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LETTER FROM THE EDITOR

Welcome to the *Journal of the International Academy for Case Studies.* The International Academy for Case Studies is an affiliate of the Allied Academies, Inc., a non profit association of scholars whose purpose is to encourage and support the advancement and exchange of knowledge, understanding and teaching throughout the world. The purpose of the IACS is to encourage the development and use of cases and the case method of teaching throughout higher education. The *JIACS* is a principal vehicle for achieving the objectives of both organizations. The editorial mission of this journal is to publish cases in a wide variety of disciplines which are of educational, pedagogic, and practical value to educators.

The cases contained in this volume have been double blind refereed, and each was required to have a complete teaching note before consideration. The acceptance rate for manuscripts in this issue, 25%, conforms to our editorial policies.

If any reader is interested in obtaining a case, an instructor's note, permission to publish, or any other information about a case, the reader must correspond directly with the author(s) of the case.

The Academy intends to foster a supportive, mentoring effort on the part of the referees which will result in encouraging and supporting writers. We welcome different viewpoints because in differences we find learning; in differences we develop understanding; in differences we gain knowledge and in differences we develop the discipline into a more comprehensive, less esoteric, and dynamic metier.

The Editorial Policy, background and history of the organization, and calls for conferences are published on our web site. In addition, we keep the web site updated with the latest activities of the organization. Please visit our site and know that we welcome hearing from you at any time.

JoAnn Carland
Western Carolina University

MERRIMACK VALLEY CHAMBER OF COMMERCE: "THE BIGGEST AND THE BEST"

Gina Vega, Merrimack College

CASE DESCRIPTION

The primary subject matter of this case concerns regional economic development. Secondary issues examined include the role of the Chamber of Commerce and the integration of business and social concerns. The case has a difficulty level of two, appropriate for sophomore level courses. The case is designed to be taught in 2 - 4 class hours and is expected to require 2-4 hours of outside preparation by students, depending on the related projects selected.

CASE SYNOPSIS

The Merrimack Valley Chamber of Commerce was the fifth largest Chamber of Commerce in New England in 2001. The Merrimack Valley region was being confronted with a series of challenges to the continued economic growth of the region, including sky-rocketing housing prices, a shortage of skilled labor, and the continued influx of high tech companies with complicated infrastructure demands. The cyclical nature of the regional economic development, highlighted from the Industrial Revolution to the high tech evolution, presents a context for understanding the "big picture" problems and macro issues that exist within the business community, as well as the immediate and pressing problems that the Chamber of Commerce had to face. The reader is introduced to the problems through the eyes of the President of the Chamber.

INTRODUCTION

Leaning against the professor's desk, Joe Bevilacqua, President of the Chamber of Commerce, said, "I hope I look casual, but I'm really excited to be here and to talk to you about the important roles the Merrimack Valley Chamber of Commerce plays in the economic development of our local community. You know, our Chamber is the fifth largest in New England (Lawler & McFadden, 1999). We believe that it is also the best and most effective Chamber of Commerce in the region. Chambers are a great way for companies to find other companies to buy from…it's essentially a B2B (Business to Business) network"

In this case, the companies were in communities that followed the winding route of the Merrimack River from its source in the White Mountains of New Hampshire southward nearly to

Boston, and from Lowell eastward to the sea. The central core consisted of the Massachusetts communities of Andover, North Andover, Lawrence, Methuen, and Haverhill (see Exhibits A, B, and C).

The students in the senior seminar in family firm management at Merrimack College listened closely as Joe described the challenges faced by the Merrimack Valley communities at the beginning of the 21st century. "We have a plateful of pressing problems that can affect the growth of our area, including job creation, education, housing prices, and population growth. One urgent challenge is the development of a skilled workforce that can meet the needs of our growing back office, service, and high tech employers," Joe said, commenting on the businesses that flocked to the region in the late 1990s, as the dot com economy bloomed.

Six months later, the same Joe "I can find anything I need" Bevilacqua dug himself out of his nest in an avalanche of papers in a back room of an upstairs office on Essex Street, in the heart of Lawrence, MA to attend the public forum held by the Education and Workforce Development Committee of the Chamber. The theme of this meeting was "How do school districts add value to the learning readiness of their students - your future employees. How prepared will they be?" The Commissioner of the Massachusetts Board of Education, Dr. David Driscoll, was a special guest at this forum, moderated by Richard Santagati, President of Merrimack College, a local four-year college. Dr. Driscoll emphasized that, "With unemployment at only 3.9 percent, the #1 priority in the area is workforce development." The committee's goal was to guarantee that every business in the region could find appropriate workers.

Massachusetts had recently introduced the MCAS (Massachusetts Comprehensive Assessment System), an exam geared to raising the standards necessary to obtain a high school diploma in the Commonwealth. MCAS was a controversial exam, with many students failing across communities, counties, and regions. Questions about the make-up, the scoring, and the meaning of the scores for students and for entire community reputations galvanized local organizations statewide.

The bad news for the Merrimack Valley was that Lawrence placed "dead last" in the Commonwealth in preliminary MCAS scores in 1999 and 2000, with Haverhill and Methuen not far ahead. The good news was that there was nowhere to go but up (see Exhibit D).

HISTORY OF THE MERRIMACK VALLEY CHAMBER OF COMMERCE

Three major cities were thriving in the Merrimack Valley in the nineteenth century. The triangle created by Lowell, Lawrence, and Haverhill was a major manufacturing center, with many mills and factories devoted to the production of cloth, shoes, and ships. As early as 1833, Lowell had become the largest of the three and the chief manufacturing city for the United States, with 22 mills in operation (Molloy, 1976). These three cities, along with myriad other towns, counted the Merrimack River as primary transportation and shipping route, providing access to the port at

Newburyport as well as to railroad transportation hubs along the way, towards Boston. The sounds of steamship and railroad whistles echoed along the Merrimack Valley, advertising industry, hard work, and a series of communities bustling with lively commercial activity. (See Exhibit E)

By the 1880s, the cotton industry began the move south to seek cheaper labor and lower costs of operation. Expensive power machinery such as looms and spindles replaced manual workers and, within 50 years, 95 percent of the cotton industry had abandoned the Merrimack Valley (Packer, 1994). At the same time, the shoe industry began its decline and Haverhill felt the impact. Although the work force was willing, the businesses lost their struggle against changing times. The disintegration of the mill economy slowly continued as the 20th century entered, bringing with it innovations that would change the world. Two world wars shifted the focus of the remaining mills and factories away from consumer goods and toward defense-related products.

The end of World War II in 1945 did not bring with it the hoped-for return to prosperity of the region, and the area slipped further into decline. As manufacturing and industrial activity diminished in the Merrimack Valley in the last half of the twentieth century, so did the effectiveness and significance of the local Chambers of Commerce. Membership was decreasing in each small Chamber, and their ability to influence government, attract new businesses, and generate local pride was also failing. The Merrimack Valley's economy was deteriorating, plagued by inflation, loss of its manufacturing base to offshore locations, and increasing poverty in its oldest cities which, in an earlier time, had stood as beacons of prosperity in New England. The middle class population base faltered, leaving the poor in the cities and the wealthy in the smaller towns to live in uneasy proximity.

COMPUTERS TURNED THE TIDE

The situation changed markedly beginning in the early 1980s. In 1981, IBM introduced personal computers to the general market. The Merrimack Valley embraced the new technology and, within five years, one out of every four new jobs in the region was involved in equipment manufacturing and development (Edelman, 1991). Wang Laboratories, one of the largest of the high tech companies that were manufacturing mini-computers, had locations in Lowell, Andover, and Methuen. Wang reached its peak of success in 1983, with annual profits topping $200 million (Stein, 1989).

But the boom did not last. The focus on PCs came as a surprise to the mini-computer companies, and they resisted adopting the newer product. A movement developed away from large, manufacturing companies and toward smaller, more agile software development companies that could piggyback on the PC industry. In 1990, Massachusetts lost over 55,000 jobs (Metz, 2000b), and the following year Digital Equipment Corporation laid off 3500 workers from its 29,900 Massachusetts workforce. Raytheon fired 500 people that same year. The unemployment rate in Massachusetts reached 8.9 percent in 1991 (Blanton, 1992), with the greater Boston area having lost

75,900 jobs compared to New York City's loss of only 15,000 jobs (June 15, 1991). The following year, Wang Laboratories filed for bankruptcy and slashed half their workforce. Fifteen hundred more jobs were lost in the Merrimack Valley. Wang sold their $6 million plant at the bargain basement price of $525,000 (Souza, 2000). The region staggered with these economic blows (see Exhibit F).

But the 1990s brought an unexpected development to the region surrounding the Route 128 ring. Due to its connection with the development of technologies, small high tech software development companies began to cluster in the area, finding mutual benefits in proximity and creating a northeastern version of Silicon Valley in the Merrimack Valley. As the companies grew, towns began to thrive. New firms opened and took root, commerce increased, the local economy grew faster than anyone could have guessed, and people moved back in great numbers, creating a mini housing boom and sky-rocketing real estate prices (see Exhibit G). The towns were all facing similar challenges as a result of the sudden swing of the economic pendulum, and their Chambers of Commerce were running competitive programs aimed at the same market of businesses.

At the same time, Joseph Bevilacqua, then city planner from Haverhill, became involved in a movement to consolidate the small Chambers of Commerce into one large, influential Chamber. "I told everyone - forget the past. We were moving forward," Joe proclaimed. Diffident about his appointment as head of the new Chamber, he recalled, "After I was hired, I was told they expected I would probably stay for one year and then the real chamber director would be hired." But, between 1992 and 2000, the Merrimack Valley Chamber of Commerce increased its membership from 400 to over 1,100 members (April 23, 2000), establishing its reputation as "the biggest and the best" in the region and securing Bevilacqua's renown in Massachusetts. He was named President of the Association of Chamber of Commerce Executives for Massachusetts. He was appointed to the Massachusetts Office of Travel and Tourism Steering Committee, and the director of that Office called upon his skills to help design a new strategic plan to market travel and tourism in the Commonwealth.

THE STATE OF THE ECONOMY - 2000

The economic pendulum had swung once more for the Merrimack Valley, this time due to three related industries: telecommunications, biotechnology, and Internet/e-business. Lucent Technologies, spun off from AT&T in 1995 as a result of the largest corporate breakup in U.S. history to that point (Metz, 2000b) ran its largest manufacturing facility in North Andover. As the largest employer in the Merrimack Valley, Lucent had 5600 people on its payroll. Other giants in high tech industries employed between 1,000 and 5,000 people each in the area, making the Merrimack Valley dependent upon the continued success of industry leaders like CMGI, founded in 1994 and Agilent Technologies, spun off from Hewlett Packard in 1999.

Some mills continued to operate, the most famous of which was Malden Mills in Lawrence. Malden Mills made headlines in 1997 when the factory went up in flames several weeks before Christmas. Aaron Feuerstein, the owner of Malden Mills, vowed to rebuild and kept his employees on the payroll even during the period when the mill was completely closed for repairs. Acclaimed for this ethical and unusual conduct, Mr. Feuerstein put Lawrence back into the public eye and generated considerable interest in the potential renewal of the depressed area. Without the help of the Chamber of Commerce, it is questionable that the rebuilding effort would have been successful. Joe's pride in the Chamber was evident in his story about the fire: "When the fire happened at Malden Mills, our Chamber did something chambers never do. We raised a third of a million dollars in cash, which we donated to Malden Mills' relief fund" to assist the employees who were affected by the fire, and worked with the City of Methuen to expedite the necessary permits required for rebuilding. In addition, the Chamber participated in the movement to secure job retraining grant funds to assist the returning employees with language and skills training, resulting in the most modern textile factory in the world, in the heart of the lowest income area of the Merrimack Valley.

And another industry found its way to the region in the 1990s. Financial services such as Putnam Investments found a home in the leafy glens and rolling hills of newly developed industrial parks. As part of their assistance in the establishment of a major facility in this area, the Chamber of Commerce conducted orientation sessions in Boston to acquaint Putnam employees with the products, services, and housing available in the Valley. Putnam's move encouraged other companies. For example, in nearby southern New Hampshire, Fidelity Investments opened a large installation. The financial services industry was experiencing tremendous growth, matching the booming national and regional economy. They needed a seemingly limitless supply of educated workers for their service jobs, data entry, and round-the-clock customer account maintenance. These workers were readily available, at least in the beginning of the boom, in the Merrimack Valley.

But the bigger success story was not about mills or financial services, but about the proliferation of high tech companies. CMGI, Agilent, Picturetel, and Lucent attracted hundreds of smaller firms and incubated start up companies in secondary industries and support arenas. These smaller firms accounted for much of the growth in the region, and they in turn attracted additional powerhouses, such as Cisco Systems, Inc. to the locale. The Merrimack Valley Chamber E-BIT program (Electronic Business Information Technology), supported legislation to assist high tech manufacturers to stay and operate in the Valley and to receive tax relief as an enticement. The nature of the economic environment and the nature of the work had changed. (See Exhibit H).

THE ROLE OF THE CHAMBER

With all this growth, the Merrimack Valley Chamber of Commerce faced great opportunities. They were in a position to do some real good for the region if they could leverage the businesses' economic vigor with political influence and legislative clout. This came in the form of acknowledgement from President Clinton, Congressman Martin Meehan, Governor Paul Celucci and others who recognized Joe Bevilacqua's work for the Chamber and the region. SCORE, the Service Corps of Retired Executives, sponsored by the U.S. Small Business Administration, awarded special recognition of Bevilacqua's "important public service rendered unselfishly and providing exemplary service to the small-business community" (April 23, 2000).

The Chamber moved forward on all fronts. The Human Resources Association began to conduct monthly meetings on topics relevant to the professional development of the membership, including such things as the improvement of organizing skills and the correct handling of sexual harassment issues. (See Exhibit I). The many small and mid-sized companies that couldn't afford to maintain their own extensive human resource departments benefited from the guidance on key issues and policies afforded by these training sessions.

The minority business development committee created two affiliate memberships - one with the Latin American Merchants Association in Lawrence and another with the Latino Resources Network, in Haverhill. As Bevilacqua said, "We recognize that Hispanic business represents a great opportunity for economic development in the entire Merrimack Valley. The Chamber had always been interested, there's no doubt about that." As a result, materials were translated into Spanish to encourage additional membership and participation from companies in these heavily Hispanic areas (see Exhibit J). The economic development committee coordinated free business counseling in English and in Spanish at its Essex Street headquarters, making such advice both convenient and accessible to the population that needed it, and partnered with the nation's first U.S. Small Business Administration's Bilingual Small Business Center in Lawrence. This committee also worked with companies considering relocation to the area, helping them to find new or renewable sites and opportunities for creative financing of both new and established ventures. Increasing numbers of women- and minority-owned small businesses point to the Chamber's success in this arena.

The Education/Workforce Development Committee sponsored regular forums with state and private educational leaders in order to bring together the educational community with the business community. Their goal was both to improve student achievement and to develop the skills of current workers to meet the needs of their employers and their own personal development. Representatives of all institutions of higher education in the Valley served on this committee, including the Presidents of Merrimack College, Northern Essex Community College, Bradford College, and Umass-Lowell, among others. Bevilacqua supported all proposals because, in his words, "I believe education is the only chance kids have. They have only one shot; the competition for jobs is international."

The community service corps sought out local service opportunities and developed volunteer programs to fill them. This committee received national acclaim for its accomplishments at the 2000 conference of the Corporation for National Service, held in Baltimore. Its Retired Senior Volunteer Program, the Foster Grant Program, and the VISTA programs have become national models for business volunteerism. Some of their accomplishments included the implementation of the only VISTA summer reading program in Massachusetts, the placement of 400 senior citizens weekly in nonprofit worksites in Andover, North Andover, Lawrence, Methuen, Haverhill, and Amesbury, and the development of education/literacy programs in Lawrence and Haverhill.

And the membership committee went into overdrive, holding networking events and marketing mixers and business-to-business expos and job fairs, telethons and other functions to capture the attention and support of the growing business community. As of 2000, the Chamber had more than 1,000 members from its starting membership of 400 in 1992.

PRESSING NEEDS

The three most critical of the many local concerns were intimately connected. Bevilacqua bemoaned the fact that as more and more high tech companies found a comfortable, less costly home north of Boston in the Merrimack Valley, these same employers were discovering an unexpected shortage of skilled personnel for the many jobs they created.

According to Peter Vanier, executive director of the Lower Merrimack Valley Regional Employment Board, wages and salaries in Merrimack Valley increased through the fourth quarter of 1998 because "We're drawing [employers] out of metro Boston" (Mehegan, 1990) The area had become known as a "mecca for computer, high-tech, and electronics companies" (Metz, 2000a) and demand for programmers, database administrators, systems analysts, computer engineers, and computer support staff grew disproportionately quickly. Mean salaries for computer programmers in 1998 in this region had grown to $54,642, for computer support personnel to $47,362, and for database administrators to $46, 301 compared with salaries in the human service sector, which were averaging in the mid $30k's and in management support positions, which averaged at around $40,000 (See Exhibit K). These salary increases created a drain on the local pool of qualified workers and generated serious concern within the fast-growing technology sector. Some economic development specialists were concerned that a potential labor shortage would create inflationary wage spirals and would put at risk the continued expansion of the region (Metz, 2000a). The shortage of high tech workers in the Merrimack Valley was not unique to that area, however. All regions of the United States that focused on technology-based employment were experiencing this problem. The higher unemployment rate in Lawrence (about 5% while the rest of the area is below 3%) was one of the "benefits" city officials cited to companies interested in the area. Because most towns had low unemployment, an employer might have been discouraged from moving to the Merrimack Valley, but in Lawrence there was strength in unemployment (Corso, 2000).

One way to address the problem of a limited workforce had to do with educational opportunities. Local institutions of higher education struggled to keep up with the demand for specialized courses of study, and certificate programs appeared with regularity. Northern Essex Community College contracted with mega-employer Lucent Technologies to provide on-site technical training so that current workers could be redeployed to new positions within the company (Metz, 2000a). M/A-COM, a large LAN hardware and software manufacturer, contracted with Middlesex Community College to provide semiconductor training to employees who would be able, upon completion, to work as microwave technicians or in other semi-conductor related technical positions. Throughout the region, colleges and universities held job fairs, career fairs, and training open houses to attract potential students and job seekers.

But not all jobs that were going begging required a technical work force. Another area of significant growth in the local economy was in the health-care service sector. As the regional population aged, the so-called Sandwich Generation, unable to stop working because dual salaries were needed both to support young families and aging parents, sought housing and assistance for elderly relatives. Assisted living communities and retirement centers sprang up in the region. These living arrangements called for many service workers in traditionally low-paid jobs such as cleaners, food servers, and maintenance workers as well as more highly trained home health care aides and medical technicians. There were not enough people available to fill the many open positions, and consequently, there were serious service problems in many locations. Home health care workers, the fifth fastest growing field in the United States according to the Bureau of Labor Statistics (US Bureau of Census), were particularly unavailable and many jobs went unfilled.

The area experienced a housing boom along with the increases in economic activity and immigration. Employment in construction jumped along with the building boom: by 2000, more than 8,000 people were employed in construction, a 25-fold increase in only five years (April, 2000). The heavy demand for housing in the region forced prices up dramatically in the high rent districts of Andover and Newburyport, and similarly soaring prices appeared in communities throughout the Merrimack Valley, from Lowell to Haverhill. The most affordable housing in the region was in Lawrence, Massachusetts' poorest city (Staruk, 2000) and home to the Chamber of Commerce. The Mayor of Haverhill requested limits on new housing starts in that city to "give the city 'a six-month breather' as it evaluated development in the wake of the housing boom" (October 20, 1999). However, "Every place they can build, they're doing it," in Newburyport according to the building inspector (Pearson, 1999), and a wide variety of housing stock was available for purchase in Lawrence's communities.

THE CURRENT SITUATION

The MCAS was focusing people's attention on the local high schools and ways they could be improved. The situations in Lawrence and in Haverhill were particularly problematic. Lawrence was searching for its second school superintendent in two years, and Haverhill its third school superintendent in four years. Haverhill High School had been put on probation in 1998 by NEASC (New England Association of Schools and Colleges) due to problems with its curriculum, school atmosphere, and condition of its building (Palma, 2000). Lawrence High School had been taken over by Commonwealth regulators and was struggling to attain standards high enough to be returned to local control.

Suggestions for solving the many problems faced by the local schools included an offer by a Boston millionaire, philanthropist Pete Peters, to sponsor a Commonwealth charter, hire a management team, and create a business plan to get several schools in the Merrimack Valley up to speed (August 25, 2000). Other suggestions were to partner companies with schools to donate computers and other materials, raise teacher salaries, embark on an advertising campaign to promote the area to young teachers as a good place to live and work, encourage local employees to mentor students, engage college students in tutoring and Big Brother/Sister programs, and establish collaborative programs sponsored by businesses and the neighboring college communities (see Exhibit D).

The Education and Workforce Development Committee of the Chamber of Commerce had been debating as to which solution to support through lobbying and direct action for several months. Much heated discussion had taken place about each of these suggestions, but no determination had yet been made. The Committee had scheduled another meeting for the following Tuesday morning at 7:00 a.m. to have another discussion about the direction they should take.

AN AWESOME RESPONSIBILITY

Joe Bevilacqua gazed out the window of the Chamber of Commerce, watching the traffic on Essex Street and contemplating his work. The magnitude of the challenges facing the Merrimack Valley, none of which had an easy solution, and the promise of the opportunities facing the same region dueled for primacy in his thoughts. Some of the questions that repeatedly were raised from members at the 7:00 a.m. breakfast meetings ran through his head:

"Should we concentrate on attracting more business here," he wondered? "If we do, who will work in the jobs created by new business? Should we encourage more housing construction? If we do, whom should it be geared to? What can the Chamber do to attract more qualified workers to the area? Can the local colleges provide the training and education that is needed for these workers? Should we focus on retraining, on new skills development, on English as a Second Language programming, on computer literacy for underserved and potentially employable groups? How can the local schools improve education and prepare our future workers? And, if, as I believe it is, our biggest problem is the availability of a skilled workforce, what can the Chamber do to help?"

Joe's ringing phone interrupted his concentration and, after a brief introduction, the executive for a high tech company got right to the point: "We're willing to consider the Merrimack Valley for our new plant if you can guarantee enough trained workers."

Joe's thoughts flashed to the latest meeting of the Education and Workforce Development Committee. The commitments made to the public at the March meeting to guarantee an educated, appropriately trained workforce were about to be tested - could they meet this latest demand?

Clearly, there was no more time to waste in addressing the educational needs of the community. Joe had to take a stand, make a recommendation, and get the Committee moving.

"C'mon down to my office," Joe answered, putting a smile into his voice. "Let's talk."

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EXHIBIT A

Map of the greater northeast of North America and related information about the Merrimack Valley Chamber of Commerce.

http://www.merrimackvalleychamber.com/visitor/index.htm

EXHIBIT B

Map of the northeastern United States with arrow pointed at Lawrence, MA.

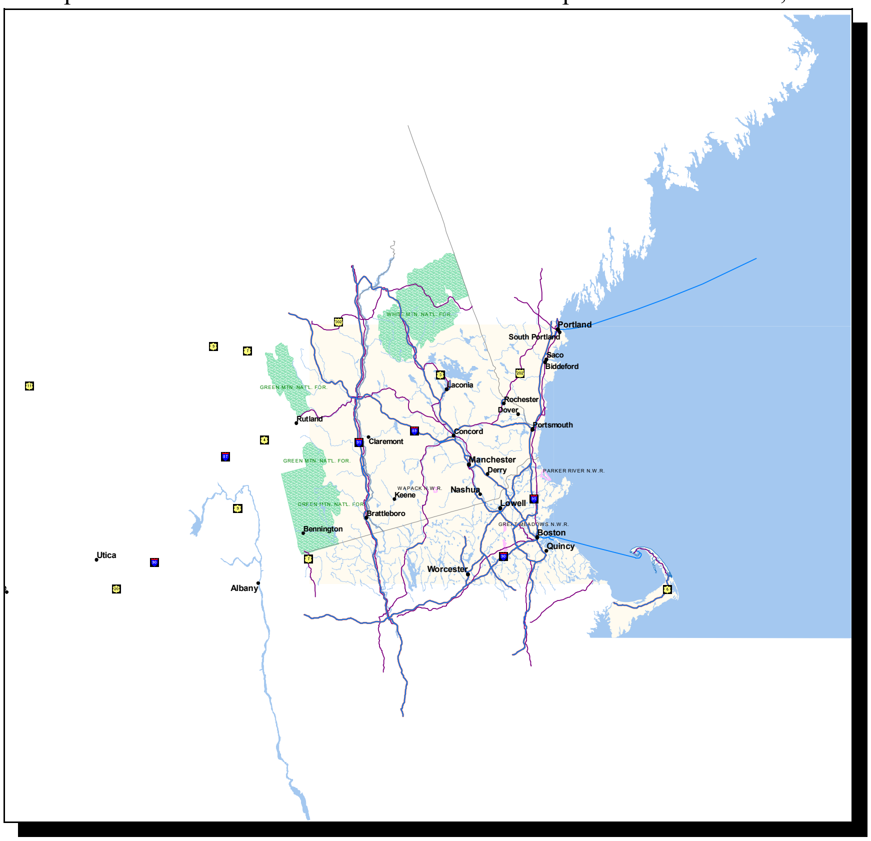

EXHIBIT C

Map of the area covered by the Merrimack Valley Chamber of Commerce with the focus on Lawrence, MA. Other maps can be accessed from this location by clicking on the town you are interested in.

http://www.mvpc.org/services_sec/GIS/Maps/lawrence.htm

EXHIBIT D

MCAS Rankings							
Area and Number of Students	MCAS Rank (2000)[1]	Drop-out Rate (1999)[2]	Atten-dance Rate (1999)[2]	Average Teacher Salary (1999)[2]	Per Pupil Expenditure (1999) regular ed[2]	Students Per Computer (2000)[2]	Computers on the Internet (%) (2000)[2]
Andover 5,808	13	0.7	96.3	$47,380	$5,284	5	99
Haverhill 8,592	109	3.9	94.1	$48,568	$4,869	9.6	57
Lawrence 12,562	126	19.2	92.9	$44,835	$5,386	4.1	15
Methuen 6,903	88	0.0	95.2	$43,748	$5,007	2.8	92
N. Andover 4,190	37	0.0	N/a	$45,823	$4,822	4.9	100
Statewide		**3.6**	**94.4**	**$45,149**	**$5,487**	**5.7**	**77**

1 www.boston.com/mcas/scores2000/globe_districts_rank00.htm
2 http://profiles.doc.mass.edu

EXHIBIT E

WORK IN THE MILL DURING THE EARLY NINETEENTH CENTURY

It was a scorching summer day. You had just entered the large red brick building and sweat already poured down your face as you climbed the stairs to your station. All day long thrashing noises assaulted your ears but, by now, you had learned how to block out the sounds that had once before made your ears ring. There were at least a hundred others just like you, doing the same job day in and day out for about $3.15 a week, $4.00 if you were one of the well paid ones. If you were one of the unlucky workers, $2.25 was all you earned for a week of exhausting labor. Yet, the loud noises, excessive heat, and long days weren't really what tore at your heart and soul. What really hurt was looking around and seeing the familiar faces, people you saw every day for hours at a time, and realizing that no one really knew you. You were here to find prosperity, but it ached more than you had imagined to lose the only people you'd ever known. The family and friends you once were so close to had been replaced by strangers in the mill. Just as your heart filled with the warmth that comes from thinking of those you love, your boss yelled to you, "Stop dreaming and get back to work!"

This description, created from accounts of that time, could have been the story of a young mill laborer in the 1830s. By 1855, nearly 28 percent of Lowell's population was comprised of children under the age of 15. This worker's father might have been a farmer or the worker herself might have been a young Irish immigrant (Mitchell, 1988).

EXHIBIT F

Employment in the Electronic Sector (by thousands) - Manufacturing and Service							
	1970	1975	1980	1985	1990	1995	2000
Manufacturing							
Computer and Office Equipment	0.139	0.139	0.201	0.315	0.179	0.145	0.122
Communications Equipment	2.335	3.419	0.757	6.009	2.819	2.83	3.017
Electronic Components and Accessories	2.277	2.343	0.726	5.828	2.848	2.873	2.528
Medical Equipment and Supplies	0.703	1.03	0.432	1.967	2.202	2.366	2.674
Service							
Computer and Data Processing	0.36	0.362	0.763	1.561	1.691	2.376	3.472
Totals	5.814	7.293	2.879	15.68	9.739	10.59	11.813
Source: Merrimack Valley Planning Commission, April 2000.							

EXHIBIT G

Residential Housing in the Merrimack Valley						
	1995 # OF SALES	1995 AVG. SALE PRICE	1997 # OF SALES	1997 AVG SALE PRICE	1999 # OF SALES	1999 AVG SALE PRICE
Amesbury	227	124,000	295	147,000	282	180,000
Andover	467	245,000	514	282,000	558	342,000
Boxford	191	244,000	206	322,500	203	385,000
Georgetown	162	169,000	192	175,000	149	222,500
Groveland	132	150,000	126	174,000	93	205,000
Haverhill	865	115,000	991	130,000	937	146,900
Lawrence	617	62,000	689	78,000	970	105,085
Merrimac	117	145,000	142	142,000	128	189,000
Methuen	638	117,000	639	125,000	795	149,900
Newbury	117	148,750	165	188,000	170	232,000
Newburyport	300	162,000	322	189,000	276	230,000
No. Andover	494	232,000	462	265,900	480	300,000
Rowley	89	166,500	103	190,000	146	267,000
Salisbury	107	105,000	186	120,000	178	151,579
West Newbury	71	218,000	72	275,000	68	322,000
Source: The Warren Group Compiled by the Merrimack Valley Planning Commission						

EXHIBIT H

WORK ON THE INTERNET AT THE END OF THE TWENTIETH CENTURY

It was a scorching summer day but you didn't even notice as the air conditioning blew a chill blast across your neck. Your mind was swirling with the complexities of trying to solve the software interface that had been thrown at your team. So far, you had had no success. Last night's pizza box still lay in your cubicle, and crumpled snack food bags littered the carpet at your feet. There were at least a dozen others working on the same problem as you, doing the same job day in and day out, for about $1500 a week, $2000 if you were one of the well paid ones, $1,000 if you were just starting out. String after string of code crowded the computer monitor, and your eyes were burning from so many late nights, so little sleep, so many demands on you. What really tore at your heart and soul was not seeing your baby son awake any time in the past week, as you worked longer and longer hours to try to meet the demands of the market. You were here to find prosperity, but you hadn't counted on its cost. You missed your family and all you wanted to do was go home. That was the thought in your mind when your boss came by to check on the team's progress. "I'm counting on you to keep going. I know you can do it," he said with a "thumbs-up" encouragement as he walked past your cubby.

