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Harvard Business School
Management Consulting Club

Case Interview Guide

Practice Case 1 (Retailer)

Question

A major retailer of clothing and household products has been experiencing sluggish growth and less than expected profits in the last few years. The CEO has hired you to help her increase the company's annual growth rate and ultimately its profitability.

- The retailer has 15 stores located in shopping malls in metropolitan and suburban areas.
- Total revenue from the 15 stores has declined, despite major back-end cost savings.

Recommended Solution

<u>High Level Plan of Attack</u>

- You need to understand why growth has slowed and profitability has declined despite cost savings.
- Do different stores experience variations in revenue? Do they all have the same approach to selling?
- Is purchasing behavior of the consumer different in the two areas?
- Has there been any new competition on the scene? In one area and not the other?

<u>Lay Out Your Thoughts</u>

- Use the profitability framework. The case tells you that cost savings have been achieved. Focus on the revenue side.
- Focus on the fact that the company has 15 different stores, in two different geographical areas. What are the key differences between the two in terms of the consumer, competition, and growth?

Dig Deeper: Gather Facts

- Are some stores more profitable than others? *Yes they are. We see variations throughout.*
- Are there differences in profitability between the metropolitan and suburban stores? *Yes there are. We see that the suburban stores are more profitable than the urban ones.*
- Is there more competition in the urban areas? *No, not really. It's proportionally the same.*
- Do the stores sell the same products? *Yes they do. All stores have the same product mix.*
    - [Given that all stores sell the same product mix and some are more profitable than others, this should lead you to look at consumer behavior]
- Do consumers in the suburban areas have different purchasing behavior than the urban dwellers? *Yes, as a matter of fact, they do. The suburban customer tends to buy more of the major appliances and electronic equipment than the urban consumer. The urban consumer buys mostly items such as clothing, small furniture items, and small appliances.*
    - [You can make the assumption that suburban consumers have higher incomes and are in more need of major appliances given the difference in living quarters between houses versus apartments in the city.]
- Is there a difference in profitability between the goods purchased by the suburban and urban consumers? *Yes. Major appliances and TVs and stereos are higher profit items than clothing and minor appliances.*
- Would you say that the current product mix is more suited for the suburban customer than for the urban? *Yes. I guess it is.*

Key Findings

- The consumer in the city has different needs and purchasing behavior than the suburban consumer. The stores in the city are not catering to the demographics of its surroundings.
- Unnecessary costs are being incurred through inventory and lost floor space in the city stores, resulting in lost revenue for the retailer.

Recommendations

- Further analyze the customer for each of the stores and differentiate purchasing behavior and income levels.
- Cater the product mix according to the customer research findings.
- Stores that cannot sustain selling low cost items should consider the possibility of closure.

Practice Case 2 (Butcher Shop)

Question

A fast food chain recently bought a bovine meat-processing outlet to supply it with fresh hamburgers and other meets. The shop process is: cows enter from one end of the shop, meat gets processed in the middle, and then the meat gets packaged and delivered at the other end.

Cows Enter → Meat Processed → Meat Delivered

The manager of the butcher shop however could not decide whether to have the cows walk or run into the meat processing room. Can you help him?

Recommended Solution

<u>High Level Plan of Attack</u>

- The first thing you want to do is to understand how much meat can be processed (the capacity) when the cows walk versus run.
- Then analyze the cost implications of the cows walking versus running.
- Next, calculate the size of the market and demand for the product.
- Finally, match demand with supply.

<u>Lay Out Your Thoughts</u>

- This is a market sizing, operation's cost analysis question. Try to lay your plan of attack on paper in a logical sequence of steps to take.

Dig Deeper: Gather Facts & Make Calculations

Shop Capacity

- Let's assume that only fresh hamburger meat is processed at the shop. Let's also assume that from each cow, you can make 20 hamburgers.
- How many hours per day is the shop open for? *10 hours, 5 days a week.*
- Now, if the cows walk in, 10 cows can be processed in one hour, given current labor.
- This gives us an estimated 2000 hamburgers that can be processed in one day if the cows were to walk (20 hamburgers/cow x 10 cows/hour x 10 hours/day).
- If the cows were to run in, let's assume that 25 cows can be processed in one hour. This gives us 5000 hamburgers per day.

Costs

- Next, we must calculate the costs associated with the two different capacities. Let us assume that labor cost increases proportionally to the increase in processed meats, and overhead increases, but not proportionally due to some sunk costs, for more equipment and other expenses. Here is the breakdown:

	Walk	**Run**
Overhead	$5000	$10,000
Labor	1,000	2,500
Total Cost	6,000	12,500
Burgers/Week	10,000	25,000
Cost per Burger	$0.60	$0.50

- This shows that by running, costs drop by 10 cents on each burger.
- *To estimate revenue, we need to calculate the demand from estimating what the market size would be.*

- Let's assume that the fast food chain has 10 outlets, and the meat-processing factory serves all 10. Each outlet serves a vicinity of about 30,000 people. Now, let's also assume that there are about 3 other competitors in each vicinity, leaving it with a market share of about 25% of the customers in each area, for a total of 75,000 potential customers.
- Of those 75,000, about 40% of them fall within the demographic target, leaving 30,000 desired customer.
- Given the trends in healthy foods, out of the 30,000 desired customers, about a third will be allowed by their parents to frequent any one of the establishment on a regular basis - leaving 10,000.
- Of the 10,000 customers, each will frequent the establishment about twice a week on average - 20,000 visits. Out of these visits, about half order a burger over another item on the menu - for a total of 10,000 burgers a week.

Key Findings/Recommendations

- Even though it's cheaper to produce more burgers, there's no demand to support it.
- Have the cows walk. This meets demand and ensures fresh hamburgers.

Practice Case 3 (Juice Producer)

Question

A major producer of juice is in the business of processing and packaging fruit juice for retail outlets. Traditionally, the producer has packaged the juice in 18-ounce carton containers. Recently, in response to demand from the market, the producer purchased a machine that packages the juice in plastic gallons (36 ounces). Over the next couple of years, sales continued to grow on average of 20% per year. Yet, as sales continued to increase, profits steadily decreased. The owner cannot understand why. He hires you to help out.

Recommended Solution

High Level Plan of Attack

- We know that sales have been increasing, so revenue is not an issue. The problem must be costs.
- Because of the change in packaging, the producer has incurred additional costs that are not accounted for, causing profits to decline.

Lay Out Your Thoughts

- Use the profitability framework. Gather information on the revenue side, but focus mostly on the cost side.

Dig Deeper: Gather Facts/Make Calculations

- Looking at the revenue side, how much did the producer charge for the 18 oz. carton? *$2.00 per container.*
- For the 36 oz. plastic gallons? *For twice the size, the producer figured he would provide an incentive to buy by selling them at $3.50 per gallon.*
- How was the cost of the new equipment accounted for in the price? *The producer ended up raising prices across the board by $.50 on all packages, both cartons and gallons, selling at* $2.50 *and $4.00, respectively.*
- What about cost of packaging? Does it cost the same to package the juice in cartons as it does in gallons? *Well, I guess not. Plastic is more expensive than the paper carton we have traditionally used. Also, we had to hire more experienced labor to operate the machine because it is a little more complicated than the carton machine. We figured that because the demand was higher for the gallons – we would cover our costs through increased volume.*
- What about overhead costs? *All costs for the factory are added together and divided by the number of units produced.*
    - This should raise alarm bells. This is now clearly an issue of cost allocation. The price on the plastic gallons should be higher due to higher costs. Now you need to see to what extent this is affecting the bottom line.

- Let's try to understand the trend in sales. What percentage of gallons versus cartons is sold? *The more our customers notice the gallons, the more they like them. As the overall volume is increasing, plastic gallons have comprised 60% of the sales. The owner has been very pleased about that.*
- It seems to me that it costs more to package in the gallons, yet the price is not higher on a per ounce basis. In fact, it's lower. Have you done any proper cost allocation to determine which type of product should carry which costs? *No, we haven't.*

Key Findings

- The major finding in this case is the additional costs associated with the plastic gallons were averaged out over all units, including cartons. This resulted in a misallocation of costs and inappropriate pricing.
- The plastic gallon products have been priced at a lower rate than they should have been. Result: the more gallons the juice producer sold, the more profit the company lost out on.

Recommendations

- This firm should conduct a thorough analysis of activity based costing to determine the overhead costs and direct costs associated with each item in the product line. They should then use this data to price accordingly.

Practice Case 4 (Chemical Manufacturer)

Question

A major chemical manufacturer produces a chemical product used to preserve foods in containers. Despite an increase in market share, the manufacturer has experienced a decline in profits. The CEO of the company is worried about this trend and hires you to investigate.

Recommended Solution

High Level Plan of Attack

- The first thing we need to figure out is what does "an increase in market share" mean? Remember, the term "market share" is a percentage, and not an absolute number. It could imply that the company has increased its share of the market by beating out the competition, or the competition exiting the market. It could also mean that the market is actually shrinking, but the sales of the company are decreasing by less than those of its competitors.

Lay Out Your Thoughts

- Use the Profitability Framework. Lay out factors that you feel would help from the Value Chain analysis, 4Cs, and 4Ps.

Dig Deeper: Gather Facts

- Has the company experienced any significant increase in cost in the last couple of years related to any additional fixed or variable cost? *No, costs have been steady.*
- On the revenue side, has there been an increase in the volume of output? *Slightly, a little bit higher than the industry average.*
- What about the competition. Have there been any new entrants on the scene? *Actually, competition has decreased. A number of players have exited the industry.*
- Why has that been the case? *They were losing money. They felt that the industry had gotten saturated, so they left.*
- Has sales decreased for the industry overall? *Yes, there has been a general negative trend in the last few years. There certainly has been less demand for the product.*
- Are substitute products being used? *Not really. Preservatives in general are being used less in foods. Fresh food is now the preferred choice for many consumers.*

- What about the makers of food? Are they experiencing decreased volume? *Yes, the entire industry has been slowing.*
- Are they forced to lower their prices to survive? *They certainly are. Additionally, to lower costs, they are using their leverage to renegotiate price structures of raw materials.*
- So is the company in question forced to lower its prices? *Yes. They are gaining market share, but it's because of a number of competitor fallouts.*
- But costs have stayed the same? *Yes.*

Key Findings

- The industry overall is shrinking. To survive, the company in question has been competing on price. It has gained market share at the expense of it competition, forcing some to exit the industry.
- Its sales have only increased slightly.
- The decrease in price has caused the company to lower its profits, despite the increase in market share.
- Profit margin has been lower on a per volume basis.

Recommendations

- Focus on cost reduction. If price is the only way to compete, then costs must decrease.
- Collaborate with the competition to increase leverage in negotiation.
- Diversify into other chemicals that are in demand. Reduce the risk of market trends via a portfolio of products.

Practice Case 5 (VieTire)

Question

A tire manufacturer in Vietnam, VieTire, has been the only player in that market due to high tariffs on imports. They dominate the tire industry. As it stands, the tariff is 50% of the total cost to produce and ship a tire to Vietnam. Because of the forces of globalization and lower consumer prices, the Vietnamese government decided to lower the tariff by 5% a year for the next ten years. VieTire is very concerned about this change, as it will radically alter the landscape of the industry in Vietnam. They hire you to assess the situation and advise them on what steps to take.

Recommended Solution

High Level Plan of Attack

- The first thing we need to understand is the current cost structure of VieTire's product.
- Next, we must determine the impending competitive situation.
- Then, Calculate the impact the reduction of tariff will have.
- Finally, recommend specific steps that VieTire can take to protect themselves from increased competition.

Lay Out Your Thoughts

- Specify what steps we must take to understand the cost differences now, and in the future, of VieTire and its competitors

Dig Deeper: Gather Facts/Make Calculations

- What would you say are the major costs associated with making a tire? *Raw material comprise about 20% of the cost, labor 40%, and all other costs such as overhead 40%. The average tire cost about $40 to make.*
- It seems that labor is a major cost, $16 per tire. Why? *Things are done more manually. Most of technological advances in the industry have not yet been implemented in Vietnam.* What about the cost structure of the competition? *An average tire manufacturer in the US produces tires at a cost of $30 each.*

- Assuming shipping cost to Vietnam of $4 each tire, and a tariff of 50%, the average cost of an imported tire in Vietnam amounts to $51. So currently, even though the cost to produce a tire in the U.S. is much cheaper due to technological advances, foreign competitors are out of luck because of the tariff.

