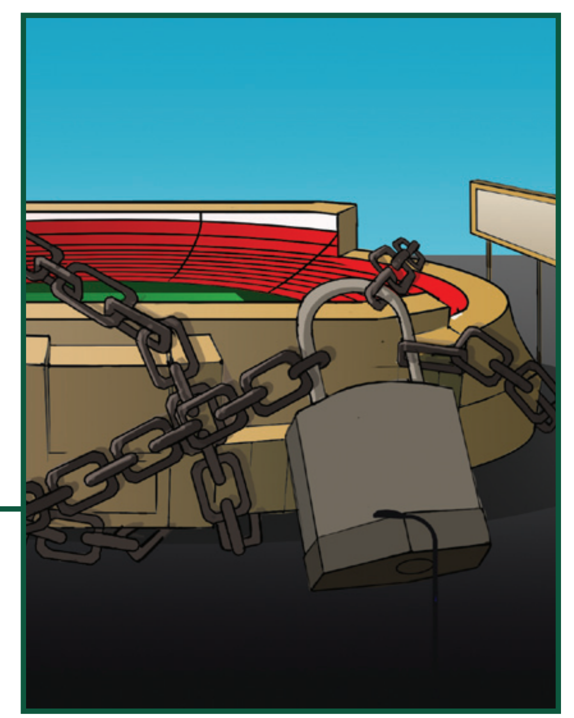

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Michael Mace

The Ivey Business Review discusses strategy with a leading technology industry expert.

Conducted by Matthew Ball and Joseph Ghobrial

About Michael Mace

CEO of Cera Technology, Inc.

Michael Mace is currently the CEO of Cera Technology, an Internet startup located in Silicon Valley. He previously served as the Chief Competitive Officer and Vice President of Product Planning at Palm and Vice President of Strategic Marketing at PalmSource. Michael is also a former Apple executive, having held a variety of senior roles including Director of Marketing for the Mac Platform and Director of Customer & Competitive Analysis. He was most recently a principal at Rubicon Consulting, where he helped companies including Nokia, Adobe and Symantec with strategy and product planning.

Michael is a prominent technology industry speaker and commentator and his work has appeared extensively in the Wall Street Journal, Bloomberg BusinessWeek and numerous industry publications. He also runs a well-regarded industry blog, Mobile Opportunity, and holds a degree in international relations from UCLA.

[*IBR*] What type of role does marketing play in the technology industry? What is the dynamic between the marketing department and product development?

[*Michael Mace*] There are two types of marketing: outbound marketing, which is giving messages to customers, and inbound marketing, which is understanding customers – what they need, how they think, and what would they respond to. A lot of companies call that product management. The problem is that many tech companies just hire junior engineers into product management roles or an engineer who was not quite good enough on the math or coding side. They are in product management because the assumption is that they are still technical enough to talk to engineers.

The result is that these companies separate the understanding of users from product development. That's why we get so many products that only an engineer would love and it's one of the reasons why Apple is able to routinely outmanoeuvre so many other companies. Apple treats product management as a separate discipline with its own skill set. Meanwhile, much of the Valley treats marketing only as an outbound function designed to tell the customers why they are supposed to love the product after it is made. That is a major problem for a lot of tech companies.

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Why is there such a resistance to the role of marketing and customer insight in product development?

For a lot of the companies, it is the engineers who are in charge. They are the ones who are funded by the VCs and are the CEOs. They think marketers are lightweights, not knowledgeable and even kind of dumb. As a result, they believe they should be excluded from significant product decision-making roles. It is a cultural thing within a lot of companies – and in many cases, it's also a self-fulfilling prophecy. The people these companies hire for outbound marketing are very communication-oriented. They aren't technical and don't really understand the details very well – so they are not going to be able to make technology decisions. There aren't a lot of product management degrees being granted out there. Apple develops these people internally; they spend years and years at Apple learning how to do that.

After solving the Product Manager problem, how do you create a process that can create great products?

When I was consulting full-time, it was very common for us to have a tech company contact us and say, "We've finished the development of the product and we need to figure out now who is going to buy it and exactly how we should market it. We need a go-to-market plan." And so we'd ask them, "What is the market we are targeting?" And they'd say "16 to 45 year olds with a lot of money." So at a lot of companies, again because of this outbound marketing and because the product is coming from and insulated engineering team, this marketing process is treated as an afterthought. When you do that, the success or failure of your products is pretty much a random draw.

The right way to do it is to get a small number of people who understand the customers and the technology really well. You need people who can honestly sit at both tables. They are not really outbound marketing people; they are people who are really good at using market research, data, talking to people, watching focus groups and thinking about customers. Getting inside their heads to the point where they can act as a proxy for the customer and can reliably say, "If we do this, the customer is going to be delighted." You can't go to the customers and ask, "If I develop this completely new product, would you like it?" because they just

can't picture it. If you can get that person to have enough technical skills that they can engage with the engineer (they don't have to be an engineer, they just need to be able to speak the same language), then they can translate those customer needs through to the engineers. Of course, you will also need engineers who are willing to take that feedback. But if it's properly done, and somebody is patient enough to explain the need credibly, there are a lot of engineers who will go along with it. It's just that it isn't done properly most places and the people who try to play this role don't really understand how to do it.

But at Apple for instance, the product managers are dictators. If you do a good job and you create a good product, you get to keep your job. If you do a crappy job, they fire you. That Darwinian nastiness very quickly produces a cadre of really good product managers.

Contrast that with someone like Google. They just don't do product management very well. Google is a playground of a bunch of engineers doing whatever they feel like doing and that doesn't produce good products, and that's why they have such a bad batting average of creating products for end users. They have some highly successful products, as well as those still propped up by the company's scale – but if you look at how many they've actually released, their success rate is not particularly strong.

Contrast that with someone like Google. They just don't do product management very well. Google is a playground of a bunch of engineers doing whatever they feel like doing and that doesn't produce good products, and that's why they have such a bad batting average of creating products for end users.

Was product management Steve Jobs' primary talent?

Steve was also a fantastic communicator, but I think his one essential skill was that he was the ultimate product manager. If he'd been a terrible communicator but a great product manager, he still could have saved Apple. But the opposite is not true.

Was this the problem at Apple while you were there? What has changed since?

A lot of the things I talk about for product management were in place at Apple. That institution existed before I got there and it was still intact when I left. What wasn't there was decisive senior management who would say, "This is how we are going to focus, even if people disagree." When Steve wasn't there, you had a lot of very bright and very strong willed people who wouldn't cooperate. There wasn't senior management intellectually strong enough to pull them in line. So, the typical Apple behaviour when Steve wasn't there was that people would appear to agree in meetings and support senior management; however, once they returned to the offices they would say, "That's a dumb idea, I don't agree with that, I'm not going to cooperate with that." Without Steve there to call people on this and fire those not helping the company, it became a dysfunctional culture where it was very hard to get things done and focus.

Can RIM compete from Waterloo, Ontario? Was it a mistake not to shift more, if not all, of its operations to the Valley?

That's a hard question. If you took the same RIM culture and put them in the Valley, it would still be dysfunctional. Strong product management doesn't have to be in the Valley. But, for one, you have to be able to pick good product managers. Number two, you have to be willing to empower them to ride roughshod over everyone else. And number three, you have to have senior management to prioritize down to the number of projects you can afford. I don't see any of those things having existed within the culture and the management structure that RIM has, so relocation to Silicon Valley wouldn't have made a difference. In fact, I know some of the people who were working for RIM in Silicon Valley, and they were pretty frustrated.

Do you have a perspective on why Palm struggled and what that has in common with RIM – a company that seems to have pushed Palm out of the market and now seems to be following it out?

In my view, RIM didn't push Palm out of the market. Palm screwed itself. There are certain things I argued for that the company didn't do and I can claim had they, things might have been different. But nobody did it to them. I need to take some of the blame for that.

Palm had problems with its senior decision making. Its primary issue was that it tried to do too much and as a result, nothing was ever done with the polish it needed. Too many bugs remained and products shipped that shouldn't have been shipped.

In addition, the company failed to make the jump from generating demand based on a couple of features, to generating demand based on a broader value proposition to customers. Palm had a lot of the attributes that Apple has – a really big base of developers and a product becoming increasingly versatile - but senior management was very focused on quarterly results and did not want to make the marketing investments that were necessary to articulate that Palm was a platform with hundreds of things and apps that you could do with it. As a result, people thought a PDA was just for contacts and address books. As soon as these aspects were built into a phone, Palm was done. It's a shame. I believe things could have been very different.

RIM has some similarities in the sense that RIM didn't pivot well from its initial position in the marketplace and they lost the focus on who their customer was. They were transfixed on the fact the iPhone was doing all these entertainment features. As a result, they believed they needed to hang out with rockstars, like Will.i.am, and focus on developing media capabilities. I wish they had said, "Let's let Apple appeal to the entertainment-oriented people. We'll create the best smartphone for business people and accept we won't own

the entire market – but we will own our segment.” There are tons of features they could have added to the BlackBerry to make it the best product for busy business people on the go. Instead, RIM transformed itself into a bad imitation of Apple across the board. You do Apple-like things less well than Apple, with less effective marketing than Apple and less well-designed products than Apple. What a shock you’re not doing as well.

I’ve been playing with Windows 8 and there are some things about it that are really cool, and then there are some things that make me think, “Do they really think they can ship it like this? Are they kidding? What exactly is going on in their heads?” I’m starting to be worried about what their adoption is going to be like and how customers are going to react when they actually start receiving this software built into their PCs.

What types of applications would have augmented their value proposition to enterprise customers?

Don’t get too focused on “enterprise,” think of busy business people. In that situation, they should have focused on tighter integration with things like Microsoft Office Suite to make life easier, especially on the go. RIM has played around in this space. They bought Tungle.me, a contact management company designed to simplify the process of finding and connecting with friends and colleagues through your “social graph.” They’ve never really done anything with these investments or opportunities. It would have been great if a BlackBerry came with a feature that would automatically find available parking spaces for me in San Francisco. There are people working on web services for this problem and eventually it will happen. But what if RIM had said four years ago, “We’re going to do it now”? They wouldn’t have needed to do a dozen of these – just three of four robust use cases – and just focused everyone and their attention on these features. At the very least, they would have been able to hang onto their core customers today – but they decided to chase Apple instead.

How did GM beat Ford in the 1920s or 1930s? It was market segmentation and the creation of specialized products for these segments. When combating a Ford-like competitor, which Apple is today, what does everyone do? Do they create specialized products – the proven model for overcoming a leader like that? No. They just try to do imitation Model-Ts. You are not going to be a better Apple than Apple. Be something else.

What is it like working in San Francisco and Silicon Valley?

There are a number of great aspects about everyone working together here. The tricky part is you have to be very careful that you don’t get caught up in the Silicon Valley “echo chamber,” where everyone is just repeating to each other what they hear, read online, and therefore assume to be true. To give you an example, there are really, really serious problems with Windows 8. It has taken a long time for that idea to just barely penetrate the mindset of people in the Valley and I still don’t think it has fully gotten there. That’s just a case where you had a lot of people talking about it, looking at the demos, hearing internal reviews, and thinking it was great. Only, you didn’t have a lot of people actually using it hands on, and the best way to know what is going on is to use the products hands on and see what they are actually like.

Is it your understanding that the product isn’t functioning properly or that people aren’t taking to it as Microsoft would have hoped?

No – it’s not even that. There are just serious problems with the product. I’ve been playing with Windows 8 and there are some things about it that are really cool, and then there are some things that make me think, “Do they really think they can ship it like this? Are they kidding? What exactly is going on in their heads?” I’m starting to be worried about what their adoption is going to be like and how customers are going to react when they actually start receiving this software built into their PCs. I had a lot of trouble actually figuring out how to turn off the computer after installing Windows 8 – I couldn’t find the off button. Compare that to the iPad. These are key problems: how do I find my apps, how do I turn this thing off, and how do I tell it to go to sleep as opposed to turning it off? I eventually figured it out but it took me a while, and if it takes me a while, I really worry about somebody getting this with no instructions and being on their own. I think a lot of these decisions are mistakes and they are going to end up regretting it.

How do you believe Windows 8 will be received on the tablet side?

Windows 8 has clearly been designed more for tablets. My question though is, and this is back to the question about RIM: Who is the unique customer that this is made for? Who is this a better product for? Or is Microsoft trying to make a better tablet than Apple and trying to sell to the exact same customers that Apple is selling the iPad to? If what you are trying to do is be a better iPad than the iPad – good luck, my best wishes to you because Apple is already there and they’re not standing still. Remember when Microsoft tried to make a better iPod than the iPod, called the Zune? I’m concerned that maybe what they are going to do is try to do a Zune.

You were hired by a billion-dollar company to defend itself against an assault from Microsoft. Can you walk us through the process?

There was a time when Microsoft, because it was trying to grow its revenue by 10% every year, was just viciously going after any new market they thought they could pick off a billion dollars in. The client was a major, well-established software company, but they were nonetheless completely freaked out because Microsoft was going straight at the center of their marketplace. We helped them

a lot in terms of understanding why Microsoft was doing it, how Microsoft was going to react, and most importantly, how to keep Microsoft away.

Essentially, Microsoft would go and attack eight different markets with the expectation that they would not win in all eight. They would then throw all their reinforcements against the markets where they were getting the most traction and abandon the others.

The trick in fighting them was exactly that: give enough initial resistance so that Microsoft would fire the guys in charge and refocus resources elsewhere. You do a lot of temporary price promotions to make it difficult for them to make any money and drag out their timetable for success. It isn't a permanent decision, but you need to recognize that you'll need to take a hit for six months to survive. Get your marketing people to relentlessly point out the flaws in their nascent product. We explained this process to them, and then we did a ton of internal coaching about "here's how to fight; this is what you want to do; if you notice this, do this; here's an idea for a marketing program you can do against them, or here is what you can do with your price."

If what you are trying to do is be a better iPad than the iPad – good luck, my best wishes to you because Apple is already there and they're not standing still. Remember when Microsoft tried to make a better iPod than the iPod, called the Zune?

We all agree information overload is a growing problem. You are currently the CEO of a startup, Cera Technology, that's focused on this problem. What can you tell us about it?

People tend to think of information overload as if it's some sort of disease. The Wall Street Journal recently suggested that those who hoard information have OCD and equated them to people who save old pizza boxes. They literally interviewed psychotherapists. The idea that you need to get rid of files is twisted, given the way hard drive storage is growing. Why should you ever throw away a file when you know you might need it in the future? It's not like they're going to attract rats.

The problem with having a whole bunch of computer files is that it's really hard to search them to find the stuff that you need. The search engines are either built around what was good for searching a 40MB hard drive in 1993 or they're built around keyword search for the web which doesn't work that well for your personal files because you may not remember the keyword that you stored something under. For busy business people (this goes back to market segmentation), who do the most information productivity work, they get totally overwhelmed with the amount of information that's constantly rolling into their lives. The meetings that they have, the documents, the emails – it's just more than they can process and retain. They start forgetting context around things they really need like, "Gee, I recognize this person's name but I can't remember what my context is with him and I can't remember, did I promise him something? I'm about to go in this meeting and I don't remember what exactly I'm supposed to do in it."

So you need a software tool that goes across all of those different places where your information is stored – your emails, documents, calendars – pull it together, and be able to follow the connections between them. Then you need an experience that lets you navigate that by whatever little bits and pieces you remember. If all I remember is the restaurant where I had a meeting with someone, I need to be able to search by the name of the restaurant. Maybe I met someone for lunch at the CES tradeshow and CES took place in the first half of January; the tool should let me just see the lunch meetings I had in the first half of January for the past couple of years. It's not a search engine, it's a context engine that will let you recreate context around things you halfway remember. For those mid-career, busy professionals who have this problem the worst, if you can make it work well, that's like the Holy Grail and they will gladly pay for an app or service that helps. It doesn't have to be perfect. As long as it gets you close, you can probably flip through files and figure out which one you are after in a short enough period of time.

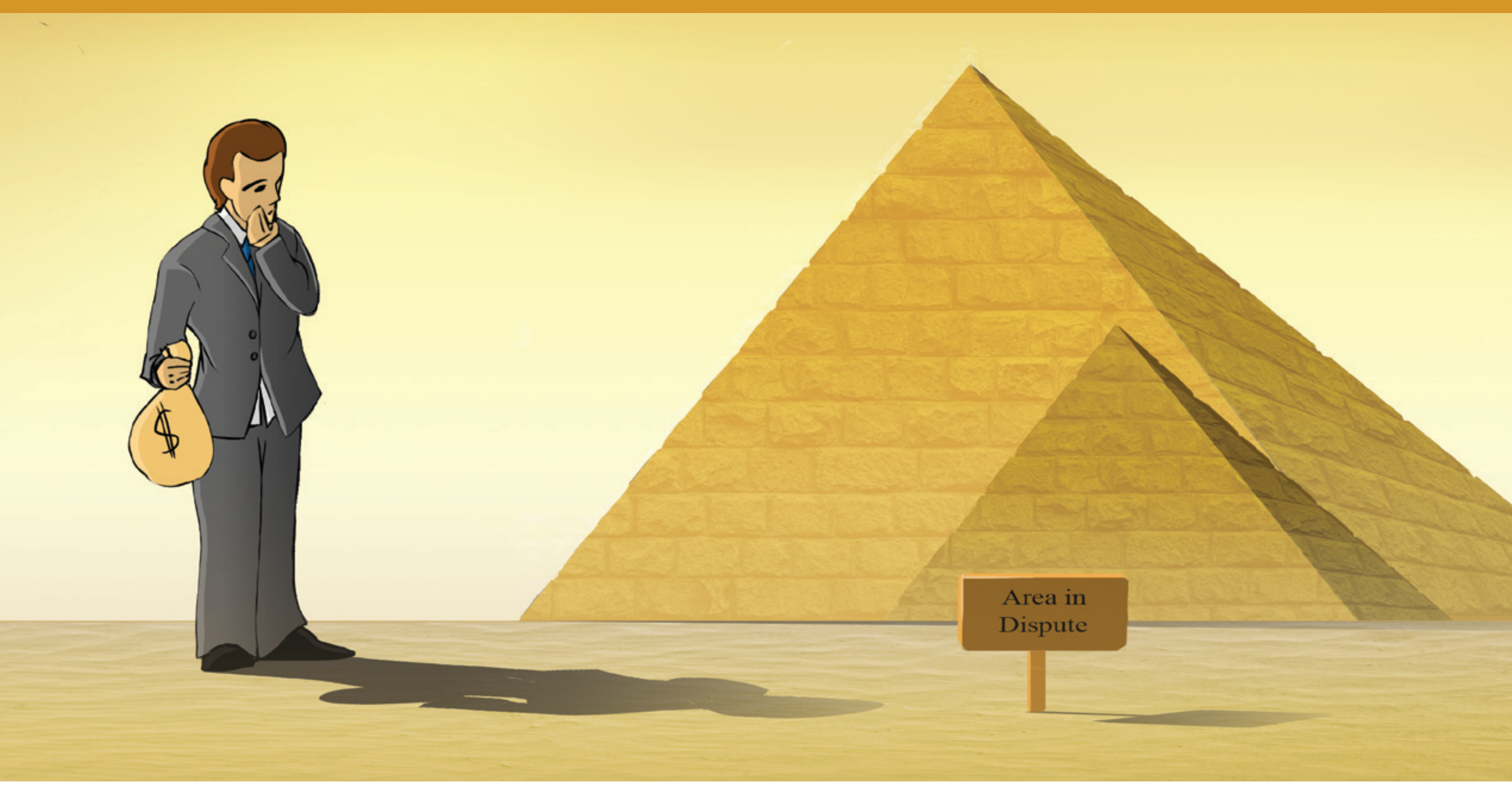
This sounds like something that's a good fit for an incumbent like Google. How serious of a threat are they for Cera?