This was your story if you were a programmer in 2000 at one of the software development companies. By that year, more than 5,000 people were engaged in some form of electronic employment in the Merrimack Valley, and there was no sign of slow down in the growth (April 2000). Job opportunities were everywhere, and employers had taken to luring workers from their competition in order to fill empty desks and handle the huge volume of work.

EXHIBIT I

List of Merrimack Valley Chamber of Commerce Committees and Typical Projects (2000)	
Government Affairs	
	U.S. Senators Luncheon
	Congressional Breakfast
	State Senators Breakfast
	State Representatives Breakfast
	Mayor's and Town Managers Breakfast
	Governor's Forum
	Monthly Business Legislative Caucus
Economic Development	
	Annual Business Expo
	Monthly Marketing Mixers
	Small Business Day Breakfast

List of Merrimack Valley Chamber of Commerce Committees and Typical Projects (2000)	
Minority Business Development	
	Small Business Counseling
	Assistance to Minorities and Women in Business
	Export Information Workshops for International Trade
Education Workforce Development and Human Resource Association	
	Women in Business
	Recruiting on the Internet
	Dealing with Difficult People
	The Use of Humor in the Workplace
	Education, Economic and Workforce Development Forum
Membership	
	"Members Only" Health Plans
	Discounts On Business Services Such As Telephones, Mailing Lists, and Certificates Of Origin
	Networking and Referrals
	Annual Golf Tournament
	Monthly Mailings and Updates
Source: Merrimack Valley Chamber of Commerce Membership Marketing Piece	

EXHIBIT J

Demographic Trends for the City of Lawrence								
	1970 CENSUS BY RACE	%	1980 CENSUS BY RACE	%	1990 CENSUS BY RACE	%	2000 CENSUS BY RACE	%
Total:	66,915		63,175		70,207		72,043	
White	65,930	98.5	54,787	86.7	45,624	64.9	35,044	48.6
Black	682	.01	1,362	.021	4,496	.064	3,516	.048
American Indian			130	.002	367	.005	583	.007
Asian or Pacific Islander			281	.004	1,358	.019	1,982	.027
Hispanic Origin			10,296	16.2	29,237	41.6	43,019	59.7
Other			6,615	10.4	18,362	26.1	26,418	36.6

Notes:

1. Numbers will not tally to 100% because of Census Bureau Collection Methods.
2. Hispanic Origin may be of any race.
3. "Other" signifies individuals who selected more than one category or who selected no category.
4. The 1970 Census did not classify race in the same way as the subsequent census. "White" included those people who self-classified as White and also those who did not classify themselves but indicated belonging to several ethnic groups or national origins, including Mexican and Puerto Rican. "Black" or "Negro" included those people who self-classified as "Black" and also those who did not classify themselves but indicated belonging to several ethnic groups or national origins, including Caribbean and Ethiopian.
5. The 1970 Census included too few American Indians or Asian and Pacific Islanders to count in Lawrence.

Source: U.S. Bureau of Census

EXHIBIT K

Wages in the Merrimack Valley - 1998		
OCCUPATION	ANNUAL	
	Mean	Median
MANAGERIAL AND ADMINISTRATIVE OCCUPATIONS		
Administrative Services Managers	$47,840	$43,701
Communications/Transportation & Utilities Operations Managers	57,824	62,629
Construction Managers	50,960	51,813
Financial Managers	55,890	49,254
General Managers & Top Executives	64,938	59,862
Marketing/Advertising/Public Relations Managers	64,251	59,051
Medicine & Health Services Managers	56,826	58,115
Personnel, Training & Labor Relations Managers	56,534	57,512
Purchasing Managers	56,950	59,363
PROFESSIONAL, PARAPROFESSIONAL, & TECHNICAL OCCUPATIONS		
Accountants & Auditors	$44,928	$40,976
Computer Engineers	66,768	71,802
Computer Programmers	54,642	53,456
Computer Support Specialists	47,362	43,347
Database Administrators	46,301	44,429
Human Services Workers	23,442	23,046
Licensed Practical Nurses	34,070	33,301
Mechanical Engineers	57,158	60,653
Occupational Therapists	37,274	38,584
Physical Therapists	49,941	46,197
Recreation Workers	17,430	15,142
Registered Nurses	45,115	44,678
CLERICAL AND ADMINISTRATIVE SUPPORT OCCUPATIONS	HOURLY	
Adjustment Clerks	$ 11.95	$ 11.19
Bill & Account Collectors	12.51	12.55
Billing, Cost & Rate Clerks	12.27	12.17
Billing, Posting, & Calculating Machine Operators	11.86	11.82
Bookkeeping, Accounting & Auditing Clerks	12.69	11.96

Wages in the Merrimack Valley - 1998		
OCCUPATION	ANNUAL	
	Mean	Median
Computer Operators, Except Peripheral Equipment	15.91	15.86
Customer Service Representatives, Utilities	14.28	13.19
Data Entry Keyers, Except Composing	11.09	10.73
File Clerks	9.70	9.64
First-Line Supervisors & Managers, Clerical & Administrative Support	16.98	15.65
General Office Clerks	10.34	10.06
Hotel Desk Clerks	8.22	8.18
Insurance Adjusters, Examiners & Investigators	18.27	17.67
Insurance Claims Clerks	10.39	10.21
Interviewing Clerks, Except Personnel & Social Welfare	10.26	9.94
Legal Secretaries	13.09	13.21
SERVICE OCCUPATIONS		
Child Care Workers	8.44	8.27
Combined Food Preparation & Service Workers	7.20	6.47
Cooks, Institution or Cafeteria	11.06	10.85
Food Preparation Workers	8.00	7.95
Home Health Aides	9.40	9.48
Janitors & Cleaners, Except Maids & Housekeeping Cleaners	9.54	9.00
Maids & Housekeeping Cleaners	7.90	7.69
Nursing Aides, Orderlies & Attendants	9.84	10.00
Last Updated on 2/29/00		
By Massachusetts Division of Employment & Training, Economic Research Dept.		

THE RETIREMENT DECISION

Michael D. Evans, Winthrop University

CASE DESCRIPTION

Time value of money is the primary subject matter of this case. Students are asked to apply time value of money techniques in a retirement planning scenario. Thus, they will be able to see a practical application of present and future value concepts. The case is appropriate for the first undergraduate course in financial management. It can also be used in a graduate survey course. The case is designed to be covered in one 50-minute class period and will likely require 2-3 hours of outside student preparation. Familiarity with a financial function calculator could significantly reduce students' preparation time.

CASE SYNOPSIS

Jim Abbott, an Executive Vice President of Bank USA, has just learned that his employer has entered into merger discussions with a large bank conglomerate. If the deal is consummated, Jim will be required to relocate and will likely have a change in his job responsibility and reporting relationship. Jim and his wife Mary have recently completed the construction of a multi-million dollar home on the lake. They are extremely active in the community so the prospects of relocating are unappealing. Accordingly, they've scheduled a meeting with Rick Johnson and Mike Davis of Wealth Management, Inc. to assess their finances and to determine if Jim is in position to retire one year from now if the merger is affected.

INTRODUCTION

Jim Abbott started his career with Bank USA in 1970 as a Management Trainee. He had a natural affinity for banking and quickly moved up through the ranks. He served as a Branch Manager for several years and achieved substantial annual increases in branch deposits, loans and profitability. Jim was labeled as an up-and-comer.

He was promoted to City Executive. In this position, Jim was responsible for all branch activity in Charlotte, NC. A few years later, he was promoted to Regional Executive where he managed all branches in the Piedmont Region of North Carolina. Jim possessed a unique combination of analytical and people skills. He moved through a series of management positions at Bank USA's headquarters. Ultimately, Jim was named Chief Risk Officer. In this position, he reported directly to the Chairman of Bank USA.

Jim's income increased substantially over the years. He now earns a base salary of $300,000 per year. In addition, he participates in two management incentive programs -- short-term and long-term. Each results in an annual bonus dependent on the attainment of corporate goals adopted by the Board of Directors. Bank USA has been very successful in meeting corporate goals. Accordingly, it has not been uncommon for Jim to receive annual bonuses totaling $3-400,000. Jim has the option to defer some or all of the bonuses. This is an annual election. In the early years, he deferred bonuses. More recently, he received bonuses in the current year in order to pay for the construction of his house. Jim has elected to defer $25,000 of the bonus to be received six months from now. The remainder will be used for construction related costs, home furnishings and new cars. His residence has a market value of $2.5 million. There is no mortgage balance.

Jim also participates in various stock option and employee stock purchase programs. He has acquired a substantial number of shares of Bank USA and has options to acquire additional shares. He participates in both qualified and nonqualified retirement plans. The qualified plans include a regular retirement plan and a company savings plan (401(k)). Bank USA makes 100% of the contribution to the regular retirement plan. Jim will receive a retirement benefit based on the accumulated account balance. The company will contribute $18,000 to Jim's account one year from now. Jim contributes 8% of his base salary to the company savings plan. The company matches the first 6% of his salary dollar for dollar. Contributions are made to the company savings plan at the end of each calendar quarter. These monies will be rolled to an IRA at retirement and will continue to enjoy tax-deferred compounding.

Bank USA has a non-qualified deferred compensation plan for its executives. Executives can elect to defer some or all of the their annual bonuses to this account. Interest is credited annually at a rate of prime +2%. Since this is a non-qualified plan, plan assets can be reached by creditors of Bank USA. The bank has taken steps to minimize exposure of plan assets to creditors. The bank also has a supplemented executive retirement plan (SERP). The bank makes 100% of the contribution to this plan. The bank will contribute $12,000 to the plan next year. $3,000 will be contributed quarterly beginning three months from now. Jim has participated for several years. Unfortunately, Jim cannot roll the assets of either the deferred compensation plan or the SERP to an IRA. Jim will make annual withdrawals from the deferred compensation plan after retirement. These amounts will be taxable in the year received. He will take a lump sum distribution from the SERP at retirement. Jim will be required to pay taxes at his marginal tax rate on the distribution. The bank will withhold income taxes. The balance will be invested along with other personal investments and will have an 8% expected rate of return.

Rick and Mike believe 8% is a realistic rate of return assumption given their twenty-year investment time horizon. They note that the historic rate of return for the stock market is approximately 11 %. Jim and Mary are not overly risk averse. Accordingly, a 70% allocation to stocks is planned for personal investments. This allocation may be reduced in later years. However, a more balanced allocation of 60% stocks and 40% bonds would also be expected to achieve the "conservative" 8% rate of return assumption over a period of years.

Mary has not worked outside of the home. She and Jim have raised three children. Each of the children has established their own household and has begun a career.

Over the years, the bank has acquired a number of other banks. It has transformed itself from a regional power to one of the largest financial institutions in the nation. Accordingly, the complexity of Jim's job has increased exponentially. Not only is Jim required to assess larger credit risks, he's also responsible for the detailed review of the loan portfolio of potential bank acquisitions. Bank USA also increased its international operations. Jim must travel extensively.

Jim has grown tired of the travel and the increase in job-related stress. He's beginning to think that this may be a good time to retire. He and Mary are in reasonably good health. They've accumulated personal and retirement assets. Why not retire and devote more time to their passion? Sailing!

Jim scheduled an appointment with Rick Jackson and Mike Davis of Wealth Management, Inc. The firm, established in 1983, specializes in providing comprehensive financial planning services to high income, high net worth individuals. Specifically, they market their services to corporate executives and small business owners. Rick and Mike are both CPAs and Certified Financial Planners. They are also experienced investment advisors.

Jim was a client of Rick and Mike at their former employer, a major CPA firm. When the two principals started their own firm, Jim took his business to their new company. Now he challenged Rick and Mike to assess his retirement prospects and review his investments. Rick and Mike will be paid a fee of $10,000 for their analysis and continued assistance during the upcoming year. This fee will be paid from the Abbotts' existing cash balance.

Rick and Mike explained to Jim that the following steps needed to be undertaken in order to assess Jim's ability to retire one year from now.

- Determine a retirement income need in today's dollars.
- Identify all relevant sources of retirement income.
- Compute the amount of required capital at retirement.
- Compute the amount of capital available at retirement.
- Compare capital required to capital available.
- Develop appropriate strategies in the event of a shortfall.

Jim was instructed to bring the most recent statement for all personal and retirement accounts. Rick and Mike learned the following.

Table 1: Investment Assets of Jim and Mary Abbott

Account	Balance
Regular Retirement Account	$692,300
Company Savings Plan	850,000
SERP	915,000
Deferred Compensation Plan	265,000*
Company Stock	375,000
Other Personal Assets	468,000

* $25,000 will be added to this account in six months.

After reviewing Jim and Mary's expenditures over the past year and anticipated lifestyle after retirement, a pre-tax retirement income goal of $300,000 in today's dollars was established. Jim and Mary are in reasonably good health. Their life expectancy is 21 years. Inflation is expected to average 3% over this period. Accordingly, their annual income goal will be $309,000 at retirement. This amount will increase by 3% annually thereafter.

The Social Security Administration has projected that Jim and Mary will receive a monthly social security benefit of $2,600 beginning on Jim's planned retirement date one year from now. This benefit will increase annually at the assumed inflation rate of 3%. The Abbotts are concerned after reading recent articles that suggest that the Social Security system may become insolvent during their retirement years. Accordingly, they've asked Rick and Mike to assess their ability to retire with and without the Social Security benefit.

Jim and Mary are in the 40% tax bracket. This is not expected to change after retirement. Jim is a knowledgeable investor and not overly risk averse.

Rick and Mike follow a top-down approach to fundamental analysis. They note that the economy has been weak the last few years. Consumer confidence is low and businesses have cut back on capital spending. The broad stock market averages have declined over 20% in each of the last two years despite a series of interest rate cuts by the Federal Reserve. The President and Congress are working on an economic stimulus package.

Rick and Mike believe the economy is near the bottom of the economic cycle. Accordingly, they are optimistic regarding the stock market over the intermediate and long term. Their analysis suggests that the stock market as a whole should generate an average annual return of 10% over the planning period. This is substantially below the unusually high returns of the 90s, but is in line with historical long-term performance.

After a careful review of the Abbotts' investments and target asset allocation, the following expected rates of return were estimated. It was decided that an 8% discount rate should be used for all present value calculations.

Table 2 - Expected Rates of Return (ROR)

Account	ROR (%)	Compounding
Regular Retirement Plan	6	Semi-annual
Company Savings Plan	8	Semi-annual
SERP	4	Quarterly
Deferred Compensation Plan	8	Monthly
Company Stock	6	Annual
Other Personal Investments	8	Annual
Cash (10% of total) Bonds (20% of total) Stocks (70% of total)		

Jim and Mary also inquired about borrowing against the equity in their home. They note that they have few itemized deductions and wonder if this is an effective tax strategy. They are considering borrowing $100,000 at 7% for 15 years.

Having gathered the appropriate data, it's time for Rick and Mike to roll up their sleeves. It's important that their analysis be complete and accurate. After all, the quality of the Abbotts' retirement years is now largely in their hands.

CHANGE MANAGEMENT-WALKER AND WALKER

Bonita Barger, Tennessee Technological University

CASE DESCRIPTION

Change Management-Walker and Walker (W & W) is designed to be used in a Human Resource Management and/or Organizational Behavior class at the senior undergraduate level or entry MBA level, and has a difficulty level of 4/5. The purpose of the case is three-fold:

- *to increase student awareness of the issues involved in managing organizational change;*
- *to raise issues relating to organizational design, culture, and interpersonal alliances in managing human capital;*
- *to provide comprehensive teaching notes and citations for educators to enhance discussion.*

CASE SYNOPSIS

This case provides a realistic scenario encountered by senior management in managing organizational change from the old to the new economy. Walker and Walker is a Southern family owned manufacturing firm struggling to expand into a global marketplace. The tensions involved in organizational change are played out in multiple arenas. The student is challenged to analyze these arenas. The instructor is provided with extensive supporting literature to facilitate this analysis.

CASE STUDY-WALKER AND WALKER

GROUNDING

Walker and Walker (W & W) is a North American leader in the manufacturing of rail ballbearings. W&W, founded in 1950, has grown from a small, family owned business in Macon, Georgia, to a billion dollar operation servicing external customers world-wide. They have grown and thrived on a central tent: Service to customers by building the best technically advanced product in the marketplace. This tradition has deep roots.

BACKGROUND

W & W believed in people. It was started by the "Walker Brothers," John and James Walker. It was built on the labor of family and community members from Macon, Georgia. Everyone knew each other, pitched in, and helped when needed. There was no need for a union, as the Walkers "took care of their own." There were commonalities that bound the employees together. They were related by blood, religion, and generations of growing up in the same neighborhoods. They shared similar values, beliefs, and ways of working. They were "family," with strong father figures providing direction, security, and a good place to work.

With a strong market demand for their products, a focused and dedicated labor force ready to follow the orders of their founders, John and James, grew W & W from 100 to 1,000 employees working in two manufacturing units located in southern Georgia. W & W had changed remarkably over what appeared to be a long history but was, in fact, quite a short period of time. W & W increased its workforce, doubled its manufacturing facilities, tripled its customer base and profits. Sales were $900,000 by 1980. W & W appeared to be well positioned to enter the year 2005.

The early 1980s were difficult for W & W. With the untimely death of James Walker, the recession, and new competitors entering the marketplace, John and the Board were faced with the possibility of laying off part of its workforce. In this small town where loyalty to employee and employer were the givens of life, this had never occurred. A difficult decision had to be made. John made it. W & W decided not to lay off employees, rather start a large-scale cost reduction effort and decrease corporate and executive salaries. This strategy worked. The recession ended, demand for products and services started to "turn around." Now John Walker and the Board realized that it could not be "business as usual."

The external environment had changed, while the internal work environment of W & W appeared to stay the same. Externally, new customers were demanding products quicker, global competitors were entering the marketplace, technology advances in the manufacturingof ballbearings were rapidly changing, and government guidelines on affirmative action and other policies were requiring new approaches to old practices. Internally, the workforce appeared to be the same. Business was the same as usual. The rules were known. The power bases were established. The resources and access to them were there. The pathway to promotion and success had been charted by seniority, loyalty, and protection. "Do your job. Keep your head down. Your time will come for the next step up the ladder," was the unspoken emotional contractual agreement between the predominately male labor force.

John Walker knew things had to change for this young company that was quickly "growing up" and maturing in the marketplace if it wanted to reach the year 2005. What had worked in the past would still work today, but not tomorrow. He was growing tired. Silently, he acknowledged that the company had outgrown him. If it was to survive, a transfusion of new blood, vision, and direction were needed.

John Walker consulted with the elders in the Walker family and a trusted business associate from the Bank of Georgia. He received their counsel and made the second toughest decision of his life to step down and pass on the management of W & W to the next generation of leadership. But he did not see that leadership among the current ranks. He and Jack Walker had focused on building the business. Succession planning was not part of that plan. In looking at the line of executives under his charge, they were very much “like him”—Southern white males from Macon, Georgia, who grew and grew up in the business. They were unable to take W & W where it needed to go.

W & W conducted an extensive search for a new CEO, using an executive search firm. It was costly, but worth the results. Roger Pulley, a young, energetic white male with international experience from New York, was hired. In spite of his youth, he had extensive education and experience in the industry. The board of directors, Walker family, and particularly John Walker were pleased with the selection. Even the vice presidents of W & W appeared to accept the new CEO. There seemed to be few reservations as to the choice made.

Roger’s entry into the organization was thoughtful, observant, and filled with insights. It was immediately apparent to all that Roger was an individual of vision and knowledge. What he lacked in relationship building skills, he made up for with an understanding of the future needs of the business.

After twelve months on the job, results of incremental changes in marketing and sales strategies were beginning to be seen in the bottom line. Employees’ initial “questioning observations” were beginning to form into “trust statements” as bonuses increased in their paychecks. Roger recognized that these incremental changes were not sufficient to move W & W to the next plateau. From his 12-month analysis of the organization, he realized that the company was dated in technology and manufacturing capability. The workforce was homogenous with similar work-related behaviors. There was a deep cultural aversion to change. The human resource staff performed administrative functions. They did not have the staff who could create, foster, and facilitate change. Overall, the information, financial, and logistic functions were composed of insufficient systems, processes, and procedures to take W & W to a two billion dollar company playing in a global arena. How could he bring about significant change within the cultural without rupturing the bottom line?

FOREGROUND

Roger chose a multilevel approach: (1) replacement of two positions on his staff created by retirement (VP of Human Resources and Marketing); and (2) a change management strategy involving the formation of a new vision for W & W.

A new VP of Human Resources, Richard Green, and Marketing, Sara Ferguson, were hired. They, in conjunction with Roger and his staff, created a change management strategy.

A change management strategy took on the following activities:

- Creation and communication of a vision and mission statement for the company;
- Acquisitions of new companies and the formation of international joint ventures;
- Creation of succession planning for mid-level management and above, hiring 25% of open positions from outside the company to staff the new ventures;
- Hiring of a Human Resource Development professional to staff the Human Resource function. (The person was to work with the CEO and his staff to create a succession planning process, in addition to work with the training staff to design and implement training models.);
- Creation of training programs for the entire workforce on multi-culturalism, globalization, diversity, and ethics;
- Extensive training programs on multiple topics and above average salary raises to position all employees at the 55%tile for the work they performed.

The strategy was put in place. Roger presented the mission statement to small groups throughout the company and welcomed dialogue. The acquisitions and joint venture agreements had been signed. Employees were being trained in the vision and mission of W & W. A cultural change module highlighting empowerment and diversity were presented to all levels within the company. New employees were hired and placed in various parts of the company. These people were hired from outside of the traditional business environment. They had experience with international private and public organizations. They brought fresh new ideas. By some, they were perceived as a threat to the "way things always have been done at W & W." By others, they were seen as the "new hope for the future."

CASE GROUNDING

The Human Resource Development Director, Jo Anna Sam was one of those new people excited about the opportunity to work in business as a "change agent." Not quite sure what the charter of "change agent" meant, she spent the first six months doing a Human Resource analysis. The findings were clear. Human Resource practices and policies were selectively being applied. Based on these findings, she created and presented a succession planning proposal to Roger and Richard. They accepted the concepts and implementation strategy. It was communicated to the management staff who were not as accepting.

Opportunities existed in the new joint ventures that required the technical expertise and knowledge of W & W Vice Presidents to "get the business off the ground." In addition, new perspectives were needed from outside the company at the management levels to foster the new direction. Senior and mid-level managers would not move and take on functional or cross-functional work outside of Macon, Georgia. An impasse had occurred. Critical positions were vacant, requiring company expertise. Management would not relocate. The succession plan was intended to create a process for movement and relocation. What was not considered was the fundamental belief that employment security was an entitlement and rooted in the culture.

A critical incident had occurred. Roger had asked several staff members to take on new roles. They silently or overtly resisted. The final straw came when Roger asked Jake Crandal, a senior management team member, to take on a new position in a newly formed joint venture in Norway.Jake refused, stating that he would not "move to that freezer where they did not speak English, and, by the way, this whole stuff around succession planning was not the way to run a small family business like W & W." Roger was shocked and not willing to accept insubordination from his staff. Roger and Jake shared little in common. They did not like each other. A business, as well as a personality, conflict existed. Roger recognized this and called in Richard (the new VP of HR) to facilitate a series of meetings with the purpose of reaching agreement about Jake's next move. It was agreed that Jake would stay in his current role for two years but would then move to Norway once the new plant was built.

Although Jake agreed to move, he never intended to move. He had stated to one of the senior management team that "I'll not move my family to that forsaken place. They don't even speak English there." "I would rather fight than switch." Initially, the implications of this were unclear, but within several weeks, the impact of this statement began to unfold.About a month later, reports were coming back through senior management that the training programs were violating the religious beliefs of certain employees. Some of the concepts and principles were perceived as "New Age." It was reported that segments of the workforce believed that W & W was possessed by evil forces, and the devil was at work. Prayer sessions were being conducted for W & W in local community churches.

Jo Anna, the Human Resource Development Director, was an outsider. She had created the cultural change model and succession planning process. She was different. She did not know or understand what was occurring during these management sessions.

She continued to do her work—training the cultural change model. As she boarded a plane for England to present the model to their European operations, she phoned the office. My supervisor said that, "Jake is stating that you are training New Age ideas and trying to brainwash the company." She was silent. Her head was spinning. Her heart was beating and she could hear it throughout the phone. She was shocked, confused, and scared. She said, "What?? What is New Age? What is going on here?" He said, "You have become a target." She responded, "A target? What does that mean?" The only thing she could envision was a cartoon from Gary Larsen of a moose with a bulls eye. The caption read: "It's difficult to be born with this on your back."

She boarded the plane in shock and confusion. What she could not see at that moment was the impasse that had occurred between Roger and Jake and the management team, nor could she see that a culture that had been supportive, protective, and nurturing was transforming, not into the vision of a globally diverse customer-focused organization of the future, rather into splintered groups possessing either primitive fears of centuries ago or visions of futures yet to be lived.

AMAZON.COM IN 2003

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CASE DESCRIPTION

The primary subject matter of this case concerns making an online retail business profitable. Secondary issues include (a) assessing the long-term attractiveness of pure online retail industry, (b) understanding and comparing strategy elements and competitive advantages in e-commerce with traditional firms, and (c) evaluating growth strategies. The purpose of this case is to provide students with enough information about Amazon's business situation, to be able to chart the course of action the company should take at a given point in time. The case has a senior or second year graduate level difficulty. The case is designed to be taught in three class hours and three hours of outside preparation by students.

CASE SYNOPSIS

Jeff Bezos opened his Amazon's virtual book store in 1995 in Seattle, Washington. Amazon's online store was a big hit, with about $5 million in the first year of operations. To expand on his success, Jeff introduced other products, including DVD, and electronics. In 2002, Amazon was the world largest online retailers. Unfortunately, the business had not yet made any profit. After four years of single-minded focus on growth, in year 2000, Amazon focused exclusively on increasing its efficiency. Beginning late 2001, Amazon shifted its focus on growth prospects again. Jeff believed that Amazon had reached a point where it could afford to balance growth and cost improvement. This balance began to pay off in the fourth quarter of 2002, where the company generated $198 million in free cash flow for the first time. After falling out of favor along with the Internet sector in 2000 and 2001, Amazon's stock staged a rebound in 2002 as investors bought back into the idea that Amazon would be around for a long time and would start generating real profits. However, it seemed that survivability was still an issue for those investing in Amazon due to massive negative operating cash flow, excessive debt, significant payments for its suppliers and bondholders, intense competition, and the slow economy.

As a low-margin retailer, the case opens with Jeff facing the dual challenge of trying to improve margins and service a large amount of debt. Numerous efforts by Jeff to advertise online and traditional media, lower prices, and free delivery had failed to attract more new customers. Jeff and some of his top level managers had different opinions on the solutions to their problems.

INTRODUCTION

Company History

After receiving his B.S. in Electronic Engineering and Computer Science from Princeton University in 1986, Jeffrey Bezos joined FITEL, a high-tech start-up company in New York. Two years later, he moved to the Bankers Trust Company and helped manage more than $250 billion in assets. He became the bank's youngest vice president in February 1990. From December 1990 to June 1994, Bezos helped build a hedge fund for D.E. Shaw & Co. In 1994, he was the youngest Senior Vice President in the history of D.E. Shaw & Co. During the summer of that year, one statistic about the Internet quickly caught his attention. The statistic revealed that Internet usage was growing at 2,300 percent a year. That was his wake-up call.

He quit his job and drew up a list of twenty possible products that could be sold on the Internet, and quickly narrowed the prospects to books and music. He thought both books and music had potential advantages for on-line sale. There were about 1.5 million English-language books in print and 3 million books in all languages worldwide. There were about 4,200 US book publishers and the two biggest bookstores, Barnes & Noble and Borders Group Inc. accounted for less than 12% of total market share, and each had only 175,000 titles. In contrast, the music industry had only six major record companies. They controlled the distribution of records and CDs and had the potential to lock out a new business, threatening the traditional record-store format.

Bezos initially chose books. In order to start his new venture, he left New York City to go to Seattle. Renting a house in Bellevue, a Seattle suburb, he started working out of his garage. He settled on Seattle, mainly because of its proximity to the Roseburg, Oregon, warehouse of Ingram, the giant book distributor. Bezos and four software designers set up shop in his garage to create the foundations of their company's Web site. He also raised several million dollars from some private investors. Bezos opened the virtual doors of Amazon.com in July 1995. Six weeks after opening, Jeff moved his new venture to a 2,000-square-foot warehouse in Seattle. Six months later, he moved once again to a 17,000-square-foot building in an industrial neighborhood in Seattle.

Business Strategy

Amazon's main goal was to be the earth's biggest online retail store, where anyone could buy anything and everything. To accomplish this goal, the company had developed three sales channels: online retail, marketplace, and third-party sellers. The principal competitive factors in Amazon's market segments included selection, price, availability, convenience, information, discovery, brand recognition, personalized services, accessibility, customer service, reliability, speed of delivery, ease of use and ability to adapt to changing conditions. For its services and third-party sellers channel, additional competitive factors included the quality of its services and tools, and speed of performance for its services.