Year	**Tariff**	**Cost**	**Result of Competition**
Now	50%	$50.00	Will not enter
1	45%	$47.90	Will not enter
2	40%	$46.00	Will not enter
3	35%	$44.50	Will not enter
4	30%	$43.00	Consideration of entrance if willing to take a cut on price
5	25%	$41.30	Preparing to enter
6	20%	$39.60	Entered the market
7	15%	$38.00	Competing on the market

Key Findings

- Depending on what price they are willing to set, the competition will start to think about entering the market in year four. In year six, the competition will surely enter as their prices become lower than domestically produced tires.
- This analysis assumes that the cost structure for the competition will remain constant. It is important to note that because of the rapid advances in technology, chances are that the costs of producing tires will decrease resulting in competitors entering the market even sooner.

Recommendations

- VieTire needs to benchmark against word class tire manufacturers and reengineer production methods and cost structures.
- They must invest in the latest advances in order to reduce their labor/operations costs.
- The company should focus on increasing the skills of labor while at the same time contain their hourly wage.
- Need to develop loyalty from their customers/consumers in order to lock in a certain percentage of the market share.

Practice Case 6 (World View)

Question

A cable TV company from Canada, World View, had recently entered the US market in the northeast to expand its market share. World View saw this move as an opportunity to capture a large part of the US market (4MM consumers) in a market with very little competition. However, in the last couple of years, much to the surprise of management, World View has been unable to make a profit. You have been hired to figure out why and advise them on their next move.

Recommended Solution

<u>High Level Plan of Attack</u>

- We need to understand why the company is losing money despite the market being uncompetitive.
- We must analyze both the revenue and cost side of the problem.
- We should also analyze the differences in viewing behavior and income between the customer base of World View in Canada and in the northeast.
- We will also determine the strength of any competitors and substitutes.

<u>Lay Out Your Thoughts</u>

- Use the profitability framework.
- Focus very heavily on the consumer.

<u>Dig Deeper: Gather Facts/Make Calculations</u>

- Let's look at costs first. Did World View incur additional costs per customer on average in the new market? *No, based on the potential number of subscribers, they have instituted the same system that was in place. Costs associated with cable wire, debt, maintenance costs, etc. are all proportionally the same.*
- What about the number of subscribers. Out of the 4MM potential customers, how many are signed up? *Only 2.1 MM.*
- Are other cable companies capturing the remaining market? *No, competition is not an issue. Those that we have not acquired as customers simply do not have cable.*

- What about substitutes and viewing behavior? How is the consumer in the northeast US different from the one in Canada? *Well, the Canadian consumer does not rely much on local stations for watching TV. Cable is a major source of entertainment and news coverage. In the northeast US, we tend to see consumers shy away from paying the $40 a month. They settle for watching local stations.*
- Does the new market lave a lower income level? *Yes, they do, by about 20% on average.*
- What about the local stations? How many are they? Do they meet most of the needs of the consumer? *There about 16 local stations that have coverage over the entire northeast. I guess they are doing pretty well by providing programming that the consumer wants. You tend to see the average consumer in the northeast watch regular TV more than Cable when compared with the Canadian consumer.*
- Do these stations have good reception and how much do they charge? *They have a very good reception and they are part of basic TV, so they are free.*
- Is World View providing any type of programming that the local stations are not providing? *Some, but the consumers don't seem to be interested. They don 't feel that it's worth $40.*

Key Findings

- There is a great deal of competition in the area, not from other cable companies, but local TV stations.
- The consumer in northeast US is quite different from the consumer in Canada with respect to television viewing habits.
- Consumers are not willing to pay $40 for a service that they already get for free.

Recommendations

- World View could try to cater its current channel offering by offering a smaller package for those that would be interested in couple of cable channels.
- Scale back its operations to a specific region.
- Educate the consumer on the extra benefit and new low price.
- If none of these strategies work, move out of that market.

Practice Case 7 (Le Seine)

Question

A French soft drink company, Le Seine, is looking to diversify its holdings by investing in a new fast food chain in the US. You are hired to determine whether they should pursue this path and, if so, how they should go about execution.

Recommended Solution

High Level Plan of Attack

- Understand the company's logic for entering into the fast food industry.
- Examine the overall trends in the fast food industry, and determine which segment is the most promising.
- Assess the overall demographic changes and major trends in eating habits.
- Determine what competencies the company can provide that will help it enter this business and be successful.
- What are some of the high level strategies that the company should consider when entering?

Lay Out Your Thoughts

- Use some elements of the 4Cs, 4Ps, and Porter's Five Forces. Identify which factors you need to address and list them in a logical sequence.

Dig Deeper: Gather Facts/Make Calculations

- Why is the company thinking of investing in the fast food industry and not another? *The fast food industry has been experiencing sustainable growth for the last few years, and we believe that it will continue to grow.*
- Why in the US market and not the French? *The US is more attractive economically and Le Seine has been present in the country for a few years.*
- Does the company know much about the fast food industry and its consumers? *Not very much. They're not sure where to enter.*
- The industry as a whole might be growing, but let's think about which segment is growing the most and where it would make sense for the company to enter. If we look at the traditional burger outfits, that segment is pretty much dominated by three players: McDonalds, Burger King, and Wendy's. I would think that the barriers to entry are pretty high for this segment. You also have pizza, Mexican, chicken, cold cut sandwiches, prepared meals (Boston Market).

- Has the company thought about which to enter? *No. But what do you think, at a high level, which segment should they enter?*
    - [Quickly run through the pros and cons of the various segments]
- Well, if we take a look at the company itself, it is more inclined to be in the prepared meals segment, given that it is French and has a European appeal. If we look at the trends, the population is getting older and more families have two working parents. Also, there seems to be a move towards eating more healthy foods. If we consider the competition, the segment seems to be at the growing stages, with only one or two known players. The barriers to entry are certainly not as high as some of the other segments.
- To distinguish itself from the competition, it can make food with a French theme, priced competitively. The company can also set up shop in major grocery stores, as more people are purchasing prepared foods as part of the their grocery shopping.
- It would be a fair assumption to say that Le Seine can capitalize on its distribution and marketing experience in the US.

<u>Key Findings</u>

- There seems to be potential in the prepared food segment (players like Boston Market).
- Le Seine seems to be a good candidate to enter and take advantage of the present opportunity.

<u>Recommendations</u>

- Based on this assessment, Le Seine should enter on a large scale. To offer competitive pricing, they must have economies of scale.
- Quickly develop strong brand equity. Look at the franchising option. Examine in detail how the most successful fast food outlets operate.
- Consider acquiring an existing chain versus starting a brand new one.
- Location is extremely important. Know your customers in every region, and focus on convenience.

Practice Case 8 (Beer Brew)

Question

A major US beer company, Beer Brew, recently entered the UK market. Two years after entry, the company is still losing money. Despite a high per capita consumption of beer in the UK market, sales have been very disappointing. What explains this phenomenon?

Recommended Solution

<u>High Level Plan of Attack</u>

- Evaluate the product mix of the company and compare it to what is selling well in the UK.
- Analyze what type of marketing Beer Brew is using.
- Understand the consumer behavior and tastes, and determine the effect on sales.

<u>Lay Out Your Thoughts</u>

- Use the profitability framework. Understand which factor under revenue or costs is driving the decline in profitability.

<u>Dig Deeper: Gather Facts/Make Calculations</u>

- Let's begin with the product mix. What kind of beer has Beer Brew been trying to sell? *Currently, Beer Brew is selling two kinds of beer, a strong tasting and a light beer.*
- How have the sales of both been doing? *The strong tasting beer is selling slightly below average and the light beer is not selling at all.*
- What about marketing? *The company has spent more on marketing than the industry average for that region.*
- Is it a highly competitive industry? *It's about average. The industry is fairly fragmented. There are no dominant players.*
- Any problems with distribution channels? *No.*
- What about pricing and placement of the product? *To be competitive, Beer Brew undercut its price significantly to try to capture customers. Their beer is sold just about everywhere other brands are sold.*
- What are the current best sellers of beers in the UK? *Guinness, Toby, and a few others.*
- What kind common characteristics do they have? *They are all moderate in alcohol level, dark, and strong tasting.*

- How does that compare to Beer Brew's products? *Beer Brew's strong tasting brand is higher in alcohol, and market tests show that it tastes better. The light beer is low in alcohol and calories, and again tastes great.*
- Are there any light beers on the market? *Very few. Mostly locally produced. Beer Brew saw this as an opportunity to cash in on the light beer industry that has taken the US market by storm.*
- What about color? Are Beer Brew's two products dark beer? *No, they are fairly light in color.*
- Since most of the beer consumed in the UK is dark, and dark signifies strong beer, does the light color of the beer signal to the consumer that somehow the beer is weak? *Perhaps, but the company figured that once the consumer tried it, the color wouldn't make any difference.*

<u>Key Findings</u>

- It seems that the consumer in the UK has unique drinking habits. After further inquiry, we find that the average British drinker values dark beer over any other factor. It seems that the dark color has a psychological impact on the consumer, relating it to strength, masculinity, getting their money's worth, etc.
- The light beer industry is undeveloped in the UK because the health movement in the US has not mobilized in Europe yet.
- Also, because the price of Beer Brew's products is much cheaper than other brands on the market, it is portrayed as a low quality "American beer." There has been a dilution of the brand equity.

<u>Recommendations</u>

- Change the color of the stronger tasting beer. Make it darker and advertise it as the better tasting darker beer, with more alcohol.
- Match the price to other premium beers that focus on the same market segment.
- Drop the light beer product line. The UK is not ready for it yet.

Practice Case 9 (Wheeler Dealer)

Question

A major auto service chain, Wheeler Dealer, has enjoyed healthy returns on its 30-store operation for the past 10 years. However, management feels that the chain needs to expand, as the current geographical areas in which they are based have become saturated.

For the past couple of years, they have aggressively pursued a growth strategy, opening an additional 15 stores. However, it seems that this approach has had negative returns. For the first time in over a decade, the chain's profits dropped into the negative zone. You were hired to figure out why.

Recommended Solution

<u>High Level Plan of Attack</u>

- You need to understand the nature of the business. What does the auto service entail?
- Focus on the customer segmentation. Are they serving more than one customer? Any differences?
- What is the profit structure of the different offerings?
- Where did they move? Are the newly formed stores operating differently or serving different markets than before?

<u>Lay Out Your Thoughts</u>

- Use the Profitability Framework. Focus on how revenue has changed given the environment.

<u>Dig Deeper: Gather Facts/Make Calculations</u>

- What type of services has Wheeler Dealer traditionally provided for its customers? *There are two main businesses under each roof: off-the-shelf car parts and the garage mechanical services.*
- Are these services provided as well in the newly developed chains? *Yes.*
- Have competitors entered the market stealing market share? A *few competitors have entered the market, but not too many. The expansion was planned to explore new markets and prevent the competition from growing.*

* What about price? Have prices gone up to help defray some of the costs associated with growth? *No, they have stayed the same.*
* Given the two types of businesses for each chain, do they have the same profit margin? *No. In fact, because the garage services cost the business a great deal more and the mechanics are very well trained, we charge a premium. Profit margin on servicing cars has twice the profit margin of off-the-shelf products.*
* Are the customers the same for both businesses? *No. The customer that uses the garage service tends to come from a mid-to-high income bracket. Those that use the off the-shelf auto parts tend to be of the lower-income bracket. They fix their cars on their own.*
* Where has Wheeler Dealer traditionally been located? *Mostly in, or very close to the suburbs.*
* Has the geographical location changed as they expanded? *Yes, They saw certain urban areas as very inexpensive. They located more in inner cities where there are a lot of used car sales.*
* So, would it be fair to assume that the more profitable business, the garage service, has deteriorated and the sale of off-the-shelf parts has increased, causing overall profitability to go down? *Yes.*

<u>Key Findings</u>

* The garage service is the major revenue generator for the business. As they expanded into the inner cities, they began to attract the wrong customer. Profit margin on the off- the-shelf products is not enough to cover costs and make a healthy return for Wheeler Dealer. A price increase is unlikely given price sensitivity.

<u>Recommendations</u>

* Scale back from the urban areas. Focus on geographical areas where you can attract the suburban customers who will use the service aspect of the business. Maintain a healthy return on the car product market from the inner city dwellers.
* Where possible, drop the garage service in under-performing areas to reduce costs and focus on the retail end.

Practice Case 10 (Travel Agency)

Question

A travel agency makes a 10% commission on all of its travel bookings. Their current profit before taxes is $1MM, while the industry average ranges from $2MM to $3.5MM. Why are they making less than the industry average?