It's interesting. They have started to back away from things that they can't build an advertising business model around. The best example is Google Desktop. For Cera, I went around and talked to VCs and angels to get their opinion on our product, and they used to raise Google Desktop and say, "Well, Google is working in this area. Aren't you going to get smoked?" and yet Google decided to kill the product. How interesting. If knowing everything they can about a consumer is so critical, why wouldn't they want to index your hard drive? I think the problem is they couldn't figure out how to put any ads against it so they couldn't make any money off it. Google really is a weird kind of beast.

What's your advice for recent graduates looking to enter the tech sector, whether through a startup or joining a Valley company?

Although the hot thing is to do a startup, I think there is a lot to be said for working for a while at a fast-growing tech company. Try to get into one that's doing well and hiring a lot of bright people. The advantage of this is that you'll develop a lot of very useful connections that you can leverage later on in your career. You'll have a shared set of skills, experiences, and vocabulary that connect you with a generation of others in the industry. Silicon Valley runs on personal connections, so I can't overstate the usefulness of getting into a "mafia" somewhere. Look at what the Netscape alumni did to shape the Internet industry.

For our complete interview with Michael Mace, including questions such as "Who should buy Twitter?" and "What's the new 'social' for VCs," please find us online at www.iveybusinessreview.ca



Deals on the Nile

Is it time to enter post-revolutionary Egypt?

By Oliver Dempsey and Vivek Ramaswami

In late December 2010, a Tunisian street vendor set himself on fire in protest of police corruption and harassment. This act triggered a series of revolts across multiple North African countries in what became the "Arab Spring." In Egypt, millions of citizens across a range of socio-economic backgrounds took to the streets, demanding "bread, freedom, and social justice." Although President Hosni Mubarak eventually stepped down, the victory was fleeting, as a group of military personnel quickly filled the power vacuum. Although this young, dynamic, and educated country still faces many of the same pre-revolutionary problems, opportunities are available to foreign firms who fit the right criteria. If these businesses enter this risky market, they could stand to gain enormously.

Why Egypt?

Although the revolution resulted in the ouster of President Mubarak, problems still linger a full year later. Without a major constitutional change, Egypt's corruption and bureaucracy persist. A 2010 survey by the Al-Arham Centre for Political and Strategic Studies found that 47% of small to mid-size enterprises in Egypt need to pay bribes to the government. Currently, there are few existing large private sector companies in Egypt. In spite of these headwinds, opportunities lie in Egypt's large, young, tech-savvy and educated population.

Despite having one of the highest completion rates of post-secondary education in the Middle East and North Africa (MENA) (29% compared to other large MENA countries such as Iran and Turkey with only 11%), Egypt's dynamic youth are highly underutilized. Unemployment amongst this group hovers around 25%, since the major private industries operating in Egypt primarily demand unskilled and physical labour. While this environment provides plenty of entry opportunities for foreign firms, some industries are better suited than others. Entering Egypt now could provide a long-term foothold for growth in the region.

Who Should Enter?

Potential entrants need to satisfy four main criteria:

1. Since the absence of any real governmental change leaves the potential for further violent uprisings, a **large risk appetite** is a precondition for any firm entering Egypt, regardless of industry or size. Companies with few opportunities in saturated Western markets may be more inclined to enter Egypt than well-established, risk-averse firms experiencing satisfactory returns domestically. For companies with the capacity and resources to take a chance on a high-risk, high-return market, post-revolutionary Egypt offers significant long-term advantages for first movers, including the opportunity to develop brand loyalty and strong supplier relationships.

2. Businesses with **low capital expenditure** requirements will have lower risk exposure. In the case of upheaval, the firm must have the ability to completely cease operations and exit Egypt at a minimal cost. Both BP and Shell, two of the world's largest oil companies, lost millions of dollars when their fixed assets fell idle during the revolution. Conversely, Sawari Ventures, a high-tech venture capital firm, and the companies it invests in survived almost completely unscathed.

3. **Resource flexibility** extends not only to physical assets, but to imported human capital as well. Suitable companies will be able to maintain a small, lean base of expatriates on the ground and retain larger groups of local labour. The French carmaker Peugeot has employed this strategy by transferring over 30 of its French managers to Tunisia to train the hundreds of locals working at its call centers. Under this organizational structure, Peugeot can smoothly align local offices with the overarching strategy, while simultaneously allowing foreign management to efficiently leave the country in case of emergency.

4. It is important to retain the support of the general public while avoiding **government interaction**, especially the military, to ensure autonomy from a corrupt and oppressive government. Firms with heavy exposure to the government, such as construction companies, could face more regulatory oversight and administrative pressure. Contracts in Egypt are often awarded through bribery and patronage, activities foreign firms cannot engage in. Small-scale, direct-to-consumer industries are better able to avoid these challenges.

The Obvious Choice - Groupon

One example of an excellent candidate to enter the high-risk, high-reward Egyptian market is the group-buy firm Groupon. Groupon sells pre-paid coupons to consumers online and then shares the revenue with retailers – usually 50% of the coupon. Thus, Groupon avoids capital investments in inventory, buildings, or expensive equipment. Armed with flexible human capital, Groupon's employees can operate remotely from virtually anywhere in the world with only a small local sales force. After obtaining simple web licenses upon entry, Groupon can connect web-savvy consumers with businesses and host ad space.

Having already penetrated all 50 states and 10 provinces in North America, Groupon has saturated its Western markets and is looking abroad for growth. Egypt offers a significant opportunity. Its growing entrepreneurial market aligns well with Groupon's value proposition – providing a platform for local businesses to acquire new customers through bulk discounting. As a consequence of the revolution, new businesses and entrepreneurial ventures emerge with reconstruction and recovery. With many young Egyptians looking to launch entrepreneurial ventures, Groupon delivers a unique and creative way to advertise their services and products to a large, tech-savvy consumer base. Furthermore, Egypt has already exhibited a penchant for group-buy websites. LivingSocial, Groupon's largest global competitor, and local deal website Cobone are growing rapidly in Egypt. Cobone experienced estimated sales growth of 300% last year, while a record 4,587 Egyptian customers bought into a discount deal for Burger King on LivingSocial in March 2012. However, it is not just multinational corporations that are popular; local Egyptian hotels, restaurants, and even dental clinics offer deals on these websites. Building lasting relationships with growing Egyptian businesses will ensure sustainable operations well into the future.

Groupon's safest entry strategy into Egypt is through acquisition, which would minimize the time and cost of entering into a risky market and provide an opportunity to retain customers. With 70% market share in the MENA region, Cobone is the obvious choice

Comparing Developing Markets

How Post-Revolutionary Egypt Compares

Country	Population	GDP/Capita	Pop. <30	Internet Use	Smartphone Penetration	Literacy Rate	Size of Middle Class	Facebook Usage
Egypt	81.1 Million	$6,500	66%	26.7%	6%	71.4%	79.7%	13%
India	1.2 Billion	$3,700	50%	7.8%	4%	75.1%	<30%	3.8%
Tunisia	10.5 Million	$9,500	54.3%	36.6%	N/A	74.3%	80%	27.9%
South Africa	49.9 Million	$11,000	67%	12.3%	15%	86.4%	26%	10.1%

Source: CIA World Factbook

for a target acquisition. Cobone claims monthly growth of up to 50% and that its more than 500,000 users have saved $10 million over the past 10 months. With more than $1 billion in cash on its balance sheets, Groupon could potentially acquire Cobone for $30-40 million and integrate itself as the dominant group-buy firm in the country.

Other Potential Entrants

Fast food is another sector that could successfully operate in post-revolution Egypt. Low inventory costs, arising from cheap, perishable ingredients, would limit losses if an exit were necessary; while capital expenditures would also be kept low through franchising. These factors, in combination with easier access to food and drink permits, resulted in the number of fast-food outlets in Egypt, including McDonalds and Burger King, significantly increasing in the past five years.

One firm with the potential to enter this market is Taco Bell. Managed by Fortune 500 Yum! Brands, Taco Bell offers a unique value proposition as a quick-serve provider of Western-style food, attractive to the Egyptian middle class. Taco Bell's "Value Picks" menu caters well to the price-conscious middle class in Egypt, where no quick-serve Mexican restaurant currently exists.

All businesses must endure some level of adaptation when entering a new market. Firms cognizant of the constraints and competencies of their surroundings will be far more likely to achieve sustainable benefits in the long-term.

Has it Worked? – Intel

Other North American firms have already found success in post-revolutionary Egypt. Intel entered the scene in March 2011 after acquiring Cairo's SySDSoft, a mobile platform software specialist. Intel's mobile communications business sells software to smartphone developers and other tablet devices at a low cost. As a software company, SySDSoft's limited need for capital expenditures and fixed costs made it a much less risky acquisition than alternative industries. This has been central to Intel's entrance strategy into the mobile market in Egypt.

Given the well-educated local labour force, Intel retained over 100 of SySDSoft's computer scientists and electrical engineers. Dr. Christian Mucke, Vice President of Mobile Communications for Intel, found that Egypt's young diverse talent pool makes the country an attractive market for Intel. Despite global pessimism, Intel now has the ability to enjoy larger sales and market share from engaging in a high-risk market.

Intel's management made it clear that this acquisition is intended to show long-term commitment to the Egyptian people as part of its global strategy. Christian Mucke reiterated Intel's commitment to Egypt by referring to it as a "strategic market." This commitment began

back in 2006 when Intel launched a Teach Essentials Online (TEO) program. Designed to integrate technology into school curricula, this pilot program trained hundreds of thousands of teachers and donated 8,000 computers to schools. A spinoff study materials website, skoool.com.eg, has received 114 million hits since inception. These corporate social responsibility programs have been immensely successful, painting a positive image for the company and helping Intel gain significant market share and increase its overall domestic sales.

Lessons Learned

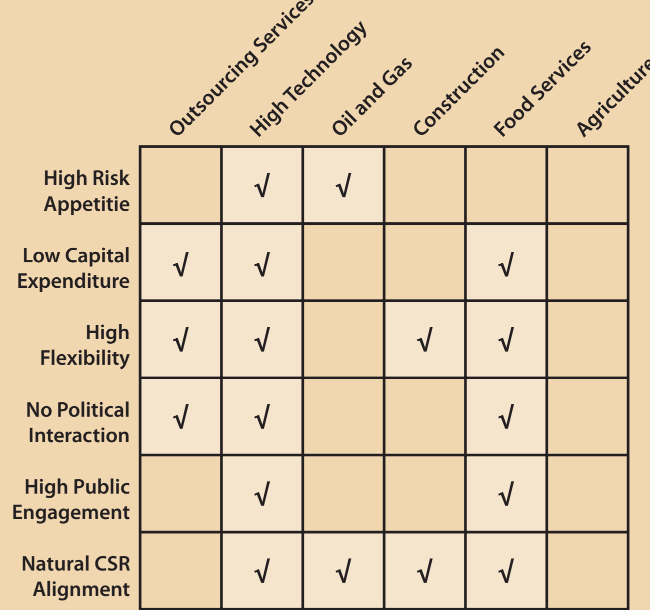
Intel proves that certain businesses can succeed in Egypt and in post-revolutionary Arab countries more generally. With little need for capital expenditures or government contracts, highly flexible firms can take advantage of the young, tech-savvy consumer base and labour pool. The political, social, and economic atmosphere in Egypt suggests that a company operating in the technology or software space is best suited for market entry. Examples of successful tech firms in post-revolutionary Arab countries, such as Tunisia, are prevalent.

Non-software related industries, such as fast-food companies, also stand to gain from this market. Although their entry may be best when these countries normalize, laying the groundwork now for future opportunities will prove lucrative. Corporate social responsibility programs, which have been successful when used to lay a foundation for further growth, should be considered by all market entrants.

Groupon may appear to be the perfect fit, but even they must adapt their global strategy to fit this entirely new market. Despite having a firm satisfy the aforementioned criteria, all businesses must endure some level of adaptation when entering a new market. Firms cognizant of the constraints and competencies of their surroundings will be far more likely to achieve sustainable benefits in the long-term. Both the opportunities and benefits of entering post-revolutionary Arab countries can be enduring, and firms with the right capabilities can become part of the foundation of a new Egypt. Although the revolution itself may be near its end, the opportunities for businesses are just beginning.

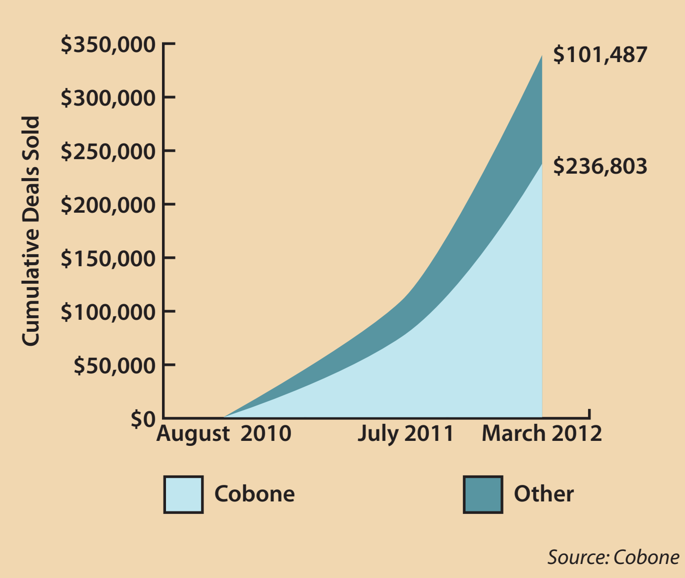
Finding a Good Fit

Industry Alignment with Entry Criteria



	Outsourcing Services	High Technology	Oil and Gas	Construction	Food Services	Agriculture
High Risk Appetitie		√	√			
Low Capital Expenditure	√	√			√	
High Flexibility	√	√		√	√	
No Political Interaction	√	√			√	
High Public Engagement		√			√	
Natural CSR Alignment		√	√	√	√	

Group Buy Market Growth in Egypt



Source: Cobone

Bit-by-Bit: Digitizing the Ivory Tower

Examining the potential of online education for Canadian universities.

By Connor Lyons and Steven Wellman

From the music industry to the newspaper business, firms have been forced to adapt their distribution strategies as digital technology is increasingly integrated into day-to-day activities. The realm of post-secondary education is no exception. For centuries, there have been few viable alternatives to the traditional brick-and-mortar university experience for accessing educational information. The emergence of online universities and academic sources, the University of Phoenix and Khan Academy, among others, signal the end of this relative monopoly on higher education. With learning no longer limited to lecture halls and musty libraries, universities worldwide must adjust to an evolving competitive landscape or risk falling behind more progressive competitors.

The ability of technology to alter the delivery of education has led 75% of public universities to cite online degrees as critical to their long-term strategy. Yet Canada's premier universities have made only minor strides in this direction. Top-tier schools such as University of Toronto, University of British Columbia, Western University, and McGill University all offer very few fully online degrees. Moreover, schools are hesitant to widely market their online offering, likely as a result of the importance placed on institutional branding. This conservative approach suggests that research-intensive universities fear entering the online degree sphere will undermine their market position, by damaging their reputation and brand equity.

An Attractive Opportunity

Virtual degree enrollment has increased at roughly nine times the rate of campus enrollment over the past decade, signaling a growing demand for online degree programs. In 2011 alone, there was 900% growth within the online segment. E-learning is now rated equivalent or superior to campus-based education by 67% of educators, a 10% increase in just a few years. Moreover, student perceptions of online courses indicate no relative advantage between the two forms of delivery in the presentation of course material and student-to-faculty interaction.

There are also compelling financial incentives for Canada's universities to expand their online portfolio. Since physical services are not required, virtual programs generate 25-30% higher margins than traditional degrees. Facing increasing financial pressure with recent cuts in government research grants, Canada's research-intensive schools can use an online strategy to sustainably stimulate cash flow by reinvesting online tuition into research and teaching. This new capital could also be used for scholarships and improvement of on-campus services in order to attract top students.

The migration to learning online is inevitable. Universities which demonstrate leadership in this area stand to reap the benefits

associated with the first mover; leaving laggards to languish. A successful online education program is the best way for strong national universities to become global thought leaders. The status quo is not the path to success. Though any change has risks, for universities with ambitions to become better educational institutions, the risks tied to online education can be mitigated.

