Are You More Capable Than Your Competitors Are Ruthless?

In times like these, when an upstart rival could be—and probably is—lurking around every corner, your very existence depends not only on your ability to identify a potential threat but also on your willingness to take on the most ruthless of competitors.

IN THE LATE 1990s, global network manufacturer Cisco Systems was sitting pretty. The maker of hardware, software and services for Internet solutions had 60 percent market share for high-end network equipment in China. But as Cisco was enjoying cover stories in the world's leading business publications, little-known start-up Huawei Technologies, which began by importing and developing PBX telephone products, quietly entered the networking industry. Formed in 1988, Huawei was unencumbered by inherited costs, was able to hire newly minted Chinese engineers at starting salaries of $8,500 a year, and enjoyed a multibillion dollar credit line from the Chinese government.

Huawei took full advantage of its competitive strengths, producing networking equipment at a cost 70 percent lower than its much larger rival, Cisco. Through partnerships with 3Com and Siemens, Huawei entered new markets, and in the United Kingdom it won British Telecom's business, ultimately forcing the domestic incumbent, Marconi Corporation, onto the selling block. From 2001 to 2005, Huawei's global revenue rose from $2.29 billion to nearly $6 billion, and it cut Cisco's market share in China to less than 40 percent.[1]

So what does it take to make a brashly competitive move like Huawei's? It is the ability to leverage competitive advantage, to foresee what other companies do not, and a ruthless willingness to use the mass and momentum of opponents against them.

Whence They Come

Ruthless competitors (RCs) such as Huawei can come from just about anywhere. Consider the factors that propelled Huawei into the networking industry—growth through partnership, low-cost labor and capital, and the wherewithal to enter a new market. These competitors employ widely different competitive strategies, but they succeed for a common reason: The RC applies a new rule in an established game, and combines this rule with the ability to cut costs significantly. Figure 1 highlights the attributes of typical ruthless competitors, which can be seen in a variety of different companies.

For example, Nike's ruthless competitor is the comparative small-fry Steve & Barry's, an established discount clothing chain that is capturing a niche market opportunity in athletic shoes. Its Starbury One basketball shoe, which sells for less than $15 a pair, is leading a full-court press on kids' current demand for budget-priced athletic shoes. Steve & Barry's applies the low-cost rule in a branded-product environment with stunning success. Three million pairs of Starbury One sneakers have sold since their August 2006 debut. In contrast, Nike's footwear inventory is 15 percent larger than a year ago and sales of the once-hot Air Jordans lag behind as youths replace them with shoes endorsed by New York Knicks guard Stephon Marbury—at a 60 percent lower price tag.[2]

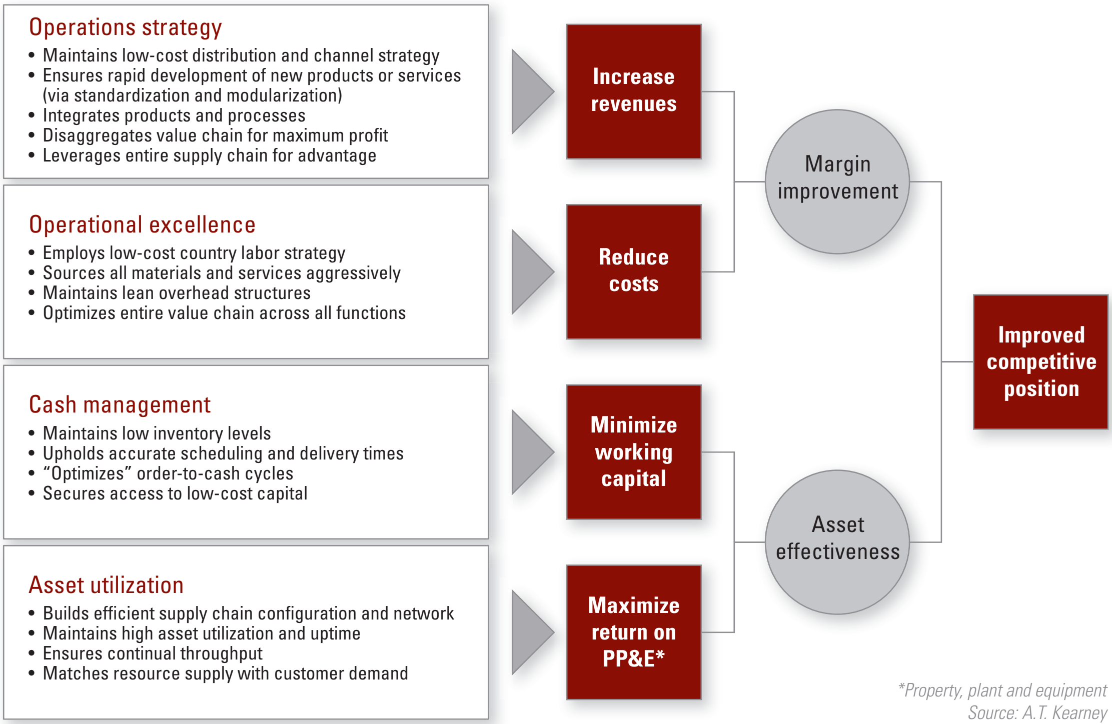
Southwest Airlines is another top-notch ruthless competitor. Although known for its no-frills, low-cost service, the most overlooked aspect of Southwest's profit-winning strategy is its superior asset utilization. By structuring flight schedules to return planes from the gate to the air in as little as 20 minutes, Southwest flies its planes 20 to 30 percent more hours than other major airlines. By deploying a point-to-point route network, instead of the hub-and-spoke model used by most major carriers,

