Marshall Management Consulting Club

Practice Case Workbook I

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Contents

Tips on Case Interviewing

Tips to help you crack the case every time (Wetfeet)

- Listen carefully to the material presented. Take notes if you want to, and be sure to ask questions if you are unsure about details.

- Take your time. You're not expected to have a brilliant solution to a complex problem on the tip of your tongue. If you need a minute or two to collect your thoughts and work through your answer, say so.

- Offer a general statement or framework up front to serve as an outline for your answer. Although the framework can be something as elaborate as a 3C (customer, company, competition) model, it need not be anything more than something like: If you're asking about declining profits, then I'd want to check into factors affecting cost, and factors affecting revenues. On the cost side..." As you proceed with your answer, draw on the outline of your framework.

- Home in on key issues. Many interviewers will be checking to see if you operate by the 80-20 rule, which means you should first address the broader issues that will get you 80 percent of the way to a good solution.

- Orient your answer toward action. Theory is good for the classroom, but it won't fly in a boardroom. Clients want to know what steps they can take to solve a problem, not pie-in-the-sky philosophy.

- Think out loud. The interviewer is looking as much for evidence of a logical thought process as for a brilliant conclusion to the case problem.

- Be conscious of resources. A lot of consulting work involves figuring out how you are going to collect the information you need to answer a question—without costing the client a fortune. If it relates to the problem, ask your interviewer about the budget, capital, and other resources that the client can allocate to the solution.

Above all, have fun with the case! Consulting is really like a steady succession of case interview questions. To do well, you need to enjoy the intellectual challenge of analyzing tough problems and coming up with reasonable solutions.

Tips to prepare for the case interview (BCG)

We want you to do your best in the case interview. Here are a few tips that may make a difference for you!

Structure

- Follow a logical structure. We suggest you approach the case by following these five steps to generate a hypothesis and supporting arguments.
    1. Listen closely to the situation and to the questions you'll be asked
    2. Firmly establish your understanding of the case
    3. Create an approach that focuses on critical issues and guides your analysis
    4. Analyze the problem. Ask the interviewer focused questions and evaluate the situation
    5. Clearly summarize your final analysis and conclusions

- Think out loud so that the interviewer understands the direction of your thinking. You may also want to write down your findings and assumptions.

- Remember, there is no "right" way of doing a case; nor is there a single answer. If you have demonstrated the way you think, you have done all you can to "crack the case."

Attitude

- Interact with the interviewer. The case should be a dialogue, not a monologue.

- Pace yourself. It's important to not rush to conclusions.

- And perhaps most important, relax and have fun.

How to Solve A Case (Mercer)

Most case interviews follow a similar pattern. They begin with some background on the case and the challenge posed by the client/interviewer. You then may be able to ask a couple of clarifying questions if necessary. Then it's up to you to determine how you'll analyze the case (which framework, structure or strategy) and get started.

Step 1. Get information

- Listen to the problem
- Ask clarifying questions

Sometimes the interviewer may leave out a key piece of information and see if you notice. That leaves the perfect opportunity for a clarifying question. Be careful, though—don't spend too much time asking unstructured clarifying questions. Try to limit them to two or three key questions before moving on to the next step and creating a structured approach.

Step 2. Create a structured approach

- If appropriate, consider a framework you may have studied
- Make sure the framework covers the areas you consider important to the case—alter the framework as necessary or just create your own
- At the very least, highlight various conceptual "buckets" into which you can organize your thoughts (industry information, customers, competition, etc.)

Do not make the mistake of forcing a framework on a case. Remember to trust your common sense and analytical abilities rather than blindly applying frameworks regardless of their applicability.

Step 3. Walk through the framework

- Generate key questions to begin the investigation and analysis of each part of the framework (or each "conceptual bucket")
- Starting with the broadest areas, ask just enough questions to probe into each concept or step of the framework, without delving too deeply or getting off track

- Continually ask yourself the "so what?" of every piece of information you receive—you will either find insight or the realization that you are wallowing in an unimportant part of the case
- Throughout the process, generate and test hypotheses

Here's where those logical thinking skills come into play. This is generally what people refer to when they talk about "cracking the case". Structure can still play an important role, so be sure to ask the key questions that will focus your analysis.

Step 4. Present a recommendation

- Determine your recommendation based on the information you have uncovered and the analysis you have completed
- Explain to the interviewer the supporting insight for your recommendation (list 3 or 4 of the top insights you gained from the case that led you to your recommendation)
- Recommend next steps and any possible caveats, if appropriate

This is where you reveal the answer. Having been through this a few times ourselves (on both sides of the table), we'd like to offer our perspective on "the answer". If you've gotten to this point in an interview through a structured approach and rigorous analysis, then two things will start to become clear.

The first thing is that the answer is probably pretty obvious, which is the good news. The second thing is that the answer is almost irrelevant. In a case interview, it's less important where you go and more important how you got there. So worry less about whether or not you got the "correct answer" and focus on how to get to an answer through a remarkably structured approach and stunningly rigorous analysis.

<u>Case Commandments (Casequestions.com)</u>

1. **Listen to the Question**

   Listening is the most important skill a consultant has. The case isn't about you or the consultant. it's about the client. What are they really asking for? Pay particular attention to the last sentence – one word can change the entire case.

2. **Take Notes**

   Taking notes during the case interview allows you to check back with the facts of the case. As someone once said, "The palest ink is stronger than the best memory." If you blank out, all the information is right in front of you.

3. **Summarize the Question**

   After you are given the question, take a moment to summarize the highlights out loud:

   - It shows the interviewer that you listened
   - It allows you to hear the information again
   - It keeps you from answering the wrong question
   - It fills the otherwise awkward pause when you're trying to think of something intelligent to say

4. **Verify the Objective(s)**

Professional consultants always ask their clients to verify their objective(s). Even if the objectives seem obvious, there could be an additional underlying objective. When the objective seems apparent, phrase the questions differently: "One objective is to increase sales. Are there any other objectives I should know about?"

5. **Ask Clarifying Questions**

You ask questions for three main reasons:

- To get additional information that will help you identify and label the question
- To demonstrate to the interviewer that you are not shy about asking probing questions under difficult circumstances (something you'll be doing on a regular basis as a consultant)
- To turn the question into a conversation. Nothing turns an interviewer off quicker than a five-minute monologue.

6. **Organize Your Answer**

Identify and label your case, then lay out your structure. This is the hardest part of a case – and the most crucial. It drives your case and is often the major reason behind whether you get called back.

7. **Hold that Thought for "One Alligator"**

The interviewer wants you to think out loud, but think before speak. If you make a statement that is way off-base in an interview, the interviewer will wonder if he can trust you in front of a client.

8. **Manage Your Time**

Your answer should be as linear as possible. Don't get bogged down in the details. Answer from a macro –level and move the answer forward. Stay focused on the original question.

9. **By the Numbers**

If possible, try to work numbers into your answer. Demonstrate that you think quantitatively and that you are comfortable with numbers.

10. **Be Coachable**

Listen to the interviewer's feedback. Is she trying to guide you back on track? Pay attention to her body language. Are you boring her or is she enthralled?

11. **Be Creative and Brainstorm**

Consulting firms like liberal arts candidates with intellectual curiosity who can "think outside the box" and offer up a new and interesting perspective.

12. **Exude Enthusiasm and a Positive Attitude**

Recruiters want people who are excited by problem solving and can carry that enthusiasm throughout the entire interview.

13. Bring Closure and Summarize

Create a sense of closure by summarizing the case. Review your findings, restate your suggestions, and make recommendations.

Practice Cases

Cases from Vault.com

A bank is trying to increase its operating efficiency. Your consulting team has been asked to look at the non-interest, non-personnel expense base in order to cut costs. How would you determine the potential size of the opportunity for operating efficiency? What issues might arise in such a study?

This is an exercise in full-value procurement (FVP). FVP is a rationalization across business units of common purchases and services. The measure of an FVP is the amount of "spend" reduced, defined as the cost savings realized by reducing the number of sources from which common products/services are purchased. (This question, and questions like it that require advanced frameworks, are much more likely to be received by business school candidates and case interviewees with significant business experience than by undergraduates with no business experience.)

In this case interview, your interviewer will impersonate the client. Case interviews often take this kind of role-playing form (which can be fun!).

You: What is your revenue level on an annual basis like?

Interviewer: In 1998 our revenues were $1.2 billion. (These seem to be the revenues of a prosperous regional bank, not a bulge bracket.)

You: What are the common items and services that all business units use? Do you have common office suppliers or housekeeping services?

Interviewer: Well, obviously we have most common office products shared across all our functions. We also have cleaning services for our corporate headquarters, our printing center, and our retail locations.

You: How many vendors provide similar products and services to the bank?

Interviewer: We buy office products from OfficeMax's corporate services in Indiana, Avery Dennison corporate services in California, and someone else, the name of which escapes me right now, for the retail banks. Also, I believe we contract regionally for housekeeping services.

You: Is consolidating branch offices or reducing ATM counts a possibility?

Interviewer: Not at this time. In fact, we're planning to expand in three different states.

You: Are your cost concerns the result of an impending merger? (Perhaps the interviewer has deliberately left out an important piece of information - the bank has undergone, or is planning, a merger or acquisition of another bank that might drive up costs.)

Interviewer: No, our growth is organic, not through acquisition. (Looks like this is a dead end. Time to move on to other considerations.)

You: Have you considered outsourcing non-critical business tasks?

Interviewer: What kind do you suggest? (Your interviewer is probing to see if you can name the kind of services a bank might successfully outsource.)

You: Well, what about information systems, call centers and customers service, bill collection, document handling, those kind of things?

Interviewer: Oh, no. That's not possible. (Remember that this is a role play. This seems a bit uncommunicative for a reasonable suggestion; you should probe a bit further. Businesses aren't always entirely reasonable in their actions!)

You: Can you explain your objections?

Interviewer: Don't you think outsourcing those processes is extreme? We're a bank, and we have a lot of confidential information on both paper and electronic media. Our integrity would be put at risk if we let others manage our internal functions.