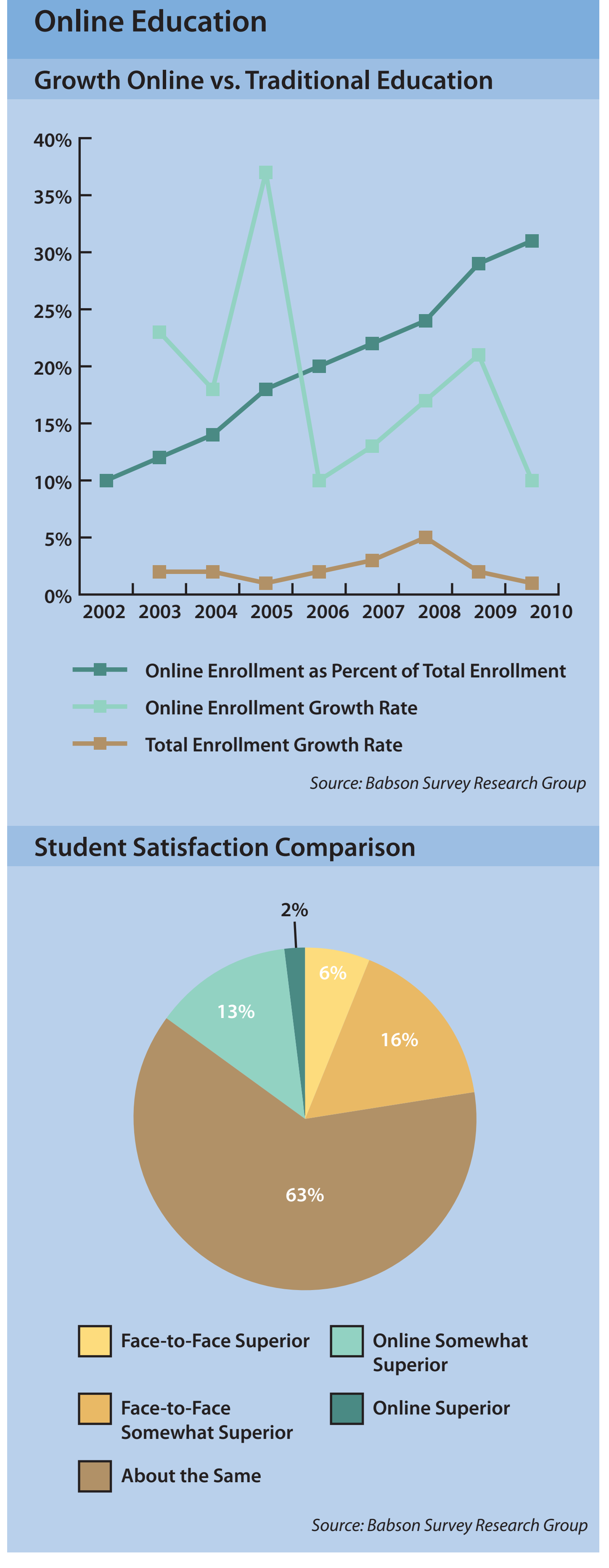
Organizational Inertia

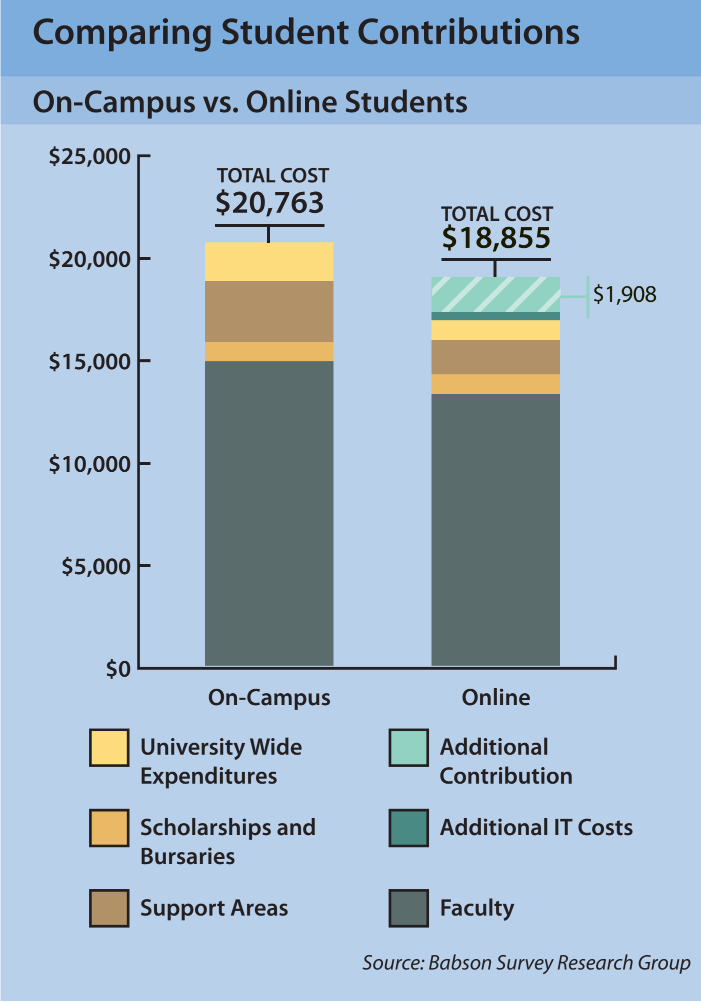
While institutions recognize that technology will eventually be integrated with education, overcoming the significant inertia of the status quo will be a struggle. Professors, for example, are concerned that online learning will minimize their importance in the learning process. The decentralized bureaucracy of Canada's leading institutions provides many opportunities for opponents to prevent implementation. Current administrations at Canada's top schools are skeptical of the ability for online education to deliver the necessary returns on the significant investment that is required to create online programs. Universities are not incentivized to take these kinds of risks with their capital when the status quo suits them just fine. Complacency can be tempting, especially if no other reputable university is pursuing this strategy and prospective students and employers believe online content devalues the institution's reputation. Furthermore, a lack of an online program does not limit access to guaranteed government funding, which begs the question, why should universities attempt to innovate?

Faculty Buy-In and Beating Bureaucracy – Given that faculty are central to the committee-based decision making at research-based institutions, to move initiatives forward means each stakeholder needs to understand how embracing online degrees is in their self-interest. Faculty must see that benefits are immediate and definite. Conveniently, given the demands of the "publish or perish" environment, the increased research time offered by online teaching directly benefits a professor's career. Due to increased flexibility, teachers will find online courses easier to manage than traditional ones. Moreover, if theoretical teachings are posted online, professors can reallocate class time to discussions, tutorials, and practical application.

Investing for the Future – All of Canada's research-based schools already have online infrastructure for students to receive some form of digital content. While additional resources will need to be allocated to fully enable online degree programming, the long-term benefits of integrating technological advancements into their provision of academic degrees will prove significant. Universities can appropriate the funds generated from their online degree programs into strengthening their traditional programming.

Preserving Brand and Reputation – Low admissions standards and over-enrollment are stigmas characteristic of many online university programs. To preserve their brand equity, schools should limit enrollment and apply the same or stricter admissions standards to their online programs to maintain legitimacy and quality of students. Initially, institutions should only offer programs of study, such as Social Sciences, which require significant independent study and would therefore be the easiest to move online while





preserving quality of education. To further legitimize their online program, universities can use the results from graduate entrance exams such as the LSAT and GRE to demonstrate that online programs are comparable to traditional classes. These metrics allow universities to continuously improve quality.

Entrance Strategy

The increased number of mature students and displaced workers returning to university provides an ample applicant pool of qualified and dedicated students. Mature students are especially well-suited for online degrees because virtual classes align with their educational priorities. Oftentimes, their motivation for enrollment is based on career advancement and the signaling effects of a degree rather than the ancillary services associated with traditional post-secondary education. Adult students value the ease of scheduling their learning around work and family; placing less importance on clubs, events, and the campus atmosphere. Moreover, targeting mature students allows schools to expand their share of the post-secondary market without cannibalizing their primary customer base – recent high school graduates.

Western University, for example, is uniquely positioned to take advantage of the sizeable gap between less reputable online educators, such as the University of Phoenix, and prestigious non-degree granting platforms, like MITx. Neither alternative provides the type of accreditation desired by mature students and potential employers. Canada's university subsidization policy amplifies this opportunity since citizens can obtain their degree from a public university for one-third of for-profit competitors' tuition fees. The only notable domestic challenge stems from the Canadian Virtual University (CVU), a consortium of lower-tier universities offering virtual degree programs. However, the CVU lacks the signaling power of well-established research-intensive universities.

Top universities can enter as consortia similar to the CVU, or players can enter alone. A joint approach spreads IT investment while helping safeguard against reputational risks. However, such a strategy would likely be met with administrative apprehension, and achieving faculty buy-in is doubtful where definitive leadership is lacking. While spreading risk may be prudent, it concurrently reduces potential reward. A lone first mover has the opportunity to realize higher profits through industry leadership.

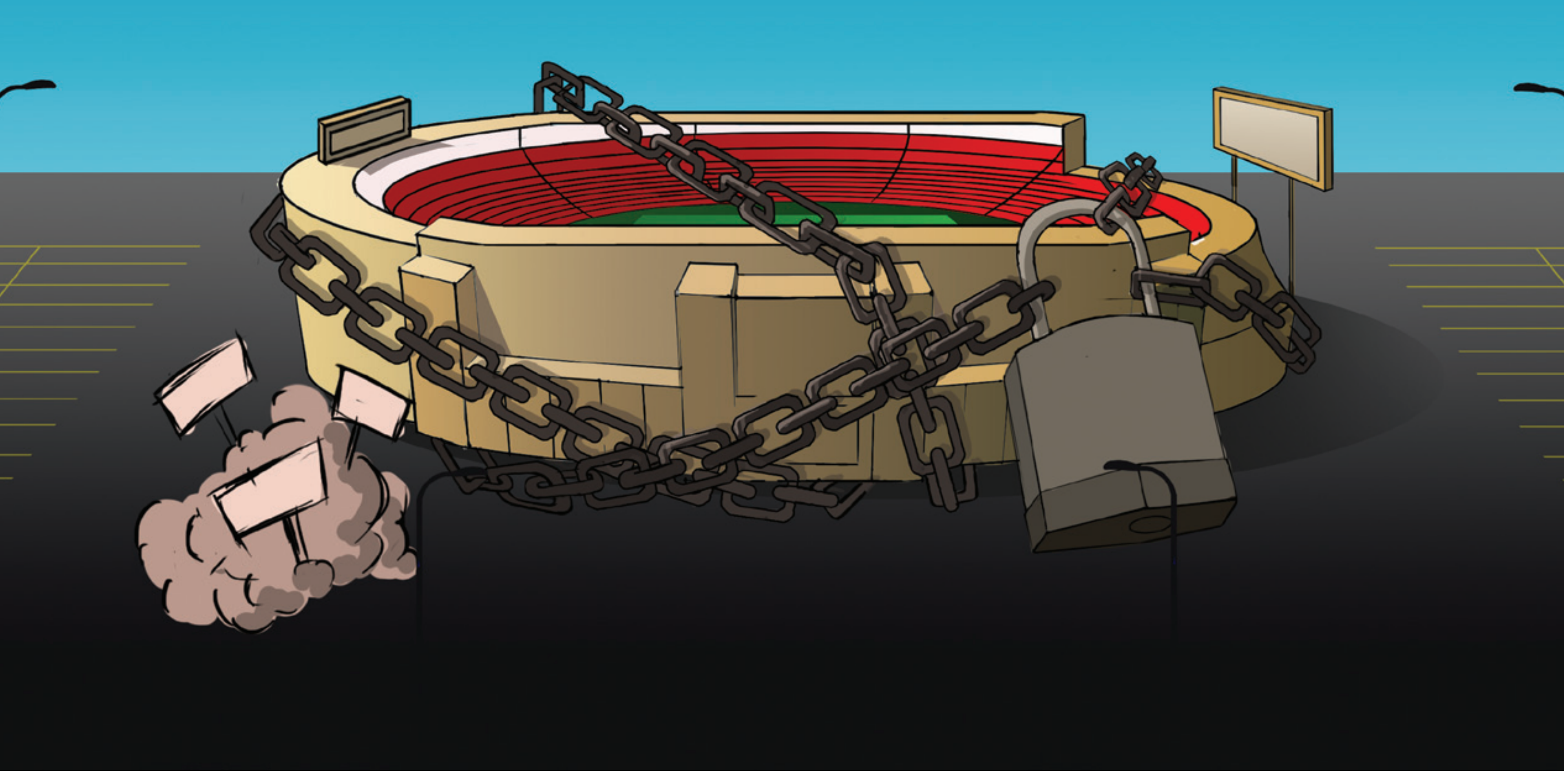
Long-Term Vision

Trends toward digital collaboration suggest educational delivery will be fundamentally different in 25 years, yet Canada's top universities are lagging behind their American counterparts. Yale University and MIT, for example, have developed online programs aimed at better understanding the impact of digital collaboration within the education industry.

Revenues from online degrees can be directed towards increased research funding, talent acquisition, and asset development. Improving these areas will contribute to brand building. A university's reputation can be significantly enhanced with funds obtained through online degree expansion. Distinguished researchers who bring international recognition often select a university based on the financial package offered. The University of Waterloo, for example, has sought to enhance its position by offering millions to world-renowned scholars.

The successful execution of an online degree strategy is also a brand builder, as institutions are viewed as thought leaders. This brand development is the key to national institutions looking to become global titans. Global players distinguish themselves primarily based on their brand. Over time, the online program will become core to a university brand; as foreign students study and work abroad, they will increase the university's exposure.

Technological advancements will continue to alter and improve the delivery of education. Funding cuts, combined with the inability of universities to raise tuition, mean that Canada's research-intensive schools must act creatively to secure the resources necessary to compete globally. A shift towards online degrees is inevitable and Canada's top universities must embrace this change. It is imperative they realize the near-term and future benefits associated with entering the quickly growing digital education market. Conservatism, which has defined the program offering of post-secondary institutions, must be done away with. Efforts should be made by Canada's well-recognized universities to position the country's education system for success.



Keys to the Lockout

Examining the strategy of labour disputes in professional sports.

By Andrew Chan and Kiva Dickinson

October 5, 2005 was one of the most significant nights in National Hockey League history. With 15 games and all 30 teams on the schedule, a puck dropped in Boston to mark the first NHL game played in 16 months. The 16 month hiatus made history; the NHL became the first major professional sports league to cancel an entire season due to a labour dispute, and despite the excitement in the air, there was no guarantee that the NHL would ever recover.

A lockout is the greatest fear amongst team owners in the Big 4 professional leagues (NHL, NFL, MLB, NBA). The MLB strike in 1994 and the NBA lockout in 1999 took the sports out of the spotlight and highlighted the image of greedy players and owners that is so hated by fans. It is these two labour disputes that drive the owners' misconception of lockouts. Owners view each of the Big 4 leagues as strong substitutes for each other in the fierce competition for fans. It is widely held that there is nothing worse for a league's brand than a lockout. History shows that these leagues recover and often flourish due to the financial agreements that play in their favor. Lockouts are ultimately not the threat they appear to be. By re-evaluating their strategic position, owners will discover the inherent power that they hold over the players union.

2011 NBA Lockout

On July 1, 2011, the NBA entered a 161-day lockout, losing two months of its regular season. During collective bargaining agreement (CBA) negotiations, owners claimed teams were losing money and proposed changes to revenue sharing with players and the salary cap structure. Before the lockout, players were paid from a pool consisting of approximately 57% of total NBA revenue. Owners, however, wanted to shrink the pool to 39%, which would have drastically cut salaries.

On December 8, 2011, an agreement was reached between team owners and the NBA Players Association. The new CBA would be 10 years long, with a mutual opt-out option after six years. While the league did not reach its target of 39%, the players' revenue share was reduced by 6%. This resulted in approximately $3 billion of salary savings for owners over the next six years. Perhaps even more significantly, when the lockout ended, the fans came back. In the first month of the season, ESPN, the largest sports network in the United States, saw its NBA ratings jump 31% from the previous year, while TNT's NBA ratings were up 70% and NBA TV's ratings were up 68%. Not only did the NBA materially reduce expenses, it also grew its brand during a period of extreme vulnerability to drive top line growth.

Negotiating Power Dynamics

Understanding the Parties within Each Side

Players' Perspective	**Small Name Players** **Examples: Jerryd Bayless, Clarke MacArthur** • Primary interest is to play as soon as possible because average career is three years • Lockouts significantly affect their day-to-day lives as they have large debt obligations (car loans/mortgages) • May have to look for other financial alternatives (e.g. Delonte West working at Home Depot) • Their careers will likely not be long enough for the negotiation benefit to offset lost salary during the lockout	**Big Name Players** **Examples: LeBron James, Sidney Crosby** • Not as affected financially by lockout because they have endorsement deals and large savings to tide them over • Still want to get back to playing as careers are still limited to approximately 10-15 years • Also lose the most money from a locked out season • Negotiation does have benefits for them in the future so they are willing to hold out to avoid drastic salary reductions
Owners' Perspective	**Small Market Owners** **Examples: Cleveland Cavaliers, Nashville Predators** • Maintaining a profitable and sustainable business model for their teams over the long run • Willing to wait and extend the lockout as their primary objective is to create a CBA that will save them money • If they are currently losing money, they have nothing to lose from shutting down for a year	**Big Market Owners** **Examples: LA Lakers, Dallas Cowboys** • Primary concern is maintaining a team that is profitable in the long run • Willing to wait but also have more to lose than smaller market teams due to opportunity cost of foregone profits • In the long term, locking out is in their interest for savings and the need for sustainability of the league

2011 NFL Lockout

The NFL entered into a labour dispute in March 2011. The rookie wage scale was one of the biggest topics of discussion over the last decade as agents found innovative methods such as option bonuses to inflate rookie contracts. In the negotiations, owners argued it was financially unsound to sign rookies to larger contracts than proven veterans. A deal was struck at the end of July between the league and the NFL Players' Association. The rookie wage scale was drastically changed with a limit placed on the total amount of money given to rookies. This was expected to cut top rookie contracts by over 50%, with expected savings of $25 million in 2012, $50 million in 2013, and $100 million in 2014.

The NHL's Recovery

Many people thought the NHL would never recover. While the return of the most loyal fans was assured, the NHL risked losing the "casual" fan, a crucial category that represented the majority of the league's growth prospects. This risk looked like a very real possibility when ESPN chose not to renew its five-year, $120 million contract with the league.