The online retail channel offered a broad range of categories of new products to customers. These products included books, music, DVDs, videos, electronics, computers, camera and photo items, software, computer and video games, cell phones and services, tools and hardware, outdoor living items, kitchen and houseware products, and magazine subscriptions. Amazon purchased the products from vendors and held them in its distribution centers to fulfill orders. Historically, the company had focused its sales efforts towards the individual consumer. In 2001, in addition to focusing on the individual consumer, Amazon introduced a corporate and institutional buying program, which allowed businesses, libraries, schools, government institutions and other organizations to purchase products and services from its Web sites.

Marketplace channel consisted of Amazon Marketplace, Auctions, miscellaneous marketing and promotional agreements, and zShops. Amazon Marketplace permitted sellers to utilize their e-commerce seller services and tools to present their products on the company's Web site. In September 1999, Amazon added the zShops, where an unlimited number of independent shops could set up shop under the Amazon umbrella. Unlike retail, where Amazon sold and controlled the service to the customer, Amazon acted as an intermediary in zShops. It allowed individuals and businesses to offer popular as well as hard-to-find items. The biggest benefit for Amazon was steady cash flow without the costs associated with a warehouse of products. Each online store was charged a $9.99 monthly fee, and commissions of 1 percent to 5 percent. If any zShop chose Amazon to process its billing, the shop would pay an additional 4.75 percent of the total sale. It was believed that this arrangement would give Amazon valuable information for its database on consumer preferences and habits.

The third-party sellers channel allowed Amazon to provide other companies a set of e-commerce services and tools for the sale of their goods and services. Amazon had third-part arrangements with Toysrus.com, Target Corporation, Circuit City Stores, Borders Group, Expedia, Hotwire, National Leisure Group, Virgin Wines, and others. In 2001, Amazon begun marketing three services for third-party sellers that were designed to provide catalog retailers, physical store retailers and manufactures with cost-effective e-commerce solutions: (1) Merchant @amazon.com Program, where the third party seller offered its products for sale on Amazon's Web site, (2) Merchant Program, where the third-party seller's e-commerce Web site operated at its own URL using Amazon's features and technology, and (3) Syndicated Stores Program, where the third-party's e-commerce Web site used Amazon's e-commerce services and tools, and offered its product selection. These arrangements were complex and initially required substantial personnel and resource commitments by Amazon.

Operations

The company organized its operations into four principal segments: U.S. Books, Music, and DVD/Video; U.S. Electronics, Tools and Kitchen; Services; and International. Revenue from each sales channel was recorded in one of these operating segments.

U.S. Books, Music and DVD/Video segment included retail sales from amazon.com of books, music and DVD/Video products and magazine subscriptions. This segment also included commissions from sales of the products through Amazon Marketplace and product revenues from stores offering the products through its Syndicated Stores Program. This segment had net sales of $1.69 billion, $1.70 billion, and $1.3 billion in 2001, 2000, and 1999, respectively. Compared to the limited selection in an actual bookstore, Amazon could list a huge catalog of titles. The company's site also exploited the Net's potential to build a "community" around a product. For example, Amazon published customer reviews as well as outside reviewers. In addition, Amazon's software program had the ability to maintain records of customer preferences. Furthermore, with established distribution channels, Amazon could maintain a low inventory, ordering only the books customer requested. According to Morgan Stanley, Amazon's inventory turned over 42 times in 2002 versus only 2.1 times for Barnes & Noble. In 2001, Amazon added the "Look Inside the Book" feature, which allowed customers to view selected interior pages of thousands of books on its Web site. The company also launched its magazine store, where customers could subscribe to more than 600 magazine titles, and its e-document store, where customers could purchase and download electronic documents. In late 2002, Goldman Sachs' report on Internet retailing listed books third among 21 products ranked for their potential as online successes. Computer hardware was first, and software was second. But music, electronics, office products, cars, and specialty apparel also earned high scores.

U.S. Electronics, Tools and Kitchen segment included Amazon.com retail sales of electronics, computers, camera and photo items, software, computer and video games, cell phones, tools and hardware, outdoor living items, kitchen and houseware products, toys and video games. This segment also included commissions from sales of the products through Amazon Marketplace and commissions or other amounts earned from offerings of the products by third-part sellers through its Merchant Program. This segment had net sales of $547 million, $484 million, and $151 million in 2001, 2000, and 1999, respectively.

Amazon sourced a significant amount of inventory from relatively few vendors. During 2001, approximately 21% of all inventory purchases were made from three major vendors, of which Ingram Book Group accounted for over 10%. The company did not have long-term contracts or arrangements with most of its vendors to guarantee the availability of merchandise, particular payment terms or the extension of credit limits. In November of 2002, Amazon introduced apparel items sold by dozens of other merchants. In 2003, it expected to add several categories, some with goods sold by other companies and some with merchandise in its own warehouses.

Service segment consisted of commissions, fees and other amounts earned from its business-to-business strategic alliances, including its Merchant Program, as well as its strategic alliance with America Online. The Services segment had net sales of $225 million, $198 million, and $13 million in 2001, 2000, and 1999, respectively. In 2001, Amazon entered into numerous strategic alliances with such companies as America Online and Target in the U.S., and Virgin Wines in the U.K. The company also expanded its product offerings under its Toysrus.com strategic alliance to include Babiesrus.com and Imaginarium.com co-branded stores at amazon.com. In 2001, the strategic alliance with Toysrus.com contributed a significant amount of revenue to the Service segment. In addition, Amazon entered into strategic alliances with Expedia, Hotwire and National Leisure Group to create its travel store. In 2002, Amazon offered a variety of services to third parties, including offering consumer products sold by Amazon through Syndicated Stores; allowing third parties to utilize its technology services such as search, browse and personalization; and powering third-party Web-sites, providing fulfillment services, or both. In exchange for the services provided, Amazon received cash and/or equity securities of these companies. Much of the revenues that Amazon had recognized from its corporate partners had come as stock. In the past, Amazon had experienced losses with respect to investments in strategic companies as a result of either liquidation of such investments at a loss or decline in the fair value of these investments. In November of 2002, Amazon introduced apparel items sold by dozens of other merchants. In 2003, it expected to add several categories, some with goods sold by other companies and some with merchandise in its own warehouses. The company received a commission of about 10 percent on apparel sales.

International segment included all retail sales in its five internationally-focused Web sites: www.amazon.co.uk, www.amazon.de, www.amazon.fr, www.amazon.co.jp, and www.amazon.ca. These international sites shared a common Amazon experience, but were localized in terms of language, products, customer service and fulfillment. This segment included commissions and other amounts earned from offerings of the products by third party sellers through its Merchant Program, and product revenues from stores offerings products through its internationally-focused Syndicated Stores Program. Net sales for the International segment were $661 million, $381 million, and $168 million in 2001, 2000, and 1999, respectively. In 2001, amazon.co.uk and amazon.de each launched electronics stores, amazon.fr launched software and electronic games stores, and amazon.co.jp launched music, video, DVD, software and electronic games stores. In addition, amazon.co.jp introduced a new payment method to allow customers to pay with cash upon delivery of their orders. Amazon planned to expand its reach in international market segments. However, the company had relatively little experience in purchasing, marketing and distributing products or services for these market segments. It was also costly to establish international facilities and operations, promote the brand internationally, and develop localized Web sites. International sales and related operations were subject to a number of risks including, currency exchange rate fluctuations, local economic and political conditions, restrictive government actions, import or export licensing requirements, longer receivable cycles, consumer protection laws on pricing, and tax and other laws.

Web Site and Technology

Amazon had gotten better at merchandizing basics, but that alone didn't explain its enduring success. Amazon had great software. It performed ways to put vast inventories at customers' fingertips, and made it easy and safe to pay. Amazon's system could easily integrate new product categories or tie separate online stores into a single back end. Amazon was more than just an online storefront. Like Microsoft Windows, and Sun's Java, it was also a software platform. In much the same way, where the best e-commerce companies were licensing their platforms to other retailers, Amazon had partnered with Borders, Circuit City, Target, and Toys "R" Us to operate joint online stores. In the first quarter of 2002, Amazon generated $53 million in revenue from deals like the Target agreement, adding $10 million to the bottom line. Amazon was also negotiating to become the software engine for AOL's shopping channels.

Maintaining a viable and reliable technology was also very critical to Amazon's operations. Because its operations were dependent on the continuous use of computer software and hardware, Amazon had invested significant resources in the development and maintenance of its technology base. It had implemented numerous Web-site management, search, customer interaction, recommendation, transaction-processing and fulfillment services and systems using a combination of its own proprietary technologies and commercially available, licensed technologies. The company's strategy was to focus its development efforts on creating and enhancing the specialized, proprietary software that was unique to its business and to license or acquire commercially-developed technology for other applications where available and appropriate. Amazon spent $160 million on its Web site and technology in 1999, $269 million in 2000, $241 million in 2001, and $216 million in 2002.

The company used a set of applications for accepting and validating customer orders, placing and tracking orders with suppliers, managing and assigning inventory to customer orders and ensuring proper shipment of products to customers based on various ordering criteria. Its transaction-processing systems handled millions of items, a number of different status inquiries, gift-wrapping requests and multiple shipment methods, and allowed the customer to choose whether to receive single or several shipments based on availability and to track the progress of each order. These applications also managed the process of accepting, authorizing and charging customer credit cards. Amazon's Web sites also incorporated a variety of search and database tools and provided personalized features for individual customers such as instant personalized recommendations, personalized notifications and wish lists. Amazon's Web sites, network operations, and transaction processing systems were monitored continuously. The continued, uninterrupted operation of its Web sites and transaction processing systems was critical to Amazon's business. In addition, technology in the e-commerce industry was changing rapidly. These changes could render Amazon's Web sites and proprietary technology obsolete.

Marketing, Promotion, and Sales

Amazon's marketing strategy was designed to strengthen and broaden the Amazon brand name, increase customer traffic to its Web sites, build customer loyalty, encourage repeat purchases, and develop incremental product and service revenue opportunities. The Company spent heavily on traditional advertising and promotional methods to achieve these goals. Amazon also benefited from public relations activities as well as online and traditional advertising, including radio, television and print media, and direct marketing.

Amazon also directed customers to its Web site through its Associate Program, which enabled associated Web sites to make products available to their audiences with fulfillment performed by the company. As of late 2001, over 700,000 Web sites had enrolled in the Associates Program.

To attract more customers, Amazon also offered lower prices than a conventional store and free shipping. It was believed that the strategy of increasing efficiency and lower prices, which worked for Wal-Mart and Dell, could also work for Amazon. In one of the toughest retail markets in years, sales at Amazon.com increased 28 percent, to $1.43 billion, in the fourth quarter of 2002. During that period, Amazon sold about 56 million items. Its 2002 sales were $3.9 billion, up 26 percent. Amazon attributed much of its growth to a renewed emphasis on price-cutting, like free shipping for orders of $25 or more. The company said that it would make that offer a permanent part of its business. Amazon had waived shipping charges of $30 million in the 4th quarter but received shipping fees of $121 million. Some analysts also believed that Amazon didn't have the best brands and were out of stock a lot in electronics in 2001, but in year 2002 it had a better selection. However, few analysts believed that the Amazon's low-price strategy would put it out of business. For year 2003, Amazon predicted at least 15% sales increase.

In the fourth quarter of 2002, book sales in the United States increased 13 percent, to $606 million, compared with a 5 percent growth rate in 2001. In the United States, fourth quarter sales of hard goads, which were primarily electronics, increased 21 percent, to $261 million, in contrast to a decline of 2 percent in 2001. International sales increased 76 percent, to $461 million, slightly less than 81 percent growth in 2001. Amazon made money with book in the United States and with its international operations, but it lost money on its hard goods in the United States (See exhibit 3). The operating loss of $10 million for the hard goods in the 4th quarter of 2002 was half that of a year 2001.

Customer Service

According to Bezos, "We believe that our ability to establish and maintain long-term relationships with our customers and to encourage repeat visits and purchases depends in part, on the strength of our customer service operations, and we continually seek to improve the Amazon customer service experience." With all the marketing exchanges that were taking place in Amazon's online world, it was no surprise that customer service was critical to expanding and retaining its customer base.

Customer service representatives were available 24 hours a day, seven days a week to provide assistance via both e-mail and toll-free telephone. The company's more than 200 customer service representatives, working in six customer service centers located in Tacoma, Washington; Slough, England; Regensburg, Germany; Grand Forks, North Dakota; Huntington, West Virginia; and Sapporo, Japan. These reps dealt with a constant stream of e-mails, phone calls, and even letters. If the situations turned hostile, these reps were authorized to waive shipping charges and placate customers with gift certificates. Amazon's A-to-Z guarantee also gave protection to its customers by providing a $250 guarantee for regular purchases and a $1,000 guarantee for purchases made through its 1-Click ordering capability.

The customer service department at Amazon was a mix of old-fashioned handling, and modern technology. Bill Price, Amazon's head of customer service, had tried to turn the customer service function into a series of simple routines. Yet he readily acknowledged that the most important parts of the job couldn't be automated. "To do this job right, you need a real passion for the consumer. The best customer service reps are individuals who have a lot of empathy for frustrated customers," Bill said.

The reps worked in long rows of gray cubicles. As customers' complaints came up on their computer screens, the reps chose from a library of 1,400 prescribed remarks that were then customized with the customer's name and a few other details. There were remarks to address almost every conceivable issue. In fact, many customer complaints had more than one prescribed remark, and the reps could use their own judgment to decide which to respond with. These responses were sent out electronically. If a service rep resolved an especially difficult situation, he or she would get a "CPR" from the quality assurance department recognizing a "customer permanently retained." Another form of recognition by Amazon's management was handing out of hundreds of tiny green ceramic turtles to top service representatives. The story behind this was that an unhappy customer was like a turtle on its back. The turtle wanted to get back on its feet but didn't know how. That was where the customer service rep came in—the rep helped the turtle (the customer) get back on its feet.

Warehousing, Inventory, and Distribution

In late 1999, some e-tailer industry analysts believed that the next stage in Internet commerce was improving warehousing and delivery systems to contain costs, and control the quality of customer service. For example, Seema Williams, an information-technology analyst with Forrester Research said, "Distribution systems will be one of the things that will separate the winners from the losers." In a related move, in 1999, Amazon decided to take command of inventory and shipping activities themselves. The company knew the design of its Web site or the number of site hits would be meaningless if it failed to ship its products on time. Amazon also believed that by expanding its own distribution centers it could decrease shipping costs and make order fulfillment more efficient. As of late 2001, the company leased and operated U.S. fulfillment facilities in New Castle, Delaware; Coffeyville, Kansas; Campbellsville and Lexington, Kentucky; Fernley, Nevada; and Grand Forks, North Dakota; as well as a seasonal fulfillment center in Seattle, Washington. Amazon also leased and operated three European fulfillment centers that were located in the United Kingdom, France and Germany. In Japan, the fulfillment services were provided by Nippon Express. On an aggregate basis, these fulfillment centers comprised approximately 4.0 million square feet of warehouse space. In addition, the company leased four other facilities that fluctuated from 340,000 to 710,000 square feet of space, which supported the functions of the U.S. fulfillment centers.

Although Amazon's distribution decision promised cost savings through larger volume ordering and lower shipping costs, it also meant that Amazon needed to generate much higher sales to justify its costs. Order volume had not yet reached levels that could allow Amazon's warehouses and order fulfillment operations to realize scale economies. The cost of marketing was about 20% of annual revenue for most of land-based retailers, and 12% for catalog retailers. However, while largely empty and unused, the centers gave Amazon a leg up on online and traditional rivals in Christmas time. The new distribution centers also gave Amazon more control over the distribution process and facilitated the company's ability to deliver merchandise to customers on a reliable and timely basis.

However, by adding product lines such as electronics and toys, and building distribution centers all over the country, the job of inventory control became much more difficult for Amazon. Most of these distribution centers were highly automated, and the company had limited experience with automated distribution centers. The company was also exposed to significant inventory risks as a result of seasonality, new product launches, rapid changes in product cycles and changes in consumer tastes with respect to its products. Demand for products could change significantly between the time inventory was ordered and the date of sale. Amazon could also be exposed to inventory risk if they were unable to negotiate satisfactory terms and conditions with the manufacturers, distributors and other suppliers. In addition, Amazon' inventory forecasting, purchasing, receiving, reconciliation, accounting and payment systems were not well developed and were not well integrated. Any of these factors could require the company to markdown or write-off inventory. In 1999, when Amazon's sales grew 170% from the previous year, its inventories ballooned by 650%. In fact, on $676 million in sales in the fourth quarter of 1999, Amazon incurred $39 million write-down on inventory, which significantly decreased its gross margins.

Employees

As of December 31, 2002, Amazon employed approximately 7,800 full-time and part-time employees. The company also employed independent contractors and temporary personnel on a seasonal basis. The company's philosophy was to work hard, have fun, and make history. Many employees had a financial stake in the company's future through stock options. Some Amazon employees had three masters' degrees and some spoke five languages. Among the employees, there were people who had worked at Procter & Gamble and Microsoft, and people who had worked at *Rolling Stone* and *The Village Voice.*

The employees were not unionized. They wore jeans to work, and although casualness was encouraged, that casual attitude did not spill over to work ethic expectations. Amazon's employees worked hard at being innovative and original. The software engineers worked to develop programs that were the first of their kind, the Web site editors worked to create original content, and the Web site team worked to design site features that couldn't be found anywhere else. Competition for qualified personnel in the industry was intense, particularly for software-development. It was believed that the company's success would depend in part on its continued ability to attract, hire and retain qualified personnel.

Historically, Amazon compensated its employees mostly through stock options. But, significant fluctuation in its stock price could force the company to increase cash compensation to employees or grant larger stock option awards, which in turn could hurt its operations results or reduce the percentage ownership of the existing stockholders.

Seasonality

Amazon business was generally affected by both seasonal fluctuations in Internet usage and traditional retail seasonality. Historically, the Internet usage generally had declined during summer months. Traditional retail sales for most of the company's products, including books, music, DVDs, videos, toys and electronics usually had increased significantly in the fourth calendar quarter of each year. Insufficient stock of popular products could significantly affect its revenue and future growth. On the other hand, overstock products might require the company to take significant inventory markdowns or write-offs, which could reduce gross profits. A failure to optimize inventory in its fulfillment network would harm its shipping margins by requiring the company to make partial shipments from one or more locations. In addition, the company might experience a decline in the shipping margins due to complimentary upgrades, split-shipments and additional shipments necessary to ensure timely delivery for the holiday season.

Access of the company's Web sites by too many customers within a short period of time could create system interruptions. In addition, the company's computer and communications systems and operations could be damaged or interrupted by fire, flood, power loss, telecommunications failure, break-ins, and earthquakes, acts of war or terrorism and similar events. Amazon neither had backup systems and a formal disaster recovery plan, nor inadequate insurance coverage to compensate the company for losses from a major interruption. Computer viruses and electronic break-ins could cause system interruptions, loss of critical data, and could prevent the company from providing services and fulfilling customer orders.

Intellectual Property

Amazon regarded its trademarks, service marks, copyrights, patents, trade secrets, proprietary technology and similar intellectual property as critical to its success. Basically, Amazon relied on trademark, copyright and patent law, trade-secret protection and confidentiality and/or license agreements with its employees, customers, partners and others to protect its proprietary rights. Amazon had been issued a number of trademarks, service marks, patents and copyrights by U.S. and foreign governmental authorities. The company had also licensed in the past, and expected to license in the future, certain of its proprietary rights, such as trademarks, patents, technologies or copyrighted materials, to third parties.

Financial Situation

Amazon had incurred significant losses since it began doing business. As of December 31, 2002, the company had an accumulated deficit of over $3 billion, and its stockholders' equity was a deficit of $1.48 billion. Amazon, which had lost money in the first three quarters of 2002, posted a quarterly profit of $2.7 million. Its total loss in year 2002 was $149 million. However, as it was planned, Amazon generated $198 million cash from operations in 2002. Its cash and marketable securities at the end of 2002 was about $1.3 billion. The free cash flow was not sufficient to refinance the $2.2 billion in bond, which would mature soon.

Amazon essentially funded its revenue growth and overall operations through a variety of sources. From 1997 through 2002, the company had received $2.2 billion from its bond offering to meet its cash needs. In January 1999, Amazon sold $1.25 billion of 4.75 percent convertible bonds maturing in 2009. In February 2000, it sold 690 million euros ($681 million) of 6.88 percent convertible bonds maturing in 2010. Amazon also had $264 million of 10 percent Senior Discount Notes outstanding, maturing in 2008. The company made annual or semi-annual interest payments on the indebtedness under its two convertible notes, which were due in 2009 and 2010, respectively. Beginning in November 2003, Amazon would begin to make semi-annual interest payments on the indebtedness under its Senior Discount Notes. When Amazon issued the debt, the market for e-commerce stocks was flying, and it looked like the company might be able to call the notes and force investors to convert their notes for shares of its stock. For its U.S. debt, Amazon could call the 10-year notes for stock if the company's stock traded above $117.04 per share for 20 out of 30 consecutive trading days. All of a sudden dot-com land had changed abruptly, competition was becoming stronger, and the capital market was looking at the bottom line—profitability. In a stunning turnaround in 2000 from its previous years of growth, Amazon's sales growth in 2001 was

13%, or 55% less than what it was in 1999. That was a deep drop from the 43% growth the company had projected.

In early 2000 and 2001, investors had lost their patience with most Internet companies and punished those that couldn't show a path to profitability. Amazon's stocks and key convertible bonds started dropping sharply and top tech-fund managers began to reduce and even eliminate Amazon from their portfolios. In Late December 2002, Amazon stock was trading in the $18 - $23 range, down about $90 from its high of $113 in December 1999. Exhibit 6 shows the latest trends in the company's stock price.

INDUSTRY AND COMPETITIVE ENVIRONMENT

Several factors made the online retailing business attractive relative to traditional retail stores. Unlike a catalog or store, an online retailer had the option of offering a huge selection of products. According to Porter, the Internet technology dampened the bargaining power of distribution channels by providing online retailers with new, more direct avenues to customers. A Web site could offer a vast amount of information on those products. A Web site also eliminated the cost of printing and mailing catalogs. Yet, online retailing was not an inexpensive way to do business. For one thing, online retailers faced significant technology costs associated with operating and maintaining a cutting-edge online store. According to Merrill Lynch Internet analyst Henry Blodget, "If you're trying to service a mass market, you need to maintain an expensive Web site that costs around $50 million, whether you have $1 or $1 billion in revenue." They had to rent warehouses and stock shelves. Then there was a sizable marketing and promotion costs to build site traffic. Finally, there was the unglamorous task of processing and shipping orders, which offset many of their cost advantages over brick-and-mortar retailers.

While it was relatively easy to create a Web site that functioned like retail stores, the big challenge for an online retailer was to generate traffic to the site in the form of both new and returning customers. Most online retailers strived to provide extensive product information, including pictures of the merchandise, make the site easily navigable, and have enough new things happening at the site to keep customers coming back. Online retailers could more easily obtain extensive demographic and behavioral data about their customers, providing them with greater direct marketing opportunities and the ability to offer a more personalized shopping experience. In addition, online retailers could offer consumers significantly broader product selection, the convenience of home shopping, and 24-hour-a-day, seven-day-a-week operations available to any foreign or domestic location with access to the Internet. Physical-store-based retailers had to make significant investments in real estate, inventory, and personnel for each store location. Online retailers generally incurred a fraction of these costs due to centralized distribution and virtually unlimited merchandising space. It was cost-effective for online retailers in various ways to offer a broader range of products and information than brick-and-mortar retailers.

The Internet technology expanded the geographical market by bringing many more companies into competition with one another. It was also more difficult for on-line retailers to differentiate themselves, as they lacked potential points of distinction such as personal selling. On the Internet, buyers could often switch suppliers with just a few mouse clicks, and some new Web technologies were systematically helping switch suppliers even further. For example, companies like PayPal provided settlement services –so-called ewallets—that enabled customers to shop at different sites without having to enter personal information and credit card numbers. Content-consolidation tools such as OnePage allowed users to avoid having to go back to sites over and over to retrieve information by enabling them to build customized Web pages. In addition, the Internet technology reduced variable costs and tilted cost structures toward fixed cost, creating significantly greater pressure for online retailers to engage in destructive price competition to build volume.

Online retailers were more aggressive in discounting their prices and running special promotions like free shipping than traditional store retailers, and brick-and-mortar retailers with online stores. For example, most record companies had established online sites to sell directly to the consumer, but their prices were generally higher than those of online music retailers like CDnow and Amazon.com; this was partly to avoid creating channel conflict and angering the traditional brick-and-mortar music retailers on whom the record companies depended for most of their sales. Online retailers could offset the revenue loss from price discounting with the fees they earned from selling advertising space on their Web sites. But, the rate of growth of Web advertising was slowing in 2000.

The 1999 holiday selling season, while setting record sales, precipitated a shakeout in the online retailing industry as weaker competitors struggled to stay in business. The online book segment of retailing had experienced several changes. Competitor mergers and acquisitions, and legal wrangling over content and process patents were just a few of the major challenges facing the online retailing industry. By the middle of 2000, there was some evidence that the high-growth phase of U.S. e-commerce growth was over. According to an online retail index released by the National Retail Federation and Forrester Research, overall spending in May 2000 rose just 2.4%, from April, while sales of books, music and video products fell almost 13%. Most online retailers were plagued with losses, owing to capital expenditures for state-of-the-art Web site technology and very large marketing and advertising expenditures to build site traffic.

To turn losses into profits, online retailers had to achieve a large volume of sales and, at the same time, keep a tight rein on marketing costs and other parts of the operations. To build sales and market share, online retailers had to build strong brand awareness and generate heavy site traffic. One way of doing this was by allying with Yahoo!, America Online, and the other portals and paying them substantial sums of advertising space. Getting lots of exposure on the major portals was deemed critical to building traffic, since it was difficult for online retailers to differentiate on the basis of product selection. The big Internet retailers were willing to pay to lock up advertising space and Web links on the leading portals for as long as two to four years. To counter the exclusive promotional arrangements that several of the online retailers had negotiated with prominent portals, rivals were shifting more money to traditional media advertising. In addition, most online retailers shifted the basis of competition away from quality, features, and service and toward price, making it harder for anyone in the industries to turn a profit.

Like traditional retailers, online retailers were increasingly becoming a fourth quarter story, and needed to hit a home run in the busy holiday season. According to BizRate.com, which tracked sales at top retail Web sites, online sales during the holiday quarter of 2002 grew to $17.4 billion, compared with $12.4 billion a year earlier. In addition, companies were cutting costs on marketing to get better margins and narrower losses. According to an official with the Association of Internet Professional, “Everyone is losing money because the margins are so low. What companies are shooting for is an established market share by 2002. It is important that you be No. 1, No. 2, or maybe No. 3. You build the name, you build the brand, and then you make the money. That was what Japanese did in the auto industry in the 1980s.”

However, a growing number of analysts believed that online retailing would be a niche market, akin to catalog retailing. For example, Peter Stanger, a vice president at the Boston Consulting Group said, “There is no reason why online retailers shouldn’t be as profitable as the catalog business. Catalogers survived by being very segmented and targeted.” When Ken Weil, Vice-President of Intimate Brands took the lingerie retailer online in 1998, he relied on the same photos used for the company’s catalogs and store images. This saved tons of money because no models had to be hired, and no expensive photo manipulation needed to be done. Moreover, Weil considered his eye-catching Web site more than just an online catalog. It was a cheap marketing tool for the entire company that took advantage of Victoria Secret’s well-known name. According to Weil, “We have an advantage on the Web because we’re part of a well-respected brand. The site has been profitable since Day One.”

Porter predicted that the power of customers would rise in the future. “As buyers’ initial curiosity with the Web wanes and subsidies end, online retailers will be forced to demonstrate that they provide real benefits. And as customers become more familiar with the Internet technology, their loyalty to their initial online retailers will also decline; they will realize that the cost of switching is low,” said, Porter.

Online retailers were also subject to general business regulations and laws, as well as regulations and laws specially governing the Internet and e-commerce. Future laws and regulations might impede the growth of the Internet and online services. These regulations might cover taxation, user privacy, pricing, content, copyrights, electronic contents, and consumer protection. Currently, decisions of the U.S. Supreme Court restricted the imposition of obligations to collect state and local sales and use taxes with respect to sales made over the Internet. However, a number of states, as well as the U.S. Congress, were considering various initiatives that could limit or supersede the Supreme Court’s position regarding sales and use taxes on Internet sales. The imposition by state and local governments of various taxes upon Internet commerce could create administrative burdens for online retailers and could decrease their future sales. University of Tennessee professor William Fox and Donald Bruce estimated that the states lost $13.3 billion in taxes from e-commerce in 2001 and would miss $45 billion in 2006. That could be a juicy target for the states, almost all of which were facing budget crises.

In year 2002, the e-commerce market segments in which Amazon competed were relatively new, rapidly evolving, and intensely competitive. In addition, the retail environment for Amazon's products was generally intensely competitive and Amazon had many competitors in different industries, including the Internet and retail industries. Amazon's existing and potential competitors included: (1) physical-world retailers, catalog retailers, publishers, distributors and manufacturers of its products; (2) online vendors of products; (3) a number of indirect competitors, including Web portals and Web search engines that were involved in online commerce; (4) Web-based retailers using alternative-fulfillment capabilities; and (5) companies that provided e-commerce services, including Web-site developers and third-party fulfillment and customer-service providers. For example, in year 2002, Wal-Mart operated its discount stores in all 50 states. The average size of its discount store was approximately 95,262 square feet. It operated 1,736 discount stores with total estimated sales of $122 billion in year 2002. Each store carried a wide variety of merchandise, including apparel, electronics, books, CDs, sporting goods, and toys. With so many discount stores across the country, some analysts believed that Wal-Mart could bring many more people online and shift the balance of the online shopping scene away from pure Internet businesses to traditional retailers. In a possible advantage over Internet-only retailers, Wal-Mart could closely tie its Web site to its stores. It had the ability for in-store return and pickup, said John Buck, president of Fingerhut Business Services.

