

How Apple's Corporate Strategy Drives High Growth

10/2012-5860

This case was written by Oh Young Koo, Institute Fellow of the INSEAD Blue Ocean Strategy Institute, under the supervision of W. Chan Kim and Renée Mauborgne, Professors at INSEAD. It is intended to be used as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

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Apple Computer was founded in 1976 by Steve Wozniak (24 years old) and Steve Jobs (20) in the garage of the latter's parents.¹ Their first product, the Apple I, was a personal computer kit, engineered and hand-built by Steve Wozniak. In 1979, Apple Computer introduced its second product, the Apple II. Equipped with colour graphics and open architecture, the Apple II was aimed at enlarging the customer base beyond 'hobbyists' – 98% of whom were males aged between 25 and 45 with the knowledge to program their own routines.² Apple wanted to erase the perception of a computer as something scientific and complex, and make it easy to use for ordinary people. Whereas the PCs in the market were kits for hobbyists to assemble with no monitor, no keyboard and no software, the Apple II was designed to be of practical use for the consumer. With an all-in-one design in a plastic casing, including the keyboard, power supply, and graphics, it came with software for home and office use such as the Apple Writer word processor and the VisiCalc spreadsheet. The Apple II was a considerable success and helped the company stand out among other garage start-ups in the newly formed US\$3 billion industry.³ In December 1980, Apple Computer went public, resulting in an overall market value of more than US\$1 billion. Over the next four years, Apple Computer developed several PC models – the Apple III, Apple IIe, Lisa, Apple IIc, and so on. During this time, John Sculley, president of PepsiCo, was hired as CEO.

Apple Computer aimed to make an “every person's computer” that was easy to use in the same way that people drive a car without having to understand the mechanics. On 22 January 1984, Apple Computer launched the Macintosh (Mac), offering an unprecedented graphic user interface and allowing users to operate the computer by clicking the mouse. At that time, users of IBM compatibles had to memorize the DOS commands and enter them using a keyboard in order to operate the computer. The graphic operating environment of Microsoft's Windows 1.0 was not released until November 1985. The easy and intuitive computer experience that Mac offered was warmly received by the market. Four months after its launch, Apple Computer reported that 70,000 Macintosh computers had been shipped and 180,000 more units would be expected by the end of 1984.

In the following year, after a power struggle between Steve Jobs and John Sculley, Jobs abruptly left the company he had founded. During Sculley's tenure, Apple Computer developed new computer product lines such as the Centris, Quadra and Performa, in addition to various models in the Macintosh line. Furthermore, Apple Computer expanded its business to computer peripherals such as laser printers, and pioneered the new personal digital assistant (PDA) device market by introducing Newton in 1987.

Meanwhile, Microsoft's Windows PC was gaining market share under the slogan “Windows everywhere”. Windows PC contrasted with Apple Computer, which focused on the existing market of sophisticated and creatively inclined users to sell elegant, high-margin computers.⁴ As Windows attracted average PC users with a strong integration with complementary

1 In founding the company, Ronald Wayne had also partnered but left the company within less than a year selling his 10% stock for US\$800.

2 Clare C. Swanger and Modesto A. Maidique, “Apple Computer: The First Ten Years,” Stanford University No. BP-245 (California: Stanford Business School, 1985), p.5.

3 *Ibid.*

4 Daniel Eran Dilger, “1990-1995: Why the World Went Windows,” October 14, 2006, post on blog “RoughlyDrafted Magazine,” <http://www.roughlydrafted.com/RD/Q4.06/3EC02E78-FD4D-4CDF-92A0-9C4CBDFAB3D2.html>, accessed January 11, 2012.

software applications such as Microsoft's Office suite and Exchange server, Apple Computer seemed to be losing the battle. In 1992, it earned over US\$500 million, but sales dropped sharply to US\$90 million the following year.

In 1993, Sculley was replaced by Michael Spindler, the president of Apple Europe. The new CEO made efforts to turn the company around by pushing Macintosh lines and making thousands of lay-offs, but the company saw its market share fall 9% to 7.4%, and it had made a US\$68 million loss by the end of 1995. In 1996, Apple Computer replaced Spindler, appointing Gilbert Amelio, a veteran IT expert, as CEO. He instigated many changes, which included massive lay-offs and bringing Jobs back to the company as an advisor. However, the financial situation got worse – the company lost US\$2 billion in two years and its market share plummeted from 7.4% in 1995 to 3% in 1997, as did the stock price. In 1997, when Amelio resigned, Apple was again under the leadership of Steve Jobs as interim CEO.