The NHL survived. Its recovery can be traced to an unprecedented level of bargaining power during the lockout. New limits on expenses, combined with a major re-branding effort on the part of the league, resulted in the most profitable years the league has ever experienced. The league is on pace to surpass $2.9 billion in revenue for the 2011/2012 season, continuing the trend of record revenues post-lockout. When ESPN finally returned with a new TV offer in 2011, the NHL turned it down in favor of a 10-year, $2 billion contract with NBC.

The lockout should not be feared. From the right perspective, that of a united collection of businesses, lockouts are an opportunity to leverage the power that the owners unknowingly hold.

A Common Theme?

Instinctively, like every major negotiation or labour dispute, the aftermath leads to a discussion of winners and losers. At first, it might seem as if the union holds a lot of power in the relationship. The labour market in the Big 4 creates a unique situation: the players are irreplaceable. The next best alternative would be the use of replacement players, who could not possibly achieve the level of marketability and commercial potential as the likes of Lebron James or Sidney Crosby, despite the contrary message of a certain Keanu Reeves film. Why is it then that in the most recent labour disputes, the owners could be considered the "winners" in all three?

While it is easy to think of the union as being represented by its stars, with 15-year careers and annual salaries over $10 million, the union is actually in place to protect the majority. The average career of an NFL or NHL player, as of 2012, is only three years. More importantly, most players play less than three years in the league. While Peyton Manning can afford to sacrifice a year of salary, for

the average player this represents over 33% of his career earnings in professional sports and a vast majority of his future wealth.

At the root of the issue lies the fact that neither party is a homogenous group. The union consists of both big-time stars and small-name players, while the league includes owners in both large and small markets. The success of each side depends on its ability to find common interest within its diverse membership. For the owners, this means an understanding that while the lockout represents a significant opportunity cost for big market owners, the league cannot exist without a sustainable business model for small market teams. With that understanding, the deep-pocketed league can create a united front that can wait out the union in negotiations. At the same time, the players union has less common interests. Small-name players have only three years to recoup their forgone salary during the lockout. Meanwhile, given the long-term ownership of a professional sports team, owners have years to turn the forgone profits of a lockout into an NPV positive investment. At the end of the day, the only common interest within the players union is to end the lockout and return to playing as soon as possible.

How to Take Advantage

It is rare to find a business that benefits from shutting down for a year, so it makes sense that league owners fear locking out their players. At this point, however, as the owners approach negotiations they have the benefit of learning from precedent. Precedent shows that owners should not be worried about the fans coming back after a lockout, but rather what can escalate over the life of a CBA. In the NFL, rookie contracts ballooned to outrageous levels, which could not be corrected until the expiration of the CBA. In the NBA, salary structures left small market teams unable to re-sign their star players, which needed a 161-day lockout to fix. In the NHL, player contracts had reached a point where two-thirds of the league could not turn a profit until a salary cap was instated.

In virtually every business negotiation there will be a diversity of interests within each side, and true victories can only stem from a united front. Sometimes that can come with a natural understanding of the situation, but often it requires a re-evaluation of the stakeholders and the balance of power. In the context of sports, that means proving to big-market owners that the long-term sustainability of the league is more valuable than next year's revenues. It also means convincing owners that care more about the sport than the business. It is well known that Dallas Mavericks owner Mark Cuban would much rather beat Lebron James on the court than in a boardroom.

With a united front, the owners hold all of the power, a fact they have yet to realize. They fear that the fans will flee to other sports, but the Big 4 are not perfect substitutes, and history has shown that the fan support post-dispute is even stronger. They fear the players may flock to other professional leagues, but the Big 4 have successfully monopolized the North American market for their respective sports. They fear that TV contracts will not return, but live sports are the most valuable asset in TV, as the one recurring avenue immune to the PVR. Finally, they fear the opportunity cost of an un-played season, but a long-term view, coupled with successful negotiations, shows that a lockout can be worthwhile.

The lockout should not be feared. From the right perspective, that of a united collection of businesses, lockouts are an opportunity to leverage the power that the owners unknowingly hold. In a fixed-cost business, where player salaries are a major expense, forcing down $1 of salary leads to a $1 increase in profit. The negotiation of a CBA is the best time to achieve this in a scalable way; signing long-term CBAs simply makes this opportunity less frequent. By creating shorter CBAs, owners can better manage their costs by renegotiating salary issues with the player unions.

After NHL commissioner Gary Bettman presents the Stanley Cup in June 2012, his focus will shift towards renegotiating the first CBA since the one that ended the lockout. This time, rather than following in the footsteps of the NFL and NBA, the NHL owners must avoid a 10-year CBA in favor of a shorter one. The negotiating table has been a successful arena for team owners. They should not be afraid to go there more often.

The Walt Disney Company: Renovating the House of Mouse

How a business at its peak financial performance is missing opportunities to realize its true value.

By Michael Zawalsky

Only 11 days after the worldwide release of "John Carter," Disney projected the film would lose $200 million and push its studio division into the red. The film, which Disney hoped would be the start of a new blockbuster franchise, is now the biggest box office bomb in history. Yet, Wall Street analysts didn't flinch – and Disney's own management seemed unconcerned. Why? Because unlike most movie studios, The Walt Disney Company does not live or die by the success of a single film, quarter or year. Last year, films made up only 7% of Disney's $8.8 billion profit.

To many, Wall Street most of all, the conglomerate model is dangerous, dilutive, and dead. But at Disney, it's in full force. The company's diversified base of brands, franchises, and assets paint a promising picture for the company. However, this utopian perception is sadly contrasted with management's inability to realize the full potential of its properties.

The Walt Disney Company

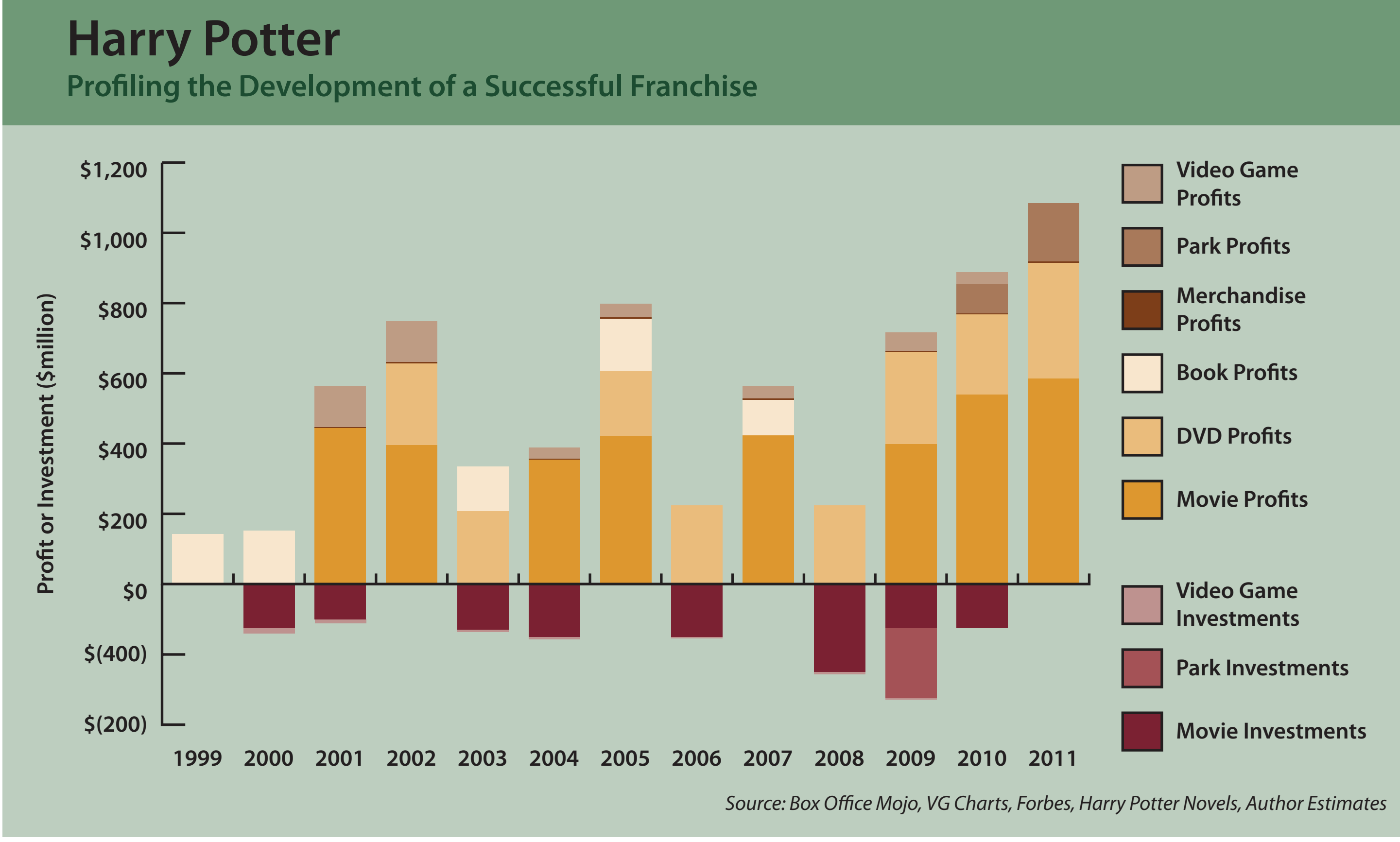
Disney's current structure is a collection of largely independent and disjointed operating units. At its core, Disney sells stories through a multi-media experience. Management understands the purpose of its core business, but is mistaken in believing its "peripheral" businesses must act as slaves that monetize this content. This way of thinking is a legacy from Disney's days as a pure-play film studio, which undermines its potential to seamlessly integrate its storytelling experience across all business platforms.

Disney's high-level strategy of late is to produce a few, large budget films per year, especially ones that continue existing franchises and then distribute this content across its value sphere. Although Disney is arguably not using its business units to the fullest, analysts praise this strategy due to its low risk and utilization of the company's core competencies. In reality, this strategy recently flopped. Huge budget films may no longer be a sustainable cash cow on their own, but Disney is in a unique position. The Walt Disney Company's conglomerate of business units has the potential to augment a pipeline of potentially blockbuster content.

Righting its Course

Disney needs to take five specific actions to help its stories achieve their highest potential:

1. Divest assets that generate content that cannot be monetized across all Disney media, most often the content that doesn't tell a "story."



2. Acquire assets that fill gaps in how the story can be told.

3. Set up all businesses as content-generating units.

4. Set up all businesses such that content from peripheral units can be easily shared; restructure the company as a "Disney Family."

5. Protect all owned brands and ensure the "story" is told consistently.

Focus and Finance: ESPN

It is a little-known fact that ESPN generates 40% of Disney's cash flow and is its largest asset. Many would consider ESPN to be Disney's crown jewel – live televised sports programming is some of the only content immune to piracy and PVRs. ESPN's earnings power makes it a financial asset, but not a strategic one. It is fundamentally dissimilar from all of Disney's other properties and its content cannot be properly monetized across the company's other channels. By divesting some of its position in this giant, Disney could rid itself of a possible conglomerate discount and refocus resources on creating a "content ecosystem" that truly leverages its unique story-telling capacity. Selling 60% of its 80% ownership in ESPN could net up to $15 billion in capital that can be diverted to businesses that support the creation of this ecosystem.

The Missing Pieces of the Puzzle: Acquisitions and Growth

Disney's conglomerate structure can realize tangible synergies by distributing content through multiple channels. The company can therefore maximize value by owning as many unique channels as possible. This structure will not only capture the cash flows from these channels, but provide a truly multi-media storytelling experience that is difficult to replicate. By providing multiple avenues to consume the same story, the costs associated with generating the story can achieve meaningful economies of scale.

It is important to note that Disney is not limited to generating content in one or two business units. The company has the resources to restructure each business into a content generator and deliverer. By labeling the film unit as primarily a content generator and other units purely as distributors, the company leaves many combinations of generation and distribution unexplored, and diminishes its capacity for reinventing what it means to tell a story.

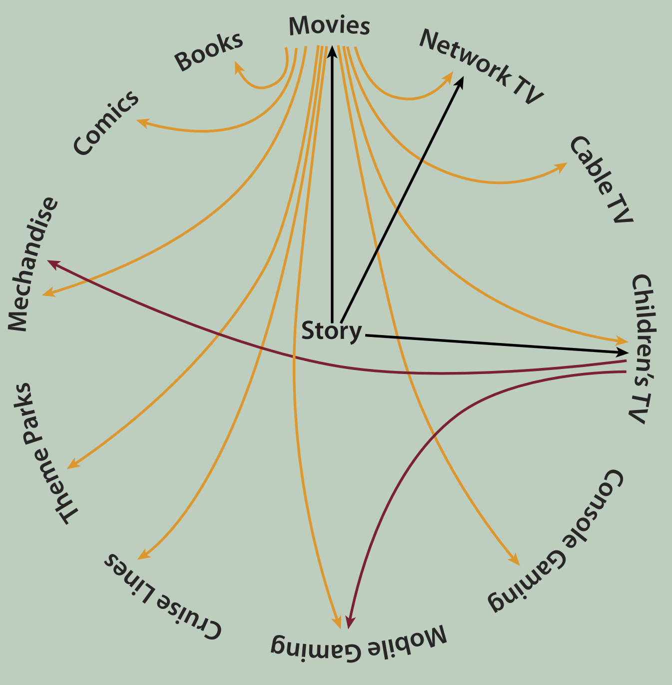
Video Games

Disney has made forays into video games but has yet to make a bold move into the space. So far, the company has captured value from the video game market by licensing its intellectual property to publishers rather than creating titles itself. Acquiring a major console-game producer and publishing its own titles would allow Disney to reach its potential in this space.

Not one of the top 10 grossing movie titles of 2011 spawned a top 100 selling video game. These games fail to gain traction for many reasons, but ultimately fail to succeed because they are treated like merchandise. Licensees generally take two hours of film content and attempt to spread it over a twenty-hour gameplay experience; it regularly feels like an afterthought.

Content Value Sphere

Disney's Dependence on Movies for Growth



> *"John Carter" is an excellent case study for the telling of a risky story. Disney spent over $350 million bringing the film to market despite a lack of consumer awareness for the source material.*

This has two main implications for Disney. First, the mediocrity of film-based video games has the potential to hurt the movie's brand and alienate fans of the franchise. Second, and more importantly, Disney's writing talent and competency for telling stories is underused in the context of video games. Leveraging these capabilities in the video game space can allow the company to tell a story via film and game, adding a completely new dimension to the narrative and providing an immersive experience unmatched by EA and Activision. If executed correctly, Disney could add hundreds of millions in revenues over the lifetime of a story franchise.

Publishing

Disney currently owns Hyperion, the publisher that releases books based on Disney, ABC, and ESPN content. "Artemis Fowl," a Hyperion-published novel, had eight-figure sales over several volumes but a film franchise was never developed. Hyperion needs to place greater focus on producing original novels that have franchise potential. Book series such as "Harry Potter, "The Hunger Games" and "Twilight" reflect consumers' demand to experience content through multiple avenues. Launching a book is less risky than producing a movie and could allow Disney to test the waters of a risky story. A book's success could prove to be an excellent way to kick-start a franchise.

"John Carter" is an excellent case study for the telling of a risky story. Disney spent over $350 million bringing the film to market despite a lack of consumer awareness of the source material, yet when it was first published in 1917, it was critically acclaimed. Disney could have easily used Hyperion to re-launch the series in print and grow awareness through that medium. It would have required far less investment (and less of a loss in the case of a flop) and could have slowly developed a new fan base, which could have been offered a film as a secondary way to experience the story.

Internet Distribution

Disney is currently developing its Keychest prototype: an online store for all of its content. Launching Keychest as a subscription-based service would be extremely valuable. Revenue from the service would be used to finance Internet movies and television shows generating a large volume of new content. Micro-financed productions would have the freedom to create risky and original content for little cost – stories that, if received well, could be scaled up. Joss Whedon saw success when his self-financed production "Dr. Horrible's Sing-A-Long-Blog" not only won an Emmy, but through sales of DVDs and soundtracks generated positive returns and had fans clamoring for a sequel. For a low-capital investment, he was able to build the foundation of a potential franchise.

Cable Television

Disney should acquire AMC Networks and its associated channels. AMC's stable of content includes "Mad Men," "Breaking Bad," and the "Walking Dead," some of the most critically acclaimed series on television. This acquisition has already been identified as a good fit by numerous analysts who note that it would allow Disney to reach a new demographic. Further, Disney could capitalize on AMC's strong international sales team to reach new markets.

The true benefit of AMC, however, is its ability to fill another gap in the content value sphere. Disney currently does not have a dark and dramatic outlet like AMC, which could be used for more experimental, medium-budget projects.

Piecing Together the Puzzle: Creating a Disney Family

Growing and acquiring these businesses alone will perpetuate Disney's inefficient conglomerate structure. The proposed Disney model only works if there is new content to monetize; therefore, the volume of content is a key piece to the puzzle. Disney needs to fundamentally alter its culture to one that nurtures content creation. To do this, Disney must create loyalty amongst its talent, such as higher job security to incentivize risk taking, and a lowered cost structure to allow more daring and original productions.

Franchise Performance

Movie Rankings vs. Game Adaptations (2011)

(Tickets Sold) Movie	Rank	Rank	Game (Units Sold)
(48.3MM) Harry Potter and the Deathly Hallows Part 2	1	1	Call of Duty: Modern Warfare 3 (11.3MM)
(44.7MM) Transformers: Dark of the Moon	2	2	Kinect Adventures! (5.1MM)
(35.7MM) The Twilight Saga: Breaking Dawn Part 1	3	3	Pokemon Black/White Version (4.4MM)
(32.3MM) The Hangover Part II	4	4	Just Dance 3 (3.8MM)
(30.6MM) Pirates of the Caribbean: On Stranger Tides	5	5	Gears of War 3 (3.0MM)
(26.6MM) Fast Five	6	…	
(26.5MM) Mission: Impossible - Ghost Protocol	7	NR	Cars 2 (920K)
(24.3MM) Cars 2	8	NR	Transformers: Dark of the Moon (470K)
(23.7MM) Sherlock Holmes: A Game of Shadows	9	NR	Harry Potter and the Deathly Hallows Part 2 (350K)
(22.9MM) Thor	10	NR	Thor (160K)

"NR" = No Rank (Sales too low)

Source: Box Office Mojo, VG Charts, NATO

To execute on these three points, Disney needs to actually hire talent rather than follow the traditional freelance model popular in Hollywood today. Instead of freelancing directors, writers, editors, actors, and producers, the company should sign them to three to five-year contracts. This job security would be a rarity in Hollywood, and the value of this certainty would allow Disney to secure talent at a lower cost per unit of time. By owning this talent, it could be leveraged across multiple platforms for a lower cost than any one production would allow.