Recommended Solution

High Level Plan of Attack

- We need to understand the revenue stream and cost structure of the travel agency and conceptualize how each transaction contributes to the bottom line.
- Focus on the types of customers the agency services and how each type relates to profitability.

Lay Out Your Thoughts

- Use the Profitability Framework, with a focus on the cost side of the equation.
- Break your analysis down to the two types of customers: business and leisure.

Dig Deeper: Gather Facts/Make Calculations

- What is the total gross revenue for the agency per annum, on average? *$10 million.*
- How does the revenue compare to other agencies with similar size? *They are about the same.*
- What about the product line? Does the agency handle any bookings other than travel tickets? *No. They just book tickets for their customers.*
- What are the different customer segments that the agency services? *There's the business traveler segment, which comprises about 40%* of *total revenue, and the leisure traveler segment with the remaining 60%.*
- How many total transactions does the agency process and what is the break down for each customer segment? *The total number of transactions is around one million per year. On average, about 300K go to the business segment, and 700K to the leisure.*
- Is there a cost associated with each transaction? *Yes, each transaction, regardless of which segment, costs $9.*

- [Now you have all the necessary information to calculate the profitability of transactions for each segment. If you run the numbers, you will find the following information.]

Segment	Share	Volume	Total Revenue	Revenue / Transaction	Cost / Transaction	Profit / Transaction	Gain
Business	60%	300,000	$ 6,000,000	$ 20.00	$ 9.00	$ 11.00	$ 3,300,000
Leisure	40%	700,000	$ 4,000,000	$ 5.71	$ 9.00	$ (3.29)	$ (2,300,000)
			$ 10,000,000				$ 1,000,000

Key Findings

- The leisure travelers are draining your profitability. Either the cost per transaction is too high or the revenue per transaction made on the leisure is too low.

Recommendations

- Benchmark the cost structure of other travel agencies.
- Negotiate with the airlines on the possibility of charging a premium for leisure tickets or capture a larger commission through cost charged to the customer.
- Look into the possibility of reducing cost per transaction for the leisure travelers.
- Offer the leisure traveler other products to increase revenue per transaction such as hotel bookings and travel packages.
- Become a niche player and focus only on the business traveler

Practice Case 11 (Hospital)

Question

Our client is a 350-bed hospital in a mid-size city. The organization has historically exhibited strong financial performance, and had a 1-3% operating gain each year for the last five years. However, they are projecting a $12 million operating loss this year, and expect this situation to worsen in the future. As a result, the CFO believes that they will be out of cash within five years. They have asked us to identify the source of this sudden downturn, and to come up with alternatives to restore them to a break-even position. They are one of the largest employers in the market, and will not consider layoffs as a possible solution.

Background

This question addresses company profitability. The interviewer is looking for a candidate's business intuition and ability to apply this intuition to identify potential sources of the problem. In addition, the interviewer is looking for potential solutions to the client's problem.

Response

Candidate: Profitability is a function of an operation's revenues and costs. The first thing I'd like to focus on is the company's future revenue stream. As I understand the hospital industry, revenues may be fixed for several years due to long-term contracts with insurers. Is this the case for this hospital?

Interviewer: Your intuition is correct. Revenues have dropped approximately 15% so far this year due to aggressive pricing on capitated managed care contracts that were signed in January and declining admissions and length of stay for their fee-for-service contracts, most of which are still reimbursed on a per diem basis. All contracts are binding for three years, and cannot be renegotiated.

Candidate: In that case, it is important to understand the company's cost structure to see if it can adjust to this declining stream of revenue. Does the client have considerable fixed costs that will be difficult to reduce in the near term?

Interviewer: Hospital occupancy is approximately 70%, resulting in high fixed costs that are not covered by the current contribution margin. The organization is currently staffed for 80% occupancy.

Candidate: Since revenue is declining at a fixed rate and fixed costs are high in the short-term, the hospital will have to analyze its variable cost structure. I would surmise that staffing costs are the main source of variable costs. However, the hospital cannot address this due to its policy concerning layoffs. I would think that the other main driver of variable costs for the hospital lies in its utilization of resources. Am I headed down the right track?

Interviewer: In fact, you're right. The utilization of diagnostic and therapeutic services during a patient's stay is approximately 15% higher than what was expected when contract pricing was negotiated.

Candidate: Given that information, the hospital should focus on changing physician behavior since physicians ultimately control the utilization of resources. The hospital may want to align MD incentives with those of the hospital by sharing risk, giving physicians data and education on their use of resources versus the competition. Other ways to reduce expenses could be to sign exclusive contracts with a distributor in order to generate volume discounts and economies in purchasing, or by reducing choice by limiting the pharmacy formulary to generics and decreasing the number of vendors utilized for high volume items such as prosthetics and heart catheters.

Interviewer: That's a good discussion of cost implications, but have you given up on recommending ways to increase hospital revenue?

Candidate: Now that you mention it, the situation is not hopeless in this regard. The hospital may want to increase revenue by signing contracts with additional insurers, by putting salaried physicians on staff to guarantee that they admit to our client's hospital, or by creating an affiliated physician organization to increase their share of admissions. In addition, they can potentially leverage their distinctive competencies by developing Centers of Excellence that can be marketed to managed care contractors as an exclusive provider for those services within the region, and possibly outside the region.

Interviewer: Are there any other solutions that may be feasible?

Candidate: One final thought that keeps coming back to me centers on the company's current competitors. What does the local market look like?

Interviewer: There are two other 350-bed hospitals in the city. One is an academic medical center, the other a catholic hospital recently acquired by a for-profit chain. Additionally, total admissions in the marketplace have dropped by 5% and total patient days have declined 10%.

Candidate: In that case the hospital may want to consider affiliating with a competitor in the market. This may help to decrease capacity across the city by rationalizing the services offered at each institution. This may allow one hospital to close, thereby reducing fixed costs.

General Summary Comments

The candidate should fully address the components of this issue (profit = revenue - costs) and should be able to demonstrate an understanding of fixed vs. variable costs. Moreover, the candidate should be able to brainstorm possible solutions to the problem, both from a revenue maximization and cost minimization perspective.

Practice Case 12 (E-Grocery)

Question

The client is a grocery store chain that is considering whether or not they should enter the emerging Internet-based grocery shopping/delivery market in the Boston area. This regional chain is currently one of the leaders in the traditional grocery store market in northern New England.

In their core market, two competitors have emerged in the Internet/at-home grocery shopping business, and are rapidly gaining market share. One of the companies that has already entered this new marketplace is the client's primary competitor in the traditional market. The second player is a chain that does not have grocery stores in the target region, but has entered the Boston area with Internet shopping delivery services.

Should the client enter the market? If so, how, and what concerns should they have? If not, how do they protect market share from the emerging market that is threatening to steal business?

Background

This is a market strategy issue. The interviewer is looking for a discussion of the client's customers, competitors, costs, core competencies and the overall market dynamics. In addition, the candidate should be able to present a solution and identify the key success factors for this solution.

Response

Candidate: The client must first do some preliminary work examining the market for groceries delivered over the Internet. I would like to get a better sense for the company's current customers, as well as potential customers, to see if the Internet is a viable delivery mechanism for the company. Can you tell me more about the client's customers in the area?

Interviewer: The client serves primarily upper-middle class customers.

Candidate: That's important to know. I would guess that prospective users of an Internet-based delivery system are upper-middle class. Can you confirm this and elaborate on the growth prospects for this market?

Interviewer: Your guess is correct. Users of the Internet delivery system are typically upper-middle class. As far as the market is concerned, home grocery shopping among Internet users is growing rapidly and the percentage of homes with Internet access is also growing.

Candidate: We've established that the market is an attractive one, however I still need more evidence before presenting a recommendation. I'd like to now turn to the two competitors described in your opening. Can you explain their current market share?

Interviewer: All three local players (including yourself) have an equal market share - roughly 15%.

Candidate: And can you address recent growth trends among the competition?

Interviewer: The competitor without stores in the target region is gaining market share more rapidly than the company with stores in the target region.

Candidate: We've established pretty convincingly that the market is attractive. I'd like to now focus on our client. Clearly not all companies are prepared to put their operations on the Internet. There are two central issues I'd like to better understand. First, the company's core competencies—does it have the requisite skills to address the Internet user? Secondly, I'd like to understand the company's cost structure. Is such a move feasible for the client? Do you have any information on the company's distribution capabilities? Specifically, is it able to address the Internet market?

Interviewer: The company's current distribution facilities are not adequate for the delivery system.

Candidate: How about the company's employees? Are they sufficiently trained to handle delivery tasks associated with the Internet?

Interviewer: The current employees cannot perform these tasks without more training.

Candidate: Those are some important considerations to ponder. However, given the market attractiveness for Internet groceries, the client would be crazy to pass up this opportunity. Its customers are Internet users, the competition has already shown a willingness to invest in the market, and the competitor with no stores in the region (i.e. totally reliant on Internet sales) is growing the fastest. That said, the company must be willing to invest in this market to succeed. First, it must improve its distribution capabilities. Further analysis must be done as to whether it should improve its current operations or develop a stand-alone capability exclusively devoted to the Internet market. Next, it must develop an inventory management system so that it can effectively track what it orders from suppliers, what customers are ordering, and where the product is delivered (Internet vs. traditional). Finally, it must spend enough money to cross-train its employees so that tasks associated with Internet delivery can be effectively performed.

Interviewer: Are there any other considerations?

Candidate: When the company rolls out its Internet operations, it must not disappoint customers. Many of the Internet-based customers will be cannibalized from the traditional operations. In itself, this is not bad. These customers obviously prefer the alternative, and it's better for the company to retain them versus losing them to competitors. However, failure to deliver on Internet delivery will cause customers to consider switching to the competition. As such, the company must be sure it can effectively deliver on its promises from the moment it enters the Internet market.

General Summary Comments

The candidate does not necessarily have to recommend market-entry for this case. If the candidate believes the company should not enter the market, it must present a compelling business reason why and craft creative alternatives for market share protection. In either case, the key components of market strategy must be understood and addressed.

Practice Case 13 (Formula Producer)

Question

The client is a manufacturer and distributor of infant formula. They sell their product nationwide, and are in the middle of the pack in terms of market share. They are currently trying to boost their market share while maintaining profitability.

There is a government welfare program called WIC (Women, Infants, Children) that allows individuals living below the poverty level to receive vouchers for infant formula for their children. Unlike most welfare programs, this one is subsidized by the actual producers of infant formula. On a state-by-state basis, infant formula producers bid for the right to be the sole supplier of infant formula to welfare recipients in that state.

In addition to paying the government for the WIC contract, the client also provides rebates to retailers for WIC sales. As a result, income received from WIC sales is substantially less than that received from normal formula sales. In fact, sales to mothers that remain in the WIC program for more than 12 months result in a net loss.

In trying to determine how much to bid on a WIC contract for a given state, what factors should you consider?

Background

This case is fairly wide open, and presents an issue that is most likely unfamiliar and ambiguous. One challenge will be for the interviewee to find one or more issues that they can explore more in-depth. The basic focus of their analysis should deal with the relative profitability of a WIC contract.

Response

Candidate: I think for this case I would first look at who the typical WIC customer is, and the dynamic of the relationship, meaning how long are they a customer, and what kind of loyalty is there. Since I don't have any children, could you tell me more about a typical WIC customer, in regards to buying formula?

Interviewer: Sure. Obviously the typical WIC customer is poor, since this is a form of welfare. But some things you might not know are that 1) the average WIC recipient stays in the program for less than 12 months, 2) mothers typically remain loyal to a brand through infancy for their first child, but for subsequent children recipients often switch back and forth between brands, and 3) infants typically require formula the first 22 months of their life.

Candidate: Thanks. With that knowledge, I can start to think about the issues facing this company. In trying to decide the terms for the contract, profitability is the primary driver. There's obviously some issue of social-enterprise here, but even so, I think profitability will drive much of the decision. Since the WIC recipient gets rebates in addition to the subsidized cost of the product, we need to quantify that rebate in order to understand what the profitability per recipient is. Can you tell me that?

Interviewer: For the purposes of this interview, let's assume that the rebates average an additional 10% (off of the retail price).

Candidate: OK. So the profit per customer might be determined by (WIC revenue - rebates - COGS). So if the revenue is $100/customer/year, and the rebates are $10, and COGS are $75, we make $15 per customer per year. As long as we're paying less per customer for these rights to be the sole-supplier, we're in the black.