[1] Huawei 2005 Annual Report; *Bruce Einhorn, "Cisco's Middle Kingdom Alliance,"* BusinessWeek Online*, 23 November 2005; Craig Simons, "The Huawei Way,"* Newsweek International Edition, *16 January 2006.*

[2] *Stanley Holmes, "Changing the Game on Nike,"* BusinessWeek, *22 January 2007.*

FIGURE 1

Attributes of a ruthless competitor



*Property, plant and equipment
Source: A.T. Kearney

Southwest minimizes the domino effect of flight delays and gains maximum use of its assets.

Some ruthless competitors emerge without warning. Blockbuster was stunned in 1999 when Netflix came up with a brilliantly simple online concept: rent DVDs by mail for a flat monthly fee. Netflix ushered in the age of DVD delivery and the beginning of the end for the video store, late fees and all. Blockbuster scrambled to adjust its strategy, but too late. Netflix now has roughly four times more subscribers than Blockbuster—5.7 million to Blockbuster's 1.5 million.

Even Wal-Mart and Ikea, ruthless competitors in their own right, must constantly be on alert for the next threat. Their retail model of selling low-cost branded items is being challenged by Muji, a Japanese retailer that applies high-concept minimalism to an unbranded environment. Muji's full name, Mujirushi Ryohin, translates into "no-brand quality products." The retailer, well established in Europe and Asia, is now moving into the U.S. market—with the New York store expected to turn a profit within a year, and stores in Boston, Chicago and San Francisco to follow.[3]

Essentially, you must be prepared for any company to become a ruthless competitor. A current partner, a supplier or even your contract manufacturer can walk away with key elements of your value chain, establishing its own operations on a modest scale and positioning itself to

[3] *Kenji Hall, "Zen and the Art of Selling Minimalism,"* BusinessWeek, *9 April 2007.*

take more value later by moving upstream or increasing its leverage. That same contract manufacturer might cross boundaries to apply what it learned in one industry to break into another. Huawei's challenge to Cisco is a good example.

At the same time, a ruthless competitor will be more focused than any you've run into before. It wastes very little energy on activities that are not considered core. The matrix in figure 2 illustrates how a typical competitor can become a ruthless one as it masters integrating core competencies with strategic activities.