This type of structure would give staff the security to take artistic risks, lower the cost structure of each project, and create talent-brand strength. The volume of available projects as a result of the new distribution channels would ensure that the talent always has a project to engage in. As a result, Disney could have one of its film stars appear on a struggling television show, or anchor the launch of a new Internet series when they aren't filming. This type of production model is only possible to achieve at present by a well-aligned conglomerate that behaves as one close-knit family.

Disney needs to focus its divisions around storytelling in a multi-media context. It needs to create structures that will ensure properties are seamlessly integrated across channels – creating maximum value.

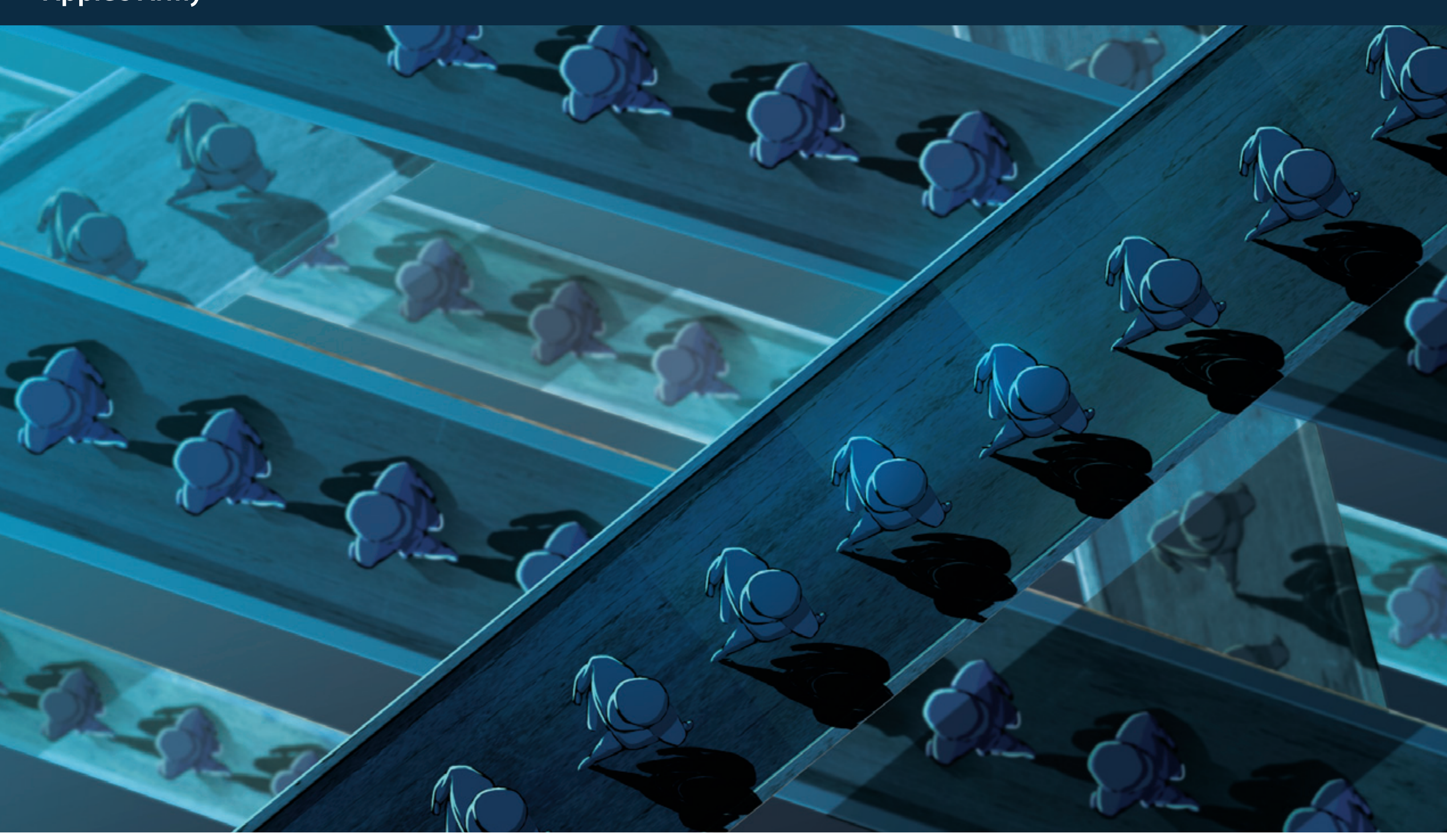
Protecting the New Mouse House

Developing an idea into a viable franchise takes commitment and investment over a long period of time, which is why Disney's stories are its most valuable asset; stories are timeless, they never die. But if improperly managed, whether through overexposure or neglect, a story's value can be significantly damaged. It is essential that Disney take action to protect its franchises because, when properly managed, they become lucrative perpetuities.

To this end, Disney should form steering committees for all of its major franchises. These teams, comprised of both brand managers and creative personnel from Disney's various business units, would report directly to the CEO. They would serve the dual function of ensuring that all extensions don't dilute the brand and that stories are integrated across channels seamlessly. This steering committee structure would facilitate the sharing of ideas and talent across departments. Such integration would immerse fans in the brand to a degree that competitors cannot achieve.

The Next Act

Disney has suffered managerial incompetence before and managed to survive because its assets are resilient and its conglomerate structure insulates them from risk. But the current structure also prevents it from realizing the true value of its properties. Disney needs to focus its divisions around storytelling in a multi-media context. It needs to create structures that will ensure properties are seamlessly integrated across channels – creating maximum value. To structure itself as such will require immense resources, provided by the divestiture of the majority of its safety net, ESPN. It will take dedicated work at all levels to implement this strategy. But if it doesn't, Disney runs the risk of becoming a real Mickey Mouse operation.



Apple's Army

Resuscitating Foxconn's profitability.

By Jiemi Gao and Kevin Zhou

Three decades ago, Terry Gou, Foxconn's Taiwanese founder and chairman, bought his first plastic moulding machines to make knobs for black and white televisions. Today, Foxconn employs 1.2 million workers worldwide and manufactures and assembles crucial components for companies like Apple, Microsoft, and Samsung. What started as an independent venture, funded by a $7,500 loan from Gou's mother, has grown into a fully-integrated electronics manufacturer with $115 billion in revenue.

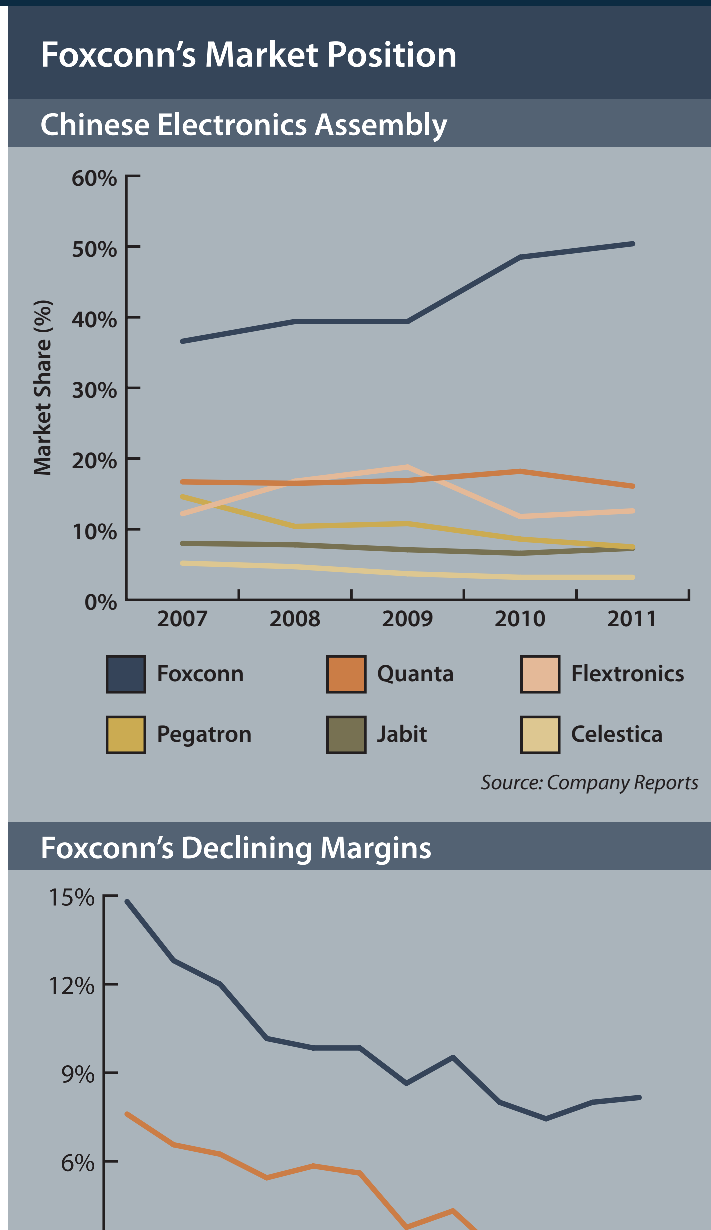
Foxconn represents the ultimate paradox. The firm manufactures an astounding proportion of all consumer electronics, is irreplaceable to the world's most prestigious electronics companies, and operates with a level of precision and scale that simply cannot be matched. Despite this, the company has seen its margins steadily decline over the last decade, and rising wages are poised to accelerate that trend.

A Silent Giant

Far and away the leader in its industry, Foxconn manufactures over 40% of all electronic devices produced on Earth. According to the Consumer Electronics Association, the average American household owns 25 consumer electronic products – of those, Foxconn has manufactured 10. It's the silent giant on our walls, on our desks, and in our pockets.

Foxconn employs a vertically-integrated business model positioned as a one-stop manufacturing and assembly shop for consumer technology companies. With a mission to manufacture affordable electronics for consumer products worldwide, it has developed unparalleled expertise and scale. The company's ability to create high-quality products in great quantities with extremely low lead times has allowed it to capture a growing number of leading customers, most notably Apple. The story of outsourcing manufacturing to Foxconn is not only about price; in today's market, it is also about quality of service – measured by flexibility, speed, and expertise.

One anecdote from a former Apple executive describing how Foxconn was able to respond to a last-minute change in the iPhone's screen perfectly captures this value proposition. When redesigned screens began arriving at Foxconn at midnight, management roused 8,000 workers from inside its dormitories, gave each a biscuit and a cup of tea, and guided them to a workstation. Within half an hour, workers had started a 12-hour shift fitting the new screens into their frames; within 96 hours, the plant was producing over 10,000 iPhones a day. The company's flexibility extends beyond the use of just existing workers. According to Jennifer Rigoni, Apple's worldwide Supply Demand Manager until 2012, "They could hire 3,000 people overnight."



The company has also fortified its expertise in manufacturing over the last decade, developing over 25,000 patents. The firm now employs over 50,000 toolmakers and 2,000 highly skilled workers who focus solely on developing the moulds and dye related to the manufacturing process. This move into higher margin products and services has allowed the company to subsidize its less profitable final assembly business, allowing it to continue competing aggressively on price against pure-play assembly companies.

Foxconn's customers have profited immensely from its scale, flexibility, and manufacturing expertise. Apple's most recent quarterly earnings, $13.87 billion with 28% net margins, were the highest in the history of corporate America. Foxconn, conversely, reported earnings of only $1.1 billion with 3% net margins over the same period. In general, the company earns a measly 2-5% net income margin compared to its customers that make more than 20%. Worse yet, while Foxconn has seen revenues increase over the last decade, the company's gross and operating margins have been steadily declining.

Volume, Volume, Volume

Foxconn's relatively weak financial performance seems extremely counterintuitive in the face of its immense scale, industry-leading position, and successful customers. How has the company responsible for many of the world's most popular products seen its profitability decline even as its end market soared?

The story of Foxconn's growth presents a partial explanation. Throughout its history, the company has pursued a strategy that favored increased volume over profitability. The company maintains a deeply-rooted philosophy of catering to its customers, often sacrificing margins to keep its customers happy and increase market share. For example, in order to secure Dell as a legacy customer, Foxconn purchased a manufacturing plant in the U.S., close to the final market as requested by Dell. Although the plant was ultimately unprofitable, Foxconn managed to secure a long-term customer.

While this strategy allowed Foxconn to grow into the giant it has become today, it also typecast the firm as a low-margin, limited value-add manufacturing partner. As labour costs have increased due to higher minimum wage requirements instituted by the Chinese government, Foxconn was expected to accept the increased costs themselves instead of passing them along to their customers. Direct labour costs have increased 63.1% and 15.7% consecutively in the last two reporting periods compared to revenue, which increased 50.1% and declined 15.8%. This diverging trend is likely to continue in the future, threatening Foxconn's ability to remain profitable and compete in an industry underscored by speed and flexibility.

The Imbalance of Power

For most of its history, Foxconn relentlessly pursued volume in the hopes that its scale would eventually turn the power balance between Foxconn and its customers on its head. Wal-Mart serves as an illustrative example of a firm who succeeded by pursuing a strategy that sacrificed margins for volume as it grew. Over time, Wal-Mart's volumes had grown enough that it was able to place enormous amounts of pressure on suppliers to increase margins without raising prices on consumers. Foxconn's strategy was predicated on being able to exert pressure forward in the value chain on global consumer electronics giants, rather than backwards as Wal-Mart has.

Foxconn succeeded in achieving meaningful scale, but they've been unable to translate that into material bargaining power as

Wal-Mart did. This difference emerges from the companies' relative positions in the value chain. Taking the production of the iPhone as an example, Foxconn manufactures only low-value parts, such as buttons and casings, and assembles the final device. High-value components including semi-conductors and the phone's display are manufactured elsewhere by Samsung, Texas Instruments, Taiwan Semiconductor, and others. This role limits the firm's ability to pressure its customers into paying higher margins.

As much as its scale, flexibility, and experience allow Foxconn to provide value to its customers, at its core, the company succeeds through its ability to mobilize huge amounts of unskilled labour at a moment's notice. Alone, this ability does not represent a sustainable competitive advantage; with enough money and time, it can be replicated.

This fact becomes especially important in Foxconn's relationship with its largest customer: Apple. While Foxconn's scale makes it the only supplier large enough to serve Apple exclusively, this has not translated into bargaining power. Apple requires approximately 19% of available electronics assembly capacity in China. The next largest manufacturer in China, Quanta, only supplies 16% of the market. If Apple were to switch suppliers, they would need to coordinate between multiple suppliers, complicating the supply chain and potentially increasing lead times. Conversely, it is estimated that Apple will contribute 39% of Foxconn's overall 2012 revenue, up from 34% in 2011. While Apple and Foxconn would both be harmed if their symbiotic relationship were to dissipate, Foxconn would find itself in a much more precarious position.

Apple has not been averse to using its cash balance to shore up its supply chain, including making large up-front payments to secure components and invest in supplier manufacturing facilities. It is conceivable, then, that Apple could finance the creation of a new Foxconn over time, should the relationship sour. This situation drastically limits Foxconn's ability to exert power over Apple.

Shifting Strategy

In response to rising labour costs, Foxconn has pursued a cost-cutting approach that is ultimately unsustainable. Moving to inland cities with 30-40% lower expected minimum wages may provide some temporary relief. Cities in China's interior are estimated to account for 50% of Foxconn's production in 2012, up from 30% in 2011. Rather than hiring migrant workers, allowing them to live close to their families could also boost morale and lower suicide rates among Foxconn's workforce. However, the concern with moving inland is that lead times will increase and Foxconn will sacrifice one of its key competitive advantages – flexibility. Furthermore, wages inland will eventually rise and Foxconn will once again find itself in the same position.

More importantly, Foxconn has recently taken strides to provide higher value-added services through the manufacturing process. The company recently invested $1.6 billion into Japan's Sharp Corporation. Sharp's LCD technology and its portfolio of intellectual property will allow Foxconn to manufacture the parts that distinguish Sharp products. By making this strategic move into a specialized and differentiated part of the industry, Foxconn diversifies its product base and raises its customer's barriers to exit. Preemptively acquiring a stake in Sharp and subsequently developing experience in manufacturing high-value-added LCD parts not only allows Foxconn to supply Apple with screens for current devices, but also increases Foxconn's bargaining power if and when an Apple TV set is launched. The more products it provides to its customers, the greater the economies of scale.