On 15 August 1998, Apple introduced the iMac, an all-in-one desktop computer in a translucent, candy-coloured plastic casing. The computer was designed to be optimal for accessing the internet. Whereas PCs with a Windows system had a complicated wizard for internet connection, iMac aimed to simplify users' internet connection experience. Apple said 'i' stood for 'internet' – it took only two steps to set up and connect to the internet. In its first five months, 800,000 iMacs were sold.

On 23 October 2001, Apple introduced its first digital music player, the iPod. The first generation of the iPod Classic was sold in two models – the 5GB for US\$399 and the 10GB for US\$499. Less than six months later, Apple launched a new service, the iTunes music store, which offered a wide selection of copyrighted quality digital music for 99 cents per song. As the iPod was a huge success, Apple started to milk it by spinning off various product lines and lowering the price. In three years it introduced four generations of the iPod Classic and launched a new iPod Mini. The device became smaller, with long-lasting batteries, different colours, and the price dropped even further. People could buy the iPod Classic Photo 40GB for the price of the iPod Classic first-generation 10GB model (US\$499). Five years from the first iPod launch, the product line had evolved into the fifth generation of the iPod Classic (starting at US\$249), two Mini series, one Shuffle, and one Nano model. Meantime, the iTunes music store evolved to offer not only music but also TV shows and movies. Using the iTunes software, iPod users simply purchased, downloaded the music, video, and podcast and synchronised them with their devices.

On 9 January 2007, Apple dropped "Computers" from its name, marking its expansion into the consumer electronics market in addition to its focus on personal computers. On the same day, Apple introduced the iPhone to the world. The iPhone had minimal user interface hardware, featuring only four buttons. It had a full multi-touchscreen user interface that maximized the user's ability to browse the internet, view multimedia and play games. The iPhone was offered in two models – the 4GB for US\$499 and the 8GB for US\$599. Less than three months after its release, Apple dropped the price of the iPhone 8GB to US\$399 and discontinued the 4GB model. The most distinctive feature of the iPhone was to enable users to customize their phones to their own needs and interests (business, games, sports, social networking) by hosting a marketplace called the App Store. The iTunes App Store was launched on 10 July 2008 and allowed iPhone users to browse and download applications (or "apps") developed by Apple and third-party programmers. Apps could be also used for the

iPod Touch, launched on 5 September 2007, which added the iPhone's Wi-Fi connectivity and multi-touch graphical user interface to the iPod.

On 3 April 2010, Apple launched a 9.7 inch (diagonal) tablet PC, the iPad. Using a multi-touchscreen, users could listen to music, watch videos, browse the internet, play games, read e-books, and so on. The built-in battery lasted for 10 hours of video and 140 hours of audio playback. Its weight and size fell between smartphones and laptops. Like the iPhone, users could purchase apps available in the iTunes App Store and customize their own iPad. The first generation of iPad was offered in two versions – one with Wi-Fi and the other with both Wi-Fi and 3G – within which three models existed: 16GB, 32GB and 64GB.

The powerful comeback of Apple was accompanied by its expansion into the retail business. One of Job's priorities after returning to Apple was ending almost every big box retailer's ties to Apple, as those computer and electronics stores that Apple had relied heavily on often had poorly trained and ill-maintained Mac sections that fell short of providing customers with a unique and pleasant purchase experience.⁵ Apple decided to open its own retail stores to service its customers and sell Mac computers, software, iPods, iPhones, iPads, third-party accessories and other consumer electronics such as Apple TV. A typical Apple store has a sleek layout and design with surgical grade stainless steel walls, backlit signage, wood tables and stone flooring. Many Apple Stores feature a theatre for presentations and workshops and a studio for training with Apple products. And in every store there is a Genius Bar for technical support and repairs, as well as free workshops available to the public. Staff members in the Apple Store are normally well-trained young workers who are passionate about Apple products and who take pride in helping their customers. About 30,000 of the 43,000 of Apple employees in the US work in Apple Stores. With Apple Stores, Apple was able to "turn the boring computer sales floors into a sleek playroom filled with gadgets."⁶ Apple opened its first retail stores in the US in 2001 and rolled out more stores in the US and around the world in the years that followed. Within ten years, Apple has risen to be ranked among the top retailers in the world; the number of Apple Stores worldwide has grown to 363 as of June 2012, with global sales of US\$16 billion in merchandise in 2011. The Apple Store chain ranks first among US retailers in terms of sales per unit area in 2011, with sales of US\$3,085 per square foot, almost doubling Tiffany & Co, the second retailer on the list.⁷

On 24 August 2011, Steve Jobs resigned as CEO and was replaced by Tim Cook, the COO. As shown in Exhibit A, over the previous ten years under Steve Jobs' leadership, Apple's value had escalated exponentially. The company's stock was up 3,000% since the launch of the iPod, 125% since the launch of the iPhone, and 20% since the launch of the iPad.⁸ Apple

5 Janet Meyer, "Best Buy and Apple Together Again," June 27, 2006, post on blog "Apple Matters," <http://www.applematters.com/article/best-buy-and-apple-together-again/>, accessed July 6, 2012.