Interviewer: For the most part, your logic is correct. But is there anything else that might be a factor in determining profit?

Candidate: Well, related to the actual profitability of the WIC product I'm not sure. But maybe there are some hidden costs or revenues that I'm not thinking about. In fact, maybe there are some synergistic revenues that the company can achieve. If they get the contract, that gets them additional shelf-space in the stores. And not just WIC recipients shop in the stores. So maybe they will be able to increase market-share, just by being on the shelf. Of course, they are getting full retail price for those sales. So I might add in an additional sales minus COGS to the equation. But to try and get an idea of that figure might be tough. How long to these contracts last?

Interviewer: Typically, several years.

Candidate: Ok, so knowing that a contract is several years, say 5, we can begin to get a total dollar value for the contract. If we know how many WIC recipients there are in this state that we're bidding, we can calculate expected revenues. Also, if we can get an idea of how much shelf space we would have, we can quantify the synergistic sales.

Interviewer: Good. I'm not going to make you go through the math on it, because we're about out of time, but you're right. There are 1.2 million WIC recipients in the state, and shelf-space is awarded based on volume sales. So for this company to get the contract, it can help them have more sales volume, and thus more shelf-space, and hopefully then more market share.

General Summary Comments

Ultimately, they should come up with some sort of explanation for how numbers would be run to estimate an appropriate contract bid. One example might be:

(WIC revenue - rebates - COGS) + (synergistic non-WIC revenue - COGS) >= Contract Bid

COGS takes into account economies of scale.

Real world situation is that synergies are strong, and WIC recipients bounce in and out of program but stay loyal to product for first-borns. Not only are the synergies positive, but also on average WIC recipients are profitable because they pay retail for nearly half of the formula that they purchase over the first 22 months of their child's life.

Practice Case 14 (Pharmaceutical Company)

Question and Background Information

Our client is the U.S. pharmaceutical division of a multi-national corporation. In about six months the division will receive FDA approval to launch an anti-depressant drug. Despite this apparent good news from the FDA, the U.S. division is not elated. It has concerns over the market potential for this drug and its ability to reach the key prescribers in this therapeutic category. We have been asked to help determine whether they should 1) launch alone, 2) co-market with a partner, or 3) sell, license or swap the drug.

The concerns over market potential center on whether the drug can gain adequate competitive advantage in a market segment having two dominant, patent-protected competitors and nearly 100 generic competitors. Additionally, a higher technology antidepressant, which appears to offer therapeutic advantages, was recently introduced by a competitor.

Gaining the professional endorsement of psychiatrists is crucial to success in this therapeutic category since they write approximately half of the prescriptions for antidepressants. However, the division has no experience marketing drugs to this physician group. Consequently, it would have to hire a sales force and/or enter into a co-marketing agreement to gain access to psychiatrists through someone else's force. The client would be able to leverage its existing sales force to reach the other half of the prescribers (Internal Medicine Specialist and Family and General Practitioners).

How would you help them decide whether to 1) launch alone, 2) co-market with a partner, or 3) sell, license or swap the drug to a third party?

Commentator: *Note here what is being asked, "How would you help them decide." What is not being asked is "Which is the correct option to choose?" The Interviewer is looking more for how this problem is approached than for the "correct" answer.*

Also note that it is totally appropriate to take some time to organize your thoughts before launching into the case discussion.

Response

Candidate: In helping the client decide which option they should choose, I will want to guide them to the option that will create the most value. To understand main value drivers (i.e., profitability drivers), I will first explore the market attractiveness and our competitive position within that market in order to determine revenue potential. After that, I will explore the major cost issues.

Starting with the revenue, I'll want to understand first what the overall market revenue opportunities are for this type of drug in addition to our product specifically. Now, the client expressed concern over the market potential for this drug. How big is the market and what is its potential growth rate?

Commentator: *Here the Candidate has done several things. First, the Candidate has stated the overall objective, value creation. Next, the candidate stated the method of walking through this problem, looking at revenue by using a market economics and competitive position framework, then looking at costs.*

The Candidate provided a roadmap. Now the interviewer understands the approach and expected direction of questioning. This helps the interviewer understand the student's thought process - how he or she thinks through business problems.

Interviewer: The overall antidepressant drug market is relatively attractive at $1.1 billion per year and is growing well in excess of the population growth rate.

Candidate: You mentioned that concerns over market potential center on whether the drug can gain adequate competitive advantage in a market segment having "two dominant, patent-protected competitors and nearly 100 generic competitors." You also mentioned that a higher technology drug had entered the market. Is the antidepressant market segmented by technology?

Interviewer: Yes.

Candidate: And the two patent-protected competitors along with the 100 generic competitors are within our technology segment?

Interviewer: Correct.

Candidate: So, the overall antidepressant market is attractive at $1.1 billion, but within that market, there are segments based on different types of technology that may or may not be attractive.

Interviewer: That's correct.

Candidate: What is the technology associated with our client's product?

Interviewer: Tricyclic antidepressants.

Candidate: How fast is this technology segment growing?

Interviewer: As a matter of fact, substitution by the new technology may cause a decline in sales over the next 5 years. Additionally, the existing competitive environment is very intense and will only increase if the market shrinks.

Candidate: So, the overall segment is not very attractive.

Interviewer: Correct.

Candidate: What percent of the volume do the two main competitors have?

Interviewer: In our own technology segment, the leader has approximately 10% and the number two player has about 4%. The rest of the 100 competitors each has less than a 2% market share. By comparison, the new technology has captured a 20% market share of the total antidepressant market.

Candidate: How much will our client's product be able to differentiate itself within our technology segment?

Interviewer: Not much. In a market research study we commissioned, the product was seen as very similar to the number two product in our technology segment, slightly inferior to the number one product, and slightly better than the generic products. The new technology was viewed as far better due to a lower level of sedation.

Candidate: So to summarize the market environment, although the anti-depressant market is attractive, the segment that we would be participating in is relatively unattractive and runs the risk of becoming smaller and more competitive over time. Additionally, within this unattractive segment, we have limited ability to differentiate ourselves relative to our competitors, and thus, will not be able to charge a premium price.

I would think that this unattractive market and relatively undifferentiated position within that market would translate to a lower market share. I would estimate that our share might be lower than either of the branded products given our new presence in the market, say maybe a 2-4% share and this, like the rest of the segment, would probably decline over the next couple of years.

Interviewer: That sounds about right.

Commentator: In understanding the revenue potential, the Candidate did several key things.
1) Disaggregated the antidepressant market.
2) Established the overall attractiveness of the relevant market segment.
3) Established the client's relative attractiveness to competitors within that segment.
This enabled the Candidate to come to the correct conclusion that an undifferentiated position within a relatively unattractive market will limit the revenue potential.

Also, note that the Candidate is doing most of the talking. Use the interviewer to clarify questions or provide information, but the Candidate must lead the discussion.

Candidate: Knowing that our revenue potential is relatively low puts more pressure on minimizing the costs if we were to market the drug. I want to see what area within the cost structure impacts profitability the most. What percent of net sales is COGS?

Interviewer: About 20%

Candidate: And what is the bulk of the remaining line items?

Interviewer: Most of it is selling expense. There are some overhead/admin and advertising and promotional expenses, but most of it is selling expenses.

Candidate: So, selling expense is the largest portion of the cost structure, which means that whichever option we choose, launching alone vs. with a partner will certainly impact the selling expense (in addition to the number of prescribers reached, thus revenue potential).

Commentator: You can pick up good "tips" here. Spend time on things having high impact and feel free to test and see how important they are. Tests might include how large something is as a percentage of sales, how important it is to the customer, or how much of an impact it has on manufacturing economies, etc.

Candidate: In understanding the effect of the co-market agreement on number of prescribers reached, I think it would be helpful if I could get an idea of who makes the purchasing decision.

Interviewer: Well, there are four main parties involved. There are the manufacturers (such as our client), the doctors (who prescribe the drug), the druggists (who fill the prescription) and the patient (who initiates the transaction). Selling is concentrated on the doctors, since they are the group that determines if medication is needed and, if so, what type.

Candidate: Is the growth in managed care going to influence the dynamics of this?

Interviewer: Yes, but for the purposes of our work, let's not address that.

Candidate: So, for the purposes of our work, the doctors make the purchasing decisions, this includes two groups of physicians, the Psychiatric group and the Internal Medicine/General Practitioner group.

Interviewer: Correct.

Candidate: You noted that we don't currently have connections to psychiatrists. This group prescribes half of the antidepressants. Can we launch the drug by only marketing to IMs and general practitioners and ignoring psychiatrists?

Interviewer: No, they are at the top of the pyramid of influence and thus must endorse the drug before their colleagues in the IMP/GP will endorse it.

Candidate: So if we are to market this product, we cannot do so without the Psychiatric group. The weight of the decision then becomes a matter of what is the most efficient and effective way to reach them—either through a newly hired sales force or with a co-marketing agreement.

Interviewer: Correct.

Candidate: What are the advantages and disadvantages of marketing the drug ourselves?

Interviewer: In terms of having our own sales force, the main benefit would be that we would be concentrating on our product only and this may help sales. On the downside however, the cost of this focus is all attributed completely to our product, and having a dedicated sales force representing only one product would be expensive.

Candidate: Do you have any other psychotheraputic drugs in development or plans to expand this part of your portfolio through licensing?

Interviewer: Nothing is planned for the next three years.

Candidate: So by entering a co-marketing agreement, the costs of the sales force is spread across several products, and, if the co-marketer did not have a competing product, then our product would get the appropriate selling attention warranted. Also, since this sales force has existing relationships with the psychiatrists and doesn't need to take time to further establish these relationships, sales of our product might peak sooner. So, all in all, I would think that if we were to market this product, it would be a less costly and higher value option to enter into a co-marketing agreement rather than go it alone.

Commentator: Here, as with most case interviews, the Candidate has the opportunity to go "deep" into an issue. The Candidate has chosen to do this here with one type of cost, the sales force. The Interviewer is looking to see if the Candidate can identify some of the key "value" drivers of the function being explored. In the case of the sales force, the Candidate correctly identified the key value drivers as being:

1) The ability to spread the cost of a sales call across multiple products.
2) The ability to choose a co-marketer that needs this product in their existing product line.
3) The ability to leverage an existing psychiatric sales force infrastructure to reach peak sales sooner.

Remember, there are many value drivers. We have touched on a few, but don't be concerned about identifying the "right" ones, just try to identify what type of issues affect the situation the most.

Interviewer: OK, and what about the third option, to sell, license or swap the drug to a third party?

Candidate: Again, the client would want to choose the option that was more value creating. There could be several reasons for going with the third option:

1) We might sell our drug because the sum of the promotional or overhead costs may make it unprofitable for us to market whereas a company having a similar product line might be able to carry this product at a very small incremental cost.
2) We might license it for the same reasons we would sell it.
3) We might swap it if we could find a company needing this type of drug while having a drug that might fit more with our existing infrastructure.

In any case, for the options being considered, I would want to forecast cash flows and discount them back to see what option is more value creating before making a final recommendation.

Interviewer: OK, thank you for your input on how to approach this problem.

Commentator: You'll note here, that the Candidate doesn't actually make a final recommendation. This is fine. The Candidate has demonstrated how he would approach the problem, and in doing so, has hit on many of the key issues you would find in a real client case situation.

Recapping the steps the Candidate took into evaluating the client's options:

On the revenue side:

1) *Segmented the market to the appropriate technology level.*
2) *Determined that the segment was unattractive .*
3) *Determined that the client's product was not significantly differentiated.*
4) *Concluded that for these reasons, the revenue potential was limited.*

On the cost side:

1) *Determined that selling expense was a key component to profitability.*
2) *Determined that the Psychiatric group needed to be included in the selling efforts.*
3) *Determined that it would be less expensive to co-market vs. go it alone.*
4) *Determined that there are other considerations to evaluate when comparing co-marketing vs. selling, licensing, or swapping the product.*

Interviewer: Provide summary comments and wrap-up.

Practice Case 15 (Scotch Manufacturer)

Background

We have been contacted by a large distilled spirits manufacturing and marketing company to develop a new strategy for one of their brands.

Before getting into the details on this particular case, how would you define strategy?

- Participation
    - Geography
    - Customer
    - High-Level Product Segment
- Offering
    - Product
    - Service
- Pricing
    - Product
    - Service
- Operating Configuration (cost/asset)
- Distribution

What would be your process to develop a new strategy?