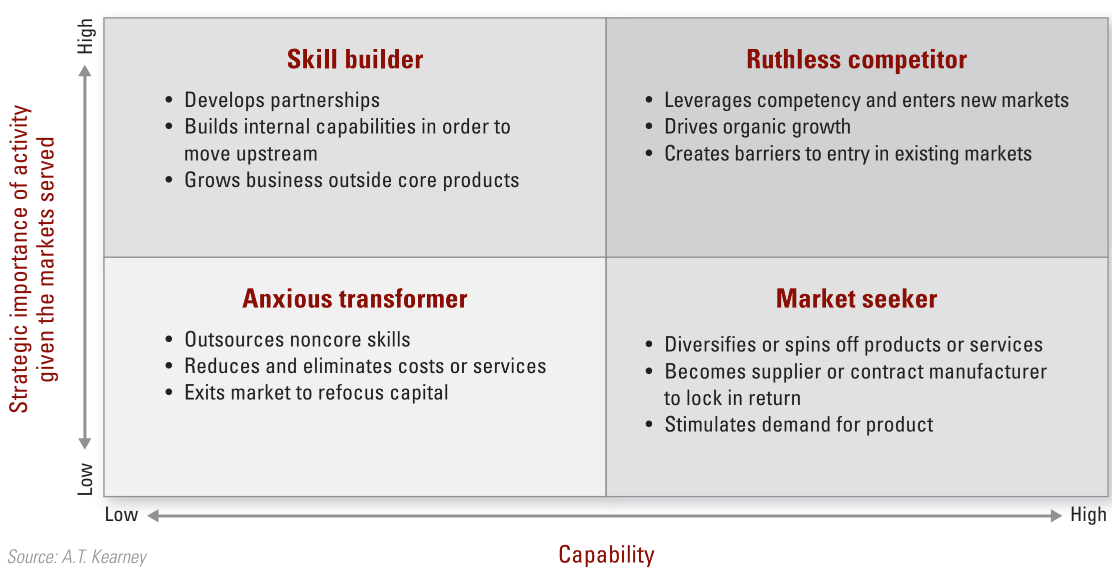
Ruthless Competitor Analysis

Many companies fail to recognize a ruthless competitor until it's too late. One reason is that they develop their business strategies in functional silos and according to internal objectives, without fully considering the entire spectrum of competitor strategies or changes to the external environment. In other words, you perform a competitive analysis by benchmarking your position against the preexisting value chain. While this can build the case for change and help you gain traction for internal initiatives, it isn't realistic to continue benchmarking peers in the traditional way in today's world of the extended enterprise. With more diffuse industry barriers, your competitors are outsourcing some parts of their value chains and building partnerships in others. This obscures the true competitive picture and multiplies the number of benchmarking variables.

Instead, we suggest conducting a ruthless competitor analysis. It is a method of studying competitors that digs deeper than the qualitative, theoretical approach of war-gaming or the internally focused tools of business process redesign and lean manufacturing—and is more pragmatic than the hypothetical what-ifs of scenario planning. Better yet, it complements

FIGURE 2

Ruthless competitors capitalize on their core competence



Source: A.T. Kearney

these approaches by encouraging out-of-the-box thinking and providing steps to thwart an aspirant ruthless competitor. Essentially, what we all need when undertaking a competitive analysis—company and consultant alike—is a practical way to identify current and future competitive threats. The ruthless competitor analysis solves these problems. The goal is not so much to compete against the ruthless competitor or defeat it, but to compel actions that allow you to become more competitive and grow or maintain a profitable position in your market segment. The analysis involves the following steps.

Identify potential RCs. Potential ruthless competitors are identified by tying competitive strategies to areas along the value chain. This spans all of the potential RC's characteristics—from design and procurement to assembly, marketing and support—in order to pinpoint its specific advantages, strengths and sources of value creation. For example, in design engineering the RC might be the company that focuses on a cost-effective design process rather than unique product design. In procurement, the RC is probably one that involves suppliers early in the process, during initial product design and development. In ordering and distribution, the analysis should never rule out an RC's ability to engage untried channels. When upscale Kobold Watch Company bypassed high-end jewelers

Winning with Chess-Like Elegance

When a preferred supplier keeps too much "value" for itself, a ruthless competitor analysis can produce better terms during negotiations and help preserve the relationship. This was the payoff when a large North American heavy equipment leasing company suspected it was not getting the advantage it should have enjoyed given its size and purchasing muscle. Its 20-year partnership with a heavy equipment supplier was still its most important, but in recent years the relationship had deteriorated. The company had not compared its supplier's terms with those of its competitors, but any review of the equipment acquisition strategy would have to do more than reveal a gap—it would have to anticipate the supplier's market moves and do so with absolute confidentiality to preserve the company's advantageous position.