Ebbing the Tide

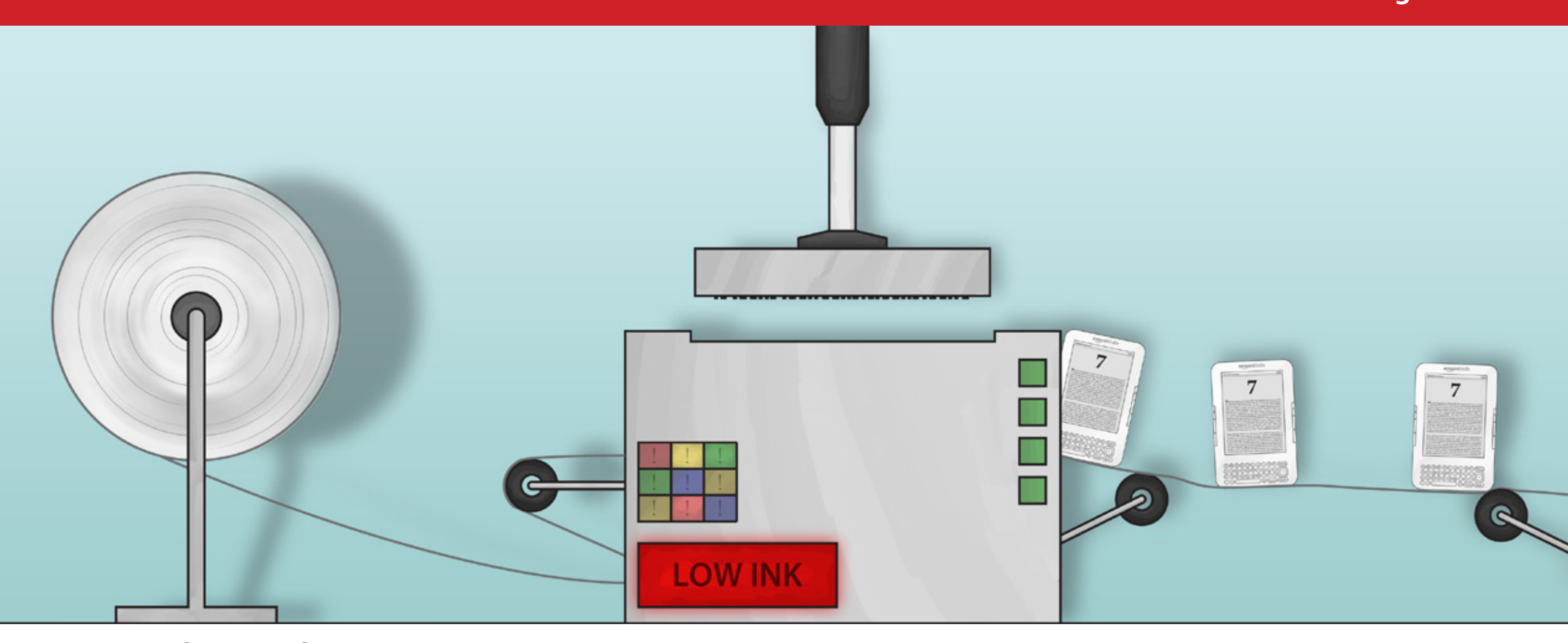
Today, Foxconn is a best-in-class company in a low margin, low value-add industry facing a rapidly escalating cost structure. It has a limited ability to control its costs or to pressure customers into providing higher margins.

Ironically, it may be the current social climate rather than its relative industry positioning that could prove to be advantageous for the company. Reminiscent of Nike's problems with sweatshops and child labour, as consumers become increasingly concerned with poor working conditions and associate it with Apple's brand image, mounting customer pressures could force Apple to subsidize increases in labour costs. Given Foxconn's razor thin margins, it could argue that they do not have enough money to pay their workers well. At the very least, Foxconn can demand that its customers share the burden of increasing wages. While this won't improve Foxconn's margins, it will help stem the current decline.

To reverse the pressure, Foxconn needs to shed its volume-first philosophy and take steps to add more value in the supply chain. The company's recent investment in Sharp is a step in the right direction, and the firm has a war chest of more than U.S. $8 billion to fund future investments in new plants, to develop new processes, or to acquire minority stakes in adjacent industries, such as semiconductors – a necessity in the innovation-driven smartphone and tablet market.

As it has with its recent investment in Sharp, Foxconn should enter the early stages of the value chain by building its manufacturing capabilities for less commoditized, high value-added components. Moulding a casing and assembling an iPad is one thing, but manufacturing a new LCD screen is another. Transitioning their core competency away from simply mobilizing human resources to engineering and manufacturing high-value-added components will be critical for the long-term survival of the company.

Foxconn has promised to take major steps to improve worker conditions, wages, and eliminate overtime. These promises will further weaken Foxconn's competitiveness unless it is diligent and utilizes its cash reserves and manufacturing capabilities to increase its value in the supply chain. Foxconn must make dramatic changes to ensure it does not tumble from its lofty industry position. If it fails, Foxconn will fade as an anomaly of the market instead of becoming the titan it has the potential to be.



Printing Pressed

How publishers can squeeze margins from an online bookstore.

By Mathew MacFayden and Jared Schachter

In the six years since Sony released the world's first e-reader, e-books have revolutionized the consumer book industry. Between 2010-2011, e-book revenue grew to over $1 billion, a staggering 280% increase, while sales of adult paperback and hardcovers fell 18%. The recent liquidation of the United States' second-largest book retailer, Borders Group Inc., highlights this shift to digital format and underscores even the most dominant bookstores' struggle for survival.

Such drastic change and growth in the industry presents both opportunities and threats for the publishing industry, whose role is becoming obsolete. Large content aggregators like Amazon are in a unique position to not just squeeze publisher's margins, but potentially eliminate them altogether. Conversely, e-books present a sizeable opportunity for publishers to reach a much larger population – over 18% of adults now own either a tablet or e-reader compared to the 15% of Americans who regularly read books. Publishers can encourage more readership and take advantage of this new and convenient medium, the only question is how.

Self-publishing success stories like Kerry Wilkinson, whose novel "Locked In" was the top seller on Amazon UK for the last three quarters of 2011, are bringing attention to this increasingly popular opportunity. Authors keep far more royalties of each book sold when they publish independently.

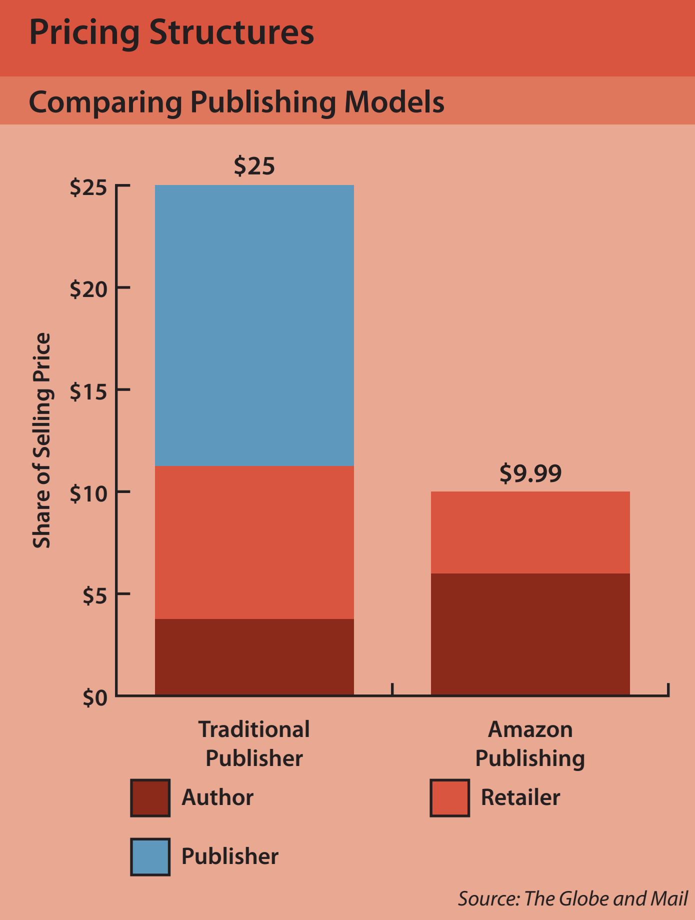
Lessons from the Music Industry

The music industry faced a similar transformation only a decade ago following the introduction of digital audio. Today, digital music sales account for more than half of all music sold in the U.S. market. Record labels found themselves at a crossroads, unable or unwilling to analyze and react to rapidly changing circumstances. Afraid to lose market share, they chose litigation to halt online file sharing rather than develop tools to service digital demand. Consequently, they had little bargaining power when iTunes negotiated the online pricing system for music. Though piracy may pose much less of a threat to books, publishers stand to walk in the shadow of record labels if they fail to embrace this new paradigm.

The Problem

Major publishing houses are still profitable, but Amazon's activity in this area gives rise to concern. Publishing companies typically perform four main functions: scouting and talent development (identifying authors and cultivating their work), financing book production, distribution, and marketing. E-books undermine the middle two roles because authors can publish their work independently, through a handful of avenues with little risk. The shift to digital form eliminates the need for much of the publisher's traditional role: financing a printing operation, physically printing the book, and delivering to retailers.

Self-publishing success stories like Kerry Wilkinson, whose novel "Locked In" was the top seller on Amazon UK for the last three quarters of 2011, are bringing attention to this increasingly popular opportunity. Authors keep far more royalties of each book sold when they publish independently.



Promoting and marketing a book, such as having it reviewed by critics in popular media, managing book tours, and selling potential film rights are also value-added activities. Without the reputation and network of a major publisher, it is difficult to access these opportunities.

Thus, Publishers need to demonstrate that higher sales volumes achievable through their process can offset lower royalties. This argument becomes weaker as e-books become more popular. Although there are few successful self-publishing stories, going alone is a very compelling prospect when experiences like Kerry Wilkinson's are recalled.

Amazon offers publishing services somewhere between independence and the traditional route, though the company has yet to sign a blockbuster author. Authors under Amazon may face difficulty getting their product into brick-and-mortar retailers, who are not particularly interested in supporting parties contributing to their demise. Amazon has significant financial resources, however, and a growing roster of established authors. Amazon's higher royalties are luring established authors, including best-selling thriller-writer Barry Eisler, who recently turned down a $500,000 contract with St. Martin's Press for Amazon, citing higher royalties. Although Amazon Publishing is distinct from self-publishing, it poses the same threat to traditional publishers because it is positioned to take advantage of the industry shift to e-books.

E-books negate a publisher's most well-known role, distribution, and substantially reduce the financing requirements for printing. To escape obsolescence, publishers must examine which of their current offerings actually add value in an increasingly digital world. Publishers need to embrace a digital medium and take action to build a presence in the digital environment.

Moving Forward: Where Publishers Add Value

Due to the upfront investment in time and the cost of publishing a printed book, publishers previously acted as a gatekeeper for aspiring authors. Consequently, publishers developed competencies in identifying creative talent and cultivated their work to its fullest potential. This competency is still valuable for readers, potentially now more than ever. Mediocrity is inherent in the self-publishing model because there is no content filter. Identifying quality content may become increasingly difficult depending on how the self-publishing phenomenon plays out. Moreover, the time required to read a book poses an obstacle to effective peer reviewing. A publisher's role of filtering content and giving a stamp of approval still adds value by legitimizing a book for readers.

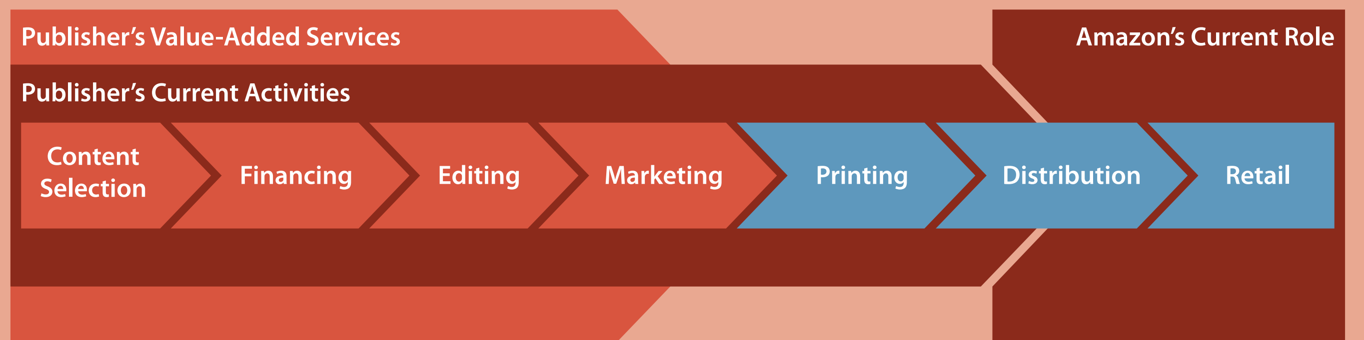
Promoting and marketing a book, such as having it reviewed by critics in popular media, managing book tours, and selling potential film rights are also value-added activities. Without the reputation and network of a major publisher, it is difficult to access these opportunities. By taking care of the marketing aspect, publishers allow writers to focus on what they do best: writing. St. Martin's Press recently signed Amanda Hocking, who was selling roughly 100,000 copies of her self-published works through Amazon every month. She had grown tired of the burden of marketing and editing roles that publishers fill efficiently.

Action Plan

Publishers must accept the inevitable shift to e-books while communicating the value they still provide. While a publisher's brand is still valuable in literary and news circles, it has little pull with the common reader. However, with the oncoming flood of self-published works, publishers have an opportunity to create a relevant brand amongst everyday readers. To build a consumer brand, publishers need to create a strong brand-quality association similar to that of Pixar, whose brand plays a critical role in the consumer's decision to watch a movie. This is no easy transformation, because consumers identify with brands that represent specific experiences. For instance, Pixar fans know to expect a smart, well-made computer generated film. Currently, publishing houses produce books in a wide variety of genres that appeal to different tastes. Their diverse offerings prevent readers from identifying a publisher with a particular brand perception. If

The Publishing Value Chain

Examining the Roles of Key Players



Though Amazon currently occupies a space adjacent to publishers in the value chain, it is moving into roles traditionally claimed by the publishers and is threatening the usefulness of the value-added services they provide.

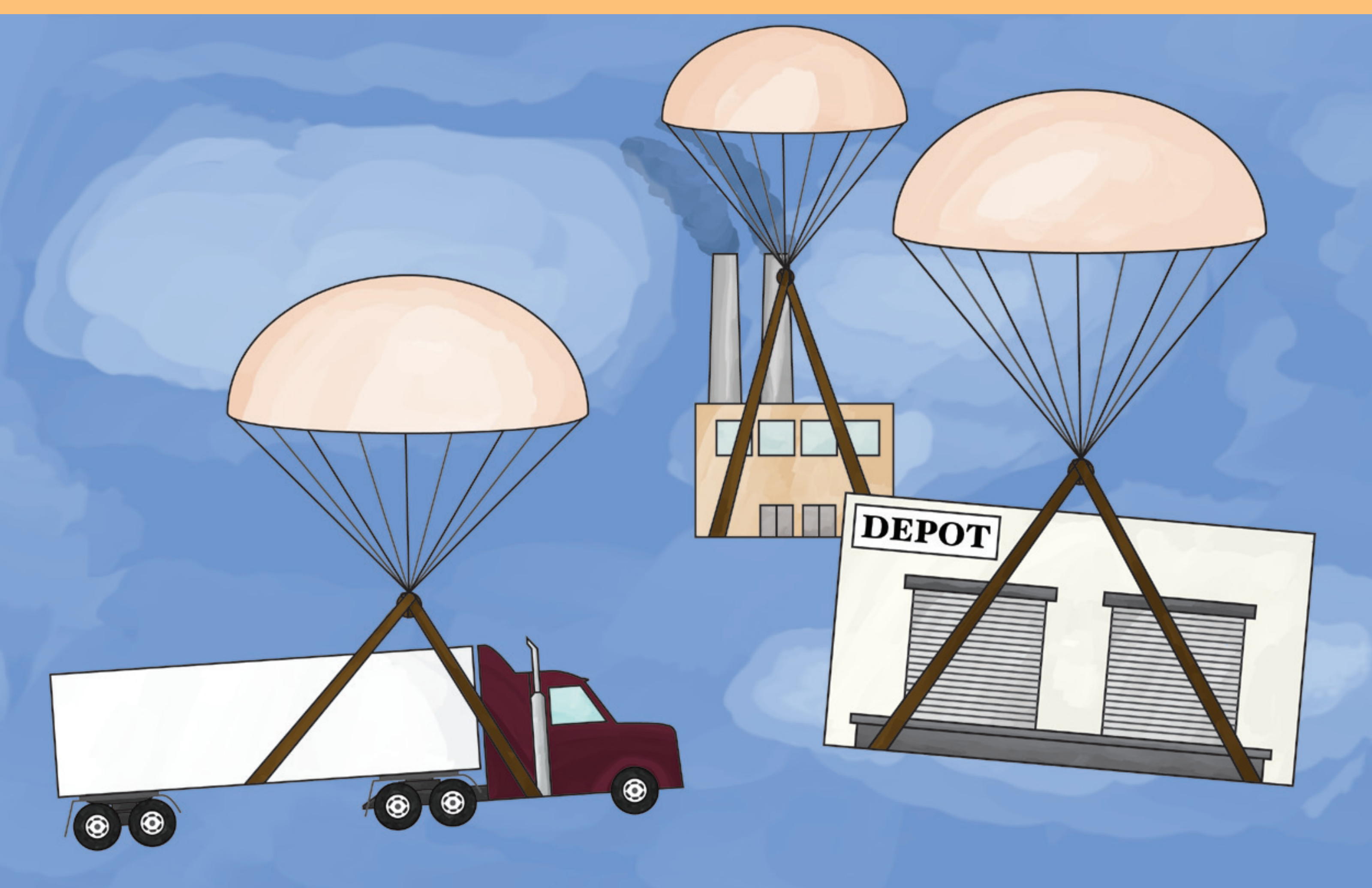
publishers create sub-brands focused on particular niches, which develop a reputation for offering consistent and entertaining content, they can very possibly build consumer brands.

Moving online also provides traditional publishers with many opportunities. Just as publishing online is a low-cost venture for individuals, it is also low cost for publishers. This route can serve as an incubator for titles that seem too risky to launch in a physical sense but may very well prove successful when given the chance. Additionally, niche markets that are currently underserved because of diseconomies of scale in printing can be targeted with lower-cost online publishing.

Self-publishing poses a threat to traditional publishers, but it could also be managed as a recruitment opportunity. Successful self-published authors are often unable to manage their work as it becomes a mass-market offering. The core competencies of a publisher become a real value proposition to these authors who simply cannot manage their book's success. As Nathan Maharaj, merchandising director of Toronto-based Kobo Incorporated describes, "the future of publishing may not be a battle of small versus large; it may become small publishers feeding market-proven content to large ones."

Self-publishing can serve the interests of publishers, rather than hinder them, by serving as a farm for talent. By funnelling consistent content and owning a genre, a publisher can one day build a consumer brand that will resonate with a profitable consumer segment.

The business community at-large views publishers as dinosaurs with outdated value propositions. Although this view has elements of legitimacy, the outlook for publishers is not necessarily as grim as it appears. Publishers are in a somewhat more fortunate position than record labels because they can learn from the music industry's failures. Resources must be diverted from printing and distribution to make room for an offering that makes sense considering current industry realities. Identifying and developing talent, as well as marketing content, is not only an area that has room for entry, but an area that may see huge voids as self-publishing and ubiquitous mediocrity grow in prominence. Self-publishing can serve the interests of publishers, rather than hinder them, by serving as a farm for talent. By funnelling consistent content and developing recognizable sub-brands, a publisher can one day build a consumer brand that will resonate with a profitable consumer segment. The publishing industry stands on a precipice, but fortunately for this space, it may not be too late.