- Position Assessment (i.e. understand sources and drivers of profitability)
    - Business Profitability
    - Strategies
    - Market Economics
    - Competitive Position
- Alternative Identification
- Alternative Evaluation
- Business Plan

In the first meeting with the client to "scope out" the potential project, what might be some of the things that you would like to know?

- Ulterior motives for the work (are there politics involved)
- What other work have they done on the subject?
- What do they want to find out?
- How would they like to work together?
- Are there any time constraints?
- Who would they like involved in the project?
- Basic information on the brand (profit, volume, etc.)?
- Any hypotheses on the key issues?
- Any thoughts on the likely alternatives?
- Any key questions that have to be answered regardless of the strategy?

What might be some of the reasons that you would NOT want to accept this project?

- Politics
- Not committed to value
- Looking for scapegoats
- Inability to satisfy the BU manager
- Difficult client in general

Here is a little background information on the scotch industry

The first scotch was introduced in North America in the early 1940s, and grew steadily and rapidly in popularity until the 1960s. The industry has subsequently declined in volume every year to 1996 at a rate of about 3% per year. From 1996-1998, the volume declined at only 1% per year for these two years.

What kind of information would you want to understand in order to determine the reason for the steady volume decline up to 1996, explain the "kink" in the volume decline, and then forecast what market volume is likely to do over the next several years?

- Is the answer to slower growth explained by fewer people drinking scotch, or by drinking less overall, or both? *(fewer people have been drinking scotch)*

What kind of information would you want to understand in order to determine why fewer people have been drinking scotch?

- Demographics
    - Male versus female
    - Age of typical scotch drinkers
- Popularity
    - Substitute products
    - Health reasons

What kind of analysis would you complete to quantify the reduction in number of scotch drinkers?

- Review census work
- Complete literature searches
- Interview customers
- Interview distribution channel members
- Interview other producers
- Complete market research studies
- Review the client's information gathered over time

Here is some additional information on the scotch industry

Scotch consumption has been declining because fewer people have been drinking scotch. Fewer people have been drinking scotch for two reasons. First is a general decline in the popularity of scotch. Other distilled spirits, such as vodka and wine have increased in volume and become more popular. Second is a decline in the age group that traditionally drinks scotch (the 35-50 age group). As the baby boomers age, this segment of the population is growing, so even if popularity doesn't change, the scotch market should improve going forward due to the growth in this segment. In addition, scotch is becoming more popular, especially the unique single malt scotches.

What information would you like to know about the industry, in general?

- How is the scotch market segmented?
    - There are three segments in the market, low-end (such as private label CVS whisky), premium (typically seen on the back bar in a bar), and super-premium (including Chivas Regal and single malt scotches).
- What are the sizes of the segments?
    - 40% of the volume in low-end, 50% in premium, and 10% in super premium.
- Is the scotch market profitable?
    - Yes, all segments are economically profitable.
- How is profit concentrated?

- 20% in low-end, 60% in premium, 20% in super-premium.

- What are customer needs?
    - Taste (do people like the taste of the scotch -- either in blind taste tests or do they "think" one brand tastes better because it has a darker color, or is a more thick liquid, etc.)
    - Fashion (is it fashionable to drink)
    - Badge (does the brand make me feel important/different/mature/sophisticated)

Would you think that the scotch industry is profitable? Explain structurally, and elaborate

- High barriers to entry, takes a long time to establish a brand name in scotch
- People are very brand loyal and won't switch easily
- People think it's bad for your health and it's difficult to get them to start drinking
- People think it tastes bad and it's hard to acquire a taste for scotch
- Customers are not price sensitive
- Regulatory pressures are high (high taxes, it's expensive)
- Competitor intensity is not that high (little price based competition, noticeable, but not outrageous investment in advertising)
- As a result, overall, the industry is very profitable, but volume is declining, so profit is declining

What information would you like to know about the brand?

- What segments do we participate in?
    - Only in the premium segment and with one brand
- Where is our brand positioned?
    - Tied as the #2 brand with 25% market share of volume (#1 has 35%, #2 has 25%, we have 25%, #4 has 10%, others have 5%)
    - Priced slightly above the industry average (10%)

- How have competitors performed?
    - #1 has gained share from us, the #4 and other brands, but mostly from us
    - #2 has held share
- How profitable are we relative to competitors?
    - We all have same cost of goods, differences are in selling costs and advertising costs
    - #1 has highest selling costs and advertising costs, #2 has second, #3 has third, and so on
    - #1 and we have a price premium, #2 is priced at the industry average, #3 and all others are slightly below the industry average, but no one is dramatically different than the industry average
    - #1 has a lower per unit profitability but has the most share of profit given its highest market share

What are your potential hypotheses that you would want to test to understand our relative performance?

- Customers perceive our brand as having poorer rankings on the key attributes
    - We have a disadvantaged taste, disadvantaged badge, but competitive fashion
- We do not have the same distribution/availability as competitors
    - We actually have advantaged distribution
- We are priced too high relative to our attributes
    - True
- Customers are not aware of our products (advertising awareness)
    - False, people remember our advertising
- Customers are not convinced to buy our product from our advertising (advertising effectiveness)
    - True, we have very poor advertising effectiveness

Why has our advertising effectiveness been poor?

- We don't spend enough
  - True, we spend about 25% too little money
- We don't spend in the right media
  - True, we spend a lot on billboards because they're cheap but they don't reach the right audiences
- We don't spend at the right time of the year
  - True, we spend a lot at Christmas to get the impulse buyers but we don't get the brand loyal buyers
- Our advertising copy is bad
  - True, we have had poor campaigns while the #1 brand has had very good campaigns

How would you determine how much money to spend on the advertising budget?

- Set a target number of customers to reach and a frequency target, and then back out the required investment to achieve the targets, based on the media used, time of year, quality of layout, etc.
- Spend as much as competitors
  - This would require a 100% increase in advertising investment
- Spend the same % of revenue as competitors, or set a % of revenue target
- Look at the competitors, index their advertising investment relative to the price premium they receive, and thus index our investment relative to the price premium we receive (in other words, #1 brand has a 10% price premium and invests $10MM/year in advertising and the industry average is $5MM/year. So they have 100% more advertising for a 10% price premium. We want a 0% price premium, so we'd invest at the industry average of $5MM. Or, we want a 10% price discount, so we'd invest at ½ of the industry average, or only $2.5MM per year)
- Continue current spending
- Spend a % of our cost structure
- Do a break-even analysis and spend up to where we are economically break-even

If our goal was to make money, and not necessarily to gain/maintain market share, what might be some alternatives?

- Reformulate the product to change its attributes
- Change pricing
- Reduce costs
- Change distribution
- Change advertising/promotion strategy
- Sell the brand
- Milk the brand

Which of these is likely to offer the greatest profit potential and why?

- Milk the brand
    - Because market volume is declining so much, we will never recover the advertising investment to turn around the brand (the best strategy).
- Sell the brand
    - Because market volume is declining so much, we will never recover the advertising investment to turn around the brand, and the value of the brand declines every year as the volume declines.
- Invest to build the brand
    - Convince other producers to spend on advertising so the entire industry convinces more people to drink scotch and all producers win. We could also encourage people to switch from wine/vodka/other drinks to drink scotch (e.g., link with cigars to appear more fashionable).

Which of these will be easiest for the company to implement and why?

- Is this the largest brand for the company? (i.e., if this brand declines, will the entire company decline?)
    - This brand is only a small part of the company's portfolio.
- Fit with other brand strategies (i.e., are all of the other brands in the portfolio growth brands so that this is the only declining brand?)
- Fit with management time and attention (is there so much time focused on fixing this brand that other brands suffer and offset the potential improvement in this brand)?
- Because market volume is declining so much, we will never recover the advertising investment necessary to turn around the brand, and the value of the brand declines every year as the volume declines
- Invest to build the brand
    - Convince other producers to spend on advertising so the entire industry convinces more people to drink scotch and all producers win. We could also encourage people to switch from wine/vodka/other drinks to drink scotch (e.g., link with cigars to appear more fashionable).

Practice Case 16 (Regional Jet Corporation)

Initial Handout for Interviewee:

Regional Jet Corporation is a U.S. manufacturer of regional airplanes-airplanes with 100 seats or less. Its business consists of two types of aircraft: (1) jet engine, 80 to100-seat aircraft and (2) propeller, 20 to 30-seat aircraft. In fiscal year 1999, Regional Jet delivered 100 jet engine aircraft and 150 props. This represented a unit volume increase year-over-year of 10% and 5%, respectively, and revenues of $730 million and $225, million, respectively.

Although overall profitability for Regional Jet in 1999 was a competitive 5% economic profit margin, profitability varied significantly by business. The prop business generated a stellar 30% profit margin, while the jet engine business was unprofitable with a margin of 3%. Over the past several years, Regional Jet has experienced eroding profitability in its jet engine aircraft business. Its prop business, despite being profitable, has been flat in most recent years.

At a January 5th analyst conference (a meeting with the investor community) Regional Jet's senior management team announced that the company was committed to managing for value.

To this end, Regional Jet has hired you and a team of consultants to help the company develop and implement the value-maximizing strategies for its businesses.

For our case discussion today, please focus on the jet engine aircraft business:

- How would you go about further analyzing this business?
- What recommendations would you like to make to senior management?

Regional Jet Corporation
Profitability by Business (1999)

	Jet Engine Aircraft Business		Propeller Aircraft Business	
	Amount ($mm)	**% of Total**	**Amount ($mm)**	**% of Total**
Revenues	$730	100%	$225	100%
COGS	$(588)	(81)%	$(86)	(38)%
SG&A	$(84)	(12)%	$(16)	(7)%
Delivery & Other	$(42)	(6)%	$(8)	(4)%
Taxes (40%)	$(15)	(2)%	$(46)	(20)%
Net Income	$1	0%	$69	31%
Capital Charge (10%)	$(21)	(3)%	$(3)	(1)%
Economic Profit	**$(20)**	**(3)%**	**$66**	**30%**

Note: Assume debt-to-total capital of 70%

Interviewer's Discussion Guide

<u>Case Summary (for Interviewers only)</u>

Regional Jet Corporation is losing money in one of its two business units: jet engine aircraft. However, the market for jet engine aircraft is profitable. Although Regional Jet has a parity offering and operating position, it has a disadvantaged overall competitive position, driven by a pricing disadvantage in serving its large lessor customer segment. Lessors, in purchasing large volumes of aircraft, have been able to exert significant buying power over our client to achieve large price concessions.

Jet Engine Regional Aircraft Business

I. Market Economics

An "A " candidate should seek to understand market size, growth and profitability, as well as conduct an indirect structural assessment of the industry, e.g., suppliers, customers. Information to be provided to student if asked, although some may require prompting:

- <u>Market Size</u>: In 1999, the U.S. jet engine, 100 seat or less aircraft market was ~$5 billion.
- <u>Competitors</u>: There is no dominant competitor in the jet engine, 100 seat or less market. The market leader has 20% market share. There are 4 other competitors with market share from 12% to 18%. Regional Jet Corporation has ~16% share.
- <u>Market Growth</u>: The market has been growing ~5% (in units delivered) each year for the past 5 years and is expected to continue to grow 5% over the next decade. In 1999, a total of 625 jet engine regional aircraft were delivered to customers.
- <u>Market Profitability</u>: *Ask the student whether he/she thinks the market is profitable, and how he/she would go about assessing market profitability.* (Answer to be provided post discussion on structural forces below):
    - <u>Supplier Power</u>: The supplier base for regional aircraft parts is highly fragmented and Regional Jet uses approximately 50% proprietary parts in its jet engine aircraft. Hence, supplier power is **low**.
    - <u>Intensity of Direct Competition</u>: Fairly concentrated market with only 6 jet engine regional aircraft manufacturers. Hence, intensity of direct competition is **low-to-moderate**.

- Customer Power: In 1999, there were 225 customers. Types of customers include airlines, aircraft lessors, local and national governments, businesses and private individuals. Hence, customer power **varies by segment**.
    - *Only if the student asks about customer power, share with him/her the following facts:* Aircraft lessors (i.e., Regional Jet's aircraft customers who lease jets to airlines, governments, businesses and individuals) make large purchases (often 20 or more aircraft) during a buying cycle and hence exploit their negotiating leverage over manufacturers, such as Regional Jet. Hence, aircraft lessors have **high** customer power. All other customers have **low-to-moderate** buying power, depending on their credit worthiness.
- Intensity of Indirect Competition: Larger commercial jets (100 seats or greater) with longer range manufactured by large commercial aerospace and aircraft manufacturers can be used on regional routes. However, these larger aircraft are expensive for customers to operate solely on a regional basis. Hence, intensity of indirect competition is **low**.
- Barriers to Entry: Jet engine, regional aircraft manufacturing requires significant capital investment in production facilities and equipment, as well as strong relationships with various labor unions. Hence, barriers to entry are **high**.
- *Based on the information provided thus far, ask the student if he/she thinks the market is profitable or unprofitable.* The market is profitable with the average competitor generating 4% economic profit margins over the past 5 years.