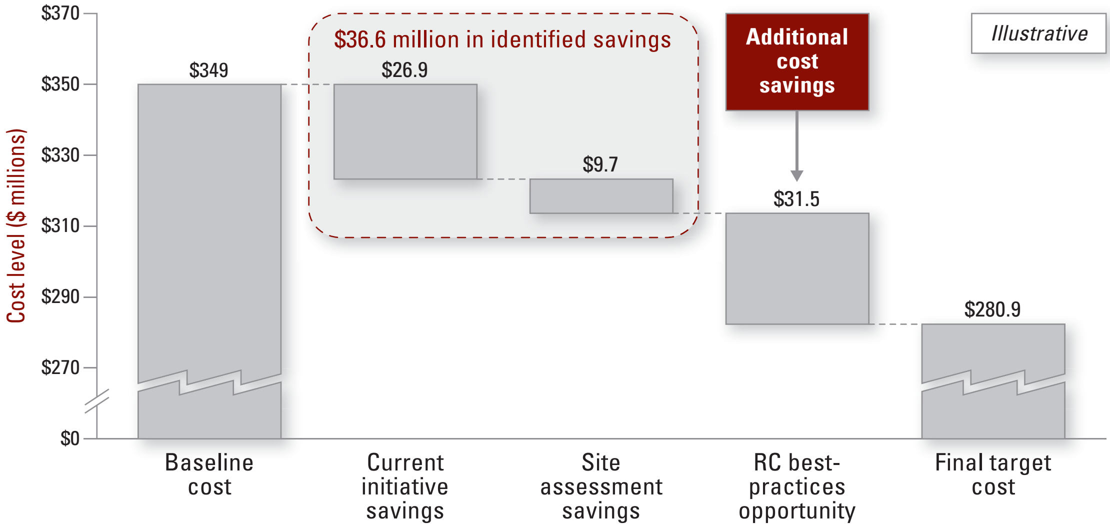
Countercyclical buying, or buying when prices and industry performance are low, stood out as a particularly valuable strategy in this industry. If our leasing company, from now on called LeaseCo, quantified the value the supplier put on capacity utilization, it could negotiate a better price. From the ruthless competitor analysis, we learned that LeaseCo was paying a 15 percent premium over the rock-bottom price the supplier would likely take rather than risk idle capacity. A scenario analysis then played out potential reactions to LeaseCo's improved position. In essence, the analysis was a chess match to test strategies three and four moves deep before making them in the marketplace.

Then the real contest began. During negotiations, LeaseCo showed off its newfound understanding of the supplier's costs and operating alternatives, and its own opportunities to acquire lower-priced products from other sources. Then LeaseCo took action. It moved a portion of its equipment spend to an alternate supplier. Stuck with excess product, the supplier's next move was to enter the leasing market itself. This move, which had been anticipated by the ruthless competitor analysis, was countered by two factors: Lease prices fell as excess units entered the market, and the supplier quickly realized that its scale would relegate it to a price-taker position. Eventually the supplier acquiesced and gave LeaseCo a 10 to 12 percent price cut.

Today LeaseCo enjoys a more balanced position with better knowledge and transparency, while the supplier maintains this important account without upsetting its market position.

FIGURE 3

Total-cost analysis reveals RC advantage



Source: A.T. Kearney

to market and sell its rugged timepieces via the Internet, the Pittsburgh company was capitalizing on a distribution channel that few luxury goods companies had tried. Overnight, Kobold became an RC, taking on the likes of Rolex, Omega and Breitling.

Perform a total-cost analysis. A total-cost analysis is used to translate the RC's competitive advantages into a hypothetical total-product or service-cost analysis. The analysis reveals the RC's "should cost" compared to the actual costs. For example, an RC's low-cost country design operations might reduce product overhead by 20 percent or more. This approach often illustrates the huge cost advantages to be enjoyed by either the RC or you—if you take action. Figure 3 shows what happened when a global electronics component supplier used a total-cost analysis to identify potential threats by an RC with a more efficient supply chain. The analysis was based on detailed plant-by-plant assumptions, which were validated against known cost structures both inside and outside the company. We found that by employing RC best practices, in addition to identified savings, the company could cut costs by 20 percent or more.

