TOMORROW'S CHALLENGES

7 GENERIC STRATEGIES TO RESPOND TO DIGITAL DISRUPTION

HOW CAN ESTABLISHED BUSINESSES RESIST UPHEAVAL BY NEW ENTRANTS?

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Digital disruption is a hot topic these days. The news is full of stories about how companies and industries are being disrupted by digitally-savvy startups and new entrants. There is even a new word for this – uberize – which means to disrupt a traditional industry in the way that taxis have been disrupted by Uber in many markets.

Yet, lost behind these stories are the strengths that industry incumbents have to fight such disruption. Below are 7 generic strategies that industry incumbents – those large, legacy businesses – can use to fight against digital disruptors.

1] The Block Strategy
The Block strategy involves the incumbent utilizing all means available to inhibit the disruptor. These means can include claiming patent or copyright infringement, erecting regulatory hurdles, and using other legal barriers. Blocking works well as an opening strategy, and has been used effectively by payment providers to block new entrants such as PayPal, and by movie companies to block YouTube and other video sites. If not used, or when used incorrectly, the results can be disastrous, as has been the case with the music industry. The advantages of this strategy are that it provides a relatively inexpensive way to preserve markets, and builds on the market power and extensive web of industry relationships that most incumbents enjoy. The major disadvantage is that it is only effective in the short to medium term. The Block strategy only buys time to develop and implement other strategies.

2] The Milk Strategy
This strategy involves extracting the most value possible from vulnerable businesses while preparing for the inevitable disruption. The Milk strategy has three sub-components. First, *harvest*, or maintain margins as high as possible for as long as possible. Second, *elevate*, or raise the perceptions of value in the minds of average consumers. This elevation can be achieved by adding features and investing in brand building. Third, *rationalize*, or plan for the necessary cuts and layoffs, and execute them ruthlessly when the disruption arrives. The advantage of this strategy is that revenues and margins for the vulnerable business can be maintained much longer if managed carefully. The disadvantage of the Milk strategy, like the Block strategy, is that it is hard to maintain over a long period of time.

3] The Invest in Disruption Strategy
This strategy involves actively investing in the disruptive threat, including disruptive technologies, human capabilities, digitized processes, or perhaps acquiring companies with these attributes. The invest strategy prepares for the disruption head on, but may lead to strong internal resistance from legacy business areas. It can also be expensive, and comes with an uncertain payback. Amazon and Microsoft have both been very active in developing or acquiring capabilities that carry the potential to disrupt their core businesses. The Invest strategy can be implemented in conjunction with the Block and Milk strategies.

4] The Disrupt the Current Business Strategy
This strategy involves launching a new product or service that competes directly with the disruptor, and can be very effective as it allows the incumbent to leverage inherent strengths such as size, market knowledge, brand, access to capital, and relationships to build the new business. The disadvantage is obvious – the new lines can severely cannibalize existing businesses. However, if timed correctly, self-cannibalization is a much better outcome than business lost to a competitor. Clearly, timing is critical when disrupting a core business, and the likelihood of internal resistance is significant. For these reasons, this strategy is rarely used, leading to damaging disruption in many industries such as mapping, cameras, and retail. However, there are occasions when it has been used successfully, by companies such as Intel (with the Celeron chip cannibalizing the Pentium), Apple (with the iPhone 5c cannibalizing the iPhone 5s), and Amazon (with the Kindle app cannibalizing the Kindle reader).

5] Retreat into a Strategic Niche
This strategy involves focusing on a niche segment of the core market where disruption is less likely to occur. The Retreat strategy often results is a much smaller market size than the legacy core segment. However, these smaller niche markets can remain profitable, and existing capabilities can be used to serve them. Examples of companies that have used this strategy are travel agents switching from generic travel services to focus on complicated travel itineraries and corporate

accounts, Barnes and Noble moving into college bookstores, and Kodak offering high end printing services. By itself, this strategy will result in massive restructuring due to the smaller market size, but in conjunction with other strategies, it can provide a profitable niche business.

6] Redefine the Core Strategy
This strategy involves building an entirely new business model, often in an adjacent industry where it is possible to leverage existing knowledge and capabilities. On the plus side, this strategy side steps the challenges and constraints of the disrupted legacy business. On the negative side, it is extremely difficult to redesign an organization to compete in an entirely new business area. Nevertheless, there are some examples of organizations that have pursued this strategy successfully. Fujifilm took their capability in attaching chemicals to film and entered the cosmetics industry, and IBM moved a large part of their business from hardware to services and consulting.

7] Exit Strategy
The final strategy involves exiting the business entirely and returning capital to investors, ideally through a sale of the business while value still exists. Most companies that fail to avoid disruption wait too long and end up capturing only a fraction of their legacy value. Examples of companies in this category include Blockbuster, Borders, and Radioshack. However, some companies have managed to extract substantial value for disrupted businesses, like Nokia selling its handset business to Microsoft, and MySpace selling itself to News Corp. Strong brands and an effective Milk strategy can maintain value for longer periods of time, allowing the Exit strategy to become a viable one.

These 7 strategies will most often be used in combination, and there is a logical flow to their use. Companies that have managed to survive or thrive in a digitally disruptive environment have almost always utilized more than one strategy. These examples include Fujifilm (as opposed to Kodak), Barnes and Noble (as opposed to Borders), and Apple (as opposed to Nokia).

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