You: Well, sir, I understand your objections. However, many major corporations use organizations that centralize activities like copy centers and conference planning, all of which also have trade secrets and confidential information.

Interviewer: That sounds interesting, and I'd like more information. (Your interviewer graciously acknowledges the wisdom of your suggestions.) But can you give me a concrete suggestion my supervisor will like?

You: (Time to return to a less controversial aspect.) What would you estimate your spending to be for things like office products?

Interviewer: I estimate about $100 million on office products, corporation wide, in 1998, though you'd have to talk to our operations people, of course.

You: I think, based on your information, that there are ample opportunities for cost savings that I can identify right now. Reducing your vendors down to one or two will allow you to use economies of scale to extract cost savings. Outsourcing promises even greater savings.

You have been appointed the manager of a rental car company. How do you measure its efficiency?

This case question is a good candidate for the Value Chain approach.

- What are your expenses (cars, insurance, rental of car office, advertising)?
- What is your average rental time period? (On average how long is a car checked out?)
- How fast is a vehicle turned around (from drop-off to back on the line)? What is the industry average for this turnaround?
- What percentage of your fleet is down for repairs on average? How does this compare to the industry?
- What percentage of your employees call out sick every day on average? How does this compare to the industry?
- Does the business exhibit any seasonality (for example, are you located near a ski resort that sees business boom in the winter)? How do you account for these effects?

Another way to look at this question is to use a real-life "out-of-the-box" approach. Why not simply look out on the lot and see how many cars are rented out at any given time, and what kind they are - and do this over a period of time in different locations? This kind of real-world approach will win points with consultants, who actually have to drive around and look at parking lots at 4 a.m. (and other such hijinx) more often than they would probably like.

2. Our client has engaged us to assist them in reorganizing their sales force. They want to cut $50 million in costs from this area over the next two years.

This is an organizational change question. What is especially important here is to balance the financial realities of the situation against the organization impact of head count reduction, the introduction of new technologies, etc. Questions that would help focus this situation include:

- What is the primary business for this client?
- What is the timeline for the reorganization process?
- What is the early estimate of how many people could be involved?
- What is the scope of change? Does it include downsizing, the introduction of technologies, closing/selling-off of locations, reengineering business processes?
- What is the early assessment of the organizational climate for change? Are they receptive or resistive? What are the reasons for resistance if any?
- Can you describe any dynamics unique to this client's business that put the success of the project at risk?
- What are the major risk factors surrounding this project?
- What are the measurements of success for this project?

3. Your client is trying to decide whether or not to invest in a helicopter company. You have been asked to assess the long-term attractiveness of the helicopter market.

Since this case is primarily asking for an industry analysis (is this an attractive industry?), Porter's Five Forces is one framework useful in formulating your recommendation.

4. A large health care company has hired you to determine a strategy for improving profitability through growth. The company hopes to reach its goal in three years. What do you advise?

Note that your interviewer will often impose deadlines and other "constraints" that represent the wishes of the client (for example, the client wants to reach its goal within six months; the company wants to reach its goal without spending more than $5 million; etc.). You should not necessarily be constrained by the company's hoped-for timelines or budget constraints, unless your interviewer tells you otherwise. In this case, you should question whether three years is a realistic or even optimal timeline. Your job is to recommend the best course of action, including an optimal timeline, not to take your client's wishes as representing the best course of action.

5. Our client, ABC Airlines, is losing money. Why?

Remember to consider the firm's actions as well as external market forces such as the competitive environment. Questions include asking whether other airlines are losing money, or suffering drops in profits. If so, why? Causes might range from a rise in the cost of fuel, to the need to replace most of ABC's fleet due to stringent new government regulations, to a general slump in the economy that reduces the number of tourists and causes business customers to tighten their belts.

6. You are head of a large American corporation. Your company must build a new paper plant. You must decide which country to build the plant in. What factors would you consider?

Analyze your supply chain. Where do you incur your costs? If your paper plant is highly automated, it might make more sense to build it in America or another developed country where you have access to skilled labor. If, on the other hand, your paper plant requires thousand of employees, you may want to consider a country or region of America where the cost of labor is lower.

7. Your client is a major airline that wants to reduce the amount of money it spends per passenger on food service, ticketing, and baggage handling. What would you advise?

Benchmarking is one good starting point for this type of case. You would certainly want to know (or at least be able to estimate) how much other airlines spend on each passenger for food service, ticketing, and baggage handling. Are your client's costs in each of these areas high or low for the industry?

You would also want to examine "best practices": which airlines have the lowest costs in each of the three areas of food service, ticketing, and baggage handling? What are they doing right, and how can we emulate it? (Remember that best practices for a particular process may be found outside the airline industry. For example, how do passenger railroads or cruise ships ticket their passengers? Are companies in that industry doing anything particularly well that may apply to the airline business?)

You are the consultant to a company that produces large household appliances. Over the past three years, profit margins have fallen 20 percent and market share has tumbled to 15 percent of the market from 25 percent. What is the source of the company's problems?

This is an example of the type of question an undergraduate student (or an MBA student in an early interview round) might receive. The interviewer has done you the favor of defining the problem - your client is in something of a slump! This dialogue illustrates how you, the perspicacious candidate, might drill down into the core of the woes besetting the firm.

You: How would you characterize the current marketplace for these products? Emerging? Mature?

Interviewer: The product line is considered mature.

You: How would you characterize your manufacturing process relative to your competition? (You're looking to see if the company has a strategic advantage.)

Interviewer: Can you be more specific?

You: Do you benefit from an advantage in technology, economies of scale, exchange rates, or other manufacturing element over your competition?

Interviewer: We have not updated our manufacturing process since 1988. We manufacture our products exclusively in the United States. As one of the oldest manufacturers of these products, we have a reliable customer base and a good reputation. As for price, we are one of the lower-priced in the market, though not the lowest.

You: Do any of your competitors manufacture overseas?

Interviewer: Our number one competitor produces all of its appliances in Indonesia. (Here's your clue - manufacturing outside the country significantly lowers costs.)

You: It probably suffices to say that some of your decline in profit can be attributed to the increased costs you are facing relative to older manufacturing techniques and higher costs associated with manufacturing domestically. This is especially toxic in a mature market where consumers are mostly aware of the product category and the product may be considered a commodity. (A commodity marketplace is one in which customers make their purchasing decisions largely on price. For example, toilet paper is largely a commodity market, where consumers buy whatever's on sale.)

Let's talk about market share now. Can you tell me about any recent market research you have regarding the strength of your brand, price, your products' position, and any promotional activity you have had?

Interviewer: Our market research department has told us that consumers are confused about the product category, that they do not understand the differences between our brand and our competitors' brands. We sell to all major appliance retailers in the U.S. We promote aggressively twice a year, and have smaller promotions once a quarter. (This is consistent with the description of a commodity product. The ways of breaking out of commodity markets include promotions and making value-added differences in the brand - like, in the case of toilet paper, introducing new designer colors and specially quilted cotton-blend paper.)

You: What form does your promotional activity take?

Interviewer: We offer a price discount to consumers twice a year. We regularly advertise in major magazines targeted to our consumer, and we have an active outdoor campaign underway.

You: It would appear you are competing in an undifferentiated marketplace and there may be an opportunity to capture additional share through an aggressive brand differentiation effort. I believe it would also be worth investigating the efficacy of your current promotional programs, relative to your competition. The consumer may be responsive to other types of promotions that haven't been utilized by the company as of yet.

A restaurant owner is currently setting up a new restaurant and making some basic decisions on how to fit it out. He is today making a decision on the facilities to place in the restrooms for customers to dry their hands. Initial research suggests that he has three options - paper towels, roller towels and hot air dryers. What should he consider in his decision-making process?

In the initial analysis, you might ask a number of questions, which will influence your decision.

- What type of restaurant is it going to be - luxurious, budget, middle-market?
- How many customers does he expect? (How many tables? Is it open during the day? In the evening?)
- Has he done any customer research to see what customers would prefer?

Fairly soon in the process, you should start asking questions about the economics of the three options - in which case the interviewer will give you some more information:

In the initial research, the restaurant owner has found out the following information from the suppliers of the drying facilities:

- Dryers have an initial cost of $500 each (but you'll need two - one for each restroom) and monthly service charge of $100 per month. The supplier estimates that the lifetime of a dryer is four years.

- Paper towels cost 5 cents each and the number of paper towels that you will need (varies directly) with the number of customers. So if you expect 50 customers a night, they will use 50 towels.
- If you use toweling rolls, they will cost $5 per roll (and again you'll need two - one for each restroom). The rolls will be changed daily if the restaurant has more than 2,000 customers per month or every other day if there are less than 2,000 customers per month.

At this point, it's obvious that from an economic standpoint, the option you select will vary with the number of customers. Therefore, it makes sense to look at a break-even calculation.

First of all, take the dryers. They cost $100 per month, plus an upfront charge of $1,000 that you should depreciate over their lifetime (i.e. an additional $1,000/(4 x 12) per month = $21 per month). Therefore their total cost is approximately $120 per month - and this does not vary with the number of customers coming into the restaurant.

Secondly, look at the paper towels option. These vary directly with the number of customers in the restaurant, at a cost of $0.05 per customer. Therefore with a low number of customers per month, paper towels will be cheaper than dryers will. How many customers would have to come to the restaurant each month to make the dryers more cost effective? The cost of towels would have to exceed $120 per month, equating to $120/$0.05 = 2,400 customers per month.

Is this break-even affected by the rolls option? At less than 2,000 customers per month, the rolls would cost $10 every other day or $10 x 15 days = $150 per month. This in itself is more costly than both the dryer and the towels option, and with more than 2,000 customers, it will only look more unfavorable.

Therefore the real economic decision is between towels and dryers. At less than 2,400 customers per month (or 2,400/30 = 80 customers per night) you would prefer the towels. Once the number of customers increases above this, you'd switch to the dryers' option.