6 Stephanie Clifford and Miguel Helft, "Apple Stores Chief to Take the Helm at J.C. Penny," *New York Times*, June 14, 2011, <http://www.nytimes.com/2011/06/15/business/economy/15shop.html>, accessed July 6, 2012.

7 David Segal, "Apple's Retail Army, Long on Loyalty but Short on Pay," *The New York Times*, June 23, 2012, <http://www.nytimes.com/2012/06/24/business/apple-store-workers-loyal-but-short-on-pay.html?pagewanted=all>, accessed July 6, 2012.

8 Mark Sigal, "Apple's segmentation strategy, and the folly of conventional wisdom," O'Reilly's Radar, September 29, 2010, <http://radar.oreilly.com/2010/09/apple-segmentation-strategy-an.html>, accessed January 11, 2012.

had influenced the digital lifestyles of people through its iPod, iPhone and iPad, and during that time the company's value hit a record high of US\$340 billion, making it the second most valuable company in America.

Managing the Business Portfolio at the Corporate Level

Other giants in consumer electronics and computer industries had the opportunities to create new market space as Apple did, but they simply missed them. Sony Corporation, founded in 1946 in Japan, has been a leading manufacturer of electronic products, including the Sony Walkman and PlayStation. Since the 1980s, when it revolutionized the audio-cassette with the Walkman, Sony had grown into a global conglomerate. As of April 2011, the Sony Group was engaged in (1) the consumer and professional electronics market, (2) the music industry, (3) the motion picture industry, (4) manufacturing of mobiles, and (5) financial services.

Despite its cutting-edge technology based on vast R&D and a globally renowned brand reputation, Sony turned in a lacklustre performance. Net income dropped from US\$1.5 billion in 1999 to US\$851 million in 2004, and then to (US\$2.6 billion) in 2011. The share price hit a 24-year low in November 2011. CEO Howard Stringer recalled Sony's missed opportunities to create compelling products like Apple's iPod and iTunes music store, in an interview with *Businessweek*: "Steve Jobs figured it out. We figured it out, we didn't execute. The music guys didn't want to see the CD go away."⁹

The same logic Drives the misstep at Microsoft when it killed its Courier tablet project. At the time when Apple was developing the iPad, Microsoft was also pursuing its own tablet (the Courier) but there were conflicting visions for its development within the corporation. One group, led by J. Allard in the Xbox division, favoured a sleek, two-screen tablet, responsive to a fingertip or pen. It was designed to run a modified version of Windows and did not need Office applications such as Microsoft Word and Exchange. The other group, led by Steven Sinofsky in the Windows division, wanted to keep Courier on its Windows platform, but the development of a tablet-friendly Windows was two years away. The Microsoft leadership decided to cancel the Courier (envisioned by Allard) for the sake of protecting their old products, as they were concerned that it would not clearly align with the Windows and Office franchises, according to some sources.¹⁰ As a result, Microsoft lost the momentum to enter the rapidly growing tablet market that Apple's iPad created.

9 Bryan Gruley and Cliff Edwards, "What is Sony Now?", *Bloomberg Businessweek*, November 17, 2011, http://www.businessweek.com/magazine/what-is-sony-now-11172011_page_4.html, accessed November 23, 2011.

10 Jay Greene, "The inside story of how Microsoft killed its Courier tablet," CNET news, November 1, 2011, http://news.cnet.com/8301-10805_3-20128013-75/the-inside-story-of-how-microsoft-killed-its-courier-tablet/, accessed January 10, 2012.

Questions for Interactive Class Discussion

Please prepare your answers to the following questions for the class discussion as you read this case and accompanying press articles.