II. Competitive Position

An "A" candidate should seek to understand competitors and Regional Jet's offering, pricing and operating position..

Information to be provided to student if asked, although some may require prompting:

- Offering position: Overall, the company's offering position is at **parity**.
    - *Commonality:* The company's jet engine aircraft has a cockpit that is similar to the industry standard and results in low switching costs for new customers (pilots and flight crew do not need extensive re-training).
    - *Performance:* The company's aircraft offers a range of 500 miles, which is similar to the market average.
    - *Maintenance and Asset Life:* The majority of the fragmented jet engine aircraft maintenance companies have the capabilities and parts to service Regional Jet's aircraft. For the aircraft customer, maintenance costs over the life of the asset is in line with regional jets of the company's competitors. On average, the life of the aircraft is 20 years.

- <u>Pricing Position</u>: *Question for the student: Based on the discussion thus far, what does he/she think that the company's pricing position is relative to competitors?* Answer: Regional Jet is pricing below the market average, since it is gaining market share (unit volume is growing at 10% vs. market growth of 5%) with a parity offering. Hence, Regional Jet is pricing for share, i.e., in 1999 it had a **disadvantaged** pricing position.

- <u>Operating Position</u>: Regional Jet's operating cost per aircraft is at **parity** with the industry. Every jet engine aircraft the company delivered in 1999 cost approximately the same to produce. *The student should recognize that achieving scale is critical to the spreading of fixed costs, and hence, the lowering of per unit costs.*

III. Regional Jets Customers

- <u>Customer Segments</u>: Regional Jet serves 3 types of jet engine aircraft customers:
  - Customers who purchase only 1 aircraft in a buying cycle (approximately every 5 to 15 years, depending on the customer)
  - Customers who purchase 3 aircraft, and
  - Customers who purchase 20 aircraft

- *At this juncture, the student should inquire about customer segment profitability. Provide the student with the handout: "Jet Engine Regional Aircraft Business - Profitability by Customer*

- *<u>Description of Segments:</u>*
  - *Customers who buy only 1 aircraft during a buying cycle are comprised mostly of small aircraft customers with moderate-to-high credit risk.*
  - *Customers who buy 3 aircraft are comprised mostly of medium aircraft customers with moderate credit risk.*
  - *Customers who buy 20 aircraft are comprised of creditworthy aircraft lessors.*

- *<u>Key Driver of Segment Profitability</u>:* If the student has not discussed it already, at this point in the case, he/she should recognize that the 3 aircraft lessors (i.e., Regional Jet's aircraft customers who lease jets to airlines, governments, businesses and individuals) in making large purchases (often 20 or more aircraft) during a buying cycle exploit their negotiating leverage over Regional Jet. The data to support this can be quickly calculated by the student by referencing the "Profitability by Customer Segment" handout: *$408M/60 aircraft = $6.8M average sales dollars per aircraft from aircraft lessors, compared to $8.4M to small aircraft customers and $8.0M from medium aircraft customers.* [Ask the student to compute average price by customer segment, if he/she has not done so without being prompted.] Of course, the student should be able to conclude that the main driver of profitability between segments is solely price without doing any math, since operating cost per aircraft produced and delivered is the same regardless of the intended customer.

IV. Overall Competitive Position

Question for the student: Does he/she think that the company's overall competitive position is advantaged, disadvantaged or at parity?

Answer: Regional Jet is competitively disadvantaged overall with negative profits (compared to a profitable market) driven by a disadvantaged pricing position, particularly to the large lessor customer segment.

V. Alternative Generation

Key Question: What are some strategy alternatives that Regional Jet can pursue in order to improve its jet engine aircraft profitability?

- *<u>Potential alternative #l</u>: Aggressively pursue new small and medium, non-aircraft lessor customers <u>and</u> do not increase sales to existing aircraft lessor customers.*
    - Ask the student what key questions he/she would seek to answer in the evaluation of this alternative. *Key risks may include a slow road to profitability and unlikely to result in the doubling of the jet engine aircraft business' value.* Ask the student to compute how long it would take for Regional Jet to double the economic profit of the business given the company acquires new small and medium, non aircraft lessor customers at the market growth rate of 5%.
- *<u>Potential alternative #2</u>: Aggressively pursue new small and medium, non-aircraft lessor customers <u>and</u> do not serve any aircraft lessors.*
    - Ask the student what key questions he/she would seek to answer in the evaluation of this alternative. *Key risk may include the inability to achieve scale (currently at 100 units, with 60% of units purchased by aircraft lessors), and hence, profitability in any customer segment.*
- *<u>Potential alternative #3</u>: Regional Jet to increase its negotiating leverage vis-a-vis aircraft lessors by entering the aircraft leasing market.*
    - Ask the student what key questions he/she would seek to answer in the evaluation of this alternative. [See discussion below]
- *Others?*

Potential Alternative #3: Enter the Aircraft Leasing Market

Some facts to share with the student:

- *The jet engine, regional aircraft leasing market is large and growing*
    - *In 1999, the new aircraft leasing market represented almost 50% of all new aircraft delivered (with operating leases comprising half) and is expected to grow 5% per year.*
- *The aircraft leasing market is profitable with the average competitor generating ROEs of ~15% (cost of equity ~10%).*
- *Three aircraft lessors (also Regional Jet's customers) dominate the market wish a combined share of 65%.*
- *The key driver of profitability is cost of funds.*
- *Regional Jet currently provides vendor- or manufacturer-financing on a very limited basis in the form of leases.*
- *Regional Jet would be at parity in terms of cost of funds.*
- *Regional Jet has marketing relationships with all aircraft end-users who are leasing their aircraft from the company's aircraft lessor customers. Regional Jet works with these end-users to help them configure the plane during the front end of the sales process.*

Additional Handout for Interviewee
Jet Engine Regional Aircraft Business Per Aircraft Economics and Profitability by Customer Segment (1999) Per Aircraft Economics (1999)

(thousands)	**Per Aircraft Cost**
COGS	$(5,880)
SG&A	$(840)
Delivery & Other	$(420)
Taxes	$(504)
Capital Charge	$(214)
Total Economic Cost	**$(7,858)**

Profitability by Customer Segment

(millions)	**Customers Who Buy 1 Aircraft**	**Customers Who Buy 3 Aircraft**	**Customers Who Buy 20 Aircraft**
# of Customers	5	11	3
Revenues	$42	$280	$408
COGS	$(29)	$(206)	$(353)
SG&A	$(4)	$(29)	$(50)
Delivery & Other	$(2)	$(15)	$(25)
Taxes	$(3)	$(12)	0
Net Income	$4	$18	$(20)
Capital Charge	$(1)	$(7)	$(13)
Economic Profit	$3	$11	$(33)
# of Aircraft Delivered	5	35	60
Share by Segment	2%	33%	50%

Practice Case 17 (British Times)

Case Background:

You're a new senior strategy associate and have just finished your orientation training. You are immediately assigned to our British Times team.

The British Times is an upscale, highly respected newspaper. It is the most widely read newspaper in Great Britain, especially its very strong business and financial section. The paper is a cross between the Wall Street Journal and the New York Times, both in content as well as in reputation.

The team has already had one meeting with the newspaper's online spin-off: BritishTimes.com. You are going to join the team for the second meeting, which will be held with only the CEO of the BritishTimes.com. Currently, their web site is nothing more than an online version of the newspaper, otherwise called brochureware.

The newspaper's and the web spin-off's single biggest asset is the highly respected brand name: British Times. The purpose of this second meeting is for the consulting team to present its response to the CEO's current predicament: how to realize greater revenues from their current online spin-off (BritishTimes.com).

Company Background:

Your team has provided you with the following information as background about BritishTimes.com:

- BritishTimes.com conducted a viewer survey, receiving a high enough number of responses to be statistically significant, allowing them to feel comfortable using the following information for planning purposes.
    - Their web site has a large number of hits, only 30% fewer unique visitors than the number 1 site in the UK.
    - Their hits are from viewers in the 75th percentile of customer income.
    - Their viewers are also highly educated: 60% have a university education and 30% of whom have graduate degrees.

- BritishTimes.com is a spin-off from the newspaper.
    - However, the same parent corporation owns both.
    - The CEO of the dot-com does not report to the CEO of the newspaper.
    - The dot-com CEO has worked for the newspaper for a long time and knows its operations well.
- The brand name is very strong in the UK, but not outside.
    - The newspaper's content is primarily focused on the UK, but it does have an international section.
    - The CEO wants the dot-com to use the newspaper's content and brand, but otherwise has no need to connect to the newspaper.

Your Challenge:

Create 3 or more ideas for the BritishTimes.com company to increase their revenue through their Internet strategy.

Possible Solution:

Candidate: In general, it's fair to say that the bulk of Internet revenues comes from three sources: advertising, subscriptions, and transactions. I think that the key to helping the CEO is to tailor these initiatives to British Times.com core assets.

[Great way to start. The candidate did not try to use an ill-fitting framework such as 3Cs or 5 forces to approach this case. Instead he's showing a good understanding of the Internet's major sources of revenues. He also acknowledges that further discussion of the company's core assets is critical to formulating a robust solution.]

Interviewer: Good points. Can you give me more details on each of these sources of revenues?

Candidate: Well let's look at advertising first. We could suggest two avenues: banner ads and corporate sponsorship. Upscale or corporate banner ads such as insurance companies, banks, or brokerage firms would make a lot of sense with our audience. They are highly educated and more importantly, have the highest level of disposable income. In addition to banner ads, we should look into corporate sponsorship. We should take full advantage of the fact that the strong business section can obtain corporate sponsorships; for example, banks or e-trade companies pay for their section of the site.

[Well-structured answer. The candidate is using the case facts to support his answer.]

Interviewer: Good. They do some of that already but probably not as much as they could. You also mentioned other sources of revenues. Could you explain your subscription model?

Candidate: We could imagine a three-tier approach. For example, in tier 1, readers could have access to today's news for free. For a small fee, Tier 2 subscribers could research up to one-week-old articles in the archive. Finally, in the last tier, subscribers could have access to the entire archive.

Interviewer: Coming from a traditional publishing company, they are fairly familiar with these two models. I would be interested in hearing more about your third option.

Candidate: One way to "monetize" their attractive audience would be by offering targeted products and services. Some examples could be a tollbooth model similar to Amazon Z shop concept or selling tabs on their site. This would clearly require a deep analysis of the competitive landscape and of the company's capability (technical, people...) to start a completely new line of business.

These products or services would have to be:

- High margin,
- Upscale,
- Highly profitable vertical businesses; for instance: golf store, tax advice, investment advice, upscale travel (cruises, etc.)

Interviewer: Golf equipment? This is interesting. How would you go about sizing the market for golf equipment in the UK?

[The interviewer decides to test the candidate’s ability to do some real time analysis, to articulate a methodology, and to make reasonable and explicit assumptions in order to arrive at a ballpark estimate. Here the interviewer could have chosen to discuss more in detail how the candidate would have thought about launching a completely new line of service.]

Candidate: To determine the golf store's (equipment only) first year total revenue, we would have to figure out the following:

- The population of the UK
- The percentage connected to the Internet in the UK
- The number who browse this site
- The number who browse the golf store
- The number who buy from this site: the buy to browse ratio
- The average amount spent per transaction
- The number of times they buy per year
- The commission received by BritishTimes.com

There are approximately 60 million people living in the UK. If we assume that a third of them are connected to the Internet, we have:

60M x 1/3 = 20M

[It's always a good idea to take numbers that are easy to manipulate. Do not hesitate to round up the number to help your calculations. The examiner is not looking for an accurate answer.]

If we assume that 20% of the people connected will visit the British Times site, we now have:

20M x 20% = 4 million visitors

Not all of them will click on the golf site. Probably about 20% will do. We can now estimate the number of people browsing the golf site:

4M x 20% = 800,000 visitors

If we assume that only 10% of them will actually purchase on the site, we now have:

800,000 x 10% = 80,000 buyers.