FUTURE OUTLOOK FOR AMAZON.COM

Jeff believed the company had a promising future. Nonetheless, he knew the challenges ahead were formidable. The company had a weak balance sheet, massive negative operating cash flow, competition was becoming stronger, and all of a sudden dot-com land changed abruptly and the capital markets were looking at the profitability. Amazon had lost over $3 billion since it opened, with the accumulated deficit of over $1.35 billion. The company's cash and marketable securities at the end of 2002 was about $1.3 billion.

Amazon's debt load was also a source of concern. It raised $2.2 billion to meet its cash needs. Bondholders were being paid over $130 million interest payments a year. There was still another issue that related to the company's efforts to implement its strategy for growth. In year 2002, Amazon shifted its focus on growth prospects as it had in its earlier years. By adding more product lines, and building distribution centers all over the country, the job of policing its inventories became much more difficult. Some bond analysts following the company felt that the excessive debt and poor inventory management would make Amazon's operating cash flow situation worse the more it sells. Moreover, the company was more susceptible to macro factors than its own specific ones. With improving cost structure, still the main threat out there was the slow economy.

Although Jeff still wasn't giving up on his empire-building dream, he was beginning to wonder whether Amazon would run out of money soon, and default on its notes payments. He had to decide which business model and strategy made the most sense for Amazon. It seemed that there were some main questions out there for investors: What was the longer-term growth of this company? What was the prospect of making profit in 2003? How could the company get to double-digit operating margins? Should Amazon go to the stock market to raise money to pay its debt? Would any bank take out the existing bondholders? Jeff Bezos, founder and chief executive officer of Amazon.com was wondered, "What to do?"

EXHIBIT 1: AMAZON'S STATEMENTS OF INCOME, 1997-2002

($000s, Except Per Share Data)

	12/31/97	12/31/98	12/31/99	12/31/00	12/31/01	12/31/02
Net Sales	$147,787	$609,819	$1,639,839	$2,761,983	$3,122,433	$3,932,900
Cost of Sales	118,969	476,155	1,349,194	2,106,206	2,323,875	2,940,300
Gross Profit	28,818	133,664	290,645	655,777	798,558	992,600
Operating Expenses:						
Fulfillment			237,312	414,509	374,250	345,220
Marketing	40,077	132,654	175,838	179,980	138,283	137,350
Technology & content	13,384	46,424	159,722	269,326	241,165	215,600
Genl &administrative	6,741	15,618	70,144	108,962	89,862	114,330
Stock-based comp	1,211	1,889	30,618	24,797	4,637	0
Amort all intangibles	0	42,599	214,694	321,772	181,033	74,400
Restructuring, M&A	0	3,535	8,072	200,311	181,585	41,600
Total Operating Expenses	61,413	242,719	896,400	1,519,657	1,210,815	928,500
Income (Loss) Operations	(32,595)	(109,055)	(605,755)	(863,880)	(412,257)	64,100
Interest Income	1,901	14,053	45,451	40,821	29,103	23,700
Interest Expense	(326)	(26,639)	(84,566)	(130,921)	(139,232)	(142,900)
Other Income (Exp) – net	0	0	1,671	(10,058)	(1,900)	5,600
Other gains (losses), net	0	0	0	(142,639)	(2,141)	(96,300)
Net Int Inc (Expenses)	1,575	(12,586)	(37,444)	(242,797)	(114,170)	(209,900)
Loss before equity in Affiliates	(31,020)	(121,641)	(643,199)	(1,106,677)	(526,427)	(145,800)
Equity in Affiliates	0	(2,905)	(76,769)	(304,596)	(30,327)	(4,200)
Loss before change in accounting principle	(31,020)	(124,546)	(719,968)	(1,411,273)	(556,754)	(150,000)
Accounting change	0	0	0	0	(10,523)	800
Total Net Income (Loss)	(31,020)	(124,546)	(719,968)	(1,411,273)	(567,277)	(149,200)
Net income (loss) per common share	($0.12)	($0.42)	($2.20)	($4.02)	($1.53)	0.40
Weighted avg common shares outstanding	260,682	296,344	326,753	350,873	364,211	378,400

Source: Amazon annual reports.

EXHIBIT 2: AMAZON'S QUARTERLY INCOME STATEMENTS, 2001-2002

($000s, Except Per Share Data)

	Three Months Ended March 31,		Three Months Ended June 30,		Three Months Ended Sept. 30,	
	2002	2001	2002	2001	2002	2001
Net sales	847,422	700,356	805,605	667,625	851,299	639,281
Cost of Sales	624,297	517,759	587,438	487,905	635,132	477,089
Gross Profit	223,125	182,597	218,167	179,720	216,167	162,192
Operating Expenses:						
Fulfillment	89,815	98,248	85,751	85,583	90,342	81,400
Marketing	32,244	36,638	28,832	34,658	26,728	32,537
Technology and content	55,497	70,284	58,165	64,710	52,907	53,846
General and administration	20,911	26,028	19,425	22,778	18,698	21,481
Stock-based compensation	10,931	2,916	23,148	2,351	(832)	(2,567)
Amortization of all intangibles	1,979	50,831	1,374	50,830	1,212	41,835
Restructuring, Merger, and acquisition	9,974	114,260	0	58,650	36,757	3,994
Total Operating Expenses	221,351	399,205	216,695	319,560	225,812	232,526
Income (Loss) from Operations	1,774	(216,608)	1,472	(139,840)	(9,645)	(70,334)
Interest Income	5,652	9,950	5,650	6,807	5,600	6,316
Interest Expense	(35,244)	(33,748)	(35,651)	(35,148)	(35,922)	(35,046)
Other Income (Expenses) – Net	95	(3,884)	(402)	(1,178)	3,183	(2,203)
Other Gains (Losses) – Net	5,516	33,857	(63,454)	11,315	2,261	(63,625)
Total Non-Operating Income (Exp.)	(23,981)	6,175	(93,857)	18,204	(24,878)	(94,558)
Loss Before Equity in Affiliates	(22,207)	(210,433)	(92,385)	(158,044)	(34,523)	164,892
Equity in Affiliates	(1,744)	(13,175)	(1,168)	(10,315)	(557)	(4,982)
Loss Before Change in Accounting Change	(23,951)	(223,608)	(93,553)	(168,359)	(35,080)	(169,874)
Accounting Change	801	(10,523)	0	0	0	0
Total Net Income (Loss)	(23,150)	(234,131	(93,553)	(168,359)	(169,874)	(169,874)
Net Income (Loss) per Common Share	($0.06)	($0.66)	($0.25)	($0.47)	($0.46)	($0.46)
Weighted Average Common Shares Outstanding	373,031	357,424	376,937	359,752	368,052	368,052

Source: Amazon annual reports.

EXHIBIT 3: AMAZON'S SEGMENT INFORMATION

Year Ended December 31, 1999 ($000s)

	US Books, Music and DVD/video	Electronics, Tools and Kitchen	International	Services	Consolidated
Net Sales	$1,308,292	$150,654	$167,743	$13,150	$1,639,839
Gross Profit (Loss)	262,871	(20,086)	35,575	12,285	290,645
Pro forma income (loss)	(31,000)	(163,827)	(79,223)	(78,321)	(352,371)
Stock-based compensation					(30,618)
Amortization of goodwill					(214,694)
Restructuring-related					(8,072)
Net interest expense					(37,444)
Equity in losses of equity-method					(76,769)
Net Profit (Loss)					(719,968)

Year Ended December 31, 2000 ($000s)

	US Books, Music and DVD/video	Electronics, Tools and Kitchen	International	Services	Consolidated
Net Sales	$1,698,266	$484,151	$381,075	$198,491	$2,761,983
Gross Profit (Loss)	417,452	44,655	77,436	116,234	655,777
Pro forma income (loss)	71,441	(269,890)	(145,070)	26,519	(317,000)
Stock-based compensation					(24,797)
Amortization of goodwill					(321,772)
Restructuring-related					(200,311)
Net interest expense					(242,797)
Equity in losses of equity-method					(304,596)
Net Profit (Loss)					(1,411,273)

Year Ended December 31, 2001 ($000s)

	US Books, Music and DVD/video	Electronics, Tools and Kitchen	International	Services	Consolidated
Net Sales	$1,688,752	$547,190	$661,374	$225,117	$3,122,433
Gross Profit (Loss)	453,129	78,384	140,606	126,439	798,558
Pro forma income (loss)	156,753	(140,685)	(103,112)	42,042	(45,002)
Stock-based compensation					(4,637)
Amortization of goodwill					(181,033)
Restructuring-related					(181,585)
Net interest expense					(114,170)
Equity in losses of equity-method					(30,327)
Cumulative effect of change in accounting principal					(10,523)
Net Profit (Loss)					(567,277)

Source: Amazon annual reports.

EXHIBIT 4: AMAZON'S BALANCE SHEETS, 1998-2002 ($000)

	12/31/98	12/31/99	12/31/00	12/31/01	12/31/02
ASSETS					
Current Assets:					
Cash & Equivalent	$25,561	$116,962	$822,435	$540,282	$738,300
Marketable Securities	347,884	589,226	278,087	456,303	562,700
Inventories	29,501	220,646	174,563	143,722	202,400
Prepaid Expenses & Other Assets	21,308	85,344	86,044	67,613	112,300
Total Current Assets	424,254	1,012,178	1,361,129	1,207,920	1,615,700
Fixed Assets, net	29,791	317,613	366,416	271,751	239,400
Goodwill, net	174,052	534,699	158,990	45,367	70,800
Other intangibles, net	4,586	195,445	96,335	34,382	3,500
Investments – Equity in Affiliates	7,740	226,727	52,073	10,387	8,250
Other Equity Investments	0	144,735	40,177	17,972	7,050
Other Assets	8,037	40,154	60,049	49,768	45,700
Total Assets	$648,460	2,471,551	$2,135,169	$1,637,547	1,990,400
LIABILITIES AND STOCKHOLDERS' EQUITY					
Current Liabilities					
Accounts Payable	$113,273	$463,026	$485,383	$444,748	$618,100
Accrued Expenses	47,484	181,909	272,683	305,064	314,900
Unearned Revenue	0	54,790	131,117	87,978	53,850
Interest Payable	10	24,888	69,196	68,632	65,850
Current Portion of long-term debt	808	14,322	16,577	14,992	13,300
Total Current Liabilities	$161,575	$659,097	$974,956	$921,414	1,066,000
Long-term debt	348,140	2,082,697	2,127,464	2,156,133	2,277,300
Total Liabilities	$509,149	$2,741,794	$3,102,420	$3,077,547	$3,343,300
Stockholders' Equity					
Common Stock, $0.01 par value	3,186	3,561	3,571	3,732	3,940
Additional paid-in Capital	298,537	1,342,574	1,338,303	1,462,769	1,649,860
Deferred Stock-based Compensation	(2,724)		(13,448)	(9,853)	
Accumulated other Comprehensive income (Loss)	1,806	(65,637)	(2,376)	(36,070)	3,100
Retained Earnings (Accumulated Deficit)	(162,060)	(1,748,161)	(2,293,301)	(2,860,578)	(3,009,800)
Total Stockholders' Equity (Deficit)	138,745	(487,167)	(967,251)	(1,440,000)	(1,352,700)
Total Liabilities & Equity (Deficit)	$648,460	2,254,627	$2,135,169	$1,637,547	1,990,400

EXHIBIT 5: AMAZON'S CASH FLOW STATEMENTS, 1999-2002 (in millions)

	12/31/99	12/31/00	12/31/01	12/31/02
Net Income	(720.0)	(1,411.3)	(567.3)	(149.1)
Depreciation/Depletion	36.8	84.5	84.7	82.3
Non Cash Items	122.7	672.0	141.6	127.0
Changes in Working Capital	230.1	286.0	171.3	175.2
Total Cash from Operating Activities	(90.9)	(130.4)	(119.8)	174.3
Capital Expenditures	(287.1)	(134.8)	(50.3)	(39.2)
Other Investing Cash Flow Items	(664.9)	298.7	(203.0)	(82.5)
Total Cash from Investing Activities	(952.0)	164.0	(253.3)	(121.7)
Insurance/Retirement of Stock, Net	64.5	44.7	116.5	121.7
Insurance/Retirement of Debt, Net	1,074.8	664.6	(9.6)	(14.8)
Financing Cash Flow Items	(35.2)	(16.1)	0.0	0.0
Total Cash from Financing Activities	1,104.1	693.1	106.9	106.9
Foreign Exchange Effects	0.5	(37.6)	(16.0)	38.5
Net Change in Cash	61.7	689.1	(282.2)	198.0
Cash Interest Paid	30.5	67.3	112.2	111.6

Source: http://investor.stockpoint.com, 2003

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HANDS OF URUGUAY

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CASE DESCRIPTION

The primary objective of this case concerns the need to resolve a worsening financial situation by establishing new strategic initiatives. Secondary issues include the role of mission in establishing strategic plans and the importance of company and country culture in strategic decisions. The case is appropriate for level 3 (Junior) or 4 (Senior) courses in international management, small business or strategic management. The case is designed to be taught in a 75-minute class period and is expected to require three hours of outside preparation by students.

CASE SYNOPSIS

Manos Del Uruguay is a non-profit cooperative based in Montevideo, Uruguay. Manos produces high quality hand-made woolen goods. Its customers include major design houses in South America, Europe, the U.S. and Japan. However, despite a 30-year history of operations, Manos is currently struggling for survival. It is experiencing rapidly falling export sales and dramatic changes in the local and global economy. The cooperative was originally formed to provide job opportunities for women artisans' producing hand crafted goods. Can Manos hold to its original mission or must it change fundamentally in order to survive? The General Manager has developed four strategic alternatives for the Board of Directors to consider in addressing this difficult situation.

MANOS DEL URUQUAY

"At this rate, in two years our exports will cease to exist!" Rodolfo Gioscia, General Manager of Manos del Uruguay moaned to himself after analyzing the year-end financial results compared with those of previous years (Appendix 1). The results showed a continuing decline in the company's export sales and a net loss for the year. In addition, the company had been experiencing cash flow problems.

It was Friday, the last week of January, and many questions whirled around in his head: "What can we do to break this pattern of losses? Do we need to make company wide changes or will a small focused effort turn things around? Is the problem with our export markets or does it extent to local markets too?"

Rodolfo Gioscia had been the General Manager of Manos del Uruguay since 1998. This position had represented a significant challenge for him because Manos was a nonprofit, co-op organization with a concept different from other companies that he had previously managed. Co-ops have significantly different risks and opportunities. One cannot manage a group of independent artisans in the same manner as regular, full-time employees.

Mr. Gioscia decided to call together his Board of Directors for a meeting at the beginning of next week. This would give him the weekend to think things over and try to generate some strategic alternatives for their consideration.

URUGUAY

Most first-time visitors from the United States are surprised that Uruguay is nothing like Mexico (apparently the prototypical Latin American image). Original colonists of Uruguay displaced nearly all native peoples resulting in a largely European-based population that is nearly 90% white. Unlike Mexico, there are no spicy foods (Uruguayans eat a lot of beef, noodles, and rice), there are no ancient ruins, and the people look different from Mexicans. Even though Spanish is the official language of Uruguay, it is somewhat different from the type most Americans learn in school. For example, a "taco" is not something you eat, but rather the heel of a shoe and a "pancho" is a hot dog, as opposed to a "poncho" which is something you wear.

Uruguay is a land of rolling hills and gauchos (cowboys). There is no jungle, and there are no mountains. The weather is quite temperate, with rare freezes, and no Amazonian heat. Cattle and sheep, and their by-products, have been the mainstay of the economy for decades. There are nice beaches and several large modern cities, the largest of which, Montevideo, is modern and vibrant. The entire country is about the size of the state of Washington with 3.3 million people, 1.5 million of which reside in the capital. Uruguay lies on the Atlantic Ocean between the two superpowers of South America - Brazil and Argentina, but boasts more economic and political stability than either of those neighbors.

Despite a large rural setting and low wages, the population of Uruguay has one of the highest literacy rates in the world. Public schools had operated in rural areas for many decades, thanks to the general opinion of society that education was a useful investment. These schools prepared men and women with a variety of skills and basic knowledge that, in rural areas, had been difficult to put to use in the local job market.

According to Hofstede's (1984) national cultural dimensions, Uruguay is very high on uncertainty avoidance indicating people prefer to follow established rules and take fewer risks. It is also ranked relatively low on the masculine dimension indicating that quality of life is considered more important than financial success. Westerners often note a more relaxed approach to time and a higher priority on personal relationships and family. Uruguay is ranked medium on power distance and individualism dimensions indicating moderate acceptance of authority and individual achievements respectively.

HISTORY OF MANOS DEL URUGUAY

At the end of the 1960's, the lifestyle of the majority of the inhabitants in cities around the world, and in particular in Uruguay, had undergone substantial change. Industrial products substituted for handmade products, and the absence of interested buyers for the handcrafted items virtually condemned handmade products to extinction.

However, in isolated rural areas of Uruguay, one could still find people, especially women, who retained various handcrafted artisan traditions. These women had continued producing handmade items without being influenced by the changed lifestyles, technology, or latest fashions. Their products were made for their families and neighbors who had often provided them the raw material - wool, leather, or horns. The articles the artisans produced were sweaters, pullovers, saddles, and containers made from horns. It was these capable people, with skilled hands and a desire to work, together with the quality of the handicrafts they produced, that provided the initial elements on which Manos del Uruguay had been built.

The importance of supporting and maintaining native artisans in rural areas of Uruguay had captured the interest of some people in the private sector, including visionaries, rural teachers, and a variety of marketing and sales executives. Five women had taken the initiative to establish Manos del Uruguay in 1968: Olga Pardo Santayana, Manila Chaneton, Sara Beisso, Dora Muñoz and Maria del Carmen Bocking. They wanted to improve the opportunities for poor women in rural areas. Therefore, they worked together to form groups of women artisans divided by geographic area or town.

The five founders were wealthy and traveled extensively abroad. While abroad, they established contact with design houses in Europe whose designers created designs for the rural women of Manos to produce. The founders were confident that there was a market for the hand-crafted woolen items which would mean significant resources for poor country people in

Uruguay. The mission of Manos del Uruguay became: "Offer the rural woman the opportunity to develop herself both economically and culturally, by means of artisan work organized as a cooperative."

The first step was to conduct a test market in the two largest Uruguayan cities: Montevideo and Punta del Este. Montevideo, as the capital, was on the itinerary of many foreign tourists. Punta del Este was a wealthy beach community that had long been a regular stop for the jet-set elite, and sailing enthusiasts. The initial results were very positive. The artisans tripled their traditional earnings! The news of these results quickly spread to other areas and many additional artisans joined Manos del Uruguay. The women were very, very proud of their accomplishments. They were working and able to significantly contribute to the family income.

Over time, Manos continued to grow and expand. The founders developed and coordinated artisan expertise in spinning and weaving, created administrative and marketing processes, and worked to create effective, stable employment opportunities.

Manos del Uruguay had received the support of several international organizations: the BID, for technical assistance and working capital; the Inter-American Foundation for the training of the artisans; and funds for the development of the cooperatives. They were also successful in obtaining a loan from the Banco de la Republica Oriental del Uruguay (BROU) and the Centro Cooperativista Uruguayo (CCU) which helped set up the cooperative system, which was rather unknown in the country prior to Manos.

Although Manos began with only five groups of artisans, in a matter of only a few months Manos grew to more than 12 groups. By the end of 1969, they had more than 260 artisans in 18 groups. By the end of the second year of operations (1970), Manos had 31 cooperative groups consisting of more than 560 artisans!

Their spectacular and rapid growth was owed principally to the great reception of the products in their primary markets of Montevideo, Punta del Este, and neighboring Buenos Aires, Argentina. Nevertheless, rapid expansion also produced a series of organizational, administrative, and financial difficulties that for many years marked the history of Manos del Uruguay.

To solve these problems, a Central Services unit was created in Montevideo. This unit had the primary responsibility for coordinating the supplies of raw material and machinery, acquiring capital financing, marketing, and general administration. Originally, Central Services was made up of women volunteers from the Montevideo area, but later paid employees were added, with the responsibility of effectively managing distinct sectors of the company such as financing, marketing and supply management. The need for paid employees led to charging the customer an additional percentage on top of the artisan price to cover Central Services payroll expenses.

In addition to the establishment of Central Services administration, measures were taken to improve work techniques, with the goal of improving the quality of the products. In the human resource area, efforts were made to train artisans on the skills necessary to actively participate in the management of the company. During the 1970's, the company relied heavily upon the free counsel of people and institutions that volunteered their experience and this served them well.

By the end of the 1970's, fashion magazines like Vogue, Elle and others featured Manos del Uruguay products on their covers. Celebrities like John Lennon, Robert Redford and Brook Shields wore their garments. While the artisans were not earning a lot of money, they were very proud that their products were of a quality good enough to compete in the very demanding European fashion market.

On more than one occasion Manos won the Export Prize awarded by Banco de la Republica Oriental del Uruguay (BROU). Manos received these prizes for responding to a real need of the artisans for living wages which in turn made an important contribution to the economy of the country. Manos served national and international clients that had again become eager to obtain handcrafted products. The hands logo of Manos del Uruguay sent a special message about the viability of handmade items in a highly competitive economy. Likewise, on a personal level, the products carried the pride of the people who made them.

Manos del Uruguay puts special emphasis on the social aspect of women working together. In the view of many artisans it is this value system of putting the "group" first that sets Manos apart from other companies. This is a hallmark of cooperative organizations.

A COOPERATIVE ORGANIZATION

As an organization, Manos Del Uruguay follows a cooperative organization structure. A cooperative is an association of people voluntarily united to meet common goals. These goals are often economic, social and cultural. The cooperative business is jointly owned and democratically controlled by its members and operated for them on a non-profit basis. Cooperatives are generally based on the values of self-help, caring for others, democracy, equality, and solidarity. To understand co-ops one must understand their network nature and the strong underlying culture that supports this type of relationship. The cultural values of solidarity, caring for others, and joint participation were key aspects of Manos. The culture of Manos reflects the basic notion of a cooperative. The members of Manos del Uruguay think of themselves as a "system," because Manos unites different organizational units with common objectives. The members feel united by a close interdependence.

Central Services had the responsibilities for product design, quality control, and marketing. Product design was done exclusively by product development teams at Central Services. The cooperatives produced what Central Services ordered. The cooperatives received the design, a prototype with technical notes, and the production materials from Central Services. Every artisan received salary and benefits from their cooperative.

For the products made for sale under other labels, product development had typically been a very long procedure. The process began with Manos presenting colors, materials and models to designers from the clients, the designers then develop specifications, Manos made a prototype, the client approved it or made changes, then Central Services developed the final prototype and assigned it to the cooperatives for production. Central Services made payments to the cooperatives after receiving the completed products and verifying quality.

Governance of Manos was primarily conducted through the Board of Directors. The Board of Directors is constituted of honorary members - people who have a personal commitment directly related to the objectives of Manos. They receive no payment and they included lawyers, accountants, etc. There were also four elected representatives from the artisans voted in by members of the cooperatives. In some cases they helped give shape to the committee and helped to determine its function; in other cases, they collaborated to gather specific knowledge essential for leading the organization. The Board's role is to ensure that the overall goal of Manos continues to be helping give the artisans and their families a new place in the economic and social order.

Under the Board of Directors you find the General Manager, whose job is to guide the organization towards its objectives. Likewise the General Manager manages various day-to-day situations, and spends a large portion of time making business contacts, especially in the foreign market. Reporting to the general manager, are the manager of Administration and Finances, the Leader of Sales and Exports, and the Production Manager.

The production manager is in charge of the quality. Each cooperative group has a leader or guide who reviews the quality of the products before they are sent to Montevideo. Once received at Central Services, garments are again inspected. If a garment is not of sufficient quality, the artisan does not receive payment for their work. Or, they may be given a chance to rework the garment.

CHANGES IN GLOBAL COMPETITION

By 1994, Manos del Uruguay had more that 800 artisans located throughout the country. Approximately 80,000 units of wool blankets, tapestries, garments, baskets, and rugs, all made from natural fibers, were sold in local and international markets.

Manos had been successful at generating new job opportunities for women that lived in remote rural areas, such as Dragon, on the Brazilian border and Paso la Crus on the Argentinean border; as well as regions close to the capital city of Montevideo. With their labor, the artisans of Manos del Uruguay preserved and promoted the traditional Uruguayan handcrafts that dated back to the birth of the country. Manos continued to play a key role in the preservation of the history and traditions of rural life. Their marketing efforts helped ensure that other countries would know Uruguayan traditions for wool making and dying as well as their craftwork.

In 1994, the Uruguayan government declared a change in economic policies that included some progressive new priorities in the economic area. After 30 years of a relatively closed economy, Uruguay aimed for a deeper deregulation in trading policies and opened their markets to create a more competitive economy. Efficient production and well-run organizations became essential to remaining competitive. Manos found itself having to adapt to the changes thrust upon it by these new developments without the help of the government policies that had specifically protected the artisans in the past. The company worked hard to respond to new and greater client demands, penetrate new markets, and face new competition.

The invasion of all types of imported products created real competition for the local craftspeople. Manos attempted to rise to the challenge. In 1999 Manos produced almost three times as much per person as they had in the previous five years. Simultaneously however, the number of participating artisans dropped to about 350 grouped into 17 cooperatives from a variety of rural counties in Uruguay: Soriano, Tacuarembo, Florida, Cerro Largo, Flores, San Jose, Paysandu, Canelones, Rio Negro, Lavalleja and Durazno. This reduction in artisans was mainly a result of the emphasis placed on greater productivity.

Along with the greater emphasis on productivity, the Manos organization also had evolved to include benefits such as paid vacations, bonuses, medical insurance, and retirement pensions for artisans. In the words of the general manager, "These changes were more and more necessary. We needed new answers for new situations, continually adapting ourselves to the new circumstances."

Manos' primary products at this point were sweaters, capes, ponchos, blankets and bedspreads. All products were still made of 100% virgin wool, spun by hand and woven on a handloom. The designs were fashionable, original and creative - a trademark of the business, which identified the business not only on a national level but also internationally. Products were marketed in Uruguay through stores owned by Manos, four of which were located in Montevideo (Ciudad Vieja, Centro, Montevideo Shopping and Punta Carretas Shopping) and one in Punta del Este. Other stores included specialty boutiques in Mercado del Puerto in Montevideo, in the city of Colonia del Sacramento, in the city of Salto, in the spa Atlantida and in Piriapolis.

Manos had also continued to export to Paris, Tokyo, and New York. In their attempts to grow, Manos recognized three alternatives for penetrating the North American market: 1) specialized stores, 2) name brand labels (e.g., Polo, Ralph Lauren, Michale Koors, Jhane Barnesand Donna Karan in New York), and 3) department stores (e.g., Bloomingdale's and Nordstrom's). When products were made for other labels, Manos competed directly with many other suppliers. The retail clothing industry was historically fickle with many rapid product cycles. Major brands changed suppliers frequently. Manos knew they were in a very fragile position when selling in the USA under other brand labels because the clients changed suppliers very easily.

Staying competitive with designs created a longer production process as Mr. Gioscia described, "The coordination of the production process is very difficult. For example, we travel to the U.S. and meet with Donna Karan's designers. Then the design people start sending and receiving specifications and sending wool samples. Once the sample of wool and the design is approved, we have to coordinate who will dye the wool and who will produce the garment. Quality control is done on an individual basis with each artisan. So, the process is very lengthy and hard to coordinate."

Consequently, Manos' exports had been declining. The drop in foreign sales was primarily due to intense competition and increased buyer demands. Cooperatives had difficulty responding to rapid production requests and planning mechanisms were inefficient. The organizational culture gave greater priority to the problems of the artisans than the needs of the customers. For example, when an artisan had to attend to a situation in the home, she would temporarily stop working. "We cover for each other. We organize ourselves so as not to jeopardize the organization, but the person comes first and then the work," one of the artisans stated. While this priority was inherent in the culture and cooperative system, it was tremendously challenging for Manos to be successful in the new highly competitive markets. In addition, the South American economy had been struggling with severe financial and economic problems including double-digit (or greater) inflation rates.

Since Manos saw its niche in labor intensive products that were not easily replicated by machines, the most intense competition came from other low labor-cost countries. China for example, owing to low salaries, had produced similar handmade articles at substantially lower prices. Mr. Gioscia noted, "We wonder how China can produce the goods at such low prices which sometimes seem to be lower than the cost of the wool alone." With the lowering of international trade barriers, the demands of buyers for top line labels that had historically purchased Manos' products had grown more and more intense. Even though Manos had been able to establish close relationships with its clients, they believed that this was not a sustainable advantage in an environment of increasing competition.

Vertical integrations seemed improbable also. For a few years, Manos ran its own store in New York, but the bottom line was unsatisfactory, and the store closed. The result was that Manos only sold internationally when a design was requested by a brand name label, which then used their own name on the label (in particular Polo, Ralph Lauren,

ORGANIZATION STRUCTURE

"We, the members of Manos del Uruguay, think of ourselves as a "system", because Manos unites different organizational units (groups, cooperatives, and central services), with common objectives, united by a close interdependence." "We are interrelated parts that form a 'whole', one entity where each part is distinct, yet connected to the other."

In recent years, the cooperatives produced what was ordered by Central Services. The cooperatives received the design, a prototype with technical notes, and the production material from Central Services. Every artisan received salary and benefits from their cooperative. The cooperatives elected four representatives that participated on the Board of Directors.

Central Services had responsibility for product design, quality control and marketing. Product design was done exclusively by product development teams at Central Services. For the products made for sale under other labels, product development had typically been a very long process. Mr. Gioscia explained, "the process begins with Manos presenting colors, materials and models to designers from the clients, the designers then develop specifications, Manos makes a prototype, the client approves it or makes changes, we develop the final prototype and then assign it to cooperatives for production. Central Services makes payments to the cooperatives after receiving the completed products and verifying production quality."

