The consumer electronics industry squeeze play

Introduction
Industry observers have watched as a steady stream of nontraditional competitors continues to flow into an already crowded consumer electronics marketplace. Signs of change are everywhere.

Consider the choice of keynote speakers at the 2001 Consumer Electronics Show, the roster of businesses highlighted in ZDNet.com’s “Ten hottest products at CES;” or the chair of the committee charged with adding a wireless dimension to IEEE 1394. New entrants — whether “no name” competitors or industry crossovers — are rapidly earning lead positions and displacing established players.

As if bracing for a competitive onslaught is not enough, consumer electronics makers must face another challenge — affordable supply. Shortages inevitably occur. Which manufacturing partners will suppliers favor — the traditional electronics manufacturer, the conglomerate with a broad array of products and services, or perhaps their very own product line? Where will loyalties lie? With significant pressure mounting on both ends of the value chain, what will keep you — as a consumer electronics company — from being squeezed out of play?
Who will win with the consumer?

As industry lines blur and enterprises search for new sources of revenue, it’s worth taking a closer look at some new competitors, including what’s driving them to consumer electronics and the assets and capabilities they bring with them.

**New device makers**
Bent on taking advantage of growing trends, such as wireless access and device convergence, new entrants are springing up to offer specialty products with simple interface designs and highly desirable functionality. Since their inception, products built for mobile use have typically been bundled with some type of services package, which helps buffer device makers from the cyclical nature of hardware sales. Because of their relative youth, these businesses are often more agile; they have internalized the “need for speed” enterprisewide, evidenced by how quickly they bring products to market.

**Content providers**
These companies control what consumers spend discretionary dollars for: entertainment. Based on years of experience, they’ve become quite adept at getting their products delivered through others. (Just think about the channels for selling a movie.) Whether popular broadcast companies or successful Web portals, these providers carry considerable clout with consumers.

Aligning with a strong content provider can spell success for an electronics company … or just the opposite. Some manufacturers—particularly established companies diversifying into consumer electronics—are acquiring popular content providers in order to accelerate market acceptance of their own products.

**Access providers**
Businesses that electronically enter homes to deliver services to consumers—from electricity to Internet access—are having to decide whether to battle for control of the networked home themselves, concede to other, “better connected” competitors, or join forces with their peers. As telephone, television and computer networks converge, who will be the gatekeeper? Many argue that set top box manufacturers will eventually dominate the interactive relationship with the end consumer, since their product will serve as a home’s electronic command center. Whether based on existing wire, new wire or wireless technologies, leading access companies will expect innovative home-networking plans from their electronics partners.

**Computer hardware and software companies**
Typically, these businesses enter the consumer electronics market with a large installed base of loyal customers. They initially promote gadgets that use, connect to or in
some way complement their existing products. Although many still sell through retailers, most have also invested heavily in developing direct relationships with consumers. In fact, 24 percent of all personal computer sales occurred online during 2000. Leaders have successfully migrated to a digital supply chain, allowing them to drastically cut manufacturing costs and offer made-to-order products. With uncertainty clouding the future of the PC market, continued diversification into other industries—such as electronics and games—seems both probable and predictable.

**Appliance manufacturers**

Major appliance manufacturers that are busy Web-enabling their own product lines are gaining valuable experience, which they can easily extend into the consumer electronics space. Since their industry began, home appliance makers have focused on designing products that save people time. These companies’ consumer insights—and their respected brands—will be valuable assets as they design and promote newly announced home electronic devices. Historically, appliance businesses have focused on understanding and catering to the female buyer—a strategy that could also provide a unique perspective on consumer electronics design and marketing for the networked home.

Competition is coming from “within” as well. Major industry suppliers have announced vertical product lines of their own—competing head-to-head with established businesses and leaving the manufacturers that depend on them in a precarious position.

Over the next few years, as computing becomes more pervasive and everything around us becomes “smart,” any oversupply of semiconductors will fade into shortage. How will suppliers handle their new lever of control—particularly when they may have their own product line to support?

Imagine a situation where over 90 percent of a product’s cost comes from a couple of components procured from a single supplier. As a supplier, the temptation to undercut current device makers—with a better-priced product line of its own—would be tremendous.

With product price increases out of the question, escalating supply costs could usurp the already slim profit margin typically gained on an electronics product. A key supplier turned competitor can deliver a one-two punch by stealing market share and playing havoc with component costs.

How loyal is your team?
For traditional consumer electronics makers, the risk of slipping into commodity status—or being totally eliminated from the value chain—is real. Over the next few years, some electronics companies will be squeezed out of play; others will become pennant leaders. What will make the difference?

**Be the best at your position**
A reputation for product innovation is definitely an asset. However, with the Consumer Electronics Association reporting more new products being announced between 1998 and 2003 than during the industry’s entire history, volume and frequency of product introductions may not be the only measure of an innovative culture. Operational innovation—how one relates to consumers and interacts with suppliers, distributors and retailers—will also help distinguish industry leaders.

**Spend time with the fans**
Electronics manufacturers can no longer afford to relegate responsibility for managing customer relationships to retailers. Instead, these companies must collaborate with retailers to collect pertinent consumer data—then mine it for insights that lead to cross- and up-selling opportunities, better product designs and increased brand loyalty.

**Sign with the right team**
It is unlikely that one company—or even one industry—will dominate in such a competitive environment. Strong partnerships—with suppliers, access providers and content creators—will be key. Selecting the “right” partner will be even more important—splitting profits 20/80 with a market leader could be much more lucrative than a 50/50 split with a laggard.