Following the economic analysis, you might mention a few more non-economic points that might sway the balance:

- Are there additional staff costs of cleaning up paper towel waste?
- How many suppliers of each option are there? If there is a single supplier, might he have the capacity to raise prices in the future?

Hints on quantitative cases:

- Make the numbers easy - round up or down when possible to make further calculations easier.
- When you're jotting down numbers, make sure you keep a track of what is what, so when you pull together your recommendations at the end of the analysis, you can make comparisons between the options.
- In break-even cases, it is sometimes effective to draw a graph to illustrate the break-even decision (in this case, number of customers per month along the x-axis vs. cost of drying option along the y-axis).

Practice M&A Cases

1. Eastern Newspapers is a large newspaper chain that is considering diversifying into non-newspaper media assets and is a potential client for our firm's M&A group. How would you go

about advising this client? What information would you want to gather before you meet with the client?

2. JerseyWeb is a small Internet access provider, with $20 million in annual revenues. JerseyWeb is considering acquiring another small Internet access provider in nearby Connecticut. What would you advise JerseyWeb to do?

3. A major ski resort currently forbids snowboarding, but is considering allowing the sport. What should it consider before allowing or disallowing snowboarding?

4. The maple syrup market has four main competitors. The market share and price per unit are as follows.

Absolute Syrup share 42 percent price per unit $5.00
Beastly Syrup share 27 percent price per unit $4.10
Catchall Syrup share 16 percent price per unit $3.50
Delight Syrup share 15 percent price per unit $3.55

What kind of market is this?

5. You are Britney Spears. You are afraid that the new craze for MP3s will hurt sales of your music. What should you do?

We have been engaged by a major entertainment company to assist them in building a distribution network for home video. They currently contract their distribution through other, more established, entities but the contracts with those companies are expiring and it is unclear whether the new contracts contain favorable terms or not. There is still a chance that our client may continue to distribute their products through a third party. How would you assess whether to build a distribution network or continue the contracts with the third parties?

First of all, you need to ask your interviewer some basic questions:

- It makes sense to ask your interviewer about best practices - that is, what are other entertainment companies doing? What are the current costs? Does the company have the staff and resources to create its own distribution network?
- Of the major entertainment companies that produce video, do most distribute through their own proprietary supply chain or through third parties?
- What is the client's current cost of distribution through its contractual partner(s)?
- Has the client attempted to assess building its own distribution network before retaining us? If so, what were its findings?
- Does the client have a dedicated functional staff assigned to the project? If so, what functional areas do they represent?

After establishing some basic facts, it's time to get more detailed. Your interviewer may allude to certain avenues to discuss, or shut down others. If the interviewer confirms that, yes, the company does have enough current staff to handle setting up its own network, there's no call to delve deeper into the ramifications of reassigning personnel. Let's say that, through questioning, you've come to decide that staying with a third-party distributor makes the most sense. Now the question is - should the company stay with its current distributor, or choose a new one?

- Who are possible alternative partners? Who uses them?

- Could you characterize the relationship between the client's distribution partner and the client? Is there a possibility of retaliation on the part of the distribution partner if the client severs its ties to this party?
- How many weeks of supply are currently in the distribution partner's pipeline?
- How receptive are the client's accounts to changing distribution partners? Has a value proposition been created to show the client's accounts that a client-owned supply chain would be more efficient, valuable, etc. to the accounts?
- Does the client have any financial interest in the distribution partner that might have to be severed?

After answering these questions, make a recommendation.

Your niece approaches you and says "Since you're a management consultant, maybe you can help me. I want to buy my mother a present for her birthday, and I was thinking of opening a lemonade stand to earn the money. Tell me what you think of my plan."

Isn't she cute? Yet this is a serious case (from Bain, no less). The interviewer is trying to see if you can set up a value chain for your niece. Get out your notepad.

You: What kind of present do you want to get for your mother?

Interviewer: I want to get her a pair of gold earrings.

You: That's a very nice idea. I'm going to assume that you want to buy a pair of earrings that cost $50.

Interviewer: Actually, the earrings I want cost $100. (The interviewer is trying to raise the bar a bit.)

You: Okay. When is your mom's birthday? What's your time-frame?

Interviewer: My mother's birthday is in three months.

You: What kind of time commitment can you make to the lemonade stand? How many days a week do you plan to run the stand?

Interviewer: I have to go to school during the week, so I think just on weekends.

You: Here are some of the considerations you need to make if you want to earn $100 in three months from your lemonade stand.

What are your expenses? Let's say that you need to buy the pitcher, which is $2. Every 100 plastic cups will cost you $1 in direct costs. Those are your base expenses.

You then have to make several cost decisions. What size cups will you use? Eight-ounce cups will mean that you can serve more cups of lemonade per pitcher. (If it's a gallon jug, with 64 ounces, then you can serve eight cups per pitcher. Sixteen-ounce cups, which may be perceived as a better value, means that you can serve only four per pitcher.)

You must also decide what kind of lemonade to serve. Lemonade made from powdered concentrate is probably the cheapest - perhaps $1 a gallon. Lemonade made from fresh squeezed lemons has a definite quality advantage, but it's more expensive. At $0.25 a lemon and eight lemons to a gallon, it would cost $2 for each gallon. And you might be able to get prepackaged lemonade sold at the store for $1.50 a gallon.

Interviewer: So how long will it take me to get enough money for the earrings?

You: Assume $10 in sunk costs - $2 for the pitcher and $8 for 800 cups. You then need to decide what to charge. If you charge 50 cents a cup of lemonade - which I believe is the upward end of lemonade stand prices - and it costs you $1 to make the cheapest gallon of lemonade, then you'd earn $3 on each gallon of lemonade sold. In four weekends in three months, you would need to sell 37 gallons of lemonade. Then you'd earn $111 dollars - enough to pay off the pitcher and cups. That's three gallons a weekend, or 24 cups of lemonade each weekend.

Interviewer: Does this sound reasonable to you?

You: So far, yes. But this is just the cost-structure. You must consider other factors as well. Who are your competitors? Are there other kids trying to sell lemonade at the same time? Are you located near delis and restaurants and street vendors who might sell competing beverages?

What is the demand for your product? Is it summertime, when people drink a lot of lemonade and are spending time outdoors, generating foot traffic? If not, you may have difficulty moving your lemonade. In cold weather, you might want to consider selling hot cider instead.

Where are you located? How many potential customers will pass your lemonade stand? Can you set up your lemonade stand at a sporting event, supermarket parking lot, or flea market, where many more people will pass your stand? If you just set up on the sidewalk, you may not attract the foot traffic to make those numbers. Indoor or sheltered locations are also preferable if the weather turns bad.

You have a competitive advantage - you're young and cute. You may get business from people who approve of your young entrepreneurial actions. At the same time, lemonade stands have a reputation for relatively poor lemonade, which may hurt your overall sales if you have competition.

Do you have any subsidies? That is, would your dad be willing to cover your start-up costs - the pitcher, the cups, and perhaps the cost of the lemonade. This would perhaps permit you to offer better-quality lemonade.

Consider your advertising. You'll need a big sign to call attention to your stand. You can rely on your parents for free - I assume - word of mouth.

You should also consider offering another product besides lemonade. Perhaps selling cookies or brownies, in addition to the lemonade, might increase your profits.

You should consider other revenue-generating activities as well. If you are 14, a paper route is a possibility. You may also be old enough to babysit.

It's also possible that you might be able to choose another pair of earrings, or find the ones you want on sale. This would lower your income requirements.

You are advising a credit card company that wants to market a prepaid phone card to its customers. Is this a good idea?

Whoa! Better find out more about this prepaid phone card first before you even begin to think about recommending the phone card.

You: What is the role of our company? Do we simply market the card or must we create them ourselves? Are we expected to provide the telephone services?

Interviewer: This card will be co-marketed with an outside phone company. We do not need to perform telecommunications functions.

You: What are our expenses connected with the card?

Interviewer: We must pay 15 cents for every minute we sell. We also have to pay $1.00 as a start-up cost for the card and card systems.

You: What are our marketing expenses?

Interviewer: We normally use slips of paper that are attached to the backs of our credit card payment envelopes. We sometimes also send customers a direct mailing - in a separate envelope. Or we can have telemarketers call selected customers.

You: What's the cost of each of these marketing techniques, and what is their response rate?

Interviewer: Telemarketers have a 2 percent response rate and cost $1.00 per call. Direct mailings cost us 40 cents per mailing and have a 0.50 percent rate of response. Our payment attachments have a 0.25 percent rate of response, but only cost us 5 cents each.

You: I'm going to assume we will sell one-hour phone cards. That will cost us $9.00 for the minutes and a dollar per card - so each card costs us $10.

Interviewer: Okay, that sounds reasonable.

You: And what is our expected revenue on a one-hour phone card? What is the current market rate for a 60-minute phone card?

Interviewer: Assume it's 50 cents a minute.

You: So if we sell the cards for $30, we have a $20 profit, minus our expenditures on marketing.

Interviewer: What's our cost structure look like?

You: Okay, let's figure this out. To sell 1,000 cards through telemarketing, we would need to contact 50,000 people. That would cost us $50,000. To use direct mail, we would have to contact 200,000 thousand people, which, at 40 cents per mailing, costs us $80,000. Since the envelope inserts aren't very reliable, we will need to contact 800,000 people using that method. But at 5 cents each, it costs only $20,000 to sell 1,000 cards.

We make $20 profit on each card. But even using the cheapest promotional vehicle, at $20 profit, we would only break even, because our profits on 1,000 cards would be $20,000. We shouldn't market this card, unless we can further cut our marketing costs or increase the price of the card. If we could slice the cost of the envelope attachments a penny or so, or sell the card for $35, or convince our co-marketer to reduce our costs, it might be worth selling.

Interviewer: What are some other issues you might want to consider? (Notice how the interviewer is nudging you to add to your analysis.)

You: We should also consider the competitive landscape for this business. Is the per-minute rate for calling card minutes expected to fall? If so, and our costs are held constant, we may lose money. Of course, we can learn more from marketing these cards. It could be that the people likely to buy these cards might be frequent travelers and could be targeted for other promotions.