Each buyer may spend on average $100 each time they visit and they may visit the site 2 times each year.

If we assume a 5% margin, we now have a rough idea of the golf equipment first year revenues:

80,000 x $100 x 2 x 5%= $800,000

Practice Case 18 (Children Clothes E-Retailer)

Part 1:

Case Situation:

It's a Friday afternoon. You've just accepted an offer to join our consulting company as a Senior Associate in the Business Strategy Competency. You've just called in to confirm your start time on your first day and find out you have an excellent opportunity to be the lead business strategist on a high profile project. We have partnered with a leading bricks-and-mortar children's apparel retailer to help them analyze, design, and build their Internet strategy. There will be a kick-off meeting for the project with the client (including the client's CEO) on Monday morning. The Principal/Engagement Leader on this project has asked you to lead a discussion about how the client should think about opportunities on the Internet. Right now, the client only has a marketing and informational presence on the web (a.k.a. "brochureware"). The Principal/ Engagement Leader wants the client to think about the range of opportunities and challenges the Internet presents and whether the client should invest aggressively in pursuing any initiatives.

Company Background:

The client's web site and some associated articles found on the Internet have provided the following information.

- The client is a publicly traded company with a $3B market cap. The share price has risen from $15 to $45 in the past 12 months.
- The client has 300 stores, mostly east of the Mississippi, and all stores are within the U.S.
- Revenues are approximately $250M, and the firm has average profitability for its industry.
- The client has been on a rapid store expansion program adding about 25 new stores each quarter for the past two years. They claim to expect similar growth going forward.
- The market for this client is clothing for children 12 and under. Sales are roughly split between boys and girls.
- The company is vertically integrated: It designs all its own products, has deep relationships with contract manufacturers in Asia, and distributes all of its products through company owned stores.
- The company sells a high quality product that is priced about 25-30% lower than its chief competitors.
- The company has done only limited marketing. The brand remains relatively unknown.

Your Challenge:

- Plan for the client meeting. Structure the problem at hand. What questions would you ask?
- Then, work with your interviewer to explore and broaden those questions and brainstorm the client's hypothetical responses.

Possible Approach:

To present the best solution, the candidate must have a better understanding of the customers, the competitors and the client. Some of the important questions to ask are:

Market and Competitive Landscape:

- What are the main trends and dynamics going on in the client's industry?
- What are their competitors doing?
- Who are they?
    - What are the brick-and-mortar children's apparel retailers doing?
    - How are they using the Internet: Has there been a direct causal relationship to their revenues and/or expenses from their Internet strategy and implementation?
    - What are the Internet pure play apparel retailers doing?
    - Who could some of the oblique or peripheral competitors be?
    - Would they be likely to enter the market?

Customers:

- Who are the client's customers?
- What is the value proposition to the client?
- What are the trends in the customer base over time?

Client:

- What are the client's goals?
    - To increase revenues? To reduce costs? To increase market capitalization?
    - How could different Internet initiatives accomplish each of these goals?
    - Are these the right goals for the client to have?
    - What are the client's organizational capabilities?
    - Are they capable of supporting an Internet initiative with the existing culture? Talent? IT infrastructure, legacy, processes? Operational structure, processes, procedures, policies? Accounting processes?

[The goal of the interviewer is to assess the candidate's ability to analyze and develop questions for the client to answer. The interviewer will often play the devil's advocate and challenge the hypothesis the candidate generates.]

Part 2:

Quantitative Analysis:

After spending part of the weekend preparing for your kick-off meeting and discussion facilitation, you check your voicemail from the airport before hopping onto the shuttle on your way to the client's office for the meeting. The one new message is from your Principal/Engagement Leader asking you to provide an estimate of the size of today's online component of domestic children's apparel sales and how large it might grow in the next 5 years. As you step onto the plane, you realize that you'll have no access to the Internet or other research before the meeting starts. Instead, you will need to create a "back-of-the-envelope" analysis on the plane.

Your Challenge:

Spend about 5 minutes creating an answer to these two questions:

1. What would you estimate the size of today's online component of domestic children's apparel sales today?

2. How large do you think it will grow in the next 5 years?

[The point of this scenario is to test the candidate's ability to do some real time analysis, to articulate a methodology, and to make reasonable and explicit assumptions in order to arrive at a ballpark estimate.]

Possible Response

Assume the children's apparel category is dollars spent on clothes for kids ages 12 and under, as stated in the case facts.

There are approximately 275M people in the U.S., perhaps 15% are under 12.

275M x 15% = approximately 40M kids under the age of 12.

Assume the average parents spend $250 on each kid age 12 or under each year.

40M kids x $250 = $10B children's apparel industry for kids 12 and under.

Of the people who spend this $10B, assume 35% of them have Internet access and have the potential to shop online.

Therefore, the theoretical current maximum potential size of the market is $3.5B.

However, just because people use their online access to buy their kids' clothes doesn't mean they spent all $250 for each child online for their apparel. In fact, only a small fraction of those dollars are spent online today, perhaps 5% (a.k.a. share of wallet).

5% x $3.5B = $175M (which is not too far off the actual estimate of $130M in 1999-Forrester Report)

In the next five years, let's assume the number of kids increases to 42M, average spending goes to $300 per kid age 12 and under, Internet access rises to 55% and share of wallet rises to 20%.

The 5-year growth estimate would be:

42M kids x $300/kid x 55% x 20% = $1.4B (which is not too far off the Forrester estimate of $1.6B).

Practice Case 19 (Consumer Products)

Case Situation

It's Monday morning and as a new Principal/Engagement Leader, you've just gotten a call from a well known and respected French-based Consumer Products company. The company has offices in the US and has been selling through traditional channels throughout its history. It designs and manufactures plastic products like pens, pencils, disposable razors, etc. It's an old company that's been around for about 60 years and wants to take advantage of the Internet, starting with the US sales.

Company Background

You talked at length with the President of the dot-com part of the company and this is what you learned:

- This company now wants to sell directly to consumers through their Internet site.
- Their current online business is nothing more than a small catalog and is not doing very well: sales and hits are less than expected.
- It offers:
  - More convenience than their other channels. It is open 24x7 and has more product information.
  - But, limited selection: only high margin items.
- The President's strategy is to add key functionality to the online business to increase the hit rate and improve revenue.
- She reports directly to the CEO
- She wants your consulting team to create:
  - A multi-ship-to-functionality,
  - A site-wide search functionality,
  - An ability to add checkout sales (e.g. impulse buy items similar to end caps in grocery stores next to the register).
- She wants your consulting team to build this immediately.

Your Challenge:

This coming Thursday, you will meet with the President and her team.

Her expectation is that you will present a plan for your consulting team to build the functionality ASAP.

- What will you do on Monday?
- What will you prepare?
- What questions will you ask the President?
- What is your goal for that meeting?

Candidate Response:

There are many ways to answer this challenge, but the candidate should at least know not to accept the client at face value, realizing that the functionality the President wants will not materially improve the hit rate or revenue, at least as far as the information provided indicates.

The candidate should want to create a conversation with the President and her team to present the plan for delivering the functionality (or state that there is a plan), primarily to gather additional information to better understand the online company's business issues and goals. In other words, the candidate should want to open the eyes of the President and her team through questioning. The candidate will want to offer the notion that the additional functionality will not solve the pressing problem.

The candidate's questioning of the President should follow a logic path that includes asking about the value proposition of the line store; for instance:

- Who is the store trying to target?
- What is the store's value to the customer—its real offering (e.g. convenience, price, selection)?
- Why is it a unique and attractive offering?
- How will the online store deliver on the promise?

Practice Case 20 (The Video Store)

Question and Background Information:

Two business school classmates laud their entrepreneurship intentions and mock your interest in entering the management consulting industry. They decide that despite trends that indicate otherwise, what is needed is a video rental store closer to the HBS campus. They try to convince you to join, but in your infinite wisdom you instead join a prominent strategy consulting firm in Boston.

Their first two years meet unprecedented success. They buy matching Porches and a townhouse in Beacon Hill. Needless to say, each time you meet up for social occasions, they share with you (mostly with tongue in cheek) their success and a "I told you so" attitude. You handle their jabs well, as you feel you have had a terrific experience at your consulting firm.

The story, however, changes in about 12 months. Despite two and a half years of dramatic profit and revenue growth, profits have dramatically fallen. They call you (with a fair amount of egg on their face) and say "we don't know what happened and our mortgage and car payments are getting tougher to meet. Can you help us? We know that you help CEO's of large companies get to the bottom of their issues." With more than a little satisfaction and justice in your voice you agree to help.

What do you think the problem is?

Suggested Questions:

This is an example of a case where the student must probe to get to the heart of the matter. The student needs to ask questions which first diagnose the situation and then (and only then) talk about causes of the situation and then (and only then) talk about areas of improvement.

Here are questions that the student should ask to get to the analysis that will help them diagnose the problem:

- Have costs increased?
- Have revenues declined?
- Have prices been changed?
- Have new video stores opened in the area?
- Are fewer customers coming to the store?
- Are customers renting fewer videos?
- Have other entertainment venues opened in the area?
- Have their been economic changes in the area?

These key questions will get behind what is happening (competitive changes, pricing adjustments, macro factors, people not coming to the store, or people just not renting as many videos, etc.)

Suggested "Excellent" Response:

This is an example of a case that is founded in 3C's type issues. The student has to diagnose the problem and find out what exactly is going on and then find out what is causing it. This is how efficient analysis is performed:

If profits have declined then I assume that either revenues have declined or costs have increased, what is the case?

Revenues have decreased. Why would you think that cost is probably not the problem?

Video rental is a high fixed cost business - rent, videos, and labor are all fixed in the context of rental revenue. Thus, the business' profits will be susceptible to changes in revenues (capacity utilization). Revenues are made up of the number of videos we rent in a year and the price we charge. Has the management changed the price of the videos?

No. What does that tell you?

That means that either fewer customers are coming to the store or each customer on average is renting fewer videos. Which is it?

How would you figure that out?

The security system probably has a counter so that could tell us store traffic, and clearly the register receipts could give us number of videos rented per day. We can look at that data last year versus this year and determine whether there is a traffic problem or share of wallet problem.

Excellent. If you found out it was a share of *wallet problem, what would you think might be the problem?*

Share of wallet problems are often driven by internal execution problems (bad selection, poor service, etc) whereas, traffic is often external (or market) problems.

Again, excellent. The data shows that traffic has fallen. What now?

[Here the student should begin to think about hypothesis development. They have diagnosed the problem... i.e. fewer customers are coming into the store.]

If traffic has fallen, it is either a macro factor or a competitive situation. My inclination is that video rentals are not that impacted by economic factors, so it is probably a competitive situation. Has a new store opened in the area?

No.

Has a new movie theatre opened?

No.

Hmm... That is surprising. I was sure that this was a competitive situation and we have a fixed pool of rental community (or movie interested community) and that once a new store opened regardless of how good it was, it took share from my client's store.

Let me ask you something and maybe this will help you along. What business is your client in?

They are in the video rental business or the entertainment business or leisure business... I see there could be other entertainment preference shifts or options, etc.

That is good intuition, but have you fully defined your client's business? What does your client do? What purpose to they serve?

They rent movies for people to watch at home. They are in the home entertainment business and specifically in the home movie entertainment business. That means that the competitive set is anybody who provides movies in the home. Not just video stores.

Excellent. What do you think is going on?

Here the student has now diagnosed the problem and can make a very good hypothesis that either delivery, cable, PPV, or new Movie on Demand technology has infiltrated the market or is experiencing rapid growth, reducing the market size for video rentals at stores.

Summary Comments

There is no one right way to approach cases. Structure your case interviews to (1) perform structured analysis and fact gathering to properly diagnose the problem; (2) share your logic and hypothesis whenever you can; (3) drive to an answer/assessment.

Practice Case 21 (The English Church)

Question and Background Information:

Assume you are the new pastor of a rural English church in the late nineteenth century. Over the last three years, attendance has been declining. Your boss has just come to town to tell you that she is considering shutting down the church. You have two weeks to diagnose the problem and come us with possible solutions.

How would you think through what these problems might be and the possible solutions?

Suggested Sample Response:

There are many potential reasons why the churchgoers of the parish have stopped going to church. First, I will talk about the possibility of competitive churches; secondly, I will talk about the possibility that people in the area have simply stopped going to church.

