Customer Intimacy and Other Value Disciplines

by Michael Treacy and Fred Wiersema

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Three paths to market leadership.

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How was Dell Computer able to charge out of nowhere and outmaneuver Compaq and other leaders of the personal computer industry? Why are Home Depot's competitors losing market share to this fast-growing retailer of do-it-yourself supplies when they are all selling similar goods? How did Nike, a start-up company with no reputation behind it, manage to run past Adidas, a longtime solid performer in the sport-shoe market?

All three questions have the same three answers. First, Dell Computer, Home Depot, and Nike redefined value for customers in their respective markets. Second, they built powerful, cohesive business systems that could deliver more of that value than competitors. Third, by doing so they raised customers' expectations beyond the competition's reach. Put another way, these industry leaders changed what customers valued and how it was delivered, then boosted the level of value that customers expected.

The idea that companies succeed by selling value is not new. What is new is how customers define value in many markets. In the past, customers judged the value of a product or service on the basis of some combination of quality and price. Today's customers, by contrast, have an expanded concept of value that includes convenience of purchase, after-sale service, dependability, and so on. One might assume, then, that to compete today, companies would have to meet all these different customer expectations. This, however, is not the case.

Companies that have taken leadership positions in their industries in the last decade typically have done so by narrowing their business focus, not broadening it. They have focused on delivering superior customer value in line with one of three value disciplines – operational excellence, customer intimacy, or product leadership. They have become champions in one of these disciplines while meeting industry standards in the other two. (For a discussion of companies that excel at more than one discipline, see the insert "Masters of Two.")

By operational excellence, we mean providing customers with reliable products or services at competitive prices and delivered with minimal difficulty or inconvenience. Dell, for instance, is a master of operational excellence. Customer intimacy, the second value discipline, means segmenting and targeting markets precisely and then tailoring offerings to match exactly the demands of those niches. Companies that excel in customer intimacy combine detailed customer knowledge with operational flexibility so they can respond quickly to almost any need, from customizing a product to fulfilling special requests. As a consequence, these

Operational excellence means

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DRAWINGS BY PAUL MEISEL

companies engender tremendous customer loyalty. Home Depot, for example, is better than any other company in its market at getting the customer precisely the product or information he or she wants. And product leadership, the third discipline, means offering customers leading-edge products and services that consistently enhance the customer's use or application of the product, thereby making rivals' goods obsolete. Nike excels in product leadership in the sport-shoe category.

Companies that push the boundaries of one value discipline while meeting industry standards in the other two gain such a lead that competitors find it hard to catch up. This is largely because the leaders have aligned their entire operating model – that is, the company's culture, business processes, management systems, and computer platforms – to serve one value discipline. Knowing what they want to provide to customers, they have figured out what they must do to follow through. And with the hard work of transforming their organizations behind them, they can concentrate on smaller adjustments that produce incremental value. Less focused companies must do far more than simply tweak existing processes to gain this advantage.

Companies that pursue the same value discipline have remarkable similarities, regardless of their industry. The business systems at Federal Express, American Airlines, and Wal-Mart, for example, are strikingly similar because they all pursue operational excellence. An employee could transfer from FedEx to Wal-Mart and, after getting oriented, feel right at home. Likewise, the systems, structures, and cultures of product leaders such as Johnson & Johnson in health care and pharmaceuticals and Nike in sport shoes look much like one another. But across two disciplines, the similarities end. Send people from Wal-Mart to Nike, and they would think they were on a different planet. Moreover, homogeneity exists only among *leaders* in the same value discipline; mediocre performers are not distinctive enough to look like anything except other mediocre performers in their own industries.

customer transactions are hassle-free.

The conclusions we've drawn about the value disciplines are based on a three-year study of 40 companies that have redefined performance expectations in their markets. Through this research, we have come to understand what each value discipline demands of an organization and why.

Operational Excellence

The term "operational excellence" describes a specific strategic approach to the production and delivery of products and services. The objective of a company following this strategy is to lead its industry in price and convenience. Companies pursuing operational excellence are indefatigable in seeking ways to minimize overhead costs, to eliminate intermediate production steps, to reduce transaction and other "friction" costs, and to optimize business processes across functional and organizational boundaries. They focus on delivering their products or services to customers at competitive prices and with minimal inconvenience. Because they build their entire businesses around these goals, these organizations do not look or operate like other companies pursuing other value disciplines.