Reimagining Disaster Relief

How companies can help provide immediate assistance when disasters occur.

By Mathu Jeyaloganathan

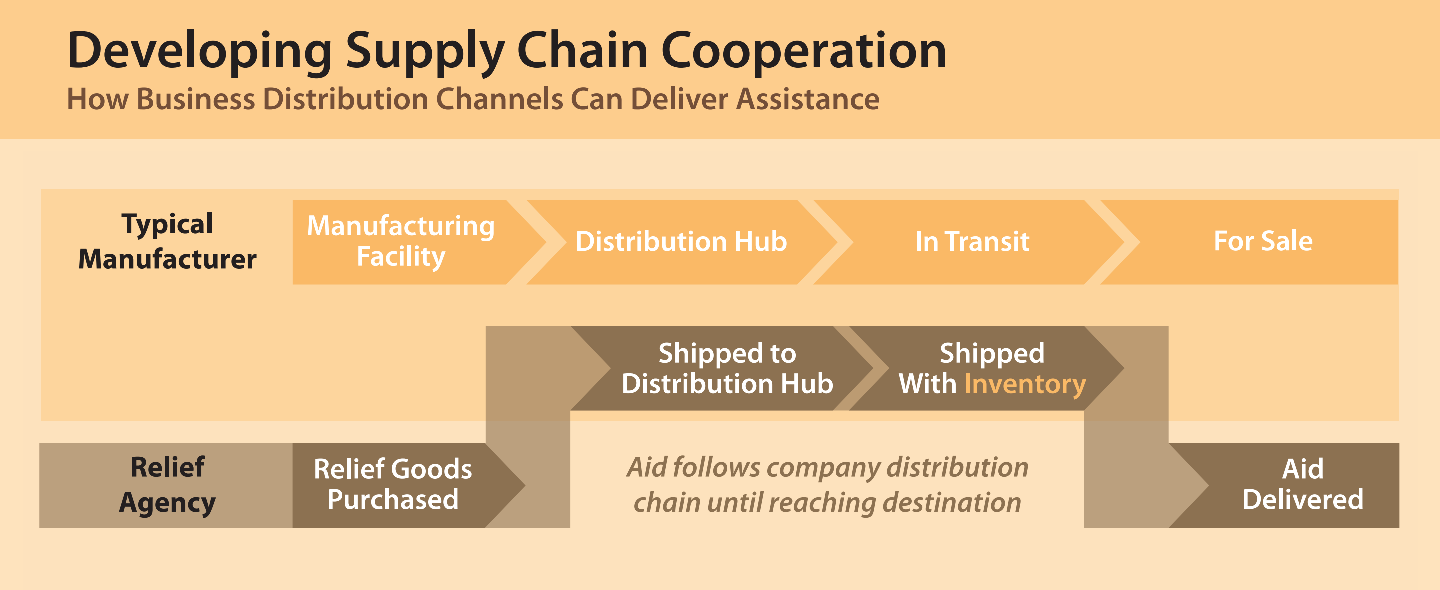
On March 11, 2011, the most powerful earthquake in Japan's history devastated the country; 15,000 were killed, 6,000 injured, and 4,000 missing. Hundreds of thousands of people were left without homes, 2.2 million without running water, and 4.4 million without electricity. A fragile economy was left in ruins with $284 billion in value withdrawn from the Tokyo Stock Exchange in the three days following the disaster. Naoto Kan, then Prime Minister of Japan, described the earthquake and tsunami as "the toughest and most difficult crisis for Japan" since the Second World War.

The international community rallied together to help rebuild the country and every effort was made to ensure timely delivery of all necessary resources. Unfortunately, efforts were met with disappointing results. Death and injury tolls were highest immediately following the disaster, but the first three days of the rebuilding effort saw only 10% of total donated aid actually delivered.

Despite every aid agency around the world employing their resources and efforts, they acted in discord and inefficiencies were rampant throughout the distribution process. Though costly and unpredictable, the response to natural disasters can be made more efficient through partnerships between NGOs and companies looking to strengthen their corporate social responsibility (CSR) position.

Void in the System

Following the Japanese tsunami, resources were not delivered on time because of excessive bureaucracy, poor distribution infrastructure, and a lack of coordination between agencies. At face value, one would assume bureaucracy is minimized when each passing minute costs lives. Unfortunately, the size, scope, and sheer number of NGOs results in layers of red tape at all levels of the organization. Since many organizations are only operational following disasters, significant time and effort must be devoted to simply build the infrastructure needed to provide aid after any



given disaster. Finally, the global disaster relief system is very fragmented – although the goal is the same, the means of achieving it are different and behaviour is disarrayed.

A Fruitful Partnership

Partnerships between private enterprises and NGOs could drastically improve the delivery of aid in the wake of natural disasters due to the efficiency, reach, and independence of private multinational corporations. The ability to execute a pre-planned strategy instantly minimizes the bureaucratic decisions made by each NGO, ultimately expediting implementation. Multinationals already have well-developed infrastructure and distribution networks in place around the globe, eliminating the need for haphazard supply chains to be assembled in foreign jurisdictions. Finally, a single-party distribution chain solves the problem of a disjointed system with different opinions, mandates, and priorities.

Unfortunately, the size, scope, and sheer number of NGOs results in layers of red tape at all levels of the organization.

If NGOs are able to leverage pre-existing supply chains instead of working independently to build temporary ones when disaster strikes, critical goods such as food and medicine can be delivered to people in need significantly faster. NGOs could then focus their resources on securing an adequate supply of aid and providing it on site.

Finding the Right Candidate

First and most importantly, the ideal private enterprise partner must have a just-in-time inventory system with minimal lead time. Disasters can happen at any second and aid needs to be expedient. The candidate must be able to transport food, medicine, or any other required good at a moment's notice.

Second, the company must wholly own their distribution system. Businesses commonly outsource pieces of their supply chains where they cannot operate as efficiently as a pure-play distributor. When disasters strike in regions where the distribution chain is not wholly-owned, coordinating the distribution of relief would become significantly more difficult and the company could lose many of the CSR benefits to the contracted party.

Third, the candidate must have a clean record; NGOs will be unwilling to work with a company that has a controversial reputation.

The Candidate's Motivation

The last decade has seen increased adoption of CSR initiatives. Companies are constantly looking for new ways to differentiate themselves from their competitors. Taking a leadership role in proactively mitigating a disaster's destructive forces would position a company's brand at the forefront of what it means to truly give back.

Helping rebuild a country boosts brand equity, especially from citizens of the affected region. If a company such as Coca-Cola were not only the first on scene, but also the primary force delivering food to a devastated community, the Coca-Cola brand would long be associated with the community's recovery. Apart from the brand's perception within the affected area, the company would achieve worldwide recognition for its CSR efforts. In addition to attracting new customers and solidifying brand loyalty, the company's gleaming reputation could make it a much more popular destination for managerial talent.

For a private enterprise, reallocating a portion of a supply chain to disaster relief efforts is not without its costs. Companies incur both direct costs related to transporting the aid, as well as significant opportunity costs in terms of lost sales or stalled production. However, the opportunity cost may not be as high as initially assumed. If a region is disaster-stricken, the shock imparted by the crisis limits the company's ability to function as usual. Partnerships

would be structured such that NGOs would cover all direct costs related to transporting the food or medicine, as well as a portion of the indirect costs. In this way, NGOs would help cover fixed costs that the firm would have to pay regardless of how much is being transported through their supply chain. For firms whose supply chains are running below capacity during a disaster, a partnership with an NGO could break even or prove financially beneficial.

Implementation of the Strategy

Companies that employ just-in-time inventory management systems often invest in excess capacity to provide flexibility when servicing variable demand. The option of utilizing this excess capacity is possible if an agency were able to coordinate and cover incremental costs. This excess capacity would serve as the distribution system for partner NGOs. Instead of being shipped to an NGO, donated medicine would be shipped to a node in the company's distribution system and subsequently moved to the disaster area along with inventory headed for that region.

To minimize the burden on the company and maximize the probability of buy-in, the NGO would have to employ a coordination specialist to manage the distribution of food or water in conjunction with the partnering company. The NGO would provide the company with a stockpile of first-response resources and people to help coordinate and facilitate its distribution to ensure immediate expedience. Since excess capacity is already built in, the addition of humanitarian resources has little effect on the fixed-cost nature of the system. Firms would lose the flexibility to meet increased demand that excess capacity is designed to allow; however, in the event of a disaster, this is likely to go unused anyways.

Case Study: Mitsubishi's Implementation in Japan

The outpouring of support from governments and NGOs after the Japanese earthquake was tremendous but slow. A partnership between the Australian subsidiaries of Mitsubishi and the Red Cross could have benefitted Japanese relief efforts if the proposed strategy were implemented.

The outpouring of support from governments and NGOs after the Japanese earthquake was tremendous but slow.

Following the disaster, Mitsubishi's plants located in the country's Southwest were unaffected by the earthquake. Prior to the tsunami, the company would import feedstock for products useful to the relief effort through their still-functional Port of Nagoya. The stockpiles of food, water, and medicine that would have been proactively shipped to one of Mitsubishi's distribution centres would piggyback the outgoing supply chain. These attached "first-response goods" would be exported by boat alongside Mitsubishi's finished inventory to be transported within the disaster zone.

The Red Cross was unable to do this independently because they lacked the documentation required by the Japanese government to use their ports. Obtaining these permits wasted valuable time and arguably cost lives. If the strategy were in place prior to the earthquake, bureaucracy would have been minimized and the relief effort could have been executed almost instantly. Lastly, there are few limitations on how many NGOs Mitsubishi could have contracted with, overcoming the disjointed behaviour of different agencies because Mitsubishi is alone in distributing the goods.

This strategy also makes financial sense. After the earthquake, Mitsubishi's sales from its Japanese business unit suffered, but the company was still required to cover its fixed costs. If a third-party organization would cover the costs of shipping and the fixed costs associated with the Nagoya Port, costs the NGO would pay regardless if they shipped relief goods independently, Mitsubishi's losses in the area could have been minimized.

Risks

Companies in the region may be faced with destructive losses to their infrastructure when disaster strikes. Therefore, multiple arrangements with different companies in the same region are required to ensure the strategy's effectiveness through diversification.

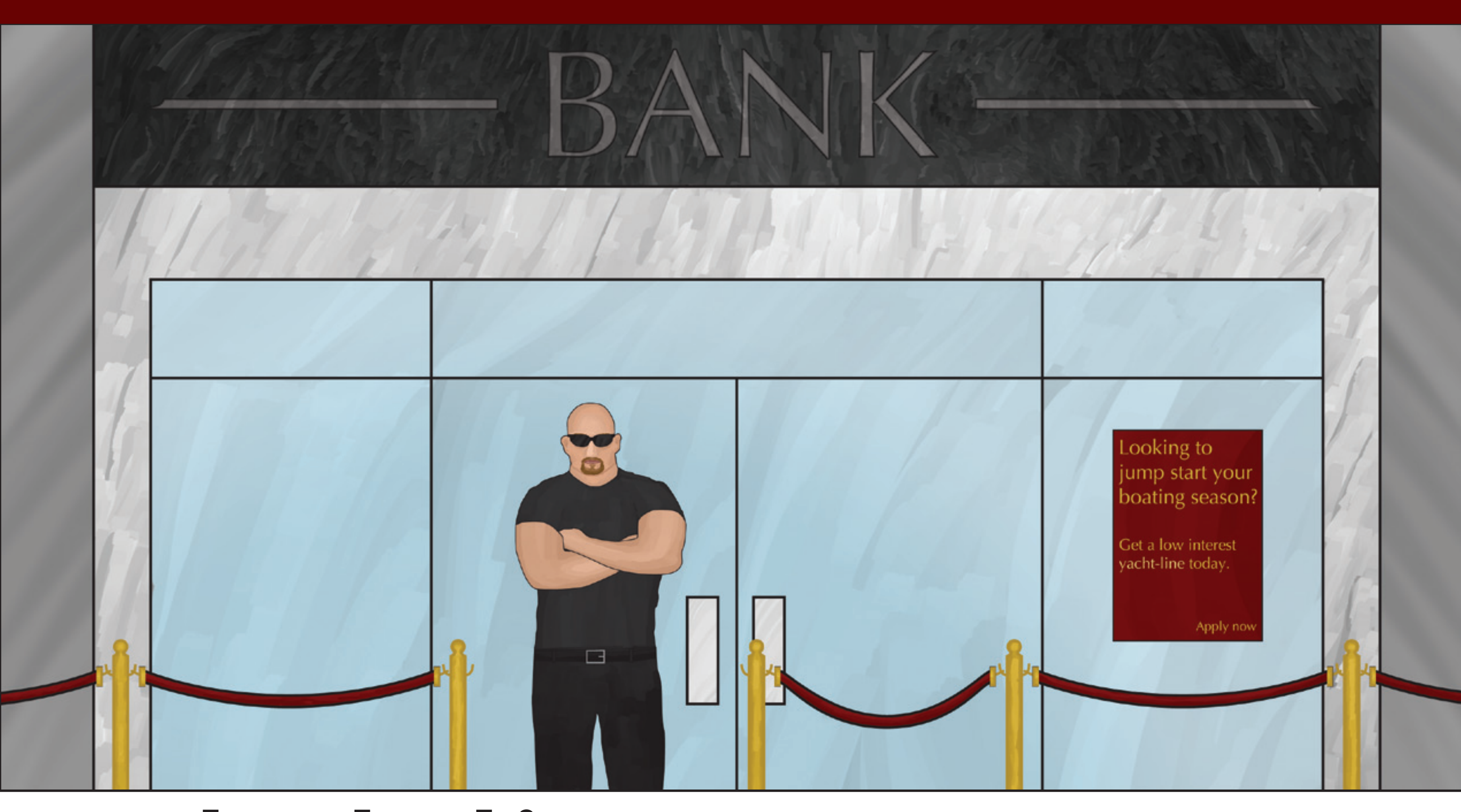
This program is very dependent on few entities, and without the continued buy-in of all parties, the strategy will not work. The short-term costs associated with implementing this strategy may dissuade potential partners from participating. A first-time financial incentive provided by the NGO may overcome this issue.

An Important Precedent

Coca-Cola has already test-run the corporate distribution approach. In 2010, Coca-Cola leveraged its corporate distribution system to expedite the delivery of essential goods to Haiti after its devastating earthquake. Coca-Cola's distribution system allowed $2 million in aid to be delivered quickly and efficiently. Once word got out of Coca-Cola's good deeds, civilian donations to a cause driven by a trusted brand increased tremendously.

A common theme in any disaster is unpredictability. If a multinational were to set up its value chain to accommodate the provision of resources to an affected area, it would minimize the lag of bureaucracy, utilize infrastructure already in place, and streamline the behaviour of all participating aid agencies. This unpredictability becomes a less relevant hindrance because a system is on standby wherever it is needed.

The humanitarian value chain concept is an underused approach to CSR. Firms that successfully take advantage of disaster relief CSR initiatives will present a unique and valuable proposition for all stakeholders, and add value to the organization as a whole. They will be known as an innovator when the time is darkest, immediately after disaster strikes.



Unbanked in America

Bringing more Americans into the realm of formal banking.

By Alex Apanovitch and Johnny Kim

We all had one. A piggy bank. A shoebox. It was the not-so-secret place where you accumulated your Christmas money, allowance, and shiny quarters from the tooth fairy. But as you got older, you started to move those crumpled bills and loose change into your first bank account. This marked a monumental day in your life, whether you were aware of it or not— a step out of the unbanked market and into the world of finance.

While this transition may seem like a natural progression in developed nations, it is skipped by a growing portion of the American population. According to the Federal Deposit Insurance Corporation, an astonishing 8.8 million American households (7.7%) are unbanked. The unbanked market has recently ballooned, with nearly U.S. $370 billion in cash flowing through the hands of those who belong in this segment, more than the 2011 nominal GDP of both Hong Kong and Greece.

Who are the Unbanked?

Unbanked households are defined as those where not one individual has a chequing or savings account. Most unbanked Americans are visible minorities, primarily due to financial, cultural, and linguistic barriers that exist between them and traditional financial services. These individuals typically lack financial literacy but require some financial services such as the ability to cash cheques and send money to distant family members.

Despite these needs, most unbanked Americans believe they simply don't have enough money to merit a bank account. Others avoid banks because they do not need to write cheques, cannot meet minimum balance requirements, fear losing their savings to service fees, or just don't see the value in an account. Some consumers harbor mistrust and simply stay away from large, "evil and unfriendly" financial institutions that, post-2008 financial crisis, have been shown in an unsavory light.

In reality, the unbanked are paying more for current alternatives than they would be for bank accounts. These alternatives capitalize on misconceptions and offer consumers ease of use and accessibility, the two most important factors for this group. In the U.S., if a cash agent is 15 minutes away, customers used their services once or twice per month. When this same agent was less than 10 minutes away, customers used their services as many as 10 times per month.

What About Traditional Banks?

Retail banks profit from the spread between the interest rates at which they lend money and the interest rate they pay on deposits,

Unbanked Consumer Profile

Comparing Unbanked Customers to Average Americans

Consumer Profile	Average Americans	Unbanked Americans
Number of Credit Cards per Wallet	5.4 Credit Cards / Wallet	No Credit Cards
Average Household Income	$55,000 / year	$25,000 / year
Age Breakdown	Older	Younger
Credit History	Substantial Credit History	No Credit History
SMS Penetration	Average SMS Users	High Volume SMS Users
Access to Home PC	PCs at Home	No PCs

Source: Reuters and Mintel

or the net interest margin. This revenue is supplemented by fees charged on bank accounts and on transactions. Regulations after the 2008 financial crisis such as the Durbin Amendment of the Dodd-Frank Act limited the amount banks can charge on debit transactions, squeezing profit margins and making it more difficult for banks to profitably serve the unbanked. With fees legislated downward, the net interest margin earned from a customer becomes increasingly critical. As one would suspect, banks require a minimum balance to generate enough interest income to offset the fixed costs associated with a customer and their respective branch. Unbanked consumers typically don't have large enough deposits to allow banks to cover the fixed costs required to maintain an account, and therefore banks have little incentive to serve them.