1. Suppose you were appointed as a new CEO of Apple, succeeding Gilbert Amelio in 1998, when the company was on the verge of bankruptcy:
 - a. How would you diagnose the problem of Apple in terms of value, profit, people?
 - b. Using the four actions framework (E-R-R-C Grid) introduced in Blue Ocean Strategy, what would you do to revive the company?
2. Reflecting on each offering of the iPod/ iTunes software, iTunes music store, iPhone, and iPad, answer the following questions:
 - a. In which industry did Apple create a blue ocean? Was that industry attractive?
 - b. Was Apple a new entrant or an incumbent in the industry?
3. Reflecting on each offering of the iPod/ iTunes software, iTunes music store, iPhone, and iPad, answer the following questions:
 - a. Where did the innovation come from? (technology/market/value)
 - b. Did Apple focus on the existing core customers?
 - c. Did Apple pursue either differentiation or low cost? Or both?
4. Reflecting on Sony's struggle in 2011, suppose you are appointed as new CEO at Sony, succeeding Howard Stringer:
 - a. How would you diagnose the problem of Sony in terms value, profit, and people?
 - b. Using the four actions framework (E-R-R-C Grid) introduced in Blue Ocean Strategy, what would you do to revive the company?

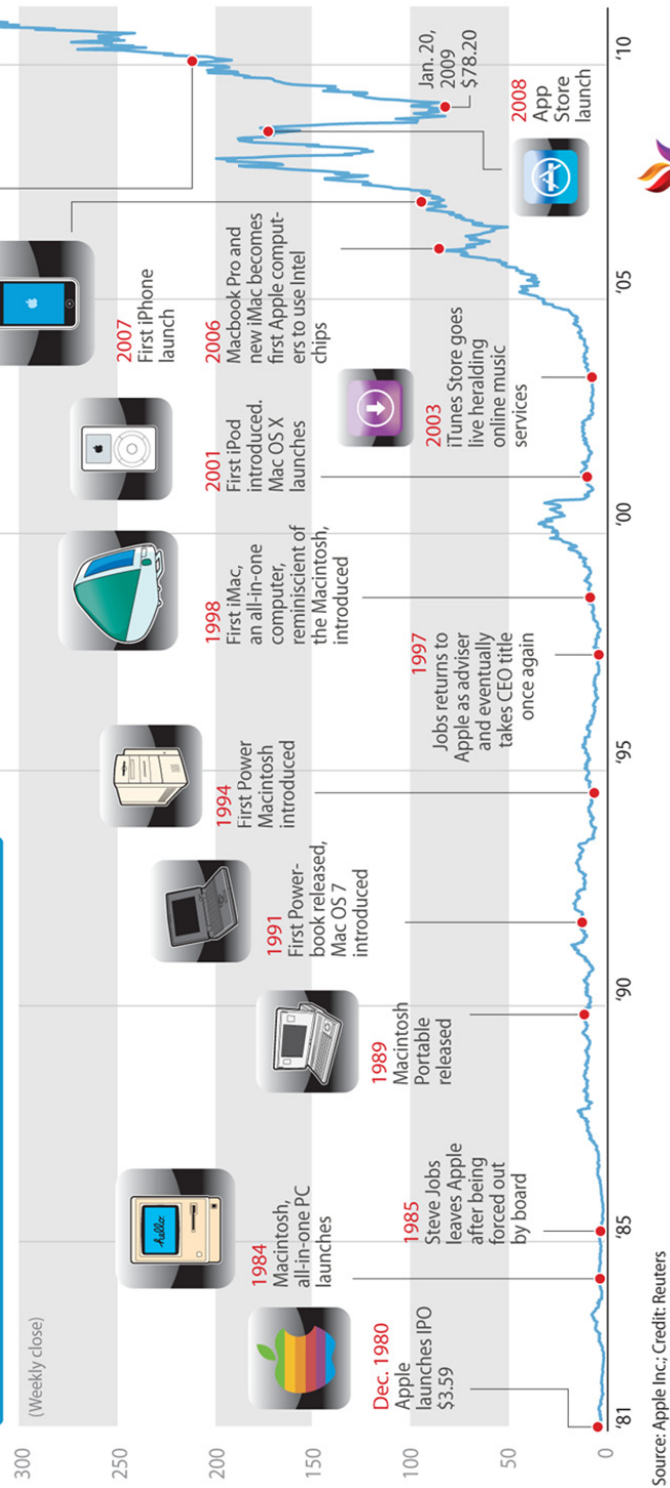
Exhibit A

Apple Inc.'s Historical Stock Prices with Key Product Releases¹¹

TIMELINE OF APPLE RELEASES

Apple released its hotly anticipated followup to last year's iPad, the iPad2

SHARE PRICES AND KEY PRODUCT RELEASES



¹¹ Kim Peterson, "What if you had bought Apple stock in 1997?," Msn Money, October 7, 2011, <http://money.msn.com/top-stocks/post.aspx?post=7ba70f76-54af-4065-baad-922b90a789b5>, accessed January 11, 2012.