There is the possibility of competing churches. There are two reasons why competing churches could be taking our parishioners away: better location, better religion, or better services. I remember from my history classes in college that some churches were located far away from pockets of the population, and churchgoers often would establish churches closer to home. Also, sometimes people change what they believe or new ways of thinking emerge. This could also be driving people to other churches.

I would also want to figure out if the nearby churches are preaching different religions. There is at least a chance that these churches are offering parishioners a different kind of religious viewpoint that is more attractive than the religion we have been preaching. Their rules regarding behavior, for instance, may be different from ours.

Lastly, I would want to understand the different services being offered at "competing" churches. There may be different value that these other churches offer that we do not. For instance, these churches might provide childcare, adult education and job training, or singles dances. These churches may offer more personal attention and guidance from the pastors.

I will also talk about the possibility that people who live in the area around the church simply may have stopped going to church. Off the top of my head, I can think of two reasons why people may stop going to church: progress and inconvenience. As science and communication advance, people may rely less on the church to explain the world and more on scientific findings and written forms of communication such as books and newspapers. This could be happening in our parish. On the other hand, going to church may be becoming inconvenient or economically nonviable. Maybe our parishioners feel that they need to stay at home to work in the fields in order to maintain subsistence. I would want to talk to these parishioners to find out why they have stopped going to church

There are many ways I could test my hypotheses. I think the most important thing is to talk to the former parishioners to ask them why they have left the church and what we would need to do to entice them back. After that, I would want to send someone (or myself) to the other churches in the area during services to understand what is being preached at these churches. To help prove if the issue is location, I would draw a map of our current and former parishioners and analyze how distance from the church affects attendance. To understand if there are other churches in the area taking away our parishioners, I would also map these new churches on my newly created map.

Once I understand why people are leaving, I would devise a plan to bring the parishioners back. I would want to be focused on the needs of my parish, by offering enhanced services, such as day care as well as flexibility, such as offering services at different times of the day. If distance is a factor, I may want to consider having services at different locations at different times, making our church more accessible.

Summary Comments

This would be a very good answer. The candidate came up with a number of hypotheses, identified ways to test those hypotheses, and formulated an action plan to address the issues. This answer shows thoughtfulness, creativity, and structured thinking. While there may be some issues that this candidate did not identify, he/she does a good job structuring a comprehensive answer. For a 3Cs answer to be good, a candidate does not have to address every single issue.

Practice Case 22 (HBS as a Business)

Question and Background Information:

You are Dean Clark. A wealthy benefactor has come to you with the news that she will give HBS $100 million. The grant is contingent, however, upon you using the money effectively. You have 1 week to propose to the benefactor where you would use the money before she will finalize the transfer.

How would you, as Dean Clark, propose to use this money?

Suggested Sample Response:

First, as Dean Clark, I need to think through what does spending the money effectively mean? This is a not-for-profit learning institution, but that does not mean that it is not a business. For Dean Clark to be successful, he needs to understand what drives his business and where he can achieve the biggest return for his investment.

There are currently 4 major "business units" that provide a revenue stream for HBS. These include:

- MBA program
- Executive Education program
- Publishing
- Grants and donations

While there are many budding initiatives, including distance learning, these are the four largest sources of revenue.

If you rank the relative profitability of these revenue streams, you would likely find that the least profitable of the four is-the MBA program. Publishing is a very profitable business but it seems to have high reliance on the education business. Executive Education is very profitable, as the fees charged to the executives are quite large when compared to the length of program. Grants and donations are virtually pure profit.

At first glance one might conclude that HBS should focus their resources and efforts on the highest return areas of securing grants, publishing and expanding the Executive Education program. It would follow then, that the MBA program would fall as the lowest priority for resource allocation. That would be an incorrect conjecture, however. Consider what draws people to the executive education program, for example. The brand cache of HBS drives the attendance and enables the price premium. Similarly for publishing, the value of the HBS brand provides the credibility behind the content and drives sales. So what drives the HBS brand? Clearly it is the MBA program.

Dean Clark must focus on maintaining the reputation of HBS as the premier MBA program to attract the best and brightest professors and students. It is then the academic and professional work of these people that contributes to the integrity and value of the brand. Obviously the professors publish, hence enabling that revenue stream. The MBA students graduate and achieve notable success, further driving the brand. Finally, the alumni are responsible, to a large extent, for the grants and donations that HBS receives.

In the end, the MBA program effectively ties in every other revenue stream both directly and via the resulting brand cache. Clearly the $100 million is best spent on the MBA program.

Summary Comments

This is not a particularly difficult case but it does assess the candidate's ability to think through the school as a business and reason through to the underlying driver of that business. A superb candidate will need little to no prompting to think through this case in its entirety.

Practice Case 23 (Fast Food Restaurant)

Question and Background Information:

Six months out of HBS, a frustrated classmate calls you to complain that the fast food burger joint that he bought has been steadily losing money for the last 3 months. He wants to know what you think he should do about it.

Where do you start?

Suggested Questions:

This is an example of a case where virtually no information is provided and the student needs to take a minute to figure out where to start probing. In this type of case, the student is evaluated based on the number of factors questioned up front plus the ability to logically pare down that list to get at the heart of the matter.

Here are some of the initial questions the student should ask:

- Have revenues decreased?
- Have costs increased?
- Have prices increased?
- Was the store making money 3 months ago? What has changed?
- Is there new competition?
- Has there been a major economic change in the area?
- Was there a major event like someone getting sick? Health code violation? Crime?

These answers will help to frame the extent of the required analysis.

Suggested "Excellent" Response:

What do you mean by "losing money"? Have profits declined or is the business in the red?

Profits have declined.

Have revenues decreased? Costs increased? or both?

Revenues have decreased.

If revenues have decreased, there are either fewer paying customers or the customers are spending less when they visit. Which is the case?

While they could both play a role, in this case, there are actually fewer customers.

Fewer customers could be due to external factors like new competition, change in eating habits, local changes like a major business closing in the area. There are also internal factors to consider such as poor food quality, higher prices, or a major event like someone getting sick or a health code violation. Recognizing that there are likely many factors involved, is the issue primarily internal or external?

The issue is external and is driven by a new competitor that opened across the street.

This new competitor must be offering a better value to have made such an impact on the burger joint. What is their value proposition? Are they offering a different type of food? Is it better quality? Is there a price disparity?

They serve chicken dinners and appear to offer a completely different experience. How would you get a deeper understanding of their value proposition?

First, I would visit and learn everything that I can from what I see and experience first hand. How is the quality of the food? Are the prices reasonable? Do they offer healthier options and more variety? How is the service? Cleanliness? How is the facility laid out? Do they have more parking? Easier access? Once I get a first hand view of the competition, I would take a hard look at the burger business and the value proposition they are offering. The same questions would apply.

Next, I would do some primary research including customer interviews at both locations. The focus of these interviews is to discern the differences in perception between the two locations. 1 would pay some customers to go to each restaurant and rate the food and experience. I would also determine how many of the customers are former burger customers but now are exclusively chicken customers, versus how many visit both, and how many are completely new to the chicken place but would not visit the burger restaurant.

Armed with the data on what customers' value, I would then create a set of options to evaluate. There are likely a number of areas that need improvement including new menu options, improved facility layout, better taste/quality. Which will drive most traffic back into the restaurant fastest? Which give the largest return on investment? After analyzing the alternatives based on the chosen criteria, I would prioritize them and develop an action plan to include timing and responsibilities.

[At this point, the case could go in several directions from leadership and project management issues, to brand marketing and promotion, to financial decisions about whether to close the facility.]

Summary Comments:

This type of case can be very intimidating since it is broad and ill-defined. The interviewer may not provide much guidance or detail; increasing the stress level. When faced with an interview of this type, the student should try to remain calm and methodical. Writing down the alternatives and crossing them out as they are ruled out is a good way to show their thought process. Thinking aloud is encouraged. The student should take a little time in the beginning to frame the issue so as not to develop a hasty hypothesis and head down the wrong path.

Practice Case 24 (Automobile Producer)

Question and Background Information:

The director of marketing at an automobile manufacturer suggests changing the current design, where two separate keys operate the ignition and the doors to a design where one key operates all lock mechanisms.

How do you think about whether this a good idea or not?

Suggested Sample Response:

The goal of any business including automobiles is profit throughput that can be measured by the Net Present Value impact of the proposed change. For the proposed change to have a positive impact on profit throughput, the change must be a net positive of change in cost structure or product demand weighed against the investment needed to implement the change. An expanding of demand in this case must come from the product meeting customer needs better than the direct competition or substitutes. Customer needs that this product may address are simplicity, security, and cost of ownership (related to security). One should also consider if the improvement is defensible or would be easily copied.

For cost structure, the relative expense of using what is assumed to be the more complex locking mechanism of the ignition on the door and trunk (assumed 5 locks that would be more complex) would have to be weighed against the reduced cost of developing or purchasing separate key and lock mechanisms. As most automobile manufacturers are very large, it is assumed that the simpler locking mechanism needed for the doors could be reused across many product lines or purchased from large parts suppliers who supply the industry as whole and the development cost of a separate locking mechanism would be low. Therefore, the change in cost structure will be driven by the relative cost difference of buying 6 complex locking mechanisms vs. 5 simple locking mechanisms and l complex mechanism. It is assumed that a more complex locking mechanism is needed for the ignition. Therefore, the hypothesis is that the net change of cost position is negative. It is also assumed that the market power of buying more complex locking mechanism would not significantly impact the price charged by suppliers or cost basis if developed internally. This hypothesis would be easy to check by looking at the relative cost position of the different locking mechanisms and the discount structure available for mass purchasing the various locking mechanisms.

On the demand generation side, the product would have to create a net positive in demand across the customer needs of simplicity, security, and cost of ownership. The fact that the marketing director suggested this change hints at the fact that customers may demand the increased simplicity of only carrying one key. This does not seem intuitively true as the two keys are almost always carried on the same key ring so the relative improvement to simplicity is probably minimal.

For security, there are two factors to consider, the theft of valuables in the car and the car itself. If more complex locking systems were to improve the security to valuables, then the value of going with the more complex locking system on the doors of the car may be a positive. The assumption, however, is this is not the case as door locks are typically compromised not by picking the lock but by compromising the areas around the lock (i.e. Slim Jim). Also, security systems, which are becoming more common on cars, mute the affect of a more complex locking mechanism, as the key lock mechanism becomes the non-primary mode of defense. I do not see how moving to one key would impact the chance of theft of the entire car, as in either case the same locking mechanism would have to be beaten. This also means the cost of ownership, which could have increased if the change of car theft increased due to insurance premiums, would exhibit no affect.

The customer reaction to a single key mechanism could be tested through surveying or product pilots where a sample set of customers are given actual cars with one key and asked to gauge their reaction. Or larger regional pilots could be run and the change in demand affect measured.

The investment required to implement the change of eliminating a separate key and lock for the doors and ignition is assumed to be minimal as key locking mechanisms are fairly standardized and the ignition key lock, which is probably more complex, could be transferred to the doors and trunk with minimal amount of rework of the parts assembly infrastructure for building the auto. The primary investment cost would then be the cost of piloting or surveying for the increase in customer demand by implementing the change. Surveying and piloting costs can be significant, but it is assumed a cheaper survey would suffice in this case to gauge demand so investment costs would be minimal.

Three final possible points to consider on demand generation. One, an increase in demand is necessary but not sufficient to improve profit throughput, as the company also needs to be able to meet the new demand generated. As auto manufactures almost always have an excess of capacity, this is not an issue. Two, even if this change was beneficial it could be easily copied by competitors and it is assumed that the change would not provide any lasting brand advantage in the customers mind or raise the demand of the sector as a whole. Therefore, in the long run, the cost reduction benefits would override the decision to go forward and we have already argued the affect would be negative. A final factor that should be considered is the assumption that the majority of cars sold in the US in the past have included two keys and the two keys have most likely generated a lot of unanticipated use that may be hard to anticipate that might cause customers to reject the change. So, from a customer perspective, I would want to see the demand for this from customers to be strong and the benefits large before implementing a change.

Because it does not appear the proposed change would positively impact cost position or increase demand significantly, the recommendation is against the proposed change. I recommend even against investing to gauge customer demand as the long run benefit would be in cost position and the assumption here is that the affect is negative.

Summary Comments

This candidate starts with a framework and works through to a hypothesis and how the answer might be tested. All the customer factors or cost impact that could be considered are obviously not included, the interviewer should look for a structured presentation that arrives at a hypothesis with ideas how to test and a proposed answer.

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