Dell Computer is one company that has focused on such operational excellence and, in doing so, has shown PC buyers that they do not have to sacrifice quality or state-of-the-art technology in order to buy personal computers easily and inexpensively. In the mid-1980s, while Compaq concentrated on making its PCs less expensive and faster than IBM's, college student Michael Dell saw the chance to outdo both IBM and Compaq by focusing not on the product but on the delivery system. Out of a dorm room in Austin, Texas, Dell burst onto the scene with a radically different and far more efficient operating model for operational excellence.

Dell realized that Compaq's marketing strategy – selling PCs through dealers to novices – could be

Masters of Two

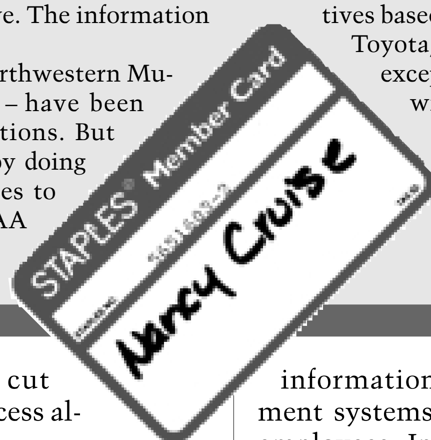
While market leaders typically excel at one value discipline, a few maverick companies have gone further by mastering two. In doing so, they have resolved the inherent tensions between the operating model that each value discipline demands. A decade ago, Toyota successfully pursued an operational excellence strategy; today, it retains its mastery in operational excellence, and, through its breakthroughs in automobile technology, it is moving ahead in product leadership as well.

USAA, a Texas-based insurer that caters mainly to people in the military, has mastered both customer intimacy and operational excellence. USAA is everything an operationally excellent company would want to be: centralized, highly automated, and incredibly disciplined. Its immense, state-of-the-art information system is an information technologist's wish come true. By virtually eliminating paperwork, it allows the company to be quick and responsive. The information system at USAA *is* the process.

Other insurance companies – Northwestern Mutual and Allstate come to mind – have been building equally excellent operations. But USAA continues to set the pace by doing a better job of tailoring its services to customers' particular needs. USAA segments its customer base by, among other characteristics, life stage – at what point a customer is in life – and develops products, services, and servicing approaches for each of those segments. In addition to execution, USAA has mastered customer intimacy.

Staples, the office supply giant, also has become adept at both operational excellence and customer intimacy. Staples achieves the lowest net-landed cost in the entire office stationery business, but it also has become intimate with a particular market: companies employing fewer than 50 people. To further the intimacy with that market segment, it has created a club. Customers join it at no cost and get at least a 5% discount on the fastest moving items. But to get the discount, customers have to show their club card, which means Staples can track sales by customer, and that gives the company all kinds of data it can use in satisfying its market. Store managers now have incentives based on customer retention.

Toyota, USAA, and Staples are today's rare exceptions. But mastery of one discipline will eventually become the minimum that a company will need to get itself into the game. Chances are that the big winners of the future will have mastered two.



outperformed by a model that cut dealers out of the distribution process altogether.

By selling to customers directly, building to order rather than to inventory, and creating a disciplined, extremely low-cost culture, Dell has been able to undercut Compaq and other PC makers in price yet provide high-quality products and service. While Dell has risen to $1.7 billion in revenue in less than ten years, Compaq has been forced to cut prices and overhead.

Other leaders in operational excellence include Wal-Mart, American Airlines, and Federal Express. Yet another, less well-known example, is General Electric's "white goods" business, which manufactures large household appliances. It has focused on operational excellence in serving the vast market of small, independent appliance retailers.

In the late 1980s, GE set out to transform itself into a low-cost, no-hassle supplier to dealers, and it designed its so-called Direct Connect program in pursuit of that objective. The Direct Connect program was ambitious. It required that GE reengineer several of its old business processes, redesign its information systems, reconfigure its management systems, and create a new mind-set among employees. In effect, General Electric reinvented its white goods business to embody its operational excellence discipline. As a result, the company has lowered dealers' net-landed cost of appliances and simplified its business transactions.