**Take a cut of the gate**
Rather than focus exclusively on product sales, leading electronics makers will find ways to create recurring revenue streams. Market winners will bundle hardware product with a service, content or “packaged solution” to address a unique consumer need. Another tactic might be to reverse roles and become an industry supplier—earning royalty payments from licensing a popular component design or software feature used industrywide. With pervasive computing and wireless technologies opening many uncharted areas, new opportunities are waiting to be explored.

**Recognize the importance of teamwork**
Consumer electronics companies can no longer operate as if they are the dominant partners in the manufacturer-supplier relationship. By cultivating win-win relationships with key suppliers and interlocking business operations through digital supply chains, manufacturers can...
make it difficult for suppliers to break ties. Leaders will carefully evaluate electronic marketplace options in light of their business strategy—participating in public e-marketplaces or establishing a private exchange when and where it makes sense.

**Stay on good terms with the umpires**
To maintain favorable legislative environments in the geographies where they compete, electronics makers should stay politically informed and involved. Today, many consumer electronics companies find themselves continually assuming a defensive posture; industry leaders play offense—combining forces with providers of complementary offerings, allies—even competitors—to build joint strategies for anticipated political challenges.

**Make the rules**
Successful consumer electronics manufacturers recognize the ability of industry standards to make or break products. They actively participate in creating “the rules”—not simply devoting engineering resources, but also committing senior business and marketing executives to the effort. By capturing a lead role in an important trade association committee, the playing field tilts in their favor.

**Have a game plan**
Sometimes it appears as though electronics makers only know how to throw one pitch—the price drop. As the game becomes more competitive, leaders will need a broader repertoire, such as a keen fastball (speed to market), a curve (unanticipated alliance) or a changeup (a unique combination of services and products). They will also require a solid management system to simultaneously nurture, coordinate and control all of their e-business initiatives—both domestic and global.
Spend a moment reflecting on your position in the marketplace. Are you where you want to be? To help pinpoint where some additional attention might be needed, assess your team using the scorecard below. On each line, circle the statement that most closely depicts your current business operations.

<table>
<thead>
<tr>
<th>Scorecard</th>
<th>Minor League</th>
<th>Major League</th>
<th>Pennant Leader</th>
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<tbody>
<tr>
<td><strong>Business strategy</strong></td>
<td>Our view of the horizon is cloudy; we react to near-term threats or opportunities</td>
<td>We’ve got a clear view of the horizon but lack the flexibility to respond before opportunities pass</td>
<td>We anticipate; our management system is flexible, and we’re well-positioned in emerging arenas</td>
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<td><strong>Value from IT investment</strong></td>
<td>Still manage a few things manually because systems don’t fully meet needs</td>
<td>We are beginning to see returns from our recent ERP application investment</td>
<td>IT offers competitive advantage enterprise-wide, and is inexorably linked to business strategy</td>
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<td><strong>Retailer relationships</strong></td>
<td>Allot limited shelf space (to meet price point in merchandising plan)</td>
<td>Support full product line—in their stores and on their Web site</td>
<td>As interdependent partners, manufacturer and retailer plan jointly and share in the end consumer relationship</td>
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<tr>
<td><strong>Influence</strong></td>
<td>Rely on trade shows, magazines and the “grapevine”</td>
<td>Devote resources to participation in cross-industry initiatives</td>
<td>Chair trade association committees on critical issues</td>
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<tr>
<td><strong>Consumer interaction</strong></td>
<td>Limited direct contact and low visibility into consumer data</td>
<td>Offer consumer channel choices—including the Web—for information, purchase and post-sale support</td>
<td>Capture and use a comprehensive view of consumer data—from a variety of channels</td>
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<tr>
<td><strong>Brand value</strong></td>
<td>Good product at a great price</td>
<td>Enhanced by valued services and content</td>
<td>Exclusive content or service; highly personalized to meet specific consumer wants and needs</td>
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<tr>
<td><strong>Innovation</strong></td>
<td>Imitate more often than innovate</td>
<td>Cross-functional collaboration fuels innovation</td>
<td>Innovation is spurred by direct consumer feedback delivered in realtime to designers</td>
</tr>
<tr>
<td><strong>End-to-end process</strong></td>
<td>Air freight shipments and emergency orders are routine</td>
<td>Supply chain management is automated and most internal systems are electronically linked</td>
<td>End-to-end electronic linkages match supply and consumer demand, and allow real-time balance with marketplace dynamics</td>
</tr>
</tbody>
</table>
After you’ve ranked yourself, try scoring your top five competitors. (Those surprised to hear that Bill Gates [Microsoft], Craig Barrett [Intel] and Barry Schuler [AOL] gave keynote addresses at CES 2001 and that Steven Bard [Intel] chairs the IEEE 1394 extended committee might also want to pencil in scores for some “new” competitors in your industry.)

Where did you end up in the standings? If you found yourself spending more time in the minors than in the pennant race, we’d like to help. Our consultants would welcome the opportunity to share some of the strategic decisions, organizational issues and implementation trade-offs IBM faced in its transition to an end-to-end e-business. We’ve also put together a simulator that helps demonstrate the effect industry best practices have on day-to-day operations. In short, we’re ready to help you move up to the next level. To explore how we might put our consumer electronics industry knowledge and experience to work for you, contact us at insights@us.ibm.com. To locate additional resources for business executives, please visit our Web site at:

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References