You're a utilities company in a small town and you're having trouble getting your customers to pay on time. What do you do?

First of all, you'll need to know what kind of company you are. Electric? Gas? Phone? Could it be that you are based in a small, rural area where customers turn to their wood-burning stoves for heat and cooking power instead of gas? Have your customers adopted cell phones en masse and are now neglecting their regular phone bills? You won't know until you pin down the problem - and then you can determine a solution for the company's woes.

Some questions you should ask:

- Where are we based?
- What is the composition of our customer base?
- What percentage of our customers are not paying on time?
- How much money do we lose from slow payers?
- How many of those slow payers never pay?
- Is there a certain segment of the population that is not paying?
- Is the area in a recession or slump that affects the ability of customers to pay their bills?
- How late are the payments of the slow payers?
- What do we currently do to motivate slow payers to pay their bills?
- Are there any government or state regulations that will affect our actions?
- At what point do we currently cut off slow payers? (Perhaps the company is so slow to do so that customers are taking advantage of the company. Or, if the town is small enough, it's possible that there are employees who refuse to cut off power to their friends and family.)

After you've determined the nature of the problem, you can make a recommendation on how to solve it. You may have more than one problem. Perhaps your small town is home to a university, and students move frequently and often neglect their last utilities bills. (Can you work out an arrangement with the university that denies diplomas or registration to students that neglect their bills? Should you start asking for second and third addresses and contact numbers? Perhaps requiring a deposit from students to turn on power?) At the same time, your company may need to start charging higher late fees to other customers who are simply taking advantage of the six months of forgiveness your utility gives.

A multi-billion dollar consumer brand product manufacturer is considering introducing its flagship brand into Asia. What would you advise?

This is an example of a broad question where you must first assess the situation in more detail. A series of "helicoptering" questions:

- Why has the company engaged our services?
- What are the risk factors associated with this project?
- What is the timing for our involvement with this client and this project?
- What is the nature of the client's business? What is their flagship brand?

- What business unit within the organization has engaged us?

You should have more information about the nature of the project after these questions. From here, you can pursue a more specific series of questions. Let's say that in response to your questions, you learn that the project involves a software package selection for automating trade promotions activity in preparation for entry into Asia. (Now you see why it's so important to ask questions) The next set of questions you should ask would be drilldowns - teasing out the finer points - on the information you've just gathered. For example:

- Have any vendors been identified for the selection? If so, whom?
- What is the timeframe for the package selection?
- What client staff will be participating in the project? What are their roles in the organization?
- What experience does the firm have with similar engagements/industries? Can we draw upon that experience for this engagement? Why or why not?
- Has a workplan been developed for this project? What is an overview of this plan?
- What are the measures that have been established to evaluate the success of this selection?

Why is Intel successful? Will they retain their advantage in the future?

Do you have a high-tech background? Does your interviewer want to see if you can think in broad strategic terms and if you've been following your industry? Then you might get a strategy analysis question like this one.

The interviewer is not expecting you to quote the latest stock price of Intel or know how much CEO Craig Barrett got paid last year. She wants you to explore what the company does right and the challenges that it faces in the future. Any business knowledge that you have will come in handy.

Well, what do you know about Intel? You should know that Intel is a producer of microprocessors (or chips), an essential component of computers. (That's about the level of knowledge you need.) Intel currently has about 80 percent of the microprocessor market. Clearly, they're doing something right, but what?

Intel is a technology company. In a rapidly evolving market like the computer industry, staying abreast of changes in technology is vital. You might point out that Intel's heavy investment in R&D has consistently enabled the company to produce better microprocessors than its competitors - and its headstart allows it to retain that R&D edge.

Intel's commanding lead in the market also allows the company to leverage its might to partner with its customers, ensuring they buy only Intel products. With 80 percent of the market, Intel has quite a bit of weight to throw around. And as such a high-volume producer, Intel has economies of scale: cost advantages and operating efficiencies its competitors can only dream of.

Intel has also successfully branded its products, the Pentium chips, so that customers know them by name and associate them with high quality. (It is unusual for a high-tech firm to brand itself so successfully. And remember all those "Intel Inside" logos? Intel partners with its customers in order to cross-promote its products.

Now you might point out Intel's weaknesses. Intel's competitors, like AMD and Cyrix, have managed to copy most of Intel's products (or surpass them in some instances). Intel has often succeeded by being first to market with its products. You might point out, however, that as society becomes more "wired," the major source of growth in the microchip market has been in lower-end, less-powerful chips - a market in which Intel's competitors are well-equipped to compete in price-sensitive markets. Already, many cheap computers rely on AMD and Cyrix chips. And the outcome of the antitrust suits both against Intel and Microsoft (Microsoft software runs on Intel chips) is a wild card.

It's 1982. You're a consultant sitting on the plane next to your client, who is the CEO of American Airlines. The client tells you that American can't seem to keep many repeat customers and wants to institute something called a "frequent flyer" program to reward loyal passengers with "points" they can redeem for free flights. He turns to you and asks you to analyze the merits and faults of the program. How do you respond?

This is a good candidate for the Four P s framework. (Note that the interviewer has deliberately set this case at a time when you cannot use online membership as a substitute or addition.) A good analysis would tee off with some scoping questions to understand the evolution of the idea:

- Are you aware of any programs currently in existence that caused you to consider this idea for American Airlines? If so, what do you feel are major advantages/disadvantages?
- Have you done any market research within your customer base to determine how well this program would be received if instituted?
- Can you sketch the purchasing habits of your top flyers for me? How much do they currently spend on air travel per year, what percentage is business vs. leisure, are there a particular set of routes this group frequents, do they stick with one airline or purchase tickets on many airlines, etc.?
- Would the current customer service business unit be charged with implementing this program or would you consider investment in a separate initiative?

Price

- Would there be a membership fee for this program? Would this program be available to all American customers or only those who fly at or over a certain threshold?
- Based on your customers' current flight habits, would you set milestones for award redemption?

Product

- Would the program be based on miles, segments, price of tickets, or another factor?
- What need would this program satisfy that does not currently exist in the marketplace?
- Would there be any redemption restrictions based on route or day?
- What other rewards would be available to members besides flights? Special member lounges in airports? Car rentals? Hotel rooms?
- What would be accumulated - points, miles, levels?
- Would these accumulated criteria ever expire?
- Would you award extremely high-volume flyers with additional perks? What would they be? Would flyers have to re-earn this status or once attained would it be good for life?

Position/Place

- Are you aware of any similar programs in today's marketplace? If so, what would differentiate your program from others that already exist?
- Based on your knowledge of your customers' behavior, would you think that a frequent flyer program would induce high switching costs, such that it would make it difficult for high-volume customers to switch airlines due to the loss of miles/status with American?

Promotion

- How would you introduce this program to your customers? Through airports, the media, travel agents? Would it be available only to frequent flyers or all the flying public?
- How would customers sign up for this program? Would it be automatic, a form, a phone call to customer service?
- Would there ever be any promotional drives such as doubling awards or offering bundle pricing (such as two-for-one)?

Be careful of using historic precedent in historic cases. While frequent flyer miles are a fact of business history, your analysis might show that the long-term benefits are not worth the creation of the program.

Biotechnology Case

- The client is a U.S. biotechnology company with one product on the market ($500MM in sales)
- Product is used by dialysis patients; target audience is nephrologists
- In 6 to 12 months, company is planning on introducing a new product to the market
- New product is for cancer patients; target audience will be oncologists
- There is one major competitor for the current product; if new product is introduced within a year, there will be no competition for at least one year
- Current sales force is comprised of 100 sales representatives
- Most reps joined company to be in an entrepreneurial environment
- Have been selling only one product for the past 5 years
- To successfully introduce the new product to the oncology market, the company will need to invest money in expanding its sales force

Your Task - The Business Problem

- Help the client think through the question, "Should we invest money in expanding our sales force?"

Additional Industry Background

- The life of a patent is 17 years; however, most of this life is spent in the R&D and FDA approval processes
- Being first-to-market is extremely important to a new product's success
- Selling cycle: sales reps call on doctors to discuss products --> doctors recommend products to patients --> patients choose and buy products to use --> health plan or insurance company reimburses patients
- Cancer products are generally very expensive; however, most of the patient's out-of-pocket costs are covered by their health plan or insurance company
- To sell cancer products to oncologists requires experienced sales people with technical backgrounds (oncologists do not see sales reps easily) -- it usually takes 6 to 12 months to recruit and train a new sales organization

Key Issues - Problem Decomposition

- What is the potential demand (in units) for the new product?
- How many cancer patients are there?

- How frequently will patients use the product?
- What is the recommended dosage per usage occasion?
- What unit price will the company be able to charge for the new product? How will price be set for the product in the marketplace?
- What is the size of the sales force investment which will be required to support the new product? What is the average annual cost of a sales rep?
- How many additional sales reps will be needed to successfully introduce and adequately support the new product?
- How many oncologists will need to be called upon?
- How often will each oncologist need to be called?
- What will be the average length of an oncologist call?
- Where is the point of diminishing returns for sales calls?
- How will potential demand be impacted by the number of sales representatives selling the new product?

Additional Considerations and Questions

- How would you estimate demand for the new product? What approach would you use and what data would you want to see?
- How would you set the price for the new product? Is this product likely to be price elastic or price inelastic?
- What if there was competition for the new product?
- If the client decided to invest, should they go with one combined sales force (for both products) or two separate sales forces (one for each product)?
- What would you want to consider in deciding between one or two sales forces?
- How similar are the two products and target audiences?
- Are the two target audiences located in geographic proximity to each other?
- Will the new product distract sales reps from selling the current product (or vice-versa)?
- What will be the likely impact of each alternative on employee satisfaction?
- If they went with one combined sales force, how would you determine how much sales effort should be spent on each product?
- What other sales channels (other than direct) might the company want to consider and why?
- What other factors might be important to consider in making these decisions?
- Strategic direction of the company
- Financial situation (cash flow, capital availability, etc.)
- Current sales organization structure and reward system
- Potential barriers to entry for new competitors
- Other investment opportunities (i.e., opportunity cost)

Cases from Deloitte Consulting

Financial Services/CIO Case

Scenario

"I am the CIO of a large, nationally recognized financial services company (over $25 billion in revenues) which has over 15 subsidiaries offering numerous types of financial products to customers all over the U.S. As CIO, I am responsible for providing for and maintaining all of the information systems a company as large as this requires to operate. This includes managing both the maintenance of existing systems as well as the development of new systems to either replace older technology or to support new business requirements. Currently, I have over 500 employees working for me in the IS organization. However, this is not enough - in fact, I rely on an additional approx. 1,000 external contractors to support the organization who are procured and managed at the business unit and departmental level.