Referring to the organizational structure of Central Services, Mr. Rodolfo Gioscia had said, "At the head we have the Board of Directors, formed by honorary members -- people who have a personal commitment directly related to the objectives of the business. They receive no pay and they include lawyers, accountants, etc. There are also four elected representatives (artisans) voted in by members of the cooperatives. In some cases they helped give shape to the committee and helped to determine its function; in other cases, they collaborated to gather specific knowledge essential for leading the organization. Mr. Gioscia is a non-voting member of the Board."

"Under the Board of Directors you find the General Manager, whose job is to guide the organization towards its objectives. Likewise the General Manager manages various day-to-day situations, and spends a large portion of time making business contacts, especially in the foreign market. Reporting to the general manager, are the manager of Administration and Finances, the Leader of Sales and Exports, and the Production Manager."

"The production manager is in charge of the quality. Each cooperative group has a leader or guide who reviews the quality of the products before they are sent to Montevideo. Once received at Central Services, garments are again inspected. If a garment is not of sufficient quality, the artisan does not receive payment for their work. Or, they may be given a chance to rework the garment. This is possible because Uruguay is a very small country. The farthest distance from a cooperative to Montevideo is only 200 miles."

Rodolfo Gioscia had been the General Manager of Manos del Uruguay since 1998. This position had represented a significant challenge for him because Manos was a nonprofit, co-op organization with a concept different from other companies that he had previously managed. Co-ops have significantly different risks and opportunities. One cannot manage a group of independent artisans in the same manner as regular, full-time employees. However, Rodolfo reflected that he accepted this position because "the high emphasis on individual, personal work and the co-operative culture were very motivating to me."

CURRENT SITUATION

By 1994, Manos del Uruguay had more that 800 artisans located throughout the country. Approximately 80,000 units of wool blankets, tapestries, garments, baskets, and rugs, all made from natural fibers, were sold in local and international markets.

Manos del Uruguay had received the support of several international organizations: the BID, for technical assistance and working capital; the Inter-American Foundation for the training of the artisans; and funds for the development of the cooperatives). There were also successful in obtaining a loan from the Banco de la Republica Oriental del Uruguay (BROU).

Manos had been successful at generating new job opportunities for women that lived in remote rural areas, such as Dragon, on the Brazilian border; to Paso la Crus on the Argentinean border; as well as regions close to the capital city of Montevideo. With their labor, the artisans of Manos del Uruguay preserved and promoted the traditional Uruguayan handcrafts that dated back to the birth of the country. Manos had continued to play a key role in the preservation of the history and traditions of rural life. Their marketing efforts helped ensure that other countries would know Uruguayan traditions for wool making and dying and their craftwork as well.

In 1994, the Uruguayan government declared a change in economic policies that included some progressive new priorities in the economic area. After 30 years of a relatively closed economy, Uruguay aimed for a deeper deregulation in trading policies and opened their markets for a more competitive economy. Efficient production and well-run organizations became essential to remaining competitive. Manos worked to penetrate new markets, faced new competition, and responded to new and greater client demands. Inexorably, Manos had to adapt itself to the changes thrust upon them by these new times without the help of a government policy that had specifically protected the artisans in the past.

"The invasion of all types of imported products, from the most sophisticated to the most simple, left less space for the relaxed paced independent artisans of Manos del Uruguay," was the comment heard most often during the mid-1990's. Manos rose to the challenge: artisans in 1999 produced almost three times as much per person as they had in the previous five years. Simultaneously, the number of participating artisans dropped. This was mainly a result of the emphasis placed on greater productivity as well as a moderate increase in the volume of sales.

The Manos organization also had evolved to include benefits such as paid vacations, bonuses, medical insurance, and retirement pensions for artisans. In the words of the general manager, "Our stores grew along with our sales organization. We now need to aggressively promote and market in all areas. These activities and goals are more and more necessary. We need new answers for new circumstances, continually adapting ourselves to the new situations."

By 1999, Manos del Uruguay consisted of only 350 artisans, grouped into 17 cooperatives from a variety of rural counties in Uruguay: Soriano, Tacuarembo, Florida, Cerro Largo, Flores, San Jose, Paysandu, Canelones, Rio Negro, Lavalleja and Durazno. Manos' products were many and varied including sweaters for men and women, capes, ponchos, blankets and bedspreads.

According to their web site in 2002, Manos' mission emphasized a focus on the customer. They wanted to achieve for their customers "excellent quality hand-knit or woven garments." Their web site also stated that their key objective was "to provide job opportunities and training to women in distant rural areas of the country."

All products were still made of 100% virgin wool, spun by hand and woven on a handloom. The designs were fashionable, original and creative - a trademark of the business, which identified the business not only on a national level but also internationally. Products were marketed in Uruguay through stores owned by Manos, four of which were located in Montevideo (Ciudad Vieja, Centro, Montevideo Shopping and Punta Carretas Shopping) and one in Punta del Este. Other stores included specialty boutiques in Mercado del Puerto in Montevideo, in the city of Colonia del Sacramento, in the city of Salto, in the spa Atlantida and in Piriapolis.

Throughout the years Manos had also continued to export to Europe, Japan and the United States. Manos has more than 20 years of experience selling their products in foreign markets ranging from Paris to Tokyo to New York. Manos del Uruguay had three alternatives for penetrating the North American market: specialized stores, name brand labels (e.g., Polo, Ralph Lauren, Michale Koors, Jhane Barnesand Donna Karan in New York), and department stores including Bloomingdale's and Nordstrom's. When products were made for other labels, Manos was competing directly with many other suppliers. The retail clothing industry has been historically fickle with many rapid product cycles. Major brands changed suppliers frequently. Mr. Gioscia noted "Manos is in a very fragile position when we sell in the USA under other brands, the clients can (and do) change suppliers very easily."

Mr. Gioscia described the production process. "The coordination of the production process is very difficult. For example, we travel to the U.S. and meet with Donna Karan's designers. Then the design people start sending and receiving specifications and sending wool samples. Once the sample of wool and the design is approved, we have to coordinate who will dye the wool and who will produce the garment. The quality control is done on an individual basis with each artisan. So, the process is very lengthy and hard to coordinate. The good thing about export business though is that you have to constantly prove and improve your quality."

In recent years, Manos' exports had been declining. The drop in foreign sales was due to a variety of reasons including intense competition and increases in buyer demands. Cooperatives had difficulty responding to production requests and planning mechanisms were inefficient. Mr. Gioscia also noted, "the organization culture gave great priority to the cooperatives and the problems of the artisans before the needs of Manos' clients." In addition, the South American economy had been struggling with severe financial and economic problems including double-digit (or greater) inflation rates.

Intense competition came from other countries too, especially China, which, owing to low salaries, had produced similar, handmade or machine made articles at substantially lower prices. Mr. Gioscia noted, "we wonder how China can produce the goods at such low prices which sometimes seem to be lower than the cost of the wool alone." The demands of buyers for top line labels that had historically purchased Manos' products has grown more and more intense. The only market niche left was for products with unique characteristics or features that could not be done by machines. "We rely heavily on close relationship with our customers," said Mr. Gioscia.

For a few years Manos ran its own store in New York, but the bottom line was unsatisfactory, and the store was closed. Manos then produced and sold internationally only when a design was requested by a brand name label, which used their own name on the label (in particular Polo, Ralph Lauren, Donna Karan New York, and Neiman-Marcus, among others.)

STRATEGIC ALTERNATIVES

During his weekend of thought and worry, Mr. Gioscia developed four alternatives which he presented to his Board of Directors the following week:

1) Continue working under existing brand name labels, but incorporate other types of products made by high-speed machines that would be more price competitive worldwide. This alternative would augment the competitiveness of the company and hopefully improve the volume of exports. On the other hand, this alternative required a large investment for three high-speed machines (approximately $100,000 per machine). High-speed production would also need to be centered in one location preferably Montevideo.
2) Increase the exposure of Manos in foreign markets with the goal of attracting and developing new sales channels including international distributors. This would require international trips to participate in trade shows, the need for a web site, and extensive R& D to determine which foreign markets to pursue.
3) Franchise Manos in markets that would know and appreciate the quality of Manos products. A good example would be to establish a store in Buenos Aires. Argentineans frequently travel to Uruguay for vacations and business. Many are already familiar with the Manos products and could be important clients for the stores in Argentina. A recent analysis shows that 20% of Manos sales in Uruguay were made to visiting Argentineans. However, franchising could rapidly increase demand beyond existing production capacity. Owing to the co-op nature of the organization, when an artisan had to attend to situations in the home, she would temporarily stop working. "We cover for each other. We organize ourselves so as not to jeopardize the organization, but the person comes first and then the work," one of the artisans stated. Failures to meet production volume and quality requirements when entering a large, important market could potentially curtail future expansion options.
4) Pursue slow, managed growth by carefully selecting and penetrating the most lucrative markets. In that way, Manos could develop international marketing experience and at the same time analyze and improve their production processes. This would allow them time to train more artisans and improve efficiencies to meet future growth and expansion efforts.

What should Mr. Gioscia recommend to his Board? What strategies can they pursue to turn around their weakening financial position? Does Manos need a new mission? What other alternatives should Mr. Gioscia put before the board?

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APPENDICES

Appendix 1: Financial Information

Table 1: Comparative Income Statement (in thousands)						
	1996	1997	1998	1999	2000	1996 to 2000
REVENUE						% Change
Sales-Local	1,500	1,800	2,100	2,000	1,950	23.08%
Exports	775	770	480	290	165	-369.70%
Bonuses	25	30	20	10	5	
Sales Discount	-80	-105	-132	-165	-130	
Net Oper Revenue	2,220	2,495	2,468	2,135	1,990	-11.56%
EXPENSES						
Sales Costs	760	910	1,100	1,200	1,270	40.16%
Export Costs	490	485	310	150	90	
Other	15	17	19	22	7	
Total Op Expenses	1265	1412	1429	1372	1367	7.46%
GROSS MARGIN	955	1,083	1,039	763	623	-53.29%
Admn. Expenses	860	960	1,000	1,019	1,038	17.15%
Depreciation	25	28	23	18	8	
.Total Admn Expenses	885	988	1023	1037	1046	15.39%
Operating Margin	70	95	16	-274	-423	-116.55%
Financial Expenses						
Interest	25	30	32	35	28	10.71%
Other	5	5	5	3	2	-150.00%
Total Fin. Expenses	30	35	37	38	30	0.00%
Net Profit/Loss	40	60	-21	-312	-453	-109.00%

Table 2: Comparative Balance Sheet						
	1996	1997	1998	1999	2000	1996 to 2000
Current Assets						%Change
Cash	125	141	149	170	162	22.84%
Accounts Receivable	365	440	477	492	475	23.16%
Total Current Assets	490	581	626	662	637	23.08%
Other Assets						
Inventory	150	140	140	130	140	-7.14%
Deferred Expenses	3	4	3	3	4	25.00%
Total Other Assets	153	144	143	133	144	-6.25%
Total Assets	643	725	769	795	781	17.67%
Liabilities						
Current Liabilities	283	185	200	220	225	-25.78%
Interest on Current Debt	30	21	29	30	31	3.23%
Total Current Liabilities	313	206	229	250	256	-22.27%
Long Term Liabilities	15	165	165	134	104	85.58%
Total Liabilities	328	371	394	384	360	8.89%
Shareholder's Equity	275	304	345	371	423	34.99%
Net Income	40	50	30	40	-2	2100.00%
Total Shareholders' Equity	315	354	375	411	421	25.18%
Total Debt & Shlders' Equity	643	725	769	795	781	17.67%

APPENDIX 2 - COUNTRY INFORMATION

Uruguay is located in southern South America between the much larger countries of Argentina and Brazil (see Appendix 3). Uruguay is slightly smaller than the state of Washington, U.S. The capital of Uruguay is Montevideo. Montevideo is located on the Rio de la Plata, a river that opens to the South Atlantic Ocean and separates Uruguay from Argentina.

Uruguay's 2001 population was just over three million. Nearly 25% of the population was fourteen years of age or younger while13% was older than sixty. The population growth rate was estimated to be less than one percent. The life expectancy was seventy-five years. The ethnicity was 88% white, 8% mestizo, and 4% black. Spanish is the official language of Uruguay. The literacy rate was very high, approximately 97%.

The climate of Uruguay is temperate to warm with freezing temperatures almost unknown. The terrain is mostly rolling hills and plains with a fertile coastal area. The country is 77% pastureland. Environmental issues include water pollution from the meatpacking and tannery industries and inadequate solid and hazardous waste disposal processes.

The government of Uruguay is a constitutional republic with three branches, executive, legislative and judicial. However, Uruguay's civilian government has been in place for only about 20 years. Uruguay was under military rule from the late 1960's until 1985. Uruguay is a member of many international organizations, notably: the United Nations (UN), MERCOSUR (a trade agreement between Uruguay, Paraguay, Argentina and Brazil), and the World Trade Organization (WTO).

Uruguay's economy includes an export-oriented agricultural sector, a well-educated workforce, relatively even income distribution, and high levels of social spending. After averaging an annual growth rate of 5% from 1996-1998, the economy declined due to decreasing demand from Argentina and Brazil, which together account for about half of Uruguay's exports. However, during the 1990's Uruguay's financial indicators remained more stable than those of its neighbors. In 2000, the GDP of Uruguay was estimated to be $31 billion, with a GDP growth rate estimated to be 1.1% for 2000, an inflation rate of 4.8% and unemployment rate of 14%.

Uruguay's exports in 2000 totaled $2.6 billion. Main export items were meat, rice, leather goods, vehicles, dairy products, wool and electricity. Uruguay imports road vehicles, electrical machinery, metal manufactures, heavy industrial machinery, and crude oil. Its imports in 2000 totaled $3.4 billion. Primary industries are food processing, electrical machinery, transportation equipment, petroleum products, textiles, chemicals and beverages.

According to Hofstede's national cultural dimensions, Uruguay is very high on uncertainty avoidance indicating people prefer to follow established rules and take fewer risks. It is also ranked relatively low on the masculine dimension indicating that quality of life is considered more important than financial success. Westerners often note this as a more relaxed approach to time and a higher priority on personal relationships and family. Uruguay is ranked medium on power distance and individualism dimensions indicating moderate acceptance of authority and individual achievements respectively.

APPENDIX 3 - MAP OF URUGUAY

JET BLUE: A NEW CHALLENGER

Thomas M. Box, Pittsburg State University
Susan E. Saxton, Capella University

CASE DESCRIPTION

The primary subject matter of this business policy case concerns the competitive strategy and background of a new, very successful airline –JetBlue Airways (JetBlue). The time frame of the case is from the firm's inception to the end of fiscal year 2002. The case has a difficulty level of four – five, appropriate for senior level undergraduates or first year MBA students. The case is designed to be taught in one seventy minute class and will require approximately two to three hours of outside preparation by the students.

CASE SYNOPSIS

JetBlue is a new, very successful low cost airline. In their first full year of operations (2001) they achieved a $32 million net profit on revenues of approximately $320 million. This is particularly notable in that the entire industry lost approximately $10 billion during the same year. JetBlue flies point to point routes – much like Southwest Airlines and offers distinctive service features –reserved seating, leather seats, seat back TVs (24 channels) and very customer oriented personnel.

JetBlue, at least superficially, appears to be an example of a Low Cost Leader. In their initial foray into the New York to Florida market they offered ticket prices about half of the existing competitor's ticket prices and a serious focus on customer convenience – including such things as no mandatory Saturday night stay to get the lowest ticket price. All tickets are sold online or through a unique Salt Lake City reservation system. They were the first airline to introduce electronic ticketing and their use of Information Technology is extensive. Jet Blue's founder – David Neeleman – is a young (43 year old) career entrepreneur with dyslexia. He is a practicing Mormon with nine children and prior to founding JetBlue had experience with two other airline startups.

INTRODUCTION

On February 11, 2000, JetBlue launched operations with its inaugural flight from New York's John F. Kennedy Airport to Fort Lauderdale, Florida. With $160 million in startup capital, David Neeleman, CEO and founder, was flying in the face of conventional wisdom. Since deregulation of the U.S. airline industry – mandated by Congress in 1978 – the market had seen the demise of 87 new airlines due to cost pressures and unremitting competition.

Neeleman was a young, successful entrepreneur with two prior airline startups under his belt. In 1993 Neeleman sold his first airline (Morris Air) to Southwest Airlines for $130 million. After a very short five month tenure with Southwest Airlines where Neeleman reports "They (Southwest executives) were as sick of me as I was of them", he was fired and forced to sign a domestic non-compete agreement. Recruited by investors in Canada, he cofounded WestJet where he employed many of the tactics and strategy he had learned at Morris Air. Neeleman also created Open Skies (based in Salt Lake City) an accounting and reservation software firm serving the airline industry. In the late 90s Neeleman sold most of his interest in WestJet and began accumulating venture capital funding and regulatory permission to begin JetBlue.

OPERATING STRATEGY

JetBlue is a low cost, highly competitive airline, serving selected East Coast and West Coast markets. Aircraft are exclusively Airbus A 320s. These 162 seat planes have a slightly lower operating cost than Southwest Airlines' Boeing 737s and are equipped with leather seats and seat back TVs. No meals are served – even on transcontinental flights – thus saving the cost of meals and galley equipment. All planes in the fleet have been purchased new from Airbus and are decorated in a distinctive blue cabin interior. Two of the distinctive competencies are JetBlue's targeted gate turnaround time of 30 minutes and its choice of airports – generally away from the congestion of the major airports.

JetBlue has a unique approach to personnel. All pilots, for example, are required to interview with top executives prior to being hired. Competency as a pilot is not enough to secure a position – attitude is evaluated and only those with attitudes fitting the JetBlue culture are employed. All personnel are indoctrinated with a sense of providing superior customer service. Neeleman has said on numerous occasions that, "We don't want jaded people working here. If you don't like people or can't deal with rude customers, you'll be fired." That sort of customer service attitude manifests itself in many ways. On one occasion when a JetBlue plane had a rough landing at JFK, all passengers were handed free roundtrip tickets on JetBlue. On another occasion a pilot on a delayed flight walked into the cabin and offered his personal cell phone to the passengers so they could make arrangements. On a number of occasions when weather delays resulted in late departures, Neeleman and other executives called passengers at home to inform them of the delay. This sort of customer service results in high levels of customer satisfaction and Jet Blue – thirteen months after its first flight – won the designation as #2 Domestic Airline in the 2001 Zagat Airline Survey.

JetBlue has also utilized Information Technology (IT) as an important aspect of its Operating Strategy. Reservations are handled either online at its website or by phone with a unique reservation system based in Salt Lake City (Neeleman's hometown). Reservation agents are independent contractors, working from home, on equipment provided by JetBlue. The advantage of this arrangement is the life style (and quality of work life) afforded to the reservation staff and the avoidance of capital investment in reservation facilities. JetBlue does not book flights through travel agents and, thus, avoids the expense of travel agent's fees. IT is also employed in the cockpits of their planes. All flight manuals are on CDs and each pilot is equipped with a notebook computer. This makes it easier, faster and cheaper to update manuals and avoids the necessity of providing storage space and administrative support for bulky traditional manuals.

Security, too, has been augmented at JetBlue. Following "9/11" they were the first and one of the few airlines to install security doors in the cockpits. Additionally, they were the first airline to install four security cameras in the cabin, which the pilots can view from the cockpit. The added expense for these security measures is probably recouped in incremental sales to airline passengers who are, quite naturally, concerned about airline security following the devastating tragedy of "9/11".

DAVID NEELEMAN:

Forty three year old David Neeleman, CEO and Chairman of the Board of JetBlue, has been a life-long entrepreneur. As a Mormon, he was required to work as a missionary in Brazil for a year. Of the $2500 of expense money supplied by his father, Neeleman managed to save $1300. Neeleman's father, Gary, attributes his entrepreneurial spirit to Neeleman's grandfather who opened the first convenience store in the United States on State Street in Salt Lake City.

Neeleman, one of seven siblings, has nine children of his own. A staunch Mormon, he neither drinks nor smokes and travels around New York City on the subway. He has a number of interesting personal characteristics. Claiming dyslexia, he focuses on innovation and creativity – something often seen in dyslexics. He is a "fountain" of new ideas and clearly thinks "outside the box" – sometimes to the distraction of friends and fellow executives. His college career was not a glowing success – he dropped out of the accounting program at the University of Utah, founded a tour business and quickly joined with two partners to start Morris Air.

He has an interesting approach to hiring executives for Jet Blue. One of his early hires was Ann Rhodes – head of HRM at JetBlue, but the executive that actually handed him his "pink slip" when he was fired at Southwest Airlines. Dave Barger, JetBlue's President, was formerly vice president for the Newark hub of Continental Airlines. Thomas Kelly, Executive Vice President and General Council, was an executive with Open Skies and Morris Air. John Owen Is Executive Vice President and CFO. He had been Treasurer and Vice president for Operations Planning and analysis for Southwest Airlines.

Testifying before the Senate Commerce, Science and Transportation Committee on March 13, 2001, Neeleman articulated the rather unique operating Philosophy of JetBlue:
JetBlue Airways is New York's low fare hometown airline.

JetBlue has a unique business model encompassing a dedicated staff, reserved seating, numerous amenities, no Saturday night "stays", very new aircraft, the highest utilization rates in the industry and extremely competitive low fares.

JetBlue serves a number of important markets in upstate New York and New England which previously had no direct to New York air service or extraordinarily high ticket prices.

FINANCIAL RESULTS

JetBlue's financial results have been nothing short of miraculous. Total Revenue in 2001 was $320 Million. With cost of revenue at $186 million, gross Profit was $134 million. Net Income from continuing operations was $38.5 million. It should be noted that this was a remarkable accomplishment during 2001 when the US Airline industry, as a whole, lost more than $10 billion.

Performance in 2002 was even better than 2001. Net income increased to $54.9 million on revenues of $314.8 million. Cost per available seat mile – a major performance metric in the airline industry – was 6.43 cents compared to an industry average of 9.58 cents.

ROUTES FLOWN

JetBlue began operations on February 11, 2000 with daily flights between JFK and Fort Lauderdale. During calendar year 2000, JetBlue added flights to Buffalo, NY, Tampa, FL, Orlando, FL, Ontario, CA, Oakland, CA, Rochester, NY, Burlington, VT, West Palm Beach, FL, Salt Lake City, UT and Fort Myers, FL. By the end of 2000, JetBlue had 10 Airbus A320s flying.

By November 9th, 2001, JetBlue had taken delivery of 10 additional Airbus A320s and had added daily flights to Seattle, WA, Denver, CO, Long Beach, CA, New Orleans, LA and Washington DC. A notable "first" in the industry was JetBlue's installation of bullet-proof, dead bolted cockpit doors in the entire fleet by November 1 – only a month and a half after the infamous "9/11" terrorist attacks on the Pentagon and New York City.

Also during 2001, JetBlue established its second focus city – Long Beach, CA and began "head on" competition with Southwest Airlines for the West Coast market. Jet Blue's entry into the West Coast market prompted Southwest Airlines to begin offering $19 one-way fares to Las Vegas from four California airports.

By the end of 2002, JetBlue was flying to 17 cities from JFK and 4 cities from its new Long Beach hub.

DISCUSSION QESTIONS

Go to the JetBlue web site (http://www.jetblue.com/) and the American Airlines web site (http://aa.com/). Pick cities serviced by both JetBlue and American Airlines, select travel dates and number of passengers and determine the difference in fares. What is the percentage difference? What does this suggest?

Go to http://finance.yahoo.com and look up the information on JetBlue. Which of their financial ratios are significantly different than the industry? What are the implications?
Do a SWOT analysis on JetBlue. What are the most important SO strategies suggested by the SWOT analysis? Are there any WT strategies?

Which of Porter's generic strategies does JetBlue seem to be following? In what ways might their generic strategy be somewhat different than what Porter suggests?

Conduct a Five Force Analysis of the airline industry. How do you assess the threat of New Entrants?

On June 10, 2003, JetBlue announced an order for 100 new EMBRAER 190 aircraft. Does this new equipment order suggest a new business model? What are the risks?

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HARDEE'S RESTAURANTS: STUCK IN THE MIDDLE OR CREATING COMPETITIVE ADVANTAGE?

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CASE DESCRIPTION

Business-level strategy is the primary focus of this case. Secondary issues examined include strategic groups and strategic reorientation. The case has a difficulty level of four, appropriate for senior level courses. The case is designed to be taught in one class hour and is expected to require one hour of outside preparation by students.

CASE SYNOPSIS

On January 21, 2003, Andrew Puzder, CEO and president of Hardee's Food Systems, Inc. stated, "We are distinguishing ourselves from the competition as the premium burger specialist among quick-service restaurants." But how much value can you really add to a hamburger? Clearly companies like Outback Steakhouse, Cracker Barrel, and Shoney's offer menu selections similar to Hardees' "Thickburger," but these restaurants set themselves apart by offering a casual dining atmosphere, a wide selection of entrées beyond hamburgers, and table service rather than order counters. On the other end of the spectrum are fast food restaurants such as McDonalds, Burger King, and Wendy's, Hardee's traditional competitors offering low cost convenience meals. Hardee's Thickburger initiative goes beyond efforts at differentiating itself from its competition. Instead, the company is taking actions it hopes will move it into a new strategic group where competition is less intense. This case examines the difficulties in strategic reorientation when such reorientation requires a business-level strategy that moves a firm from one strategic group to another. Students must decide if Hardee's new initiatives will be successful or whether the fast food franchise will be "stuck in the middle" with neither a feasible low cost nor a feasible differentiation strategy.

INTRODUCTION

After struggling with the intense competition in the fast food industry, Hardee's struck upon what seemed to be a cure for its mediocre performance of the last few years. Its Six Dollar Burger campaign in 2002 attracted consumer attention to this struggling franchise. The ability to quickly get a quality hamburger similar to what one might expect at a full service restaurant such as Appleby's or TGIFriday's seemed to appeal to customers with little time but discretionary tastes. The success of this initiative compelled Hardee's to think deeply about where it had been and where it hoped to be in the future. On January 21, 2003, Andrew Puzder, CEO and president of Hardee's Food Systems, Inc. stated, "We are distinguishing ourselves from the competition as the premium burger specialist among quick service restaurants."

BACKGROUND

CKE Restaurants, Inc. is the parent company of 1,000 Carl's Jr, restaurants, 97 La Salsa Fresh Mexican Grills restaurants, and 2,181 Hardee's restaurants. The combined revenue was nearly $3 billion for the fiscal year ending January 2003. While these are substantial revenues for a franchisor, the company has struggle recently and has not earned a profit since 1999. The company had a net loss of $150 million for 2003. After extrapolating a value for a procedural change in accounting which had a significant negative financial impact, the St. Louis based Hardee's Food Systems, Inc. segment, a wholly owned subsidiary of CKE, lost $10.5 million in fiscal year 2003 after losing $76.9 million in fiscal year 2002.

The restaurant chains within the CKE parent are franchisers, with only limited company ownership of retail stores. As with all franchises, one of the corporate parent's primary objectives is the proliferation of the franchise brand that provides desired escalation of revenue through franchise fees. Because Hardee's accounts for the "lion's share" of both retail stores and revenues for CKE Restaurants, the strategy that Hardee's employs will have a substantial financial impact on CKE.

Historically, Hardee's has been a quick service (fast food) franchise, competing mainly on price against rivals McDonald's, Burger King, Wendy's, and other fast food chains. Although each chain attempts to differentiate its products, imitation by competitors is swift, prohibiting any single chain from gaining a competitive advantage based on product attributes. Intense competition within the fast food market has forced these restaurants to focus on operating efficiencies to drive down costs in an effort to maintain acceptable net margins. Brad Haley, Hardee's executive V.P. has felt the pricing pressure in the fast food segment: "We can't compete when everybody is selling sandwiches for 99 cents. Nobody can. Even the big guys are losing at that game."

Combined with recent diminishing profit margins for the entire quick service restaurant industry, Hardee's recent losses in the past two years have forced the chain to reconsider its strategy. Rather than competing on price against its traditional rivals, Hardee's has embarked on a strategy intended to vastly differentiate it products from the traditional fast food items. In October 2001, Hardee's contracted with Mendelsohn|Zien, a Los Angeles based advertising firm to help reposition its brand. Richard Zien, managing partner with Mendelsohn|Zien noted, "No one has been able to unlock the door of advertising success at Hardee's in many years. Inconsistent advertising strategies have resulted in a variety of messages which may have served to confuse Hardee's customer base."

Soon after contracting with Hardee's, Mendelsohn|Zien recommended that the restaurant chain introduce the "Six Dollar Burger". In November 2001, Hardee's introduced this 1/2 pound, 911 calorie, $3.95 hamburger, which quickly became the fastest growing burger among all fast food chains. In 2002, the "Six Dollar Burger" won the Restaurant Business Award for Best New Burger. CKE Restaurant Corporate Affairs Director Larry Brayman noted that not only was the "Six Dollar Burger" recognized among industry critics, but also by customers. "We are very pleased to have introduced a product that has received not only critical acclaim with the Best Burger Award for 2002, but also the approval of our guests."

THE RESTAURANT INDUSTRY

According to the Bureau of Economic Analysis, restaurants have a significant impact on the overall health of the U.S. economy. Considering both direct and indirect employment, this industry supports a greater number of jobs than any other industry in the nation's economy. Other than the government, the restaurant industry is the nation's largest employer with over 11.7 million employees. However, restaurants are extremely labor intensive. In 2001, sales per full time equivalent employee were $55,351, which is notably lower than most other industries. Again for 2003, the National Restaurant Association reported that employee recruitment and retention remains the number one challenge facing fast food (quick service) restaurant operators. Due to its low-skill, labor-intensive environment, the industry employs a workforce with a high turnover rate and demographically composed of a majority of young, single, female, part-time employees averaging 25.6 hours per week. Consequentially, approximately one-third of all adults in the United States have worked in the restaurant industry at some time in their lives.