Outline potential scenarios. By outlining potential scenarios a company can find out what the RC might do to maximize its competitive advantage and threaten that company's strategic position. Will the RC reposition its strategy? Enter new markets? Launch new products? Move into new services? Be prepared, however, for these what-if scenarios will likely generate some internal angst and introspection, which leads to a crucial fourth step in our analysis: determining your best strategic moves.

Determine strategic moves. To head off and outsmart an RC, companies should not be as focused on competing against the RC as in using the information to drive operational strategy and actions that allow them to become more competitive. The analysis will prompt a host of new questions: Are we focusing on the right things to remain competitive? What RC actions could we adopt? How should we prepare to compete over the medium to long term given our current strategy? What should we focus on first to remain competitive and create value? How can we prevent a ruthless competitor from destroying us and our industry?

Ruthless Competitor in the Crosshairs

To illustrate how a ruthless competitor analysis works, let's look at how it was used to assess the direct material costs for a copier manufacturer. Most companies in this industry are either in a margin squeeze between high costs and declining prices, or their products are being commoditized by companies in low-cost markets such as China.

Well aware of these challenges, this manufacturer, let's call it CopyCo, was looking beyond known competitors to identify potential outside threats. It found two: Huawei Technologies and its current contract manufacturer. A company such as Huawei, well-known for moving into new industries, could readily become an RC if it desired—or form the low-cost backbone for yet another competitor. A year earlier, Huawei had exposed its ruthless character while winning Vodafone's business to produce its mobile phone handsets. In 2006, Vodafone announced that it would introduce its latest branded consumer mobile phone, and that Huawei was its first choice to manufacture the handset.[4] Typical of the emerging Asian white-label manufacturers, Huawei could produce the new handset at a cost 30 percent lower than Vodafone could hope to receive from a larger equipment maker. From networking components to cell phones, Huawei was proving to be a flexible and formidable force.

Another potential threat was CopyCo's existing contract manufacturer. It could use the knowledge gained in the current partnership—product designs, engineering and manufacturing specifications—to become a ruthless competitor as well.

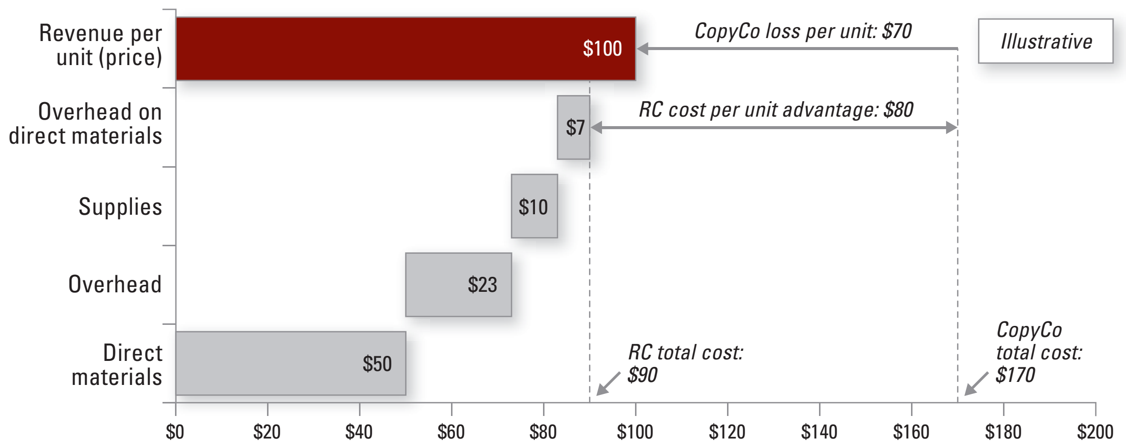
Alert to these threats, the ruthless competitor analysis identified a handful of potential foes in the market—expanding on CopyCo's list to include other white-label manufacturers—to find out specifically how they might optimally design their products, set up their value chains and manage total costs. This is where epiphanies often occur: It can be revealing for companies to see the break-even point at which they can manufacture a product and how an RC could make it for much less *(see figure 4 on page 22)*. CopyCo was already selling its smaller copiers at a loss to drive sales and encourage repeat purchases of ink cartridges. Thus, it didn't realize a profit until several replacement cartridges were sold. Meanwhile, its known competitors were closer to making money on the initial copier sale and were realizing additional profits on repeat cartridge sales. An RC would no doubt improve on these prospects even further. We did a little scenario-casting and found that an RC could harm CopyCo in the following ways:

- Enter and dominate the low-cost market segment. The RC could then partner with another competitor to move up the value chain and compete in the high-price/high-quality market segment. This would squeeze CopyCo out of both markets.
- Develop white-label products to sell to CopyCo's top customers. CopyCo would lose retail channels due to white-label competition.