"Could you provide some recommendations on what I should do to insure that my organization is bringing in the best quality contractors available at the best prices?"

Additional information to be given to the candidate

- 40 buying points
- You don't know how much you are spending
- Currently use approx. 100 suppliers (at any given point in time)
- Business unit leaders and department heads independently decide on the need for contractors, where they are going to find them, and how they will be utilized
- The company does NOT demand a large number (e.g. >20) of contractors exhibiting the same set of skills

Key points the candidate should address

- Data Collection efforts are critical in order to establish baseline
- Need to understand both the DEMAND and SUPPLY sides
    - **Demand side:**
        1. What type of contractors are procured? What are key drivers? (e.g. Specific programming capabilities such as C++, OO, Cobra or Com; familiarity with legacy systems or mainframes; etc)
        2. How can we segment or organize the demand requirements?
    - **Supply Side**
        1. Who are the potential suppliers that meet demand requirements?
        2. How can we segment or organize the supply side? (e.g. Two types of potential suppliers include "Body Shops" and "Professional Services firms" such as AC, CSC, IBM, EDS, etc.)
        3. How much does a segment or particular skill set cost/resource? What is the quality of resources? What are the performance metrics or service level agreements offered?
- A key constraint: specialized demand may limit opportunities to consolidate
- Once you understand both Supply and Demand sides, the effort should focus on leveraging the resources of the organization given supply and demand constraints
- With over 100 suppliers at any one time, there is no leveraging of buying power; in fact, it's quite decentralized and fragmented
- Need to consolidate buying points
- Need to consolidate the number of vendors used (so each gets a bigger piece of the pie in return for pricing breaks)

- Need to develop an IS strategy vis-a-vis use of contractors (e.g. Want employees to work on development projects; outsource/use contractors for maintenance projects) Developing RFIs-300 companies; RFPs-25; negotiations with a sub-set of 12 to leverage buying power

<u>Consumer Food Manufacturer Case</u>

Scenario

The president of a $500 million dollar consumer food manufacturer has asked you to come in and talk to him about how he can improve his company's performance. This firm manufactures and distributes vinegar-based products, including industrial strength vinegar, vinegar-based salad and cooking dressings and mustards. Depending upon the distribution channel, vinegar products are marketed under multiple brand and private label-brand names.

This firm has a 25+ year operating history and is generally efficient in the manufacturing of vinegar. There are 7 remote production sites scattered around the U.S. Last year, the company was purchased by a much larger international consumer goods company and has so far been allowed to operate as an autonomous division.

For the past 3 years, the company has been operating at or just-below break-even profitability. The new corporate parent has budgeted the company to grow to $1 billion in revenues in the next 5 years and to achieve a 5% ROS. The president has been asked by the corporate parent to bring you in to identify how this operation can be turned around in short order as well as to recommend steps to be taken to help achieve 5-year growth targets.

Additional information to be given to the candidate

- Vinegar industry is mature with significant entry barriers due to capital equipment requirements, and production skills needed to efficiently manufacture vinegar
- Distribution channels include grocery wholesalers and grocery store chains, specialty stores, private label food distributors, food service companies and other consumer foods manufacturers who use vinegar as raw materials for their products (e.g. pickles)
- Multiple SKUs are produced for each distribution channel noted
- Over 450 total SKUs; 20% of SKUs comprise 80% of sales
- 75% of SKUs lose money when all costs fully allocated - marketing costs are a significant cost driver
- Profitable SKUs include those that carry a specialty brand (niche) and are sold through specialty stores (low revenue) and several private label brands
- Marketing efforts not concentrated on high sale/profit SKUs
- High transportation costs due to poor location of 7 plants (not near major rail/transportation hubs, not located near primary customers)
- Variable production costs are not an issue (inexpensive labor and raw materials)
- Fixed costs (due to older facilities excess capacity) and SGA expenses are significant and the primary cost drivers

Key points the candidate should address

- Company is trying to be all things to all customers (e.g. Multiple distribution channels, unfocused marketing, SKU proliferation)
- Company needs to develop a new, focused distribution strategy and product mix
- Marketing efforts to be revamped and focused on selected channels and products
- Company should strategically align itself with those channels and product categories that are high in revenue and/or high in profitability (give up poor-performing

products/channels)

- SKU rationalization/elimination should be recommended; only keep those SKUs that fit with new distribution strategy
- Plant capacity utilization issue should be raised - possible solution would be to eliminate capacity by closing poorly located/older plants
- Plant relocation and/or consolidation should be considered relative to distribution and product mix strategy
  Integration with corporate parent should be explored to identify opportunities for shared services and other cost reduction opportunities

Medical Supplier/Market Positioning Case

Scenario

The client, a $270 million U.S. division of a $3 billion medical device and diagnostics manufacturer, makes high-volume, low-cost medical supplies such as test tubes and needles. The client has a well-established market leadership position, with over 75% market share in its major product lines, and is recognized for its high quality, reliable products. Company management has stated to the investor community that it intends to double the size of the company in the next five years, despite its current low annual revenue growth rate. As one of the largest divisions in the company, the client is expected to contribute significantly to this growth.

At the same time, competition is taking market share from the client by narrowing product differentiation and offering lower prices or value-added services to customers. Also, the client's traditional set of customers is expanding beyond clinicians, who care about product features and benefits, to include new decision-makers who want help addressing their business needs, as well as insights about how to manage their own processes to improve financial and quality of care outcomes.

We have been asked to help the client redefine its market positioning for its U.S. business so it can better express the overall value that it provides to customers, defend its leadership position and establish a framework and foundation for growth. How would you structure the analysis to this project? What information would you need to obtain? What general recommendations for change might you make?

Additional information to be given to the candidate

- Across the industry, medical suppliers are associating themselves with specific areas of the health care system, such as particular disease states or processes of delivering care, and are looking to provide broader sets of offerings within these areas
- The client has always tried to be all things to all people, resulting in marketing messages and offerings that are not linked to any overall strategy or tied to meeting specific customers' needs
- Customers see the client as a vendor of basic supplies that is transaction-oriented, not as a business partner who is customer-focused or who provides expertise that helps customers solve problems
- The client's investment in R&D and market research is significantly lower than other high-growth companies. Few new products have recently been introduced, and those that were introduced were incremental and had limited success. Furthermore, no significant new products are expected for 2 years
- Because divisions across the company have not been well integrated, other divisions' sales forces sell products that are closely linked to the client's business

Key points the candidate should address

- **Environment** (e.g. Strength of competitors, positioning of peers/competitors, industry trends): The client should broaden the scope of its business and offerings, differentiate through offerings other than product features and benefits and better leverage its market leadership position
- **Customers** (e.g. Key buyer types, their business drivers and purchasing criteria, their current and desired relationship with client): The client should develop programs to help customers solve problems, position itself broadly enough to address multiple customer types yet segment the customer base to align specific marketing messages and clearly communicate how its offerings address customers' key business concerns
- **Market Positioning** (e.g. Current value proposition, value-added offerings, strategic objectives for client): The client should try to move from a "vendor" to a "partner" relationship, be more focused in its positioning and develop solutions that meet customers' needs across broader areas of the health care system
- **Growth Foundations** (e.g. Traditional growth rate, investment in R&D and market research, internal R&D capabilities, consideration given to acquisitions): The client should recognize the challenge to achieving its growth targets given its recent performance and improve this through acquisitions or partnerships with other companies, increasing R&D investment, improving the product development process and pursuing continued market research

  Infrastructure (e.g. Skill sets, incentive compensation, overlap with other divisions of company): The client should enhance its sales/marketing skill sets to gain credibility as "partners" with customers, align incentives with new objectives and leverage other divisions' capabilities to extend its reach in the market

Bottled Water Case

Scenario
Facing stagnant sales and increased competition from micro-breweries, a leading manufacturer of beer has begun evaluating other growth opportunities. The company is already focusing its efforts on penetrating the lucrative international market; however, current five-year sales and profit growth goals cannot be met by focusing solely on the international opportunities.

A high-level executive at this company has noticed a steady and substantial increase in the consumption of bottled water products. Realizing that the assets needed to produce bottled water are very similar to that of beer products, the executive has recommended to the CEO that the company begin production of bottled water products. Needing an "unbiased" view, the CEO has asked your consulting company to analyze the executive's analysis and recommendations.

Additional information to be given to the candidate

- Domestically, annual growth in the beer market is estimated to be 3-4%. Demand for beer is highly fragmented - buyers are particularly loyal to only a few brands. Four domestic manufacturers make up approximately 90% of beer production; this company produces 28%
- The company employs a focused manufacturing strategy - each plant produces a few specific product lines
- Competition in the bottled water industry is between 3 major water producers
- After three years of 30+ % growth, the bottled water market has flattened, with growth expected to be less than 10%
- Recent industry analysis suggests current manufacturing capacity among the major water producers will not satisfy domestic demand

- No capital investments will be made by the beer manufacturer should they enter the bottled water market

Key points the candidate should address

- Structure the analysis, including finance, marketing and operations considerations
- Fit with the current line of business
- Logistics and distribution considerations - will they be able to leverage their current distributor network?
- Capital investment requirements/considerations
- Expected sales and profitability - how would you project these?
- Impact of beer market share vis-a-vis loss of production capacity due to bottled water production
- Market acceptance of beer producer in bottled water market
- Core competencies required for beer production vs. bottled water production
- If the beer manufacturer truly wanted to enter the bottled water industry, are there alternative strategies available? (i.e. Outsourcing, contracting)

Follow-up questions (if needed)

- What are the major areas of analysis you would focus upon?
- What market information would you want to analyze?
- What are the pitfalls of the company entering the bottled water industry?
- What are the advantages?
  What other opportunities might you suggest they explore? Why?