However, with the majority of workers viewing their "tour of service" as only temporary, opportunities for advancement are superior to most other industries as evidenced by a rate of eight out of ten salaried employees starting their careers as hourly workers.

With over 300,000 restaurant companies, the industry is mature and extremely competitive. Although there are differences among specific companies, the industry can be divided into two basic groups-full service (casual dining) and quick service (fast-food). The full service sector tends to have more points of differentiation including family atmospheres such as Denny's and Shoneys, buffets such as Quincy's and Golden Corral, combination full service restaurants with bars such as Appleby's, ethnic cuisine such as China Palace and many more.

The fast food sector is geared towards quick, inexpensive meals and includes made-to order sandwiches such as Subway, Mexican food such as Taco Bell, chicken entrées such as Kentucky Fried Chicken and Popeye', pizza such as Domino's and Pizza Hut, the hamburger chains such as Hardee's, McDonalds, and Wendy's, and a variety of others. Both the full service and fast-food segments include locally owned restaurants typically managed by a single individual. Currently, seven out of ten establishments are single-unit (independent) operations with less than twenty employees. Historically, these local restaurants always compete with the national chains by creating menus catering to local tastes and/or building strong personal relationships with local repeat customers.

Because the restaurant market is mature and annual industry sales growth is relatively small at about 4.5%, it is increasingly difficult to earn above average returns. Economic downturns tend to impact fast food as well as full service restaurants as indicated by the posted 2002 growth rate of 4.1% compared to 4.8% for full service. In 2000, the average check per customer at fast food was $3.71. Whereas, the average per person price for a meal at a full service restaurant is from $9.96 for casual dining to $24.59 for upscale. The total market for dining away from home in 2000 was over $241.7 billion. As projected for 2003 by the National Restaurant Association, the fullservice sales should reach $153.2 billion and the quickservice revenue should exceed $120.9 billion.

TYPE of SERVICE	2000	2003
	Sales ($Billion)	Sales($Billion)
Fullservice	134.30	153.2
Quickservice	107.40	120.9
Total	241.70	274.1

Although in 2002, the average U.S. household spent $2,137 at restaurants annually, consumers become more price sensitive during economic downturns. The way households divide their purchases between the full service and fast food segments may change, making fast food restaurants viable, less expensive substitutes. Or, the reduced discretionary income may cut into the customer counts - especially for fast food restaurants. Currently, both dynamics of consumer behavior are impacting the industry, but full service restaurants have a slight advantage in terms of gross sales and profitability. In 2002, full service restaurants average $650,000 per restaurant while fast food restaurants average a little less at $585,000. Also, full service restaurants posted an average pretax income of 6% versus 5% for the fast food segment.

Other market factors bearing on the fast food segment are: a) consumer tastes are slowly evolving toward a desire for more healthy meals. There is increasing pressure on fast food chains to offer low fat, nutritious alternatives. b) technology is changing the way Americans shop and the restaurant industry is beginning to feel the impact of this shift in consumer behavior. Over fifty six percent of all restaurants currently have web sites. c) the American population is aging which will impact the available low wage labor market and the customer behavior trends.

When it comes to restaurant spending, household income is one of the most influential characteristics. Households with an average income of more than $70,000 make up only17 % of the American households yet account for more than twenty six percent of total spending on food away from home. In general, expenditures on food away from home rise dramatically for households that bring home more than $30,000 in pre-tax income.

Annual pre-tax Household Income	Per-capita avg. spending on food away from home in 2000	Percent of American Households in 2000	Approximate Population In 2000
$70,000+	$ 1,460.00	26.3	74,110,627
$50,000 - $69,999	$ 980.00	15.6	43,959,155
$40,000 - $49,999	$ 920.00	12.0	33,814,735
$30,000 - $39,999	$ 820.00	11.0	30,996,840
$20,000 - $29,999	$ 650.00	12.8	36,069,050
$15,000 - $19,999	$ 580.00	6.5	18,316,315
$0 - $14,999	Not Available	15.8	44,522,734
Totals	$855 Average	100.0	281,789,456

Age of the head of household also is another of the most influential characteristics. Households with the head at an average age greater than 45 years but less than 65 years spend approximately twenty five percent more per-capita than age groups on either side.

Year 2000 Age of Head of Household	Per-capita avg. spending on foodaway from home	Percent of American Households	Approximate Population
Under 25	$ 925.00	6.8	19,161,683
25 - 34	$ 775.00	23.4	65,938,733
35 - 44	$ 795.00	25.2	71,010,943
45 - 54	$ 1,030.00	22.6	63,684,417
55 - 64	$ 1,010.00	5.9	16,625,578
65+	$ 750.00	16.1	45,368,102
Totals	$855 Average	100.0	281,789,456

STRATEGIC REORIENTATION

This success with its initial attempt to distinguish Hardee's from its competitors gave the company confidence to continue with a strategic reorientation of the entire business. The "Six Dollar Burger" was the precursor to a new direction intended to reposition the company within the industry. If it could successfully draw a line between its products and those of traditional fast food competitors, perhaps the company could stem the losses of recent years by adding value to what was, for the most part, a previously undifferentiated product-the common Hardee's hamburger. By setting itself apart, Hardee's hoped to reduce the price competition that had helped drive down its profitability. By competing on product attributes-fast food hamburgers that tasted more like an Applebee's or a TGIFriday's hamburger-Hardee's hoped to exploit a market niche that had been previously ignored by the industry.

To complement its new product line, Hardee's has begun remodeling the interiors and exteriors of many of its restaurants. This "Star Hardee's Program" includes new red signs with a star logo to replace the orange signs with which customers had previously associated with Hardee's. The company projects that all company-owned stores will be converted to Star Hardee's Program and franchisees will be converted by the end of 2004. The next step of this remodelling effort is a yet unannounced prototype design for the restaurant. The phenomenal success of the "Six Dollar Burger" encouraged Hardee's to forge ahead with its plan to reorient the company's strategy. By adding value to its products, the goal was to move away from the competitive rivalry inherent in the price sensitive traditional fast food market segment. To build on the success of the "Six Dollar Burger" and further set itself apart from its competitors, the new Thickburger line was introduced at the same time that 40 items were eliminated from the menu. This included 1/3 pound hamburgers, cheeseburgers, bacon burgers, and chili cheeseburger in addition to a 1/2 pound grilled sourdough burger. Hardee's top of the line Thickburger was a 2/3 pound, 1,088 calorie hamburger. A key feature of this line was that each hamburger was made from Angus beef, a premium source of ground beef. The added cost of Angus beef makes Thickburgers, ranging in price from $2.39 to $4.95, somewhat higher than competitors' hamburgers.

The new tag line in Hardee's advertising, "Hardee's: Making the last place you'd go for a burger, the first," made it clear that the company considered its new product line more than just a menu change, but instead an about face from its previous position in the industry. Hardee's CEO Puzder announced that "a premium product strategy is…being implemented at Hardee's. Over time, we hope this change-together with our continued focus on quality, service and cleanliness-will help reverse the public's perception of Hardee's as the discount variety brand to the place to go for best-in-class premium burgers. If we're successful, our strategy should build on the brand's already strong breakfast business by bringing in new customers for lunch and dinner." Executive V.P. Haley puts Hardee's new strategy succinctly: "It's not fast food and it's not sit-down restaurant food," Haley said. "It's something in between. That's what we're trying to target."

THE CURRENT CRISIS

Although it is too early to know how well Hardee's strategy will work long range, so far revenues are slumping. As of the 16 weeks leading up to May 19, 2003, gross revenues had decline 1% compared to the same period in 2002. Market share had not increased despite an aggressive advertising campaign and minor store remodeling. The company must consider its options. Is this a situation where patience will pay off once its aggressive advertising brings in more customers? If so, how long should the company wait? Has Hardee's been misguided in believing it set itself apart from its rivals with its new menu? Should Hardee's increase its differentiation beyond its menu and remodeling efforts by doing away with the order counter? If the new menu does not eventually increase revenue and net income, should Hardee's return to its original menu and keep competing on price with the other fast food chains? President and CEO Andrew Puzder is certainly struggling with these issues. What should be his next?

GROWTH FOR TIFFANY & CO.

Thomas Bertsch, James Madison University
Debra Wiseman, Rugged Wearhouse

CASE DESCRIPTION

This case focuses on the strategy needs of an upscale retailer. The subject matter is appropriate for courses in retailing, marketing strategy, marketing management, and merchandising. The case is suitable for junior and senior undergraduate students and has a difficulty level of 4/5. It can be used for a 75-minute class discussion session, a take-home exam, or as the basis for team oral presentations.

CASE SYNOPSIS

Tiffany & Co. has stores in more than 20 countries. Its retail activities focus on upscale customers, high quality-products, extensive services, premium prices, fashionable locations, sophisticated promotions, and prestige image. Management wants the company to become the preeminent jewelry retailer in the world. Consequently, adjustments are needed in strategy. Students are asked which changes should be made in Tiffany's publics, products, places, prices, promotions, performances, processes, and providers.

Students working with this case will gain increased knowledge, skills, and practical experience. Specific knowledge topics include: image positioning, market segmentation, product branding, service opportunities, pricing strategy, merchandising, store site selection, promotion media selection and message appeals, distribution channel integration, and performance measures. Skill building opportunities include: logical problem solving, oral communication, and written communication. Important experiential learning opportunities are: informative and persuasive speaking, business report writing, strategy integration, and teamwork.

BACKGROUND

Charles Tiffany and John Young founded "Tiffany & Young" in New York City during 1837. The retail store provided stationery and "fancy" things at fixed prices on a cash only basis – no haggling, no credit, and no products taken in trade. Although the retailing strategy was unusual and risky, the store became a success. In 1853, Mr. Tiffany bought full ownership of the growing business and changed its name to "Tiffany & Co" (Hoover's, 2004).

Today, the company has stores in more than 20 countries. Tiffany's retail activities focus on upscale customers, prestige products, extensive services, premium prices, fashionable locations, sophisticated promotions, and a prestige image (Business, 2004). The retailing strategy involves very diverse publics, products, places, prices, promotions, performances, processes, and providers.

PRIORITIES

Management wants the company to become the most respected jewelry retailer in the world. To achieve that end, company leadership intends to expand into more geographic markets and to add related product lines. At the same time, management intends to increase shopper awareness of its competitive advantages for shopper satisfaction. Also, management wants to improve the company's retail performance in product demand forecasting, new product development, product logistics, and merchandise display (Tiffany, 2004).

PUBLICS

Tiffany & Co. appeals to people seeking distinctive, prestigious products for personal use and for gift giving. It attracts high-income shoppers, fashion leaders, celebrities, royalty, curious shoppers, and tourists. The luxury products market has evolved into distinct segments that are very important to Tiffany. The "achievers" want luxury merchandise and have the money to pay for it. The "aspirants" want affordable, near-luxury items that offer high quality and the mental satisfaction of association with a luxury brand. Young females want jewelry that looks like what celebrities are wearing. Also, wealthy women who buy luxury jewelry for their own use tend to buy more colorful items than do male gift givers (Staff, 2003).

The company sells to businesses, governments, and not-for-profit organizations that want to give distinctive gifts or trophies. However, the employee performance award market segment is no longer served. Tiffany & Co. also sells some of its brand name products to other distributors that resell the items. In addition, the company targets fine arts groups, educational institutions, and environmental preservation organizations through its benevolence activities. It seeks to "give back" to society through its financial donations, fund raising events, and merchandise gifts.

PRODUCTS AND SERVICES

Tiffany offers more than 2,000 products. However, its major product lines are in jewelry. Other product lines include china, crystal, sterling silverware, timepieces, writing instruments, fragrances, and fashion accessories (Yahoo! Finance, 2004).

Tiffany sells merchandise under manufacturers' brand names, its own brand names, and designer collection names. The company offers approximately 100 brands from other companies.

Its own brand names include: American Garden, Atlas, Back To Glamour, Faraone, Fireworks, Intaglio, Lucida, 1837 Collection, Selections, Streamerica, Tesoro, and Trueste. The company also uses trade names and trademarks that are based on the company name: Tiffany & Co., Tiffany Blue, Tiffany Blue Box, Tiffany Classics, Tiffany For Men, Trueste by Tiffany, T-C-O Letters that overlap, and T & Co (Tiffany, 2004).

Tiffany's designer jewelry collections are: Paloma Picasso (daughter of the famous artist, Pablo Picasso), Elsa Peretti, and Jean Schlumberger. Tiffany's sterling silver flatware carries the company name and includes extra thick sterling silver. Tiffany offers twelve highly respected brands of china: Arbor, Audubon, Band, Celadon, Federal, Holiday, Moderne, Nature, Palladium, Palm, Trellis, and Weave (Tiffany, 2004). Tiffany's leaded crystal includes a California safety warning; however, most states and foreign countries consider the lead exposure to be well within safety limits. Also, leaded crystal has a reputation of being superior quality.

Tiffany's line of timepieces includes clocks, pocket watches, and wrist watches. However, wrist watches have the greatest demand. The wristwatch assortment includes small and large sizes, for males and females. The watchcases come in stainless steel, gold, and platinum. Watch faces are offered in round and rectangular shapes. Watch bands are available in bracelet style, alligator or buffalo skin, and many other exotic materials. The watch movement choices include: battery, self-winding, mechanical winding, stopwatch feature, month/day/date feature, and moon phase feature. The precision watch line even includes watches that adjust for the pull of gravity (Tiffany, 2003). Tiffany also offers scents in spray and eau de toilette, for women and men. The fragrances are offered under three brand names based on the Tiffany name.

Companies in other industries, such as furniture, apparel, and yachts, use the Tiffany name. However, the Tiffany company name, trademark, and brand names are registered – which provides legal protection, competitive distinction, and company identification.

Tiffany's retail stores offer: credit, confidentiality of personal information, gift certificates, gift registry, return and exchange privileges, jewelry appraisal, merchandise repair, and product information. In addition, they offer: personal shopping by appointment, custom product design work, engraving by hand, and shipping within the country. The retail chain also offers parties for customers and workshops on how to select, clean, use, and protect the finish on merchandise.

PLACES

Tiffany is highly selective in adding retail store locations. For example, it adds only three to five new stores in the United States each year. Overall, it has more than 150 retail store locations in the United States and foreign countries (Business, 2004).

Although uniformity among stores could help convey a consistent image, Tiffany stores differ greatly in their appearances. Most of the stores are one-story high, but some are several stories high – as in Chicago. Most have ground-level entrances, but some do not – as the King of Prussia

Mall location in Pennsylvania. Some have earth-tone marble store fronts, and others have gray slate fronts – as in New York City. Some have the entrance centered on the front façade, and others have it diagonal, on a corner of the building – as in Palm Beach, Florida. Some even operate within other stores, such as inside Mitsukoshi Department Stores in Japan (Google, 2004).

Tiffany does retailing through more than its physical stores. The company offers on-line buying from its web site, web sites of its individual stores, and e-mail contacts. The company also offers products through mail order catalogs.

PRICES

Tiffany uses fixed prices for its merchandise worldwide. However, price levels in foreign currencies and different nations are adjusted for long-term currency exchange rate changes, local market competitive prices, and gross margin maintenance.

The company offers a wide range of price choices in many product categories. For example, earrings range from approximately $110 to $32,500. Watches are about $1,250 to $10,350. Necklaces are approximately $100 to $165,000. Wedding bands are about $225 to $5,600. Engagement rings range from approximately $970 to $1,000,000. Of course, tax is extra. Tiffany offers merchandise at prices from less than $75 to $1,000,000 (Tiffany, 2004).

Tiffany uses prestige pricing, which helps to reinforce its exceptional quality image. Unfortunately, many companies sell “replicas” and “facsimiles” of Tiffany designs, which undercut company sales and reputation. For example, one Japanese-based company offers a “look alike” watch, including the Tiffany & Co. name on it, for $240 and claims that the genuine Tiffany watch retails for $3,450. Another problem is that imitations may be sold or resold on the Internet as being legitimate Tiffany merchandise. Tiffany stores may then seem greatly overpriced, or the company may be blamed for the poor quality of some imitations.

PROMOTIONS

Tiffany uses advertising, direct marketing, public relations, and personal selling for its promotional efforts. The company uses several product message appeals in its promotions – such as: precision, innovation, refinement, fine craftsmanship, patented designs, quality awards, museum quality, exacting specifications, long history, integrity, and Swiss manufacturing. It also uses several benefit message appeals – such as: pleasure, special reward, elegance, and extraordinary comfort. In addition, the company promotes which distinctive customers it has served: The United States White House, the National Football League, royalty, designers, celebrities, museums, and art collectors (Tiffany, 2003).

The company’s distinctive blue color is used on its shopping bags, gift boxes, table displays, catalogs, brochures, and other promotional materials. It provides a distinctive, unifying theme.

Tiffany advertises through its paper catalogs, brochures, on-line catalog, and individual store web sites. Tiffany's public relations activities include donations by its foundation to not-for-profit organizations. It also sponsors special events that support environmental preservation efforts and fine arts education.

Store atmosphere is upscale, coordinated, and comfortable for shoppers. The entry door is propped open at some mall locations, to invite visits, but kept closed at on-street entrances. Some Tiffany windows show products on display within the store, such as dinner table arrangements of crystal, china, and silverware. Smaller display windows have a closed back panel, to focus attention on merchandise. For example, window displays at some locations show jewelry that is artfully displayed on color-coordinated fabric, feathers, and plumes. Other locations show a stream of butterflies above a display of dinner china (Google, 2004). Some store interiors include color-coordinated carpeting, ceiling, wallpaper, and display cases. Soft, "easy listening" music may play in the background. Some floor layouts provide a free flow of shoppers around display cases, and in front of built-in wall display cabinets. Tiffany conveys an impression of merchandise prestige and importance by widely spacing jewelry in display cases. Some lighting comes from recessed ceiling lights, and indirect lighting in display cases. Furnishings include couches and chairs, artwork hanging on walls, and tabletop artwork – such as oriental style vases with flower arrangements. The price tag on most merchandise does not show, which helps focus attention on products rather than on prices and provides an opening for shopper-employee communications.

Tiffany's in-store sales people are polite, friendly, attentive, and helpful. They speak clearly and look directly at the shopper. They dress in upscale business casual, which helps build a "comfortable" relationship with shoppers who are typically dressed casually. When a prospective customer asks to see a piece of jewelry more closely, the sales person may display it on a black, velvet pad. That presentation style helps accentuate the brilliance of gems and metals reflecting the ceiling lighting.

Tiffany also hosts many special events – such as: fine arts performances, black-tie receptions, high society fundraisers, museum exhibits, and upscale bridal shows. Such evens are typically sophisticated, elaborate, distinctive, and worthy of news media coverage. For example, when Tiffany introduced a new table setting show in New York, a cocktail reception was held. Young musicians from the Julliard School of Performing Arts gave a concert for the guests. Then, cultural leaders from the area displayed four table-setting arrangements that they had created. The special event also included fund raising activities for the Julliard School and recognition of distinguished Julliard alumni (Business, 2004).

PERFORMANCES

Tiffany's U.S. retail sales account for approximately 48% of its total retail sales revenue, and foreign retail sales are about 40%. Direct marketing accounts for more than 11% of the company's retail revenue, and specialty retailing accounts for about 1%. Its total retail sales are projected to be more than $2 billion next year. Tiffany gets approximately 80% of its retail sales revenue from jewelry, and most of that comes from diamond jewelry. Its retail performance rates are approximately 63% gross margin, 23% operating margin, 37% tax rate, and 11% net profit margin (Hoover, 2004).

Tiffany's retail sales are sensitive to many environmental influences. For example, how much it sells is affected by growing competition for luxury markets and economic growth-decline cycles. When items sell is affected by holidays and changes in currency exchange rates. Which products are sold is influenced by celebrity product use, discretionary income, and fashion trends (Yahoo! Finance, 2004).

PROCESSES

Tiffany & Co. has operating units in mining, processing, designing, producing, testing, distributing, and retailing. Its holding company unit handles financial allocations among the operating segments (Tiffany, 2004).

Tiffany's store sales, e-mail sales, and web-based retail sales are processed electronically. The company carefully protects information concerning the retail chain, individual store, purchase, payment provider, customer, and producer. Any information leaks, database damage, web site corruption, or transaction alteration could damage operations and its customer relationships.

Tiffany is a founding member of the World Diamond Council, which was created to oppose the sales of "conflict diamonds". Conflict diamonds come from groups and countries that abuse human rights, such as using slave labor to mine the gems. The company was also active in gaining passage of the Clean Diamond Trade Act of 2003 which is intended to keep conflict diamonds out of legitimate channels of distribution. The leading diamond-producing nations have developed an authentication and documentation system for tracking the country of origin of diamonds. That provides information needed for enforcement of the law (Tiffany, 2004).

PROVIDERS

Tiffany makes over half the jewelry merchandise that it sells. Other companies make the substantial majority of the non-jewelry items it sells. More than 100 other companies do manufacturing for Tiffany.

Tiffany acquired partial ownership of diamond mines in Canada, which provide more raw materials capacity and greater assurance of supply. Also, Tiffany has acquired the Little Switzerland Company, gaining more retail outlets in the U.S. and Caribbean. In addition, Tiffany has invested in Temple St. Glair's Boutiques that aim at wealthy women who buy jewelry for their own use. Those U.S. boutiques have their own name, look, and reputation (Palmer, 2003).

PROBLEMS

Suppose that the company wants your suggestions on how to improve its retailing. What would you recommend? Be sure to include what retail management should do to cope effectively with the following strategic issues: 1) Appeal more to target market segments; 2) Pick additional products and services to offer; 3) Select locations for new stores; 4) Evaluate which price levels to discontinue; 5) Choose which promotional media to use; 6) Decide which outside suppliers to use; and 7) Protect on-line information provided by customers, suppliers, credit card companies, Tiffany stores, and the company's other operating units.

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THE CASE OF THE "I AM NOT A CROOK" CROOK

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Rodger R. Trigg, Columbus State University
Tom C. Moore, Georgia College and State University

CASE DESCRIPTION

This case addresses the issue of double jeopardy in an interesting way. Mr. Wanna was tried in criminal court on drug conspiracy charges and was found not guilty. However, in a subsequent trial for evasion of taxes he was found guilty of not paying taxes on the drugs the criminal court had found him not guilty of selling. In the second trial the government used additional witnesses that testified about the sale of drugs that did not testify in the criminal case. Among other issues, Mr. Wanna's attorney claims that the second trial was more about the selling of drugs than about the avoidance of taxes and that the tax court, in essence, convicted him of selling drugs thus violating double jeopardy.

CASE SYNOPSIS

When humor is effectively used the lessons learned often last much longer than otherwise. This case uses the line made famous by President Nixon to examine the transfer of knowledge between courts. We can visualize the plaintiff screaming, "But I am not a crook. I was found innocent. How can they convict me of not paying taxes on drugs that I did not sell? I am not a crook." The tax court did, in fact, convict the plaintiff on tax evasion charges even though in an earlier criminal trial he had been found not guilty on drug conspiracy charges. The primary question posed regards the results of the appeal.

U.S. CRIMINAL COURT

The following is a summary of critical instructions from Judge Hammon:

“Ladies and Gentlemen of the jury. You have heard extensive testimony about the charges of conspiracy to sell drugs against Mr. Sam Wanna. You have heard from Mr. Wanna and his wife Mary Jo that the money they spent during the four years he did not file an income tax return was earned from real estate transactions and other legitimate sources. You have also heard from co-conspirators, who were granted immunity for their testimony, that Mr. Wanna sold marijuana during those years.

"You are not to use the fact that he did not file a tax return during those years to make any inferences regarding his guilt or innocence in this case. While you have heard some testimony about the issue of tax evasion, that is another issue for another court.

"You must treat the defendant as not guilty of any offense of tax evasion throughout your deliberations.

…

"You may use any evidence that you have heard about tax evasion in this case as you see fit to find the facts of the case as that evidence is relevant to the issues generated by all the evidence and the instructions in this drug conspiracy case, as long as you do not treat the defendant as guilty of tax evasion.…You may now retire to consider your verdict."

Two days later.

Judge Hammon: "Madam Foreperson, have you reached a verdict with respect to the charges under case 12765 alleging conspiracy to sell drugs by Mr. Sam Wanna?"

"We have, your Honor," came the Foreperson's reply.

"What say you?"

"In the above entitled indictment, we, the jury, find for the defendant."

"The court thanks you for your time, and you are dismissed. The defendant is free to go."

With none of the melodramatic behavior often seen on television shows, Sam Wanna turned to his attorney, quietly shook hands, and said, "Thanks Neal."

U.S. TAX COURT, TEN MONTHS LATER

The following is a summary of critical instructions from Judge Coffin:

"Ladies and Gentlemen of the jury. You have heard extensive testimony about the charges of tax evasion against Mr. Sam Wanna. You have heard from Mr. Wanna and his wife Mary Jo that the money they spent during the four years he did not file an income tax return was earned from real estate transactions and other legitimate sources. You have also heard from co-conspirators of the drug charges, who were granted immunity for their testimony, that Mr. Wanna sold marijuana during those years.

"I want to make it very clear to you that you cannot consider that this defendant is or was in the past guilty of a drug conspiracy offense, that is, the subject of another court of the superseding indictment and about which you have heard some testimony.…

"You may use any evidence that you have heard about drug trafficking in this case as you see fit to find the facts of the case as that evidence is relevant to the issues generated by all the evidence and the instructions in this tax conspiracy case, as long as you do not treat the defendant as guilty of participating in a conspiracy with intent to distribute marijuana. You may now retire to consider your verdict." (citation in Teaching Notes)

Four days later

Judge Coffin: "Mr. Foreperson, have you reached a verdict with respect to the charges under case 18765 alleging conspiracy to evade payment of taxes by Mr. Sam Wanna?"

"We have, your Honor," came the Foreperson's reply.

"What say you?"

"In the above entitled indictment, we, the jury, find the defendant guilty."

"The court thanks you for your time, and you are dismissed. Bailiff, take the defendant into custody."

Now with a great deal of drama, Mr. Wanna screams at the jury and judge, "But I am not a crook! I was found innocent of selling drugs. How can you find me guilty of not paying taxes on drugs I did not sell?"

As he disappears from the courtroom, his attorney (Mr. Scence) shouts after him, "Don't worry. Judge Brain Dead screwed up. You will be out in no time. We will win the appeal."

Sitting in the cell next to Mr. Wanna, Mr. Scence and Mr. Wanna discuss the strategy for the appeal.

"Neal, I do not understand. I thought that once they found me not guilty of selling the marijuana I was home free. They brought in even more people to testify about the drugs in the tax trial than they did in the drug trial."

"Sam, I know. The judge should have told the jury that you had been cleared of those drug charges. They tried you twice; we will win on appeal. I will start the appeal as soon as I get out of this Contempt of Court Charge."

U.S. COURT OF APPEALS, ELEVEN MONTHS LATER

The following is a summary of critical comments by Mr. Scence, attorney for Mr. Wanna:

"Your Honors. My client, Mr. Wanna, has been done a grave injustice by the courts. He was tried in Criminal Court on charges of selling marijuana and was cleared of those charges. Then the government supposedly prosecuted him for not paying taxes on those drugs. In fact, however, the government introduced additional witnesses that testified that Mr. Wanna had sold drugs. While plea bargains, or even immunity from prosecution, are often used in the judicial system, the government should have introduced these witnesses at the first trial, not the second. The second trial should have been limited to the issues of tax evasion, not how the money was obtained. The tax conspiracy trial should have focused on the tax conspiracy in and of itself, not how Mr. Wanna earned a living during the four years that he did not file a tax return. "

"To illustrate just how gross of an injustice this is, Your Honors, note carefully that the government introduced only one witness about tax evasion yet used nine witnesses about the sale of drugs, including three that did not testify in the previous trial. This was not a trial about evasion of taxes; it was a second trial about selling drugs. By this time successfully convincing the jury that Mr. Wanna earned a living by selling drugs, the Government, in essence, got him convicted on the drug conspiracy charges they failed to get him convicted on the first time. This clearly violates our most sacred principle that in criminal proceedings the government gets only one bite at the apple; they have violated double jeopardy. Also note carefully that this is not a separate civil trial, but a second criminal trial based on the same facts. Mr. Wanna should be released immediately, with the apologies of the court."

The Assistant Attorney General prosecuting the case countered:

"Your Honors, Mr. Wanna was not found innocent of selling drugs during the first trial, he was simply found not guilty. Secondly, the Government did not try him twice for selling drugs. The second case was purely about not paying taxes on the drugs he sold. The fact that he had been found not guilty of selling drugs is totally irrelevant to the issue of paying taxes on profits from the sale of those drugs. The Government simply did a better job of convincing the second jury that he profited from the sale of drugs and failed to pay taxes on those profits. We maintain that his conviction on evasion of taxes stand."

SEVEN MONTHS LATER

You have been handed the envelope from the Court of Appeals; what does it say and what guiding principles led the Court of Appeals to their decision?

CHANGING TEXTBOOK DISTRIBUTION PROCEDURES: A CASE

Unnikammu Moideenkutty, Sultan Qaboos University, Oman

CASE DESCRIPTION

The primary subject matter of the case concerns introducing change in academic/professional organizations. The case has a difficulty level of four. The case is designed to be taught in one class hour and is expected to require nil hours of outside preparation by students.

CASE SYNOPSIS

This case describes the problems encountered when an attempt was made to change the procedure for distributing textbooks in a university in the Middle East. In public universities in the Middle East, everything, including the textbooks, is free for the students. The new procedure required faculty members to collect and distribute the textbooks in class. Many faculty members were upset by the highhanded way in which this arrangement was made and refused to cooperate. The conflict culminated in stormy meeting between the dean and the faculty members. The case is unique because it takes place in a university environment in the Middle East.

CHANGING TEXTBOOK DISTRIBUTION PROCEDURES

"I screwed up," admitted Dean Roderick. The venue was the urgently scheduled business school faculty meeting. The meeting was called to sort out the problems that resulted from the change in textbook distribution procedure.