[4] *Cassell Bryan-Low, "Vodafone to Unveil Self-Branded Mobile Phone,"* Wall Street Journal*, 27 September 2006.*

FIGURE 4

Average unit cost per copier: ruthless competitor versus CopyCo



Source: A.T. Kearney

Huawei's partnership with Vodafone is an example of such a strategy.

- Enter developing countries early, exploiting cost advantages and capturing market share. Meanwhile, CopyCo would be slow to enter and thus find it difficult to gain market share and ruin planned growth projections.
- Leverage low-cost country research and development or exploit lax intellectual property rights protection to leapfrog the manufacturer technologically, win on price and capture key market segments.

Alternatively, a separate cash-rich or debt-averse computer hardware company could acquire the low-cost RC to embolden its own capabilities.

Seeing how an RC could move against it was the trigger point CopyCo needed. And while Huawei was certainly a potential threat, the scenarios demonstrated that other, still unknown competitors could be just as dangerous to CopyCo's survival. After developing and prioritizing strategic plans, CopyCo is now deciding which plans it is most capable of implementing, and executives have begun to reevaluate their current contract manufacturer relationships.

Outfoxing the Ruthless Competitor

It is unlikely and unrealistic that any company will start with a clean sheet of paper in response to an RC. But when companies consider their situation in conjunction with a ruthless competitor analysis, they can prepare to defend against potential RCs. The following are three rules executives should bear in mind:

Don't get caught off guard. Scour your market and others for current and future threats. Recognize that RCs can come from anywhere and attack at any time. They could be a real and urgent threat. They could come from a different industry or segment. Or they could be holding back, waiting to enter the market given favorable conditions. This competitor can also be a "best of" amalgamation of current and hypothetical competitors. Engage your top managers in scenario-casting to identify your most likely RCs.

Be action-oriented. To combat a ruthless competitor, a company must be action-oriented and dissatisfied with the status quo. American automakers are continuing to lose ground to Toyota because they failed not only to see the threat soon enough but also to deploy their relevant sources of competitive advantage. They could have met the challenge when it was a potential threat rather than an actual one. Hyundai, for example, took a clean-sheet approach to the automotive value chain and came up with the car company of the future—one that avoids high fixed costs, captures the full lifetime value of a car through leasing rather than selling, outsources operations, and offers low-cost modular designs. All of these principles could be adapted one way or another by most car companies. In fact, strong quality performance is enabling Hyundai's move upstream from producing low-cost to more high-end cars.

Become a ruthless competitor yourself. Never underestimate your ability to outsmart an RC. Take, for example, the experience of a large player in the retail gas industry. With numerous small RCs pecking away at its market share, the company employed not a martial arts technique but rather a sumo wrestler's approach, by using its size and investment abilities to become an RC as well. After analyzing how an RC could use emerging technologies to reduce operating costs significantly and optimize pricing, the company invested heavily in technology to transform its field-service operations. These efforts improved deliveries, reduced fixed costs, optimized asset allocation, enabled improved matching of supply and demand, and strengthened customer service—leading to nearly 300 new customers within nine months. The investment furthermore had a very short payback period. And most importantly, the move fundamentally altered the industry's landscape and performance expectations by creating significant barriers to entry—making this retail gas company more capable than its former competitors were ruthless.[5]

The Huaweis of the world are everywhere. Once you clobber one, another will emerge in its shadows. While no industry is impervious to such competitors, the winner every time will be the company that is most prepared for the match, is the most nimble, and is willing and able to *outruthless* the ruthless competitor.

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[5] *See "Transforming Field-Service Operations: Running Faster, Longer, Smarter in Customer-Delivery Services" at www.atkearney.com.*