

LEA E-Letter – 13 September 2005
Broken Business Models
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Dear Lean Community Member

When the CEO of the mighty Wal-Mart asks the UK government for protection from competition from Tesco, one fifth its size, it is clear something significant is going on. The rise of Tesco is not because it is better at dominating its home market than Wal-Mart is in the markets it serves in the US. Both benefit from enormous scale and purchasing power.

The difference is that Tesco has developed a superior lean business model that is exposing the cracks in the Wal-Mart business model. Through its loyalty cards it knows exactly who its customers are and what they want – Wal-Mart does not - they have opened a range of formats to mirror customer circumstances – which Wal-Mart is just thinking about – and they have developed a rapid, reflexive replenishment supply chain to serve all these formats, including home shopping.

I described a walk through their supply chain in my last letter. Quite simply Tesco is getting more of its customers exactly what they want, and where and when they want it at lower costs. The good news is that none of this is a secret; competitors can follow their example. It is not an exaggeration to call Tesco the Toyota of the grocery business. They are by no means perfect and, like Toyota, they have not lost the drive to keep improving all of their processes.

Another crack in a very successful business model was also exposed last week. BMW, the proud technology-driven premium carmaker, decided it could not develop hybrid engines alone (even though Honda is doing so). For years Daimler Benz and BMW dismissed hybrids as the future, claiming that diesels and hydrogen were the way forward and that they had all the answers. In the face of the huge expansion of third-generation hybrid car production by Toyota, BMW has joined forces with rival Daimler and General Motors to develop hybrids in a bid to catch up. Toyota's path to develop a new premium position is more in tune with consumer values than product proliferation and stuffing cars full of technology most of us never want to use.

In every industry the business models of the mass production and mass consumption era are broken or creaking. The "hub and spoke" airlines dependant on feeding traffic through big hub airports are struggling to compete with "point-to-point" airlines. Banks and telecoms firms losing customers as they outsource customer support. Retailers and manufacturers are beginning to question the "low cost" sourcing of cheap products in China, as responsiveness become more critical to compete in clothing and footwear. And maturing computer technology is even undermining the ability of Dell's "build to order" model to compete with

picking up an equivalent product in the local computer store the same day.

The list could go on – add in our own experiences of waiting in queues for diagnosis and treatment in large general hospitals and in car dealers waiting to get your car fixed. Changing times mean it is time to rethink these broken business models. In each case there are examples of firms that have begun to rethink their business models. They are beginning to demonstrate the huge potential of lean not only as an approach for streamlining processes, but as a strategy for turning the tables on your competitors and providing a better deal for consumers and their employees at the same time.

In rethinking the business models most organisations naturally start by asking what products they should make in the future, what assets they will need to make them and where they should be located. Lean thinkers on the other hand begin by asking who the customers are, what problems they are trying to solve using these products and services and how best to organise to serve them.

It is not the computer, but the combination of the hardware, the software and the knowledge of how to use them that allow us to process documents and send them to others. And obtaining, installing, upgrading and replacing all these is a process involving the consumer's time and patience, just like production.

Following this consumption process reveals that many of the interfaces with the provider's process which mirrors it are broken and frustrating. Moreover they have often been outsourced so direct contact with the consumer is lost and there is no feedback loop to help redesign the product or the processes of obtaining and using it.

In our *Lean Solutions* book we show how mapping these processes back from the consumer through several layers of distributors to production and all the way back to raw materials reveals really staggering opportunities for removing layers of cost for all parties, including the consumer. It really can be a win-win-win for all concerned. Better customer service as well as greater convenience turn out to be as free as quality in a lean system.

The ability to think back from the consumer and to design provision systems that can solve their problems by getting them exactly what they want, where and when they want it at minimum cost will be critical to success in the future. The key question will not be who makes the products but who coordinates the provision of all the elements on an ongoing basis to the consumer.

In the end survival in this challenging environment will depend on the ability and speed with which firms can rethink the business models for their value streams and write off and replace old assets that stand in the way of progress. Firms that are too slow to change will almost certainly be replaced by lean entrepreneurs who figure out how to make lean,

consumer-focused business models work. Will you join them or be swept aside?

Yours sincerely
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PS. Our *Lean Solutions* book outlines a set of principles and a method for rethinking your business models back from the consumer, together with examples of firms already doing so. Join us at the Frontiers of Lean Summit in Stratford-upon-Avon on October 31st (details at www.leanuk.org) as we present these ideas and examples for the first time. And bring your colleagues, customers and suppliers.