Merger Integration Case

Scenario

Two large pharmaceutical wholesalers, East Coast Health (ECH) and Drug Land have announced a merger. In preparation, Ron Router, CIO of ECH, has asked Deloitte Consulting to evaluate his company's operating systems, as well as Drug Land's systems. The evaluation is to include a "side by side" comparison of application functionality, a recommendation of which systems should be used to run the combined company and projected cost savings. After a lengthy discussion, Ron has convinced Karen Cable, the CIO of Drug Land, to support the project even though the merger has not yet been finalized. Ron needs the recommendation in 12 weeks. His boss, the CEO of ECH, has told Wall Street that once the merger is finalized the two companies will be integrated very quickly, and large synergies can be expected.

After a conference call with both CIOs, Eric Commerce, Deloitte's project manager, questions Karen's commitment to the project. The call confirmed one thing in Eric's mind: that the stakes are high. Both CIOs have put in place large organizations to support rapid growth and evolving customer requirements. Trying to integrate both companies' systems would add risk and reduce synergies. As Eric thinks about the challenges ahead, and the possible approaches Deloitte can take, Ron calls: "Eric, go ahead and invoice me directly since ECH is funding this project… look forward to seeing you at the project kick-off meeting!"

Additional information to be given to the candidate

- Both companies sell to similar customers: Retail, Hospitals, Drug Store Chains
- System scope: accounts payable, accounts receivable, fixed assets, tax, warehousing,

purchasing, customer support
- Concerns expressed about confidentiality, as well as desire to minimize the involvement of her staff in the project
- Each company has a different system architecture
- ECH's systems are very distributed, while Drug Land's are highly centralized
- Neither CIO anticipates an IS budget reduction, yet integration scenarios estimate a 10-30% reduction in systems spending
- Information availability is critical - how much should we expect each CIO to share?

Key points the candidate should address

- **Buy-in:** Having a face-to-face meeting with Karen, establishing her trust, demonstrating fairness
- **Project Approach:** Defining business requirements, getting the two sides to agree on business requirements, collecting data from users, evaluating two different sets of applications based on their ability to meet business requirements
- **Objectivity:** Conducting an objective assessment and not "rubber stamping" a recommendation even though ECH is paying the bill; managing both CIOs' expectations in terms of what will be recommended

  Systems and Change Management Issues

Cases from Casequestions.com

1. GE developed a light bulb that never burns out? It could burn for a thousand years. The director of marketing calls you into to her office and asks you "How do we price this product?" What do you tell her?

2. A major manufacturer of chemicals and plastics, like Dupont, has developed a new material that would be great for disposal diapers. How big is the disposable diaper market? Should the company enter the market and if so how?

3. Our client is a major manufacturer in the pay phone industry. Despite a 20% increase in market share, the firm has experienced a 15% decline in profits. The CEO wants to know why and what can be done about it?

4. Our client is website that sells toys, not unlike eToys. Independent research data shows that 5% of shoppers at brick and mortar retail stores make a purchase and 40% buy items at specialty stores like sporting goods shops.

   Our data shows that only 1.7% of their on-line visits (1.3 million hits in September 2000) resulted in a purchase. It also shows that 70 percent of their on-line shoppers who fill their shopping carts bail out at the end without making a purchase. The President wants to know what's wrong and how we can fix it.

5. Should Budweiser switch from glass to plastic bottles? What are the advantages and disadvantages to such a move? And estimate the size of the domestic beer market.(1st round case)

6. AOL wants to increase its membership. It is thinking of giving a computer away with each new account that signs a three-year service contract. Is this a good idea? (1st round case)

LONGEST LASTING LIGHT BULB

GE developed a light bulb that never burns out? It could burn for a thousand years. The director of marketing calls you into to her office and asks you "How do we price this product?" What do you tell her?

Let me make sure that I understand. GE has invented a light bulb that will never burn out, and the marketing director wants me to figure out how she should price it.

That's correct.

Is coming up with the price the only objective? Or is there something else I should be concerned about?

Pricing is the only objective.

Is there any competition for this product, and do we have the patent?

We have a patent pending and we have no competition.

We know that the advantage of this product is that the bulb never burns out. Are there any disadvantages to this product? Does it use the same amount of electricity?

There are no disadvantages, except maybe the price. And that's why you're here.

What did you spend in R&D?

It cost $20 million to develop the product.

What are the costs associated with a conventional light bulb?

It costs us $.05 to manufacture. We sell it to the distributor for $.25, the distributor sells it to the store for $.50, and the store sells it to the consumer for $.75.

And what does it cost us to manufacture the new light bulb?

Five dollars.

So if we use the conventional bulb-pricing model, which would mean the consumer would have to pay $75 for this light bulb. If we use another simple model and say that a light bulb lasts a year and that people will have this bulb for 50 years, that's an argument for a price of $37.50 (50 years times $.75). Then we need to ask ourselves whether a consumer would pay $37.50 for a light bulb that never wears out. Now we're looking at price-based costing. What are people willing to pay? And is it enough to cover our costs and give us a nice profit?

The other main issue is that the more successful we are, the less successful we'll be in the future. For every eternal light bulb we sell, that's 50 or 75 conventional bulbs that we won't sell in the future. In a sense, we will be cannibalizing our future markets. So we need to make sure that there is enough of a margin or profit to cover us way into the future.

Good point.

I'll tell you, I have reservations about selling to the consumer market. I just don't think the opportunity for pricing is there.

So do we scrap the project? That's $20 million in R&D costs down the drain.

- **Not at all. We turn to the industrial market. For example the City of Cambridge probably has 2,000 street lamps. Those bulbs cost maybe $20 and have to be changed twice a year. The real expense isn't the cost of the bulb; it's the labor. It might take two union workers. In addition, you have to send out a truck. It probably costs the City $150 in labor costs just to change a light bulb. Now if we sell them the ever-lasting bulb for $400, they would make that money back in less than two years and we would make a handsome profit.**

Not bad.

- Type of case: Pricing

- Comments: First, the candidate looked at cost-based pricing and realized that the price was too high and that the typical consumer would not shell out $75 for a light bulb. Then he looked at price-based costing and concluded that there wasn't enough of a margin built in to make it profitable. He was also quick enough to realize that the company would be cannibalizing its future markets. Thus, he decided that neither pricing strategy made sense for the retail market. So instead of suggesting that GE just cut its loses and walk away from the project, he went looking for alternative markets and concluded that there was great potential in the industrial market.

CLEANING UP THE DIAPER MARKET

A manufacturer of chemicals and plastics (similar to DuPont) has invented a new inexpensive biodegradable material that would be perfect for disposable diapers. How big is the disposable diaper market? Should the company enter the disposable diaper market and if so how?

I'm just going to repeat the question to make sure have it right. There is a company that manufacturers chemicals and plastics. They have invented an inexpensive biodegradable material that would be perfect for disposable diapers and are wondering whether to enter this market and if so, how best to enter.

That's right.

What is their objective or goal in entering the market?

To increase profits.

Do they manufacture any other household goods? Anything that is sold directly to the public?

Yes. Insulation for homes.

Do they manufacturer products under other names or do private branding?

Yes.

If this company is similar to DuPont I'm assuming that it is publicly traded and does several billion dollars worth of sales each year.

That's a safe assumption.

Does this new material have any down side to it? It's biodegradable but is it safe in all other aspects?

Yes.

What I'm going to do is first estimate the size of the disposable diaper market. Then I'm going to look at the market itself to see who the major players are and whether there are any barriers to entry. Then I'll investigate the different ways to enter the market and conduct a cost benefit analysis and then make a recommendation.

Sounds like a plan.

First, let's estimate the size of the market. I'm going to assume that there are 250 million Americans. I'm going to further assume that the average life expectancy of an American is 75 years. I'm also going to assume that there are even numbers of people in each age group. And that there is the exact same number of 8 year-olds as 68 year-olds.

Go on.

You divide 250 million by 75 and you get about 3.3 million people per age group. Children wear diapers from ago zero to 3 so that's 9.9 million kids wearing diapers. So we'll round it off to 10 million kids. You said disposable diapers. So I'll estimate that 80 percent of children wear disposable diapers. So now we're talking 8 million children wearing 5 diapers a day. That's 40 million diapers a day times 365 equals approximately 14.6 billion diapers a year.

So should the company enter the market?

Let's look at the market. The major players are Proctor and Gamble with two main brands and then there is a smattering of smaller players. I know that generic brands and private labels are doing well. So while P&G dominates the market they don't do it in such a way that would cause any barrier to our entry. Would our diaper be significantly better than the P&G brands?

Yes, and cheaper too.

Then let's figure out the best way to enter the market. The three main ways to enter a market is to start from scratch, buy our way in, or do a strategic alliance. If we started from scratch we would have to spend a great deal of time and money building our brand, establishing distribution channels, and retooling our plant to manufacture the diapers. While we sell insulation to the public, we don't have a group of products directed towards the consumer. So we would truly be starting from scratch. The upside of this that if we are successful we reap all the profits and have an established brand name.

The next way in is to buy our way in. Maybe purchase a smaller player who has some brand name, but just as importantly has established distribution channels and a marketing and management team. It would certainly save a lot of time. If we can find a company at a reasonable price we should consider it. We could substitute our product for theirs and organize a major marketing campaign.

The third way in is to do a strategic alliance with an existing consumer products company. We could supply them with our product and they could take it from there. The downside is that we would have to spilt the profits and we are at the mercy of their management.

So what's it going to be?