Middle East U. provides free textbooks to the students. The usual procedure was for the library to distribute the textbooks to the students at the beginning of the semester and to collect them back at the end of the semester. This semester the library faced acute shortage of staff. The Director of the library felt that this semester he would not be able to distribute the books on time with the existing staff. The assistant director of the library, Marina Popovich, developed a contingency plan that required each faculty member to collect the textbooks for his or her class from the library and to distribute them to his/her students. The faculty member was also to be responsible for collecting the textbooks at the end of the semester and returning them to the library. Marina explained this procedure in a memo to the dean. The dean approved this procedure and a copy of the memo was distributed to all faculty members (see exhibit 1).

The first time I heard about this issue was when I saw Zarina Simmers wheeling in a trolley filled with textbooks.

"What's going on Zarina?" I asked.

"Don't you know? We are supposed to distribute textbooks to the students this time. I thought I'd get an early start. Once the rush starts, it will be hard to get hold of the trolley."

"I don't know anything about this," I said.

"There was a memo last week. Didn't you get it?"

I vaguely remembered seeing a memo about textbooks. I hadn't read it yet. I went back to my office and read the memo. Well, Zarina was right. There was no time to lose. I went to Zarina's office, picked up the trolley, went to the library, and collected my textbooks.

Next day, at the research committee meeting, someone commented, "This new textbook distribution procedure stinks! Why should we be responsible for distributing the books?"

Sheila from Operations Management said, "We as a department have decided that we will not distribute the textbooks. We don't have time for this nonsense."

"What about the students getting the books on time?" I asked.

"That's not our problem. This is our department's decision. I understand that Marketing and Accounting have made the same decision."

I wondered if I had been rather hasty about collecting the textbooks. In the afternoon there was an email from the dean calling a faculty meeting to discuss the textbook issue.

"Yes. Let's face it. I screwed up badly this time," repeated the dean. "Let me ask Marina to explain the situation."

Marina got up and started speaking in her usual monotone, "We used to have three people in the textbook section. One person left, the other person is on leave. One person alone can't do the job. If you help us, we can distribute the books during the first week of classes. If you don't want to help us, we will still distribute the books. It will take three, four weeks. But it will be done."

The dean said, "Now you see what the problem is. What can we do?"

Dr. Cem, Marketing, "This issue should have been discussed and decided in the board meeting."

"I am not going to take every silly issue to the board," said Dean Roderick, voice rising sharply.

The dean was beginning to lose his cool. The marketing department had been a thorn in his side since he took office over a year ago. Rumor had it that the previous dean (Gibbons) resigned mainly because of the recalcitrance of Dr. Cem and gang from marketing. No dean had lasted more than a year in this college. Dean Roderick felt that he had to assert his authority over this unruly group. Trying to stay calm he said, "I already said I screwed up. The question is what can we do now?"

"What is Miss Marina talking about?" interjected Dr. Naseem of Marketing. Dr. Naseem was from Egypt and he was not used to women telling him what to do and what not to do. "What does she mean, if you help us, this, if you don't help us, that. I didn't like her memo and I don't like her tone of voice now. Who does she think she is? Who is she to decide what we should or shouldn't do?"

By now, the dean's patience was at an end. All the frustrations that he experienced over the past year began to boil over. On the one hand he had a highly bureaucratic university administration that would not give him the flexibility that he needed to be effective. On the other hand he had a group of uncooperative faculty members who would not give him the support that he needed. Dean Gibbons had faced a similar situation and had given up. Would he also be a failure? The dean, normally a good-natured person, lost his temper. He leapt to his feet, banged his fist on the table and shouted, "That's it! I've had enough." He began to advance menacingly toward Naseem. "I am not Dean Gibbons. You can't push me around the way you did Gibbons. I am tired of this attitude. It's time you guys learned to play by my rules. You think you are a tough guy? Just step outside and we will see how tough you are."

There was a stunned silence in the conference room.

ASHWORTH, INC. - A CASE STUDY

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CASE DESCRIPTION

The primary subject matter of this case concerns the components of marketing communications strategy in terms of generating leads and creating sales. The case has a difficulty level of three, appropriate for junior level. The case is designed to be taught in three class hours and is expected to require two hours of outside preparation by students.

CASE SYNOPSIS

This case is about a (fictitious) company "Ashworth, Inc." and its marketing communications strategy. The manager in charge, Jeff Gill, is faced with a challenge of justifying its budget to the senior management. He has to analyze and explain his expenses in trade advertising, literature, trade shows, direct mail, and PR in terms of the number of leads generated and sales completed. He decides to outsource some of his functions to MSC, a database marketing/leads management company, and together they are able to maintain the strategy intact, and most importantly, profitable.

ASHWORTH, INC.

"I can't cut back any more," complained Jeff Gill, manager of marketing communications for a large industrial company. "I don't understand how senior management can continue to cut my budget mid-year, and expect me to help the sales team make their numbers. Don't they know you have to spend money to make money?"

Ashworth, Inc. had not reached its net earnings for January and February of the year. As a result, senior management sought cuts on expense items, and also looked to cut back on various departments that were considered overhead. Marketing communications was always one of the first departments to feel the budget cuts.

"Senior management doesn't understand how important my department is," Gill continued. "The sales team won't get any sales leads if we cut the advertising budget. And how are they going to be able to competitively bid on business without leave-behind literature? It just doesn't make any sense."

Ashworth, Inc. was a large industrial valve company based in Munich, Germany. The company had been in business for 50 years. Its North American corporate office in Chicago, Illinois had been successful in making its mark in the United States. In order to be closer to the customers, the company had four area offices and 30 regional offices in the U.S. It also had significant coverage of Canada. The United States sales teams were in the regional offices. Each regional office had a regional sales manager that managed the sales teams in their offices.

The president of the company, Thomas Wenderburg, was a real go-getter from the Germany headquarters. He believed in allowing the regional sales managers to have authority and accountability. He pushed command down to these managers and allowed them to make daily decisions that would affect their business. Accountability was key --- and as long as they made their numbers, Wendelburg was happy. Advertising and marketing communications, however, was centralized at the corporate office in order to protect the company brand, including the logo.

The marketing communications department at Ashworth had three people; small for the amount of sales in the company ($3,000,000,000 annually in the U.S.). Jeff Gill was the manager of the group; his staff consisted of one writer and a secretary. Whenever there were problems with sales revenue or poor earnings, it seemed as if marketing communications was the first department to get hit. This was the second consecutive year that the marketing communications budget had been frozen mid-year, despite good planning.

The annual marketing communications budget at Ashworth was $1.65M. It was spent as follows:

Type of Expense	Amount Spent
Trade Advertising	$500,000
Literature	$300,000
Trade Shows	$650,000
Direct Mail	$50,000
Public Relations	$150,000
TOTAL	$1,650,000

Gill needed to think of a way to get out of this rut. He had gone to a recent seminar and met a consultant from MSC, a firm specializing in database marketing and leads management. In desperation, Gill called on the consulting company for advice. A meeting was set up the following week. Megan Durant, a senior consultant at MSC, reviewed Ashworth's marketing communications budget, plans, and present databases. She then asked Gill if she could see the sales leads that had been generated from a recent trade show.

"The sales leads are immediately sent out to the field offices," responded Gill. "Since our offices are independent, they like to follow up on their own areas' leads." "Ashworth has two databases," Gill continued. "One contains customer names, and that is the one we use for billing.

The other one contains prospect names and information." "The databases are new," he continued, "and many of the regions are just learning how to use them properly."

When Durant probed on how well the programs were doing and what sales were resulting from those programs, Gill stumbled. "The sales offices don't follow up with us very regularly on how the sales leads pan out," he said. "My department isn't staffed to call every region office and check on how good the leads were that we sent them. And because our sales offices aren't centralized here at headquarters, they don't have to give us any information at all." After more discussion, Durant mapped out how her firm works.

MSC had set up a system where all their client's sales leads are funneled through their telemarketing team of 20 operators. This trained telemarketing staff would follow up on the leads by telephone, qualify them with a questionnaire approved by Ashworth, and then send them to the appropriate Ashworth sales office. After a set amount of time, MSC would follow up with the sales representatives on the telephone and ask them if they had followed up on the lead, and what the response was. Any leads that resulted in sales would be tallied and tied back to the marketing communications program from which it originated. Since MSC kept the database and could see from which marketing communications program the lead was generated, a closed-loop system was in place, and accountability for the marketing communications program firmly confirmed. It made sense to outsource this process, Durant continued. "In order for Ashworth handle the inquiries and leads in-house, you would need to lease space and pay salary and benefits for at least two shifts of telemarketers." She said to sell the idea to the Ashworth management, an approach based on cost/benefit analysis needed to be developed. Durant also pointed out that there were vast cost differences between the cost of a sales call with a qualified lead, and one without qualification, which is how Ashworth was presently operating. She mapped out how much a sales call really costs:

Annual Cost of Sales Rep, Benefits, Expenses	$73,500
Number of Face-to-Face Sales Calls per Day	2
Number of Sales Days/Year=212* X 2	424
Existing Customer Calls @ 40%	170
Total Face-to-Face New Calls/Year (424-170)	254
$73,500 / 254=$290.00 per new face-to-face sales call.	
* 365 days per year minus 104 weekend days, 11 holidays, 10 vacation days, 3 personal days, 20 days training/meetings/paperwork, 5 sick days = 212.	

Gill remembered something from the seminar where he met Durant. They said out of 50 prospect inquiries, only five of the 50 are qualified (10%), and only one sale results from those five! No wonder his department was suspect and a target for budget cuts. Gill did the math in his head. Since it takes ten prospects to make one qualified lead, total cost for prospecting for one lead under the old system was $2900 ($290 X 10). With an average of five qualified leads leading to a sale, the current process was costing $15,950 ($290 X 5)! Since MSC would be qualifying the prospects and only sending the qualified leads to the field, it would be ready for a sales call once the sales person received it. All the sales person would have to do is make the call!

MSC's program would give the sales reps better, qualified leads, leading to higher sales volume, and a more productive use of their time. Initiating the program was expensive, but once Gill put the numbers together, with Durant's help, he was able to convince his German headquarters to allow him to try the program for two years. After explaining MSC's impressive expertise in database marketing and leads management, he was also able to secure $100,000 for MSC's involvement for the first year. Based on the results of the first year, MSC's contract was going to be a subject for further negotiations.

The minute Ashworth management approved the program, Gill got started on directing all of the leads to MSC. Ashworth's 800 lines went to MSC telemarketers and the bingo cards from the trade journals were returned to MSC's headquarters, instead of to Gill. All leads were quantified and qualified, providing rich reporting data for Gill to finesse and give to his management. Each marketing communications program for the next year had a follow-up report that included the sales associated to that program.

The qualified leads were sent to the sales offices, and each lead was dated so MSC could check on the sales rep a couple of weeks later to get a verbal update on the sales process of that particular company. The sales rep would call on the lead and, in some cases, make a sale. Once a contract was signed, the new customer's name was loaded into the customer database. The database is the same one the original lead was loaded into by Ashworth. Addresses and zip codes from the addresses were matched, and the new sale is tied to the original marketing communications program that brought that prospect to Ashworth. The sales team then was able to tie back the successful sale and resulting contract to the marketing communications program that originally brought that lead to Ashworth. Revenues could be measured against that marketing communications program. Gill would finally be able to prove its worth to senior management.

The program went on for one year, and the results were staggering.

Type of Expense	Amount Spent	Leads Generated	Resulting Sales Figures
Trade Advertising	$500,000	3500	$1,250,000
Literature	$300,000	1425	$500,000
Trade Shows	$650,000	7850	$2,550,000
Direct Mail	$50,000	725	$219,000
Public Relations	$150,000	1500	$421,050
MSC's fee	$100,000	NA	NA
	$1,750,000	15,000	$4,940,050

BIG SKY CARVERS: A RURAL SUCCESS STORY

R. Sitki Karahan, Montana State University - Bozeman
Tim Christiansen, Montana State University - Bozeman

CASE DESCRIPTION

The focus of this case is on product development for a small, but successful firm. The firm has an opportunity to expand its product line through a co-branding effort, but the new products represent a significant adjustment in how the products are made and who they are sold to. An important secondary issue deals with the opportunity to develop global sources of production as a means of lowering production costs. The case has a difficulty level of four to six. It should take about two class hours and the students will need to spend about two hours outside of class to prepare for it.

CASE SYNOPSIS

Big Sky Carvers (BSC)is a small, but quite successful firm specializing in home décor and gifts based upon a wide range of wildlife, from trout to grizzlies. While BSC is small, it is still a fairly large player within the focused industry niche for this type of product. A significant success factor for the firm has been the high level of craftsmanship exhibited in its pieces, which leads to generally higher prices. The attention to detail and quality has lead to a strong customer base, among both its retailers and consumers, for its products. The firm now has the opportunity to embark on a co-branded line of products which could develop a new method of production for the firm, leading to lower prices, and a possible expansion of the market for its products.

INTRODUCTION

"When I was a kid, Dad had some old decoys around the house. They weren't rare or valuable; they weren't even very well made. But I noticed, especially when I held one of them, I was transported to another place; the memory of the brisk fall morning with autumn smells of a marsh in the air, and our yellow lab. Nancy, running around disobediently while Dad put out the decoys. Those old decoys of my Dad fueled a deep passion in me."
- Marc Pierce, Co-Founder and CEO

PROLOGUE

Marc Pierce and his family are looking forward to their annual winter trip to Cabo San Lucas, Mexico next week. However, before Marc goes he knows that he has to make a decision on a new product line for his firm. This line would be different in many ways from the products that Big Sky Carvers has sold and Marc has been seeking advice and counsel from all his key employees and retailers. But the final decision on whether to pursue this new line is Marc's responsibility and he knows that he must decide before he goes on vacation.

BIG SKY CARVERS

Eric Pierce and his son Marc founded Big Sky Carvers in 1980. In the past twenty years it has grown from a small producer of decorative duck decoys into a global leader in the decorative design industry.

After learning how to make decoys on a multiple-spindle carving machine, the Pierces moved from the mid-west to Montana in hopes of being able to successfully market their product in and around Yellowstone Park. Success was not easy to come by at first. However, with hard work and the addition of many artists and craftsmen from the Yellowstone area the Pierces' dream of being a highly successful leader in their field has been realized.

BSC now has a number of product lines which include, decoys, fish, game birds, signs, furniture, sports collectables, dogs, big game, and much more. BSC has become much more than just a woodworking shop; its expanded facilities include a foundry as well as furniture assembly and sign making processes.

While the products offer a unique view of nature and its beauty, the true identity of BSC is embodied in the employees. BSC has been very fortunate in assembling a talented group of artists. In addition to being great artists, they truly love the outdoors, wildlife and all the things that BSC products have come to represent.

The mission statement for BSC reflects how the firm embodies both the family nature of the firm and the love of its organization members for the outdoors. Marc Pierce has articulated the mission statement as "Big Sky Carvers is a team of highly motivated individuals dedicated to designing, creating and delivering products reflecting outdoor lifestyles to niche markets. Our strength lies in our ability to create win/win relationships with our customers, vendors and staff, resulting in a 'world class' model of excellence."

Existing Products

BSC is a group of people that share the common goal of providing a top of the line product with as much character as those who produce and purchase the product. The hope of the many master artists, designers, craftsmen and members of the workshop at BSC is to bring a little piece of the outdoors into the customer's home.

The company currently has seven major product lines that it markets. While all of these are sold under the BSC name, each line has its own type of pricing structure and distribution intensity based upon its target market. Many of the lines have begun as a single item or small group of items created by artists in the area. BSC has helped these artists to develop profitable products and market them nationally.

Wildlife Woodcarvings

This collection started in the tradition of the American Folk Art of decoy making and was the beginning of the BSC, but has grown to provide a great deal of options for those who have grown up as avid sportsmen. The items are produced by a workshop of artisans, crafting decorative decoys in the tradition of those before them. However this collection has expanded over the years to include several waterfowl editions, game fish, upland birds, songbirds and mammals.

The Wildlife Woodcarvings collection represents the upper level in quality and price for smaller woodcarvings in the industry. With prices ranging from sixty-nine dollars for very small items to almost five hundred dollars for larger items, there is as much parity in price as in selection.

These products are designed for people with outdoor lifestyles. Representing the very best that the industry has to offer in the wood sculpture market, with unparalleled quality, diversity and design. With the offerings of "limited edition" designs BSC increases the worldwide following of collectables and increases the desirability and value of the purchase as the items sell out.

Placement of this line is very important at BSC, with a target of mid to upscale gift/gallery stores and catalogs with a commitment to stocking inventory and display and visual merchandising. With a low to medium distribution density and medium to high price points, these products are a rarity in most stores.

Big Sky Bears and Friends

These bears, carved by chainsaw and created by the imagination of Jeff Fleming are more animated than the rest of the collections, thus they tend to appeal to a wide range of consumers throughout the market.

Big Sky Bears, as with the Wildlife Woodcarvings collection, tends to lean toward the higher price ranges and low distribution density. This collection also is rare and desirable. The prices fluctuate according to the size of the carving, starting at around fifty dollars for the smallest items to twelve hundred dollars for the Ben Table Bear.

These products are marketed to people who decorate or collect for an outdoor or lodge look in their home. These upscale carved bears and other animals have frequently been described as "cool" and "endearing." Collecting or decorating with Big Sky Bears makes people smile.

The William Herrick Collection

This collection started twenty-five years ago when William Herrick began to carve basswood. Beginning with his world famous Trout Table, then adding more tables as well as many other items over time, this collection has grown into one of the more popular collections at BSC.

With this collection consisting of large items such as tables, mirrors and cabinets, it is the most expensive collection that BSC offers. With high price points and low distribution density this collection falls into the same category as the Wildlife Woodcarvings and Big Sky Bears. Prices range from one hundred dollars for a candleholder to almost five thousand for a Round Troutstream Basswood Table.

Marketed to those with a deep appreciation for the outdoors, these reproductions of William Herrick's original woodcarvings represent BSC premium collection of exclusive designs of furniture and accessories. The presence of these items is considered a great source of pride and conversation among owners.

Meissenburg Designs

These handcrafted signs are of unique quality and design that far exceeds that of the rest of the market. Lloyd Meissenburg, the personal designer of this collection, is the leader in this field, showing a dedication to the old days of wood crafting. The production of both inside and outdoor signs is designed specifically to reflect the buyer personality.

The line of outdoor signs are for people wanting a high quality welcome sign reflecting their lifestyle or personality. These signs are the best three-dimensional personalized signs available. With a relatively expensive price and high distribution density, these signs follow the BSC pricing trend but are easier to find. Price ranges are approximately seventy to one hundred dollars.

The inside signs are marketed to those wanting to decorate their home or office with reminders of their life's passions. This collection offers a fun and decorative sign at a very reasonable price. With a medium to low price point (rare at BSC) these items are a great deal. Prices range from thirty-five dollars for a wisdom board to one hundred sixty dollars for a larger sign.

With a larger number of channels of distribution this collection is much easier to find than most BSC products. With the target placement of these items including, home & garden and general variety/hardware stores included with the usual channels of distribution used by BSC, distribution is much higher with these products.

Montana Bronze

Created by Brad Williams, these sculptures consisting of bronze, resin and pewter, appear almost identical to the much more expensive solid bronze sculptures. These limited edition sculptures all come with a certificate of authenticity for added value and desirability. These extremely lifelike sculptures are a true credit to the ability of their artists.

With prices ranging from fifty to three hundred dollars, there is a wide selection of items to fit almost any consumer. With medium to high price ranges and low to medium distribution these products are true collectors items.

This product line is designed for art collectors with outdoor lifestyles who are not necessarily buyers of real bronze sculptures. Montana Bronzes are near bronze sculptures with outstanding quality and design at reasonable prices. Collectors of Montana Bronzes get a piece of art for their home or office, which not only reflects their lifestyle and is a great value, but as editions sell out can increase in value.

Ducks Unlimited

Ducks Unlimited is a national organization that was begun by a group of waterfowl hunters in 1937 and whose goal is to save or restore the nations wetlands. Ninety percent of its current members are hunters whose participation in waterfowl hunting fuels their drive to give something back to the resources that make their outdoor experiences so enjoyable. Through the support of this sportsman constituency, DU has been able to conserve more than 10 million acres of habitat across North America-in the areas that are most important to ducks and geese.

The partnership between BCS and Ducks Unlimited (DU) was formed to raise money for DU and its cause. Selected to develop some designs that reflect the lifestyle of the DU supporter, BSC jumped at the chance to help a cause directly associated with their own lifestyle as outdoorsmen. This co-branded venture has been extremely successful for both BSC and DU, and continues to raise money to support wildlife habitats.

With medium price points and high distribution the hope is to raise as much as possible for DU, while pushing the BSC name. Prices range from one hundred to three hundred twenty dollars, determined primarily by the size of the item.

Produced and marketed especially for DU members and other people with outdoor lifestyles, the DU collection is a group of accessories reflecting the DU lifestyle. Owning DU accessories provides the buyer with a connection to that DU lifestyle through their décor, and supports DU's important conservation efforts.

Big Sky Home Accents

This collection consists of items that the owners and employees of BSC feel would appeal to their customers, but are not made by BSC. These products could come from a tiny village in Mexico, a workshop in Asia, or a small community in the low country of South Carolina. Low to medium price points and high to medium distribution, make this collection the most affordable of the BSC collections. Prices range from twenty-five to one hundred twenty-five dollars with a few products that may go as high as four hundred fifty dollars.

This product line, consisting of many items from different backgrounds, is directed to anyone who enjoys BSC products and an outdoor lifestyle. These are things that BSC employees enjoy and feel that their customers will as well.

The Distribution Channels

BSC uses a variety of different channels to sell their products; this variety has proved to be very successful throughout the life of the firm. By using so many different channels of distribution BSC has given itself a great deal of freedom and ability to reach many different markets within its industry.

Retail Stores

BSC owns and operates two retail stores which carry items from all the product lines and can order any item for a customer. One store is at the Mall of America and the other at their headquarters in Manhattan, Montana. These stores account for a very small percent of the yearly sales and also perform the duties of a showroom for soliciting larger clients such as catalogs and other forms of distribution.

Licensed Gallery Dealers

The licensed gallery dealers are a larger part of the sales picture. Currently there are over three hundred of these dealers that are licensed to sell BSC products (see table below). These dealers operate independently from BSC, and perform as separate entities within the same markets as BSC. Operating in the same way as any other store they purchase the products from BSC and then resell them for their own profit.

Big Sky Carvers Licensed Gallery Dealers by Region							
Western United States		Central United States		Eastern United States		Canada	
State	Dealers	State	Dealers	State	Dealers	State	Dealers
Alaska	10	Colorado	24	Alabama	3	Alberta	5
Arizona	2	Montana	18	Arkansas	7	British Columbia	4
California	28	North Dakota	1	Florida	2	Ontario	6
Idaho	7	Nebraska	5	Iowa	3		
Nevada	3	New Mexico	1	Illinois	8		
Oregon	16	Oklahoma	1	Indiana	4		
Utah	12	South Dakota	2	Louisiana	1		
Washington	10	Texas	3	Massachusetts	3		
		Wyoming	6	Maryland	1		
				Maine	4		
				Michigan	19		
				Minnesota	11		
				Missouri	9		
				North Carolina	11		
				New Hampshire	1		
				New Jersey	1		
				New York	3		
				Ohio	5		
				Pennsylvania	3		
				Tennessee	5		
				Virginia	3		
				Vermont	1		
				Wisconsin	16		
				West Virginia	1		

Catalog Distribution

All the various catalogs in which BSC products are featured constitutes the largest channel of distribution for its products. The ability to reach as many people as a catalog can is a great asset. With low costs and high circulation, the catalog market has allowed BSC to grow into an industry leader. Although BSC does not put out its own catalog, its products are featured in over forty major and regional specialty books that reach over forty million people every circulation cycle. With that type of opportunity for sales it is easy to see why it can be so successful.

Internet

The Internet has become an important tool in helping to support the sales of BSC products, but BSC does not sell on-line direct to consumers. Instead, the web site (www.bigskycarvers.com) provides information about its products to prospective customers and then will help direct them to the nearest licensed gallery dealer. With detailed explanations and descriptions of products and dealer information the Internet is a good "end consumer" driven support of the licensed gallery dealers distributing BSC products. In addition, retailers that would like to carry BSC products can provide contact information so that BSC can contact them and in the future BSC would like to use their web site as way for its retailers to place their orders electronically.

Conservation Groups

Alliances with conservation groups has been another successful channel of distribution for BSC. This method of product distribution not only helps the cause of the group but it increases circulation of the BSC name and products. This channel allows BSC to contribute to the conservation of the environment that it represents so well within its product. Currently over twenty major conservation groups and their member chapters use BSC products for fundraising. An example of how successful this channel can be is the partnership of BSC and Ducks Unlimited to help raise money to save, restore and manage wildlife habitats.

Profitability

BSC has been a profitable firm since shortly after Marc and his father founded it in 1980. The firm grew slowly during its early years, but growth in the last ten years has been much faster, largely due to the expanding product lines the firm produces and markets. While the firm is privately held and closely guards its financial information, it is widely recognized as a leader within its niche area within the home décor/gift industry.

Retail prices for merchandise in this industry commonly provide a fifty percent margin for the retailer. For example, if the retail price on a product is one hundred dollars, the retailer paid fifty dollars to the supplier for it. Thus, if a BSC product retails for one hundred dollars, BSC received fifty dollars for it and from that price must pay for all production costs, promotion, and overhead costs. It is not uncommon for the production costs to consume over fifty percent of the price of the product, so that of that fifty dollars BSC generally has less than twenty-five dollars to cover all promotion and overhead costs, and leave some type of profit. For many publicly traded firms in the home décor/gift industry the net profit margin ranges from eight to fourteen percent. It is also common for the lower priced retail products in this industry to produce a lower net profit margin and firms that market these products hope to make higher net profits through volume sales. While BSC is distributed nationwide, it is not carried in any of the larger discount or volume retailers for these products, and the firm emphasizes margin over volume in the sales of its products.

Promotion

The promotional efforts of BSC have largely been directed to two areas: point-of-purchase (POP) displays and personal selling. BSC recognizes that its products appeal to a small target market that is spread widely over the U.S. In fact, many of its products sell better in smaller, more rural markets where there is a larger percentage of the population that still hunt and fish. This wide and shallow distribution of the target market has always made the purchase of any type of mass media rather costly on a per exposure basis. In addition, Marc Pierce believes that advertising does not have the ability to truly represent the quality of the products that BSC markets. As a result, BSC has put a great deal of time and money into developing effective POP display items for its products. For example, a handmade, hand-painted decoy from BSC would have a display easel given to the licensed gallery dealer to put next to the product to hold a card (or number of cards) that talk about the particular species of waterfowl the decoy represents, the areas of the country where the bird can often be found, any interesting facts about the bird (such as geese mating for life), what type of wood was used in producing the product, and so on. BSC also has a number of special display units that it sells to its dealers to display the products at less than the manufacturing cost of the unit.

The second method of promotion that BSC employs is really in developing and maintaining reseller relations rather than sales from the end consumer. To help build these relationships BSC employs twelve major sales representative groups and over thirty-five sales people. In order to support these sales people BSC owns three permanent showrooms as well as six regional/representative showrooms and attends specialty and temporary shows throughout the year. BSC spends tens of thousands of dollars each year for these shows where the dealers come to see new products, make purchases, and find new vendor sources. The cost for attending these shows is expensive, but BSC feels that it is worth every penny it costs to make sure its dealers have a chance to view and purchase new products. It is also an important source for BSC in finding new dealers to represent its products, especially as the type of product lines increases and more market segments may be attracted to its products.

New Product Development

In the year 2002 BSC plans to expand their collections to include a number of new products and ideas. Not only will the existing collections be expanded, but new collections will make their way into the BSC family.

The addition of new collections of stoneware, lamps and metal ware as well as the Hearthside Santa collection will bring new variety to BSC. These new products are created in the same image and with the same character as all previous collections produced by BSC.

Along with new products BSC is also changing its logo enough to differentiate the different product lines within the firm. The goal of BSC is to develop logos and brand marks to better communicate separation of the different collections.

With all these changes at BSC it is a very exciting time within the firm. However overshadowing all of these changes and improvements that are being made throughout BSC is a project with the National Audubon Society.

THE AUDUBON SONGBIRD COLLECTION

The National Audubon Society and BSC have worked on the development of a new BSC product line which would be used to raise money for the conservation of wildlife throughout North America. The product line would be called The Audubon Collection consisting of songbirds from different areas of North America.

This project provides some new opportunities for BSC, the expansion of global business and marketing to a different customer than that of the past. If BSC goes ahead with this product line it will be the first time that BSC outsources the production of a product. The less expensive version of the collection will be made out of resin and produced in China. This new production method will allow BSC not only to experiment with outsourcing, but also with global business as BSC begins to expand to other markets around the world.

This product differs from the BSC products of the past. The items are less expensive than most BSC items. By offering a product consisting of resin BSC can sell these items for $79, far less than what is usually charged. However BSC is also offering the same birds, carved out of wood, in the traditional BSC fashion for those who have come to expect the best from BSC. This differentiation of products allows BSC to reach customers that usually would not buy BSC products due to the high price.

The Customer Profile

The customer that is targeted by this new partnership is one who sympathizes with what The Audubon Society is trying to do, protecting birds and other wildlife and the habitat that supports them. These products are designed for an outdoors person who doesn't want to see any further destruction of the environment. Many "birders" will take trips exotic or remote locations simply to see and hear special birds. However, the product is one that can appeal to people who venture no further than their backyard or the city park to enjoy the many songbirds that can be found in urban settings. It is very important to those who work with and for BSC to preserve the environment that they have grown so fond of over the years. The customer targeted is one who can recognize that goal and feel good about purchasing a product that helps the environment.

There will be two market segments that this product may appeal to. The resin birds costing $79 will allow those who don't want to spend much money on a wood carving to be able to purchase one of these items without guilt. The wood carved bird on the other hand, costing $200, allows those who have become collectors of BSC products over the years to purchase a product of the same quality as those purchased before.