What Options Exist for the Unbanked?

Credit Unions – Credit unions are established with the social responsibility to serve customers that have a similar profile to the unbanked American. However, since many of the unbanked are financially illiterate, the details of how credit unions operate are unknown to them. The onus must fall on credit unions themselves to educate unbanked consumers, but they typically lack the resources to do so at a mass level. Furthermore, because credit unions generally operate within limited geographical regions and tight-knit communities, the business model is difficult to scale.

Payday Lenders & Cheque-Cashing – The unbanked have migrated towards alternative financial services such as payday lending and cheque-cashing outlets. Their business model provides many of the same services as traditional banks without demanding the same commitment from the consumer. Growth in the payday lending and cheque-cashing industry has accelerated over the past three years to 15% per year. Although these two functions are fundamentally different in nature (one provides short term loans while the other converts cheques to cash), they are similar in the predatory interest rates and fees they charge. Nevertheless, revenues continue to grow and customer loyalty continues to build, likely as a result of their vast retail presence and ease of transacting.

Prepaid Debit – A relatively recent entrant, prepaid debit card services have been growing at a CAGR of 21.5%. These cards can be loaded with money and then used at retail locations and ATMs. By identifying and serving the unbanked's need for simple financial solutions, Green Dot has rapidly grown to become the predominant player in this market since its founding in 1999. As a first mover, it has leveraged its proprietary technology to enable card purchases, activations, and reloads at retailer locations. By tapping into the distribution network of retail giants like Wal-Mart, Green Dot has been able to bring its product offering to over 50,000 retail locations, while saving itself the fixed costs associated with operating its own. As a result, Green Dot has been able to profitably serve the unbanked without charging predatory interest rates or fees, unlike most payday lenders and cheque-cashing facilities.

Is There a Mobile Solution?

As the gap between rich and poor widens and the unbanked population grows, there is an increasingly lucrative opportunity for firms that can capitalize on serving this market; but who is best positioned to do so? The answer may be in our collective pockets. Behind every cell phone is a telecom provider who is positioned to be the next "big fish" in a growing pond.

Wireless carriers should begin offering financial services to unbanked individuals in the form of an e-money account that can be accessed wirelessly and through a prepaid debit card. To transact from this account, an individual will deposit cash or cheques at any authorized telecom agent. The customer will be able to manage this account through either a prepaid debit card or their mobile device. This service will offer several distinct advantages over existing prepaid debit card options, including the ability to manage accounts wirelessly, pay bills online, and send remittances.

Are Mobile Carriers the Answer?

McKinsey identifies four key competencies needed to serve the unbanked: financial product design, customer management, mobile service delivery, and distribution. It is clear that mobile carriers are able to succeed in the latter three but have no prior expertise designing financial products. They have a history of customer management and are most able to deliver mobile service, which is particularly relevant for the unbanked where the

penetration rate of mobile devices is over 70%. This trend suggests that the unbanked likely trust mobile carriers, unlike banks, and could benefit from the additional value mobile carriers can provide over incumbent solutions, such as those from Green Dot.

The combination of a mobile carrier's large, well-distributed retail networks and their mobile messaging and Internet infrastructure will allow them to satisfy the critical need for ease of access for the unbanked consumer. This infrastructure also allows for profitability. Unlike traditional banks that use locations for banking purposes only, mobile stores would support various business lines. Similar to the Green Dot and Wal-Mart relationship, this would offset fixed costs and allow for the banking services to profit without charging the predatory rates of payday lenders.

While mobile carriers have no experience with financial product design, the services that the unbanked are looking for in a mobile money account are extremely simple. Mobile carriers are therefore particularly well suited to serve the unbanked, even if their services may not be adequate for a more affluent group's banking needs.

Would They Do It?

Financial services don't appear to be a core business to mobile carriers. At the core, a bank facilitates the exchange of funds between the institution and the user while providing services to allow for ease and convenience of payment. For many telecom companies, such as Rogers Communications, which submitted an application to become a bank in 2011, a billing relationship is already established with the majority of its customers. This relationship is eerily similar to that between a bank and its members.

As the mobile market became increasingly saturated, major carriers have tried to expand their revenue streams. There has been an industry-wide push towards the creation of financial services arms by large conglomerates. In addition to Rogers, O2, a predominant mobile carrier in the UK, filed for an e-money license in 2011 that would allow them to facilitate mobile transactions. These recent moves suggest that mobile carriers see financial services as a profitable opportunity.

Over time, financial services customers can be converted to contracted telecom customers as they build credit histories. Currently, a significant portion of the unbanked market uses pay-as-you-go mobile plans since their low-income profile and limited credit histories prevent them from receiving contracts. Offering financial products may be a feasible solution to funnel these consumers into more valuable long-term relationships as the unbanked customers move to a structured financial future. These customers could then have high-value, long-term contracts. Combined financial services and mobile programs could complement this natural transition in several ways, such as by offering discounts on the next mobile purchase when a financial account is opened. In the mobile market, which is fast approaching saturation with 102 active mobile connections for every 100 people, this could be a unique method to acquire customers and nurture their value growth.

Examining the Unbanked Market

Retail Banks Cannot Serve the Unbanked

	Person A	Person B
Deposit	$10,000	$100
Interest Earned (revenue) *Based on 7% interest rate*	$700	$7
Fixed Overhead (cost)	($250)	($250)
Interest Paid to Depositor (cost) *Based on 1% interest rate*	($100)	($1)
Profit/Loss to the Bank	**$350**	**($244)**

Illustrative Example

Comparing Potential Service Providers

	Financial Product Design	Customer Management	Mobile Service Delivery	Distribution
Mobile Carriers	Low Competency	Competent	High Competency	Competent
Transfer Agents	Competent	Competent	Competent	High Competency
Retail Banks	High Competency	Competent	Low Competency	Low Competency

High Competency / Low Competency / Competent

Source: McKinsey

Who would provide this solution?

T-Mobile and Sprint Nextel would be natural candidates to enter this market. At approximately 25%, they have a higher proportion of pay-as-you-go customers than the national average of 19%, suggesting a high existing penetration among the unbanked. In addition, Sprint and T-Mobile have churn rates of 30% and 51%, respectively – much higher than industry average churn of 24%. These companies would therefore have the most to gain through a strategy in which fickle pay-as-you go customers are captured and nurtured into customers on high-value, long-term contracts.

Implementing the proposed model will take time. However, this is a valuable new opportunity in the increasingly saturated mobile industry. Telecom companies should reconsider their traditional strategy of pushing innovation and growth among high-value, high-income consumers. There is a massive market of the unbanked that could create significant long-term value for struggling firms like Sprint and T-Mobile – if they're willing to take the risk.

Revitalizing Medical Care

The search for ubiquity in a broken system.

By Geoff Calder and Nadeem Nathoo

With more than a third of hospitals in the United States operating at a loss and many more unable to serve all the patients that come through their doors, it appears that disaster is looming within the American healthcare system. While many consider growing healthcare costs and wait times to be stale news, the burden will only amplify as the population ages and chronic disease cripples an already broken system.

Over a decade ago, electronic health records (EHRs) were identified as a potential solution. They helped reduce inefficiencies of traditional healthcare processes by eliminating duplicate procedures, reducing lead times between physicians, and enabling consistency in decision-making—reducing the number of medical errors. It has been estimated that total drug costs can be reduced by 18% and total lab test costs can be decreased by 15% immediately if full software integration is attained. More importantly, it is estimated that annual claims could be reduced by as much as $80 billion if nationwide adoption is achieved, due to the improved treatment of chronic disease patients who account for nearly 80% of all claims. At the Brigham and Women's Hospital in Boston, annual savings of over $8 million and a 55% drop in medical errors were achieved through this initiative.

By 2008, a handful of countries, including Sweden, had established centralized systems to which all physicians, hospitals, and pharmacists had access. Simultaneously, nearly 90% of Swedish domestic institutions were in the process of adopting these systems into their daily operations. The Obama Administration hoped to drive comparable results through the HITECT Act, which made as much as $44,000 in total incentives available per physician for the adoption of EHRs. Health Information Exchanges (HIE) were developed, mainly by non-profit organizations, to digitalize and centralize patient information. However, unlike in Scandinavia, efforts to merge new information into legacy systems remained stagnant. Fewer than 20% of American physicians had made any effort to incorporate new resources into their practice

Experts have not universally identified why adoption has failed in American institutions. Some experts have focused on key social differences: the American stigma surrounding personal privacy or the change-resistant nature of physicians trained in the U.S. Others have focused on economic differences like the cost sensitivity of American clinics, which are generally smaller than their overseas counterparts. What has largely been ignored in industry journals to this point is the structure of the market's value chain. While state-run healthcare institutions shoulder the financial burden in socialized healthcare systems, the private system is more complex. Private healthcare institutions have incentive to reduce inefficiencies in order to improve treatment time and quality, however the cost of

any inefficiency can simply be passed on to the patient—who then is able to transfer the costs onto insurance companies.

The impact on insurance companies has been catastrophic. Fueled by rising deductibles, premiums have increased by 113% since 2001. The risk to insurance companies is that corporations, the stakeholders who pay the majority of the premiums in the U.S., are increasingly looking to self-insure. Therefore, insurance companies have the most financial incentive to fix the current healthcare system. When a patient is unable to get an appointment because of duplicate procedures across the industry or they are misdiagnosed, that patient is more likely to show up in an emergency room weeks later incurring a larger medical bill. Unfortunately, market conditions make it difficult for the insurance companies to develop and implement a solution themselves. Competitors are too fragmented to generate industry-wide buy-in and hosting a medical solution would be a far cry from their core competencies.

The Missing Link

An opportunity exists, however, for healthcare-driven software as a service companies (SaaS). Following a "freemium" model, a SaaS provider could charge insurance companies for the use of the EHR system, while medical institutions access the service for free, with the intent of achieving an illusive key success factor: ubiquity. This new model provides SaaS companies with a growth opportunity, allows insurance companies to realize savings in the form of reduced claims, and addresses the financial reluctance of the health institutions that can now afford to incorporate the HIEs' patient data.

A software company that charges insurance companies, rather than healthcare institutions, has the ability to drive ubiquity because:

- Insurance companies provide immediate access to a network of health institutions, physicians, and pharmacies that software companies would traditionally not have.
- As the payer of over 80% of medical treatments in the U.S., insurance companies have the power to incentivize healthcare institutions to adopt and integrate the system provided.
- Providing the solution at no charge to the institutions makes it commercially viable for practices and pharmacies of all sizes.

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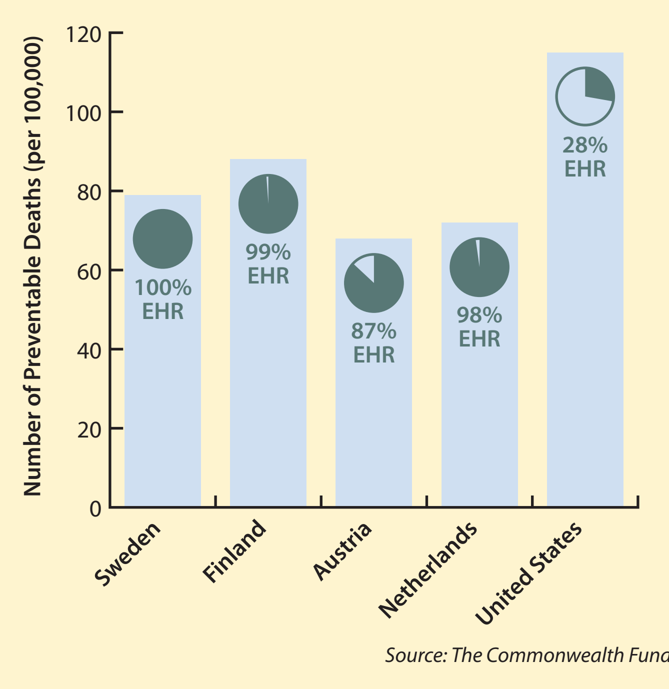
Industry precedent has indicated that insurance companies would be willing to pay for or internally develop this type of service. A handful of companies, including Aetna, have attempted to push their own EHR solutions to physicians in order to better manage their claims. However, recent legal action taken against United Health, an insurance provider, explains why it may be difficult for an insurance company like Aetna to scale their own solutions. They were sued shortly after the acquisition of Ingenix, a healthcare analytics application, when it was determined that they had manipulated customer information. This precedent will make it difficult for anyone other than a third-party vendor to provide this type of product directly.

Preventable Deaths

EHR Adoption vs. Preventable Deaths



Source: The Commonwealth Fund

Fortunately, there are a variety of third-party vendors who are well positioned to expand. Epic, the leading EHR software solution, has a comprehensive product they could market by targeting insurance firm subscriptions. NexJ Systems, a Canadian customer-centered solution that has been successfully modifying the behaviors of individuals, could also be scaled to reduce the burden on providers by increasing personal accountability. CRM companies like Salesforce.com could also leverage their core competencies to expand into this space. They have successfully managed sensitive information over the cloud in the past and have been struggling to find lucrative growth opportunities through enterprise solutions, evidenced by their decelerating increase in new billings subscriptions. Regardless, a supplier who is operationally independent of an insurance company has the ability to protect patient records from misuse and alleviate privacy concerns.

Forging the Solution

Proper implementation of this business strategy will be the lynchpin since the technology is not new. This proposal simplifies execution by aligning each member of the value chain with the processes over which they have control:

- Those responsible for paying claims are now accountable for promoting cost synergies at the institutional level; and
- Software companies are responsible only for the solutions, not driving adoption in an unfamiliar industry.

By shifting accountability to the insurance companies, implementation can also be accelerated. Incentives, like discounts on premiums or rebates, could be awarded to patients who are treated by EHR-enabled facilities. These programs would penalize facilities that have not attempted to fully integrate the system by shifting demand. This redistribution of patients would eventually reduce profits and reduce government funding for the institution. In the American system, these healthcare institutions will need to adapt to market pressures in order to survive.

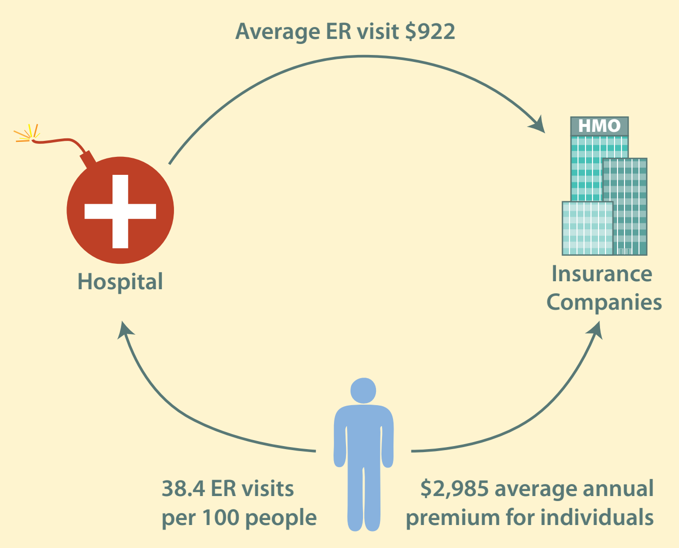
In Critical Condition

The value of an EHR system is the interconnectedness that it provides and the ability to streamline workflow. As more members tap into the same system, greater cost synergies can be realized. Until a critical mass is achieved, there is little incentive for institutions to adopt the technology. A similar situation occurred in the retail industry with the adoption of Universal Product Codes. During the 1970s, faced with withering profits and rising labour costs, supermarkets looked to the barcode as the way to govern food price inflation by automating retail checkouts. Early adoption was anemic. They suffered from the same inhibitive truth: that their usefulness required adoption by the critical mass to create value. Today, barcodes are scanned 5 billion times per day and save consumers, retailers, and manufacturers over $300 billion each year. The turning point came in the early 1980s, nearly 30 years after the barcode had been invented, when an ad-hoc committee of retailers forced manufacturers to collaborate on a standard. In healthcare, the insurance companies are the ones positioned to catalyze a similar change.

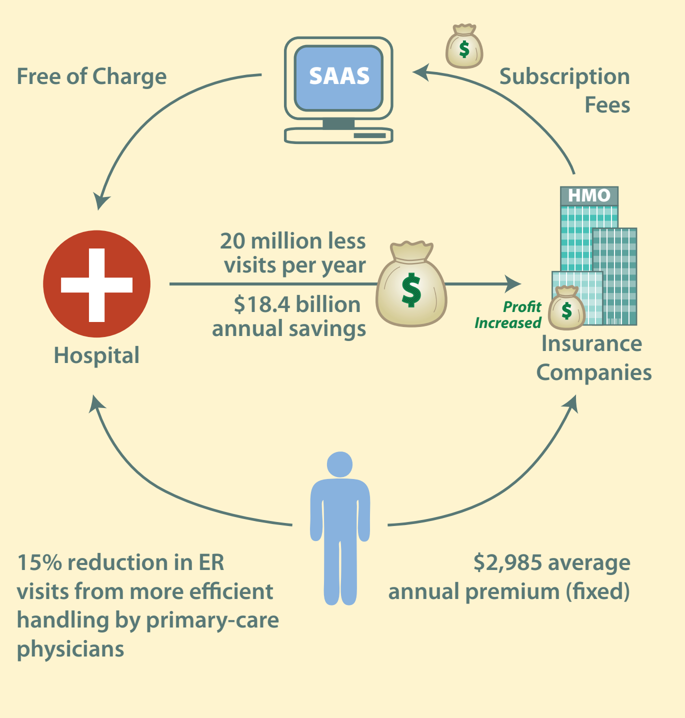
EHRs present a significant opportunity to the healthcare industry, but the history of the barcode illustrates that a standard needs to be created when there is no financial incentive for individuals to adopt the technology alone. In retail, the manufacturers waited for the retailers to demand a solution. If someone upstream had managed to provide a ubiquitous solution earlier on, the barcode design rights may not have opened up to competitive tender, and one firm may have been able to lay claim to a larger portion of the savings. Conceivably, healthcare institutions could do the same. The risk is immense, but surely RCA, Singer, Pitney-Bowes, IBM, and the rest that were vying to design the barcode would agree that letting the opportunity pass cost them the accreditation of revolutionizing the world.

The Potential of EHR

Before EHR Implementation



After EHR Implementation



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