While buying our way in has the most merit, I'm concerned because when I asked what your objective was, you said 'make money.' You didn't say you goal was to become a major player in household consumer goods or even diapers. Therefore I want to put out two additional thoughts. We could sell our technology to another company or we could do private labeling for a number of firms. If our product is that good I think a number of

companies would jump at either chance.

Summarize and give me your answer.

We have established the US disposable diaper market to be over 14 billion diapers a year. We have established that our new product would be the least expensive and highest quality on the market. So I think we should enter the market somehow. There was nothing to give the indication the company wants to be a major player in the diaper or consumer goods industry. So I would rule out starting from scratch and buying an existing player. Manufacturing is what we do so there would be no reason to sell the technology. I would recommend that we produce the diapers for a number of companies under their own private labels.

Type of case: Market sizing and entering a new market.

Comments: At first some might think that this is a developing a new product question, and they could probably make a decent case out of it. But the question really asks, "What should they do with it?" That implies that the product has already been developed and the company is searching for the best way to exploit this new technology; and thus, this is an entering a new market case.

PAY PHONES

Our client is a major player in the pay phone industry. Despite a 20% increase in market share, the manufacturer has experienced a decline in profits. The CEO wants to know why and what can be done about it?

Let me make sure I understand. Our client manufactures pay phones. Its market share has risen 20%, yet its profits are declining. The CEO wants to know why and what can be done about it.

That's right.

Besides identifying and correcting the problem are there any other objectives I should be aware of?

No if you can do those two things then I'll be happy.

What sort of market share does the company have and how has that increased?

Currently it has 55%, up from 35% two years ago.

So they've increased their market share 20% in two years?

That's right.

That's incredible. Wait. I'll assume that the overall market size of pay phones has dropped because of the increase in cell phones. Is that a fair assumption?

Yes. Pay phone orders have dropped by 15% during that same two-year time period.

Have any pay phone manufactures dropped out of the race?

Yes, two.

And is that the main reason why we've gained so much market share?

Yes. One of the reasons.

What are some others?

You tell me.

Increased marketing, maybe special contracts, such as military contracts. We've probably lowered our price which has been cutting into our profit margin.

Good. What's next?

How are our costs?

Don't make me answer this case for you.

I'll assume that costs have increased. Particularly labor, marketing, parts, and especially transportation costs with the rise in fuel costs.

That's right.

I'll also assume that the manufacturing process is pretty automated.

That's right. You're not going to squeeze out much cost savings there.

Well I believe that the pay phone market is going to get worse before it gets better, if it ever does get better. But the public will always need pay phones. Maybe we need to change what they need the phone for. Currently, people use pay phones when their cell phone batteries are too low, when they don't have a cell phone or when their cell phone coverage doesn't reach a particular area of the country, or when they don't want the call to be traced back to them…

Hopefully you've been watching too many cop shows.

Yeah. (laughs) Let's say I'm in New Orleans for the first time and my New England cell phone plan doesn't cover the Big Easy. Yet, I'm looking for a place to eat, sip a Hurricane and listen to some Dixieland Jazz. What if I could go to a pay phone and this pay phone has an LED display and touch screen. Now I'm looking for a restaurant so I drop a quarter and hit a button that says restaurants. Now the pay phone comes up with a list of restaurants and rates them. For that same quarter it connects me with the restaurant and asks if I want directions. I hit yes and a set of directions prints out. All this for my one quarter. Now restaurants or any company can place an ad which pops up as I hit restaurants as well as ads printed on the back of the directions tape like grocery stores do with their receipt tape.

So you're saying turn a pay phone into an Internet connection.

Yes. It seems like the technology is already there, it's just a problem of conversion and

phone design.

We have about two minutes left.

Okay, let me review. The industry is shrinking and costs are rising. That, along with the fact that we've lowered our prices has led us to greater market share, but lower profit margins. Now we can bail from the market and try to diversify into another technology, or we can try to change the industry standard and bring it up to speed with the future of telecommunications.

So what would you recommend?

I'd focus on costs; you can always reduce costs somewhere. I'd look to diversify into a growth industry to lessen the company's overall risk, and then I'd reinvent the pay phone as we described. And oh, the other thing I'd do is to ship the old inventory, the current pay phones, to developing countries.

Thanks.

Type of case: increasing the bottom line, growing the company.

Comments: The candidate was quick to figure out why the company's market share was increasing, yet the profits were falling. He also proved that he was quick to think on his feet – thinking outside the box. And the interviewer also gave him points for introducing a three-prong strategy, reduce costs, new product development and company diversification.

E-TAILERS

Our client is an e-tailer, not unlike eToys. Independent research data shows that 5% of shoppers at brick and mortar retail stores make a purchase and 40% buy items at specialty stores like sporting goods shops.

Data shows that only 1.7% of their on-line visits results in a purchase. It also shows that 70 percent of their on-line shoppers who fill their carts bail out at the end without making a purchase. The President wants to know what's wrong and how we can fix it.

Our client is concerned because 70 percent of their customers, who fill up their shopping carts, bail out on their purchases right at the end. And only 1.7% of their customers make a purchase, a percentage much lower than the traditional brick and mortar.

That's correct.

Besides identifying why people bail and coming up with a solution, are there any other objectives we need to be concerned about?

No.

I'd like to ask some questions first about our client and then about the industry. Are we considered a specialty store?

Yes.

Is the transaction rate at web-based specialty retailers higher then general e-tailers?

Yes. But I don't have the exact figures.

Is this a web-wide problem? Do most e-tailers have a low percentage of actual purchases? What did you say it was 1.7 percent?

Yes. It is a web-wide problem to a certain extent. Some sites have higher transaction rates than others. However we seem to be in the higher range of the bail rates, the 65% that bail after filling their carts has us really concerned.

First, I'd conduct an analysis of our competition. I would also benchmark other sites that have a higher transaction rate to see if their sites are friendlier, easier to navigate and more simple in structure. I'd review and compare our customer service program and maybe institute an 800-customer service number in case a customer gets lost or confused. We may even want to look into a customer service audio connection through the computer.

All right. What's next?

Is our pricing the same as our competitors?

Yes. Assume exactly the same.

Have we had any problems with inventory, being out of stock?

No.

How about sending the product out in a timely-manner?

No. Our distribution system is excellent.

I'd like to figure out why people bail. We know that it is not because of our reputation, that we're well respected in the industry; we haven't had any distribution problems or bad press.

That's right.

I've bailed once or twice myself. There could be several reasons. First, I'd like to list several reasons, address each one then lay out a plan for solving the problem.

Go ahead.

First is the security issue. If the web site asks for what shoppers think is invasive personal information. If the customer doesn't feel comfortable submitting their credit card information on line, if they feel that we don't have the latest cryptic technology they may bail.

Not a concern. We only ask for basic information and we have the latest technology.

Another reason I bail is because I have questions about the quality of the product.

Again, not a concern. We sell brand name toys and have a satisfaction guarantee.

What about our return policy?

We provide labels and free postage for any returned item.

Sometimes I bail when I find myself asking, "Do I really need this? Can I afford it? Is it worth the price?" I guess you'd put that under customer psychology. That's hard to quantify.

Let's skip that for now.

There may be folks who get side tracked in the middle of a transaction. Maybe their boss walked in or their kids knocked over the fish bowl. They forget about it or decide that they don't need it. We've lost the moment so to speak. Combine this with some ISP's like AOL that time out after ten minutes of inactivity.

Again, that's hard to combat.

It may be hard to combat, but we have to realize that it happens and it makes up a certain percentage of the bails. Just like window and price comparison shoppers.

So noted.

It could also be tied into some technical issues. If a customer comes over a phone line and the web site is heavy with graphics it may takes a long time going from one page to another. They can become impatient and bail.

That's not our fault if the consumer has outdated equipment.

Sure it is. Anything that keeps them from making a purchase is our fault. Maybe we should offer them an option of taking a heavy graphic site or a text-based site.

Very good. What else?

Next is web design. I know that there were times when I wanted to take something out of my cart and couldn't figure out how to do it, so I either started all over again or bailed.

All right web design that's one. What else?

This one is related. It has to do with customer service. If I can't figure out on line how to return a product then I just want someone to help me. I don't want to figure out it by reading a help button.

You're lazy.

No, but when I want to buy something it should be a pleasant experience and I shouldn't have to work for it.

What else?

Sticker shock. There have been times when I've come to the end of a buying trip and the numbers total up and it's more than I've expected. And then they throw on a shipping charge on top of that. I think people bail because of sticker shock. The Internet has a rep of having the lowest prices. When the prices aren't that low people become disillusioned.

What can we do about that?

Sticker shock can be addressed by instituting a running total for the customer to see at all times, along with shipping options and charges. This way there are no surprises.

Do you think people will buy less if they see the running totals?

There will be the possibility that the average purchase amount may fall, but the number of purchases will go up more than offsetting any lost.

Anything else?

Yes. We have to realize that some of the people who bail are children taking a fantasy trip through the toy store. They fill up their carts and bail at the end. Now I don't think that this is actually a bad thing. But we need to either realize that x percentage of the bails are kids or develop a virtual toy chest.

A virtual toy chest?

A place where they can deposit their toys, label it with their email address and then have the parents check it out for holidays and birthdays. Kind of like registering for a wedding.

We have a minute left.

Then I'd like to summarize. First I'd conduct an analysis of web sites that have a lower bail rate and higher transaction rate than we do. I'd also analyze our competitors. I'll assume that we are doing this anyway. I would also try to track down the people who bailed, send them a quick on-line survey to determine why they bailed and offer them an incentive to make a purchase, like five dollars off their next purchase. Second, I'd reexamine the reasons why people bail and address the ones we could and resign to the fact some things we can fix. I'd institute a place for kids to register their toys so that parents, relatives and friends can buy something they like.

Type of case: Increasing sales

Comments: This isn't your typical increasing sales case. It's more of the "analyze and fit fix it" variety. The student was good at identifying the real concern (the 70% bail rate). He asked some good initial questions and he used his own experience to try to identify the root of the problem. Then he came up with a simple and logical strategy and added some suggestions as well.