Another important difference for this product is the increased focus on women as the target market for the product. The songbirds represent a more delicate, softer view of nature that may appeal to more women. Many of the BSC products are of larger animals such as deer or bear and most of the birds in the current collections represent game birds like ducks or pheasants. The songbirds are a way that BSC hopes to reach out to the wife of the sportsman. While women have purchased a number of BSC products in the past, the firm believes that these have frequently been gifts for the men in their lives. The songbirds are a way for BSC to extend their reach by having women buying BSC products for themselves.

The Product

The materials used to make the resin version of the songbirds in this collection are different than what is usually used by BSC. By using resin rather than wood it is hoped that the costs will be less and those savings in turn can be passed on to the customer. One thing that BSC is not sure of is how good the resin product will look in coming out of the factory. Up to this point all of the examples of the product that the BSC have been samples that have essentially been hand made. Once a contract with the factory is signed, a wooden model will been sent over. The factory will use the wood model to create a mold for the resin version. Only then will BSC be able to see actual production versions of the songbirds.

The production of this product is going to be outsourced to a factory in China. This method of production is necessary to keep the costs low enough to be able to sell them profitably for the projected price of $79. If the resin songbird were to be made in Montana, the labor cost of the BSC employees would significantly higher than from the factory in China. An additional benefit from outsourcing the production is that it will allow more time for the production of other collections in the BSC workshop.

The Price

The new Audubon resin songbirds will be priced lower than most other products from BSC. It is hoped that the lower price will play a significant role in helping to make this product line a success. By pricing this collection lower than most, BSC will be able to sell this collection in more channels than what is traditionally used. However, since this product will be sold as a means of generating funds for the Audubon Society, a portion of the retail price will go directly to the Society. While the exact amount has not yet been determined, there have been discussions regarding whether it should be a set amount or a percentage of the retail price. BSC would like it to be a percentage of the retail price (in the range of five to ten percent) and have the retailer send the money directly to the Society. The retailers would expect a lower wholesale price based upon the lowered revenue generated from each item. The Audubon Society, and most of the retailers that BSC has talked to about this project, feel that it would be better to have a set amount per item shipped and let BSC send it directly to the Society. This amount could then be put on the display information as "X amount of dollars from the sale of this product goes directly to support The Audubon Society." The amount for each item has been suggested by The Audubon Society and the retailers to be in the range of five to eight dollars in order to stimulate purchasing.

The Distribution

Another issue for BSC is the distribution of the product. The wooden version of the songbirds will undoubtedly get sales through the channels of distribution that BSC has developed over the years. This part of the product line will be viewed by these retailers as a routine product extension for them and they will simply have to decide if they have room to merchandise this new product.

The resin songbird will not necessarily be going through the same distributors. While there is no doubt that some of the current dealers will be happy to have a lower price point product to sell, many of the dealers pride themselves on dealing in only high quality and collectible products. The resin songbird will not fit in their product mix. But there may be a number of new dealers that might be attracted to this product as it would be the first product from BSC that would really fit within the price category that their customers have come to expect. The difficulty for BSC will really be in finding those new dealers and trying to convince them to carry more than just a very small portion of the total BSC product assortment.

A final issue associated with distribution would be the sales of the product through The Audubon Society. The Society would like to put the product line on its website and its literature that it sends out to its members. The Society would then order the products necessary to fill these orders from BSC. This method of distribution is similar to what occurs with the Ducks Unlimited products, but BSC has found that it is rather expensive to ship out a number of small orders and would rather have both groups direct their members to purchase through a licensed BSC dealer. This type of arrangement may be difficult for a new product like the resin songbirds where only a few or select dealers are carrying the resin songbird.

THE DECISION

Marc Pierce has to make the decision about whether or not to include The Audubon Society Collection for the next year's product assortment before he goes on vacation. He feels that while it is not a decision that will either make or break the company, it is one which represents some significant risks and opportunities:

It would give BSC a chance to gain experience with a new product material and new production facilities that are off-shore, however, it might also upset the current workforce who could view the new product line and production method as a threat to their jobs;

It would give BSC a new product line which might open doors to new dealers and new target markets, but it also might alienate some current dealers who could view the new product offering as a lowering of quality of the BSC products;

The pricing on the product leaves little room for error and if it does not generate enough volume it will probably not generate sufficient profit.

SUPER SISTERS, INC.

Richard Gunther, California State University, Northridge
Rafi Efrat, California State University, Northridge

CASE DESCRIPTION

The primary subject matter of this case sequence is the integration of statistics and business law. Secondary issues examined include the use and meaning of descriptive statistics, regression analysis, statistical index numbers, the legal responsibilities for detaining a customer in a store, the liability of a merchant for compensatory damages arising out of the commission of a tort, and related strategic management issues. The case has a difficulty level of three, appropriate for junior level. The case is designed to be taught in three class hours. That time estimate includes a formal class presentation by a team and a challenge by another student team. It is expected to require ten to fifteen hours of outside preparation by students for the case.

CASE SYNOPSIS

After observing a customer engage in suspicious conduct, the Loss Prevention Manager of a store detains the shopper after grasping her by the arm and shoving her back to the store. Apparently, the shopper lost her balance and fell on her back sustaining significant physical damage. The shopper was then escorted to the loss prevention room where she was asked to wait for the store manager, who showed up more than an hour later. Following some questioning in the loss prevention room, the shopper was allowed to leave after it was determined that she did not engage in shoplifting. Due to the significant injuries the shopper sustained she was permanently unable to resume her work as a successful sales person for a pharmaceutical company. She is now suing the store for lost future income under the legal claim of false imprisonment.

The statistics portion of the case requires students to use Excel to compute descriptive statistics, perform regression analysis, and project future income. Students are also required to carefully define the statistical terms they are using and explain the meaning of their results In the legal portion of the case, students are referenced to legal opinions and asked to evaluate whether the shopper is likely to be able to recover under the claim of false imprisonment. The students are then expected to utilize their previous statistical analysis to conclude whether, and if so how much, the court is likely to award the shopper for lost future income. Students also need to determine if the shopper is likely to recover compensatory damages for injury and a punitive award. Finally, the *student is asked to recommend strategic management policies that would serve to avoid reoccurrences of the problem.*

This case requires students to apply materials learned in most Business School's lower division core (LDC). It is used in a course at the beginning of the junior year that has goals to integrate LDC material while developing teamwork and communication skills. Specifically, the case requires knowledge of elementary statistics and a beginning business law course. Student teams prepare the case with tutoring from faculty who provide "just-in-time" specific knowledge as requested by student teams. A team of students formally presents their case solution, another team acts as a "challenge team" and the whole class participates in an active question and answer session.

BODY OF THE CASE

Bruce Levin, Customer Relations Manager, for Super Sisters, Inc. ("Super"), was in a quandary. He pondered over a memo from Jimmie Lee, Loss Prevention Manager at Super, (Exhibit 1) and a letter addressed to him from Susan Kim, a customer, (Exhibit 2). What appeared to have been a routine shoplifting incident on the part of Mrs. Kim turned out to lack evidence. To make matters worse, the suspect was injured during apprehension. It appeared that Super faced the possibility of a lawsuit because of the incident. Donald West, Chief Administrator, had asked Mr. Levin to assess the legal and financial consequences of the case, make recommendations, and report back to him.

Super is a large stationery and drawing supplies retailer with approximately 50 stores located throughout the State of Green. The firm has been established for many years, making steady, if unspectacular profits.

EXHIBIT 1

M E M O R A N D U M

DATE: January 3, 2002

TO: File

FROM: Jimmie Lee, Loss Prevention Manager

SUBJECT: Shoplifting Incident

At 2:20 p.m. today, I observed a customer, Susan Kim, who was standing next to calligraphy sets in the store, make a sudden move to her pocket. She then proceeded at an accelerated pace toward the exit. I noticed that her side pocket was stuffed. I then proceeded directly to where the customer had been standing and noticed that a calligraphy pen set was missing. It so happened that I noticed earlier that day that the calligraphy pen sets were fully stocked up. I assumed that the customer, who I had previously observed, had shoplifted the set. As the customer was about to leave the store by then, I began chasing after her and reached her at the store's entrance. Fearing that I might lose her in the crowd, I shouted at her to stop. I then grasped her by the arm and shoved her back to the store. Apparently, the customer lost her balance and fell on her back hitting one of the checkout counters. She seemed to be hurt a little, but then I offered to help her stand up, although she continued to limp. I then asked her if she had forgotten to pay for something. She seemed surprised and said that she does not understand what I am talking about. I then directed her to follow me to the Loss Prevention room. Kimberly Youseff, one of the checkout employees, helped her walk toward the Loss Prevention room as the customer complained she was having difficulties walking and was experiencing terrible back pain. I closely walked behind the two of them.

Per store's protocol, I then advised the customer that she would have to wait until the store's manager would come back from a meeting for the investigation to begin. The store's manager, Jennifer Parker, was due to return from a meeting at 2:30 p.m. that day. Unfortunately, she only returned at 3:30 p.m. At that time, Mrs. Parker advised the customer why she was being held up and asked her to empty her pockets. However, no calligraphy set was found. Mrs. Parker then apologized for the inconvenience, gave her a $25 gift certificate, and wished the customer well.

I really did not mean to hurt the customer, but apparently her fall did some damage to her as she kept complaining that her back hurt.

EXHIBIT 2

Susan Kim
19853 Angel Blvd.
Angel City, Green

February 18, 2002

Donald West, Chief Administrator
Super Sisters, Inc.
10984 Glitter Blvd.
Beverly Flats, Green

Re: incident dated January 3rd, 2002

Dear Mr. West:

Based on permanent injuries inflicted on me by one of your employees while falsely imprisoning me on January 3rd, 2002, I demand compensation in the sum of $765,000 in medical care expense and $750,000 for loss of future income.

On January 3rd, 2002, I came to your store to locate some art supplies for my daughter's art project at school. While I was examining a number of calligraphy sets that you had on the shelves, I was not able to find the calligraphy set my daughter's teacher requested. Rushed to make it back to an appointment I had with a client that afternoon, I headed toward the store's exit. As I was about to leave the store's premises, I heard someone shout behind me ordering me to stop immediately while using some foul language. When I looked back, I saw a six-foot, two hundred pound man grabbing my arm and shoving me back to the store. Due to the tremendous force of that shoving, I lost balance and fell on my back, right against one of the store's checkout counters. I immediately felt extreme pain in my back and was unable to move. I was then helped out by a store's employee and was ordered to go to the Loss Prevention room. I was told that police would be called to the premises if I did not directly go the Loss Prevention room. There were approximately twenty-five customers watching me as I was escorted to the Loss Prevention room. I felt extremely embarrassed by the ordeal. Once we got to the Loss Prevention room, I asked the man, who accosted me at the store's entrance and who then followed me to the room, the reason for my detention. He then mentioned that it is against the store's policy for him to discuss the matter further and that I would have to wait for the store's manager. Almost an hour later, the store manager, Ms. Parker, arrived. At that point she notified me that I have been detained because one of the store's employees had observed me stealing a calligraphy pen set. I immediately denied any involvement in the matter and offered to empty my pockets. Ms. Parker was then satisfied that I have done nothing wrong. She politely apologized and allowed me to leave the store's premises.

Later that afternoon, I was admitted to Ceder Sinai Hospital emergency room as I was experiencing severe back pain arising out of my fall earlier that day. That same night, a team of surgeons operated on my back as the condition severely deteriorated. However, they were unable to successfully treat the back injuries in this and in two other surgeries that followed. I am now diagnosed with an abnormal degeneration of my spine resulting in irreparable back injury and permanent disability. This condition prevents me from ever walking again or from ever sitting down for more than ten minutes at a time. As a result of this permanent condition, I had to quit my job as a regional salesperson for Derk, a pharmaceutical company. My doctor's diagnosis indicates that these injuries to my back would prevent me from ever working again.

Besides my past and future medical bills, I am also demanding that you compensate me for loss of future income. As a fifty-five year old, highly successful career woman in the field of pharmaceutical sales, I am now deprived of any prospects of employment for the rest of my life. I am attaching a copy of my gross yearly income from my sales position during the last fifteen years. (See Exhibit 3).

Please respond to my settlement offer on or before April 15. I hope this matter could be resolved amicably.

Sincerely,

Susan Kim
Enclosures

Suppose you are Bruce Levin. You have just confirmed that, for all practical purposes, Mrs. Kim will be unable to work at all during the next ten years, including all of 2002. Write a report, addressed to Donald West, Chief Administrator of Super, which covers the questions below.

Put the data from Exhibit 3 in an Excel file. Use Excel, along with this file, to determine Mrs. Kim's real income for the last fifteen years. Do this by first converting each price index from percent by dividing by 100. Then, divide gross income by your converted (adjusted) price index. Using Excel, find the mean, median, and standard deviation of her past real income. Explain the meaning of these statistics. Can you use mean income to forecast future earnings? Take into account both statistical and non-statistical considerations.

How do you interpret the price indices in Exhibit 3? How are they constructed? Use Excel regression to analyze the relationship between the adjusted price index (dependent variable, i.e. 1.136) and year (independent variable, i.e. 1987). Interpret your regression findings by discussing the coefficient of determination (R-square), the regression coefficient, the p-values, and the regression equation. Can you use the regression equation to predict the price indices? Take into account statistical, macroeconomic, and other considerations.

Assume that Mrs. Kim's real income will not change over the next ten years. Use the mean real income from question 1 to determine projected real income for the future ten years of Mrs. Kim's work expectancy. Use the regression equation from question 2 to project adjusted price indices for the next ten years. Assume that Mrs. Kim pays 20% of her actual income in taxes and that Green will not provide significant state assistance. Use the projected real income and adjusted price indices to estimate Mrs. Kim's net actual income for the next ten years. What would be the likely amount of an award to Mrs. Kim based on a present value rate of 10%? Discuss the factors that could cause Mrs. Kim's future income to differ from your estimate.

Would the merchant's defense relieve Super Sisters, Inc. from liability under the cause of action of false imprisonment? In answering this question, please read and identify the relevant law from the following case precedent: Thomson v. LeBlanc, 336 So. 2d 344 (1976).

Assuming that Super Sisters, Inc. is liable for false imprisonment and assuming that Mrs. Kim is deemed unable to locate another job for life due to her present medical condition, is a court likely to award her compensation for loss of future income? What standard will a court consider in determining whether Mrs. Kim is entitled to compensation? In your opinion, is Mrs. Kim's settlement offer reasonable? Support your opinions with a discussion of the legal and practical possibilities. In answering this question, please read and identify the relevant law from the following case precedent: Caldwell v. Kehler, 643 A.2d 564 (1994).

What actions would you recommend should be taken to prevent a reoccurrence of a situation similar to that involving Mrs. Kim? What company policies need to changed or added? Discuss the relevant management issues.

EXHIBIT 3

Number	Year	Gross Income	Price Index*
1	1987	41,273	113.6
2	1988	42,805	118.3
3	1989	44,239	124.0
4	1990	45,724	130.7
5	1991	47,472	136.2
6	1992	49,391	140.3
7	1993	52,888	144.3
8	1994	50,547	148.2
9	1995	54,810	152.4
10	1996	55,019	156.9
11	1997	58,734	160.5
12	1998	55,879	163.0
13	1999	61,125	166.6
14	2000	59,350	172.2
15	2001	62,781	177.1

* Source: U.S. Department of Labor, Urban Consumers, 1982 - 1984 = 100

SPORTS DE FRANCE, S.A.

D.K. "Skip" Smith, Southeast Missouri State University
Claude Chamorand, University of Law, Economics, and Sciences of Aix

CASE OVERVIEW

This case poses a dilemma faced by mature retail chains: how can the company continue to increase revenues when it can no longer grow (for environmental, financial, and/or legal reasons) by inserting clones of existing stores into new markets? The case begins by indicating that Sports de France, a major sporting goods retailer with outlets throughout suburban Europe, has decided to terminate its unsuccessful 10 year initiative to increase revenues and profits by introducing retail sporting goods shops in city centres in France. At the last minute, however, the experienced manager assigned to terminate the initiative finds reasons to believe that adoption of a new retail strategy for the city centre shops could save the project. The challenge for students is to develop a new and profitable retail strategy. The case is based on discussions conducted by the authors in France. The case is appropriate for undergraduates as well as students in MBA and Executive Development programs. It is designed to be taught in a 1.5 hour long class session, and is likely to require a couple of hours of preparation by students.

CASE SYNOPSIS

Bernard LaCrois is Special Assistant to Louis Verdun, Chairman of Sports de France. The company owns and successfully operates a chain of large sporting goods stores in suburban locations not only throughout France but also throughout Europe as well. For the past 10 years, the company has been attempting to increase its revenues and profits by developing small retail sporting goods shops in city centres in France. Each of these last 10 years, however, this city centre initiative has generated losses of approximately half a million dollars. Based on the company's inability to generate profits from the city centre shops, Chairman Verdun has decided to terminate this initiative, and has assigned LaCrois responsibility for accomplishing this objective within the next 180 days. However, discussions with the retail consultant hired to help terminate this initiative have convinced LaCrois that one last attempt should be made to see whether the city centre shops can be made profitable. Data and information in the case include:

1. *Description of the challenge faced by the company.*
2. *On the company: Historical overview, current performance, and the business model underlying that performance.*

3. *Characteristics of the retail strategy which the company has been using for its city centre shops.*
4. *Characteristics of the competitive situation.*
5. *Information on the attitudes, shopping behaviors, and lifestyles of consumers living in city centres in France.*

THE SITUATION

After a ten-year effort, Sports de France Chairman and owner Louis Verdun had announced his decision to terminate the company's City Centre Shops Project. As members of the management team packed up their notes and printouts, Verdun summoned Bernard LaCrois, special assistant to the Chairman, to give him instructions regarding the termination. Verdun's instructions were simple, and focused on three points: (1) LaCrois would be in command of the liquidation; (2) Verdun did not care how LaCrois executed the closure; and (3) Verdun wanted the City Centre Shops Project and the string of loses which it had generated over the previous ten years terminated within the next 180 days.

THE INDUSTRY

Global trade in leisure and sporting goods has increased dramatically, based on increased interest in sports from the French and many other nationalities. Over the last 25 years, the number of sport and leisure stores in France has doubled, and the number of employees working in such shops has quadrupled. The sector now employs 45,000 people (more than 2% of all retail employees), working in nearly 11,000 shops. On average, there is one sporting goods store in France for each 5,300 inhabitants. Over the last five years, sales turnover for this sector has increased 20%; during the same period, sales for all nonfood retailers grew only 10%.

While independent sporting goods shops still exist, sporting goods and apparel is a strongly concentrated industry. Worldwide, as indicated in Table 1, the top 11 brands account for more than 2/3 of total sales.

In France, two giants (Sports de France and Go Sport) dominate the sector. Go Sport operates a chain of more than 100 sporting goods stores, mostly in France but also in Belgium and Poland. GO Sport's stores have shifted focus away from apparel sales, to selling and renting sporting equipment. The company markets well-known sports equipment names as well as its own brands of sporting goods under the "GO Sport" and "Wannabee" labels. French parent Rallye (a food retailer), which owns 70% of the company, plans to merge GO Sport with its sports shoe retailing subsidiary, called "Courir." Courir operates more than 130 stores. In France, Sports de France and

Go Sport hold an increasing share of the sporting goods market. In this category, and as indicated in Table 2, specialty stores dominate other all other vendors of sporting goods.

SPORTING GOODS-RELATED BEHAVIORS AND ATTITUDES IN FRANCE

Ten years ago, the primary market would have been sportsmen in search of reliable and functional technical gear. Today, however, a third of French consumers practice sports at least once per week. Furthermore, many people today buy sporting goods to improve their physical well-being, their comfort, and/or their health. At 120 euros per capita, spending in France on sporting goods is higher than in any other country in Europe except Germany and Sweden. The percentages of these expenditures spent on sporting equipment, sporting apparel, and sporting footwear are 29%, 42%, and 22%, respectively. Part of the explanation for the fact that high percentages of sporting goods expenditures are for apparel and shoes is that consumers use these items not only for sport but for casual wear as well. In 1996, sporting apparel and shoes in France represented a market of more than two billion dollars.

THE COMPANY AND ITS CITY CENTRE SHOP PROJECT

Thirty years ago, Sports de France (hence, SDF) launched the idea of large (7000 square meters) self-service retail sporting goods stores in suburban shopping malls in France. The basic idea was to offer a wide assortment of sporting equipment and sports-related apparel to the young adults and families living in suburban France. For these customers, typical shopping behaviors would include driving to the mall once a week, parking in the lots surrounding the store, making their purchases, and then driving themselves and their purchases home.

SDF's "self-service large sporting goods stores" concept was successful, and the company grew rapidly, both in terms of revenues and profits and in terms of number of stores. However, the suburban customers targeted by the company were price-sensitive. For this reason, about 10 years after opening its first store, SDF began introducing its own private brand sporting equipment. These products were manufactured by third parties to specifications which SDF set at world-class levels and monitored intensively. Ultimately, the range of products manufactured by SDF and sold under one of its brand names included archery equipment, bicycles, fishing tackle, hiking and mountaineering gear, riding equipment, running shoes and clothing, team sport-related clothing and equipment (cricket, rugby, soccer), windsurfing clothing and equipment, etc. The products were manufactured not only in France and other European locations, but also in South America (Brazil and Mexico) and in Asia (Bangladesh, China, India, Korea, Japan, Taiwan, Thailand, and Vietnam).

For SDF, this private brand strategy had two important advantages: (1) It allowed the company to sell at lower prices than major sporting goods manufacturers such as Aididas, Solomon, and Nike; and (2) Under French law, only producers are allowed to advertise on national television. Because SDF was now selling its own private brand equipment, it was now allowed to advertise those brands on national television.

The private brands allowed SDF to offer its sporting goods customers very good value for money compared to national and/or international brands such as Aididas, Nike, and Solomon. Consequently, sales from existing stores grew rapidly. The company continued to add new locations, both in France and overseas. As it approached its 30th anniversary, SDF had more than 300 stores, approximately 2/3 of which were located in France. All but a few of the remainder were located elsewhere in Europe (specifically, Belgium, England, Germany, Italy, Netherlands, Portugal, and Spain). In recent years, total revenues from the stores have exceeded two billion dollars. Because its margins on the private brand goods are high, SDF has been highly profitable.

As indicated above, SDF's "self-service large sporting goods store" concept has been highly successful. However, as the number of stores increased and the number of attractive suburban markets in Europe (and especially, in France) without a SDF store decreased, the company found it was becoming difficult to grow. For this reason (i.e., in an attempt to find new ways to grow its business), 10 years ago the company launched an initiative to put small shops (500 square meters) in town and city center locations. Initial characteristics of the City Centre Shops Project (hence, CCSP) initiative included:

1. Except for sleeping bags and climbing ropes, the products carried in CCSP locations were limited to sports-related apparel such as SDF's private brand ski jackets, jogging suits, swimming suits, etc. Management's rationale for this decision was that because many shoppers would be on foot (parking in city centres is difficult, and many city centre customers do not own a car), it would be difficult for CCSP customers to go home with heavy equipment such as golf clubs, skis, windsurfers, etc. Compared to the internationally-branded sporting goods equipment and clothing on display in competing city centre shops and stores, the product assortment on display in CCSP shops was not impressive.
2. Because the number of CCSP locations was small, promotional efforts used newspapers in local markets, instead of the national television used for the large suburban stores.
3. Other elements of the marketing strategy for the CCSP locations were similar to those used at SDF's large suburban stores. Prices at the CCSP locations were the same as prices at SDF's suburban stores; in other words, CCSP prices were very low compared with prices at surrounding city centre retail shops. Levels of customer assistance, service, and staffing were similar at the CCSP locations as at SDF's self-service suburban locations, that is, very low compared to the service available to other city centre shops.

Over the following ten years, SDF's CCSP project lost half a million dollars each year. Ultimately, the executive in charge of the CCSP was fired, and (as indicated earlier) Bernard LaCrois, special assistant to the Chairman, was assigned the task of terminating the project.
To help him fire CCSP staff and dispose of the CCSP properties which SDF had purchased or leased, LaCrois hired a consultant with many years experience in managing city centre retail stores in France. Over the next several days, LaCrois spent hours listening to the consultant's comments about the attitudes and behaviors of customers living in city centres in France. Comments made by the consultant included the following:

1. As indicated earlier, 75% of the French population lives in urban areas, so the retail potential of city centre shops could be huge. In short, the retail consultant confirmed the fact that SDF's interest in using CCSP locations to grow the company was in fact a reasonable idea.
2. The assumption that only old people (that is, grandparents) live in city centres is not correct. While city centres in France do include old people, there are young families living there as well, many with children. Of course, city centres in university towns have large numbers of students.
3. Adults (both singles and married couples, with or without children) and children living in city centres tend to be busy. They also tend to be on predictable schedules. Older consumers tend to go out and visit shops between 9:00-10:00 am, after having breakfast. Working adults living in French city centres tend to be free for lunch from 1:00-2:00 pm each day. Children going to school in city centres tend to be released from school for lunch from 11:30 am-12:30 pm. Mothers not working outside the home are likely to spend the time from 4:30-5:00 pm (just before children get out of school) shopping. The 30 minutes just before dinner (6:30-7:00 pm) is a time when both adults and children (including teenagers) are likely to shop. While customers patronizing suburban locations are likely to do one large shopping trip each week, customers in city centre locations may shop several times each day, making small purchases each time.
4. Because city centre customers are likely to make multiple small purchases each day, shop staff who are both knowledgeable on the one hand and able and willing to build personal relationships with customers on the other can be very important. In other words, close bonds between shop staff and customers can impact powerfully on the performance of retail shops located in city centres.
5. Older customers in France (both men and women) tend to favor blue and/or black colors. Children and teenagers prefer brighter colors. As for young adults (both married and unmarried), research conducted by SDF suggests that young women are far more likely to patronize city centre shops than young men. SDF research also indicates that the young women patronizing city centre shops are looking for clothing

that is not only fashionable, colorful, and correct-sized, but also has the technical characteristics (for example, waterproof, breathable, etc.) of serious outdoor equipment.

6. For big purchases, city centre customers are likely to shop the suburbs during weekends. However, city centre customers are also likely to come to the city centre shops during the week to see what sorts of products and services are available. In other words, during the week these consumers may collect information for their upcoming large weekend purchases in the suburbs.
7. For city centre customers, price comparisons are likely to be based on the prices they see in other city centre shops. For this reason, special promotions by city centre shops can be very effective. Most city centre shops carry national and/or international brand names (Aididas, Solomon, Nike, etc.). City centre shop patrons appear to have strong preferences for these national and/or international brands, as opposed to the private brand products which SDF has been selling successfully in its suburban stores.

THE CHALLENGE

Assume you are Bernard LaCrois. Based on what your consultant has told you about the attitudes and behaviors of consumers living in city centres in France, you have decided to make one last quick attempt to achieve success with the CCSP project. What will you do, and why?

Table 1: Total Revenues for Major Sporting Goods Chains

RANK	NAME	NATIONALITY	TOTAL REVENUES 2001
1	Intersport International	Suisse	5,909
2	Foot Locker	USA	4,379
3	Sport 2000 International	Germany	2,931
4	Sports de France	France	2,409
5	The Sports Authority	USA	1,416
6	Alpen	Japan	1,188
7	L.L. Bean	USA	1,140
8	Dick’s Sporting Goods	USA	1,075
9	JJB Sports	Great Britain	1,065
10	Footstar Athletic	USA	1,016
11	Canadian Tire	Canada	974
12	Karstadt/Quelle	Germany	967
13	Gart Sport	USA	936
14	Bass Pro Shops	USA	850
15	Cabela’s	USA	850
16	Academy Sports	USA	775
17	Rallye	France	769
18	R.E.I.	USA	740
19	The Finish Line	USA	701
20	Xebio	Japan	697
21	Pacific Sunwear	USA	685
22	Big 5 Sporting Goods	USA	623
23	Forzani	Canada	566
24	Blacks	UK	494
25	Galyan’s	USA	483
26	Joshuya	Japan	474
27	Sports Soccer	UK	461
28	Model’s	USA	460
29	JD Sports	UK	355
30	Victoria	Japan	340
31	Sport Eybl & Sports Experts	Austria	331
32	El Corte Ingles	Spain	328
33	Kaufhof	Germany	313
34	Journey’s	USA	301
35	Cisalfa Sports	Italy	282
36	Migro	Suisse	273
37	Himaraya	Japan	271
38	Sport Scheck	Germany	267
38	Stadium	Sweden	267

Table 1: Total Revenues for Major Sporting Goods Chains			
RANK	**NAME**	**NATIONALITY**	**TOTAL REVENUES 2001**
40	Play it again	USA	259
41	Gander Moutain	USA	250
42	Copelands	USA	245
43	Hibbett	USA	241
44	Dunham's	USA	240
45	Giacomelli Sports	Italy	231
46	Sport Chalet	USA	227
47	Golfsmith	USA	225
48	All Sports	UK	213
49	MC Sports	USA	210
49	Bob's Stores	USA	210
51	Edwin Watts	USA	200
52	Nicki Golf	Japan	189
53	Minami	Japan	181
54	Eastern Mtn Sports	USA	180
55	Honma Golf	Japan	178
56	Gresvig	Norway	176
57	Hervis	Austria	171
58	Murasaki	Japan	170
59	Ochsner	Suisse	148
60	Takamiya	Japan	140
61	Manor Group	Suisse	131
62	Rebel Sports	Australia	123
		TOTAL	34,059
Source: SGI – 2001 (millions of dollars) * CA TTC			

Table 2: Percentage of Sporting Goods Purchased from Various Categories of Retailers	
Specialty Stores	42%
Department Stores	19%
Apparel and Furniture Stores	15%
Hypermarkets and Grocery Stores	9%
Other Specialty Stores	7%
On Line and Catalog Stores	4%
Convenience Stores	2%
Brand Stores	2%
Source: F.P.S 2001/pays France	