Historically the appliance industry had endorsed the theory that a loaded dealer is a loyal dealer. If a dealer's warehouse were full of a manufacturer's product, went the argument, the dealer would be committed to that company's product line because there was no room for goods from anyone else. Manufacturers' programs and pricing had been built around the idea that dealers got the best price when they bought a full truckload of appliances and were offered the best payment arrangements if they adhered to the manufacturer's floor plan.

But changes in the retail end of the industry caused GE to question that assumption. For one, the loaded-dealer concept was costly for independent appliance dealers, whose very existence was being threatened by the growing clout of low-price, multibrand chains like Circuit City. Independent stores could hardly afford to carry a large stock of appliances, especially when faced with competition from multibrand chains. Moreover, the chains could put price pressure on manufacturers, causing makers' margins to shrink.

Realizing that it had to supply high-quality products at competitive prices with little hassle, General Electric abandoned the loaded-dealer concept and reinvented its operating model – the way it made, sold, and distributed appliances. Under the company's new Direct Connect system, retailers no longer maintain their own inventories of major appliances. They rely instead on General Electric's "virtual inventory," a computer-based logistics system that allows stores to operate as though they had hundreds of ranges and refrigerators in the back room when in fact they have none at all.

To make Direct Connect work, retailers acquire a computer package that gives them instantaneous access to GE's on-line order-processing system 24 hours a day. They can use the system to check on model availability and to place orders for next-day delivery. The dealers get GE's best price, regardless of order size or content. Direct Connect dealers also get, among other benefits, priority over other dealers in delivery scheduling plus consumer financing through GE Credit, with the first 90 days free of interest. In exchange, Direct Connect dealers make several commitments: to sell nine major GE product categories while stocking only carryout products, such as microwave ovens and air conditioners; to ensure that GE products generate 50% of sales and to open their books for review; and to pay GE through electronic fund transfer on the 25th of the month after purchase.

> With Direct Connect, GE manufactures in response to customer demand – not inventory.

Under the Direct Connect system, dealers have had to give up some float time in payables, the comfort of having their own back-room inventory, and some independence from the supplier. In return, they get GE's best price while eliminating the hassle and cost of maintaining inventory and assembling full truckload orders – and their profit margins on GE products have soared.

Virtual inventory, it turns out, works better than real inventory for both dealers and customers. "Instead of telling a customer I have two units on order," says one dealer, "I can now say that we have 2,500 in our warehouse. I can also tell a customer when a model is scheduled for production and when it will be shipped. If the schedule doesn't suit the customer, the GE terminal will identify other available models and compare their features with competitive units."

Meanwhile, GE gets half the dealers' business and saves about 12% of distribution and marketing costs. And since dealers serve themselves through the network, GE saves time and labor in order entry and in responding to inquiries. At GE, the new Direct Connect system *is* the order-entry process. Most important, GE has captured a valuable commodity from its dealers: data on the actual movement of its products. Most appliance manufacturers have been unable to track consumer sales accurately because they can't tell whether dealers' orders represent requests for additional inventory or actual customer purchases. With Direct Connect, GE knows that vendors' orders are, in fact, actual sales to customers.

GE links its order-processing system to other systems involved in forecasting demand and planning production and distribution. The company now, in effect, manufactures in response to customer demand instead of to inventory. It has reduced and simplified a complex and expensive warehousing and distribution system down to ten strategically located warehouses that can deliver appliances to 90% of the country within 24 hours.

Other businesses that vigorously pursue a strategy of operational excellence have reinvented their companies in similar fashion. They have reengineered the process that begins with order entry and ends with product or service delivery in a way that emphasizes efficiency and reliability. Specifically, they have adopted automated inventory replenishment and invoiceless payments and have integrated formerly disparate logistics systems. Companies that have adopted a strategy of operational excellence also have built their operations around information systems that emphasize integration and low-cost transaction processing.

Customer Intimacy

While companies pursuing operational excellence concentrate on making their operations lean and efficient, those pursuing a strategy of customer intimacy continually tailor