Should Budweiser switch from glass to plastic bottles? What are the advantages and disadvantages to such a move? And estimate the size of the domestic beer market.

What's Budweiser's objective?
To increase both profits and market share.
What kind of market share does Budweiser have?

Anheuser Busch and its thirty products have 46 percent of the domestic market. Bud and Bud Light make up 20 percent of the market.
Is that 20 percent of the 46 percent or 20 percent of the overall market?
It's 20 percent of the overall market.
Let's first take a minute to figure out the size of the domestic beer market. I'd like to break it down between drinking beers at home and drinking beer in public, like bars and restaurants. I'll assume that there are 280 million Americans and 2.8 people per household. That means we're talking about 100 million households.
Out of the 2.8 people per household I'll assume that beer-drinking adults account for 1.0 people. Knowing that adults in their 20s and 30s drink more beer than people over 40 I'll estimate that the average person drinks 3 beers per week at home.
So that's 3 beers per week, 12 beers per month 144 beers per year. That means we multiply 144 beers times 100 million people and we get 14.4 billion beers. Let's round it off to 15 billion beer consumed at home.
Now beers consumed in public. That represents beers drunk in restaurants, bars, sporting events, and at parties in someone else's home. We take the same 100 million beer-drinking adults. However, I'm thinking that given a wider choice of alcoholic refreshments that people might choose wine or hard liquor. And because of the designator driver I'm going to cut that number in half and say 50 million.
So we have 50 million partiers drinking 3 "public" beers a week that's 12 beers per month 144 beers per year equals 14.4 billion beers or 15 billion beers.
Now do you want this in a dollar amount or calculated by the bottle?
By the bottle.
Well we came up with 30 billion beers. I'll assume that bottle out sell cans. Maybe a 60/40 split. So that means we are talking 18 billion bottles of beer. Now you mentioned that Bud and Bud Light make up 20 percent of that market so we're looking at 20 percent of 18 billion, which is 3.6 billion bottles of Bud, and Bud Light sold each year.
Okay, good. Let's move on to the rest of the question.
I have a few questions. Does plastic have the same shelf life as glass and aluminum?
Yes, if the bottle is brown.
Does the plastic bottle stay as cold as glass and aluminum?
It stays as cold as long as glass, colder and longer than aluminum.
Does the bottle affect the taste?
No.
I assume that the weight of plastic is about half of what glass is.
Actually plastic weighs one-seventh of what glass weighs.
So it is lighter, which will save on shipping costs. Is it cheaper?
Yes. It's about half the price. Assume that it costs Bud 6 cents for each glass bottle and 3 cents for each plastic bottle.
Do they have to retool the plant?
Good question. There will be some modifications. Beer is hot when it is bottled. So between the heat and the pressure in which the beer is forced into the bottles, unless the beer is cooled first, the plastic bottle could get disfigured. In addition, the capping system is different. Plastic will have screw on caps.
What is the expected cost of retooling the plant?
Ten million dollars.
Do they expect to sell more Bud because it's in a plastic bottle?
What do you think?
I think that there is an emotional bond between beer drinkers and glass. I'd like to go back and find out what the industry did to introduce the metal cans.
That's a good idea, but we don't have that info right now.
Well, first I think that if you switched completely from glass to plastic you would lose the loyal middle-aged beer drinker. I would just offer it as a packaging option. People could buy plastic if they wanted to, but they could still get glass. I'd try to test market it for eighteen months in half a dozen cosmopolitan cities. I'd also gear my advertising toward the young adults. People who are in their twenties and thirties who grew up drinking

soda out of a plastic bottle. I'd also mimic the soda in the sense that I would package the beer in 12 ounce and 20 ounce "Tall Boy" bottles. That way you'd sell more beer. The other huge market I see is the sports stadium. It's probably safer for everyone if beer was sold in plastic bottles during baseball, basketball, football and certainly hockey games. Plastic would also be perfect for taking beer to the beach or around a pool. Oh, I almost forgot, there would be less breakage, both while drinking and shipping the product.
What are the economics of this decision?
We came up with 18 billion bottles of Bud sold each year. The price of a plastic bottle is three cents less. So 3 cents times 18 billion equals 540 million which is significantly more than the 10 million it will cost us to retool the plant. Add in the money we will save money on shipping cost and less breakage. So economically it makes sense to at least test market it.
Okay, good. So summarize for me. What are the advantages and disadvantages? And what would you tell Bud to do.
I would tell Bud that they should test market the plastic bottle and maybe have it as a packaging option. I would also tell them that I would never get rid of the glass bottle. There is too much history here. They would certainly lose market share. They may even want to try it out first in one of their lesser brands.
Since the objective is to increase profits, I'd like to break the advantages down in two ways, reductions in costs and increases in revenues. Let's start with the savings in costs. One, plastic is cheaper than glass. So we would save money in the manufacturing, because the fixed cost would go down. Two, our shipping costs would be less because plastic weighs one-seventh of what glass weighs. In addition there would be less breakage during shipping.
We would be able to increase sales because we could sell the beer in larger sized bottles. We might even be able to increase our market share with beer drinkers between the ages of fifteen - I mean twenty-one and thirty nine.
The disadvantages might be image. After all we are the "King of Beers." But if we offer it as a packaging option then the traditionalists might not care. The other disadvantage might be that if we produce beer in plastic bottles younger drinkers might gulp beer as they do soda. This could cause more drunk driving accidents. We would need to keep a close eye on that.

Good job.

AOL wants to increase its membership. It is thinking of giving a computer away with each new account that signs a three-year service contract. Is this a good idea?

So AOL wants to increase its membership and is investigating whether they should give away a computer to entice more subscribers.

Yes.

One objective is to increase its membership, are there any other objectives that I should be concerned about?

Yes, profits.

How many subscribers does AOL currently have?

As of the end of October 2000 they had 25,000,000.

How many new subscribers did they get last year?

Approximately five million new subscribers.

Five million? That's a 20% increase. What kind of percentage increase are they looking for?

They want to increase 40 percent every year. In 1998 they went from 10.7 million subscribers to approximately 15 million, that's 40%. In 1999 they went from 15 million subscribers to 20 million. That was a 33%.

So they are peaking out at around 5 million new subscribers each year.

Right, and as the subscriber base goes up that five million becomes a smaller percentage.

And now they want to give away a computer to entice new subscribers?

Yes.

How much is AOL's monthly subscriber fee?

Figure twenty dollars.

I'd like to look at the economics behind this decision. Is AOL thinking new computers, refurbished computers or Home Internet Appliances?

You tell me?

Let's say that a computer manufacturer will sell AOL a new computer for $600, they can buy a refurbished computer for $400 or buy a HIA for $300. If their mission is to get more people on the Internet than they might want to look at the HIA. But let's take a minute to think about whom would take advantage of this offer. It seems like the elderly are going on line as well as the less educated and lower income families. I think both of those groups would take advantage of this offer. The other thing is that this would probably be a first computer for those groups. Others to take advantage of this would be middle income families looking for a second computer, possibly one to send off to college with their kid. Wait, let me shift directions for a second.

If there are 25 million subscribers and AOL wants to increase that by 40 percent we're talking 10 million new accounts – that's almost double what they're usually bringing in. That's around 4 percent of the US population or 10 percent of the US households. The other issue to think about is where are they going to get 10 million new computers or even HIAs? We also need to realize that they are going to buy and give away 10 million Internet devices when 5 million people would have signed up anyway.

Assume that our projections show that if we ran the ad campaign with new computers we could sign up 10 million new accounts. If we used refurbished computers we'd sign up 6 million new accounts and if we offered HIAs 8 million new accounts.

Let's assume that they can get their hands on 10 million new computers and that they can buy them for $600 a piece. That's $6 billion. It would probably cost you $200 million in shipping and handling as well. The revenues from this will be $20 a month times 36 months times 10 million. That's - $7,200,000,000. That's a profit of $1 billion. If they didn't make this offer and increased their subscriber base by 5 million – like in years past - their profit would be 5 million times $720 which equals – one second please – it equals $3.6

billion. The numbers would suggest that we not do it.

What about the others, the refurbished or the HIAs?

For the refurbished you said 6 million at $400 each which is $2.4 billion in costs, not including the shipping costs. The revenues would be 6 million times 720 around $4.3, which means a profit of $1.9 billion, which is still below the $3.6 billion. Besides finding 6 million refurbished would be a nightmare.

And the HIAs?

HIAs at $300 times 8 million is $2.4 billion in expenses plus we'll assume 100 million in shipping charges. So that's $2.5 billion. Now our revenues would run $720 times 8 million. Let's see that's approximately $5.7 billion. The balance is $3.2 billion. Again, 400 million below what we could bring in if we stick with the current marketing plan.

Besides, if AOL is giving away computers or HIAs the manufacturers will probably take some heat from the retail stores because it's cutting into their market and supply would be limited. I don't even know if they can make 10 million HIAs a year. If they are running full capacity and have to run extra shifts while paying overtime the price of the computers or HIAs is going to rise significantly. The last thing you want is to promise 10 million new computers and then not to be able to deliver on that promise.

So what would you tell the marketing department of AOL?

First, I might convey to them that their goal of getting 10 million new accounts is very ambitious. I would tell them stick with the current marketing plan or maybe explore ways to bundle AOL with the sales of new computers or HIAs through the manufacturing side.

Interesting. Beside that question have you ever failed at anything?

(Chuckle) Of course. But before I talk about a failure, where did I go wrong on the question?

You didn't. I just wanted to see if you could take criticism without getting upset.

Type of Case: Strategy case based on numbers.

Additional Comments: She asked some great questions in the beginning getting the AOL's subscribers numbers and translating them into percentages and then back again. She started to go off in the wrong direction by trying to define who these new subscribers would be, but she caught herself and looked at the numbers. She also had the instinct to look at the logistics of the offer and the foresight to state that she thought the goal was ambitious. And finally, she rolled with the punches and maintained her sense of humor when the interviewer tested whether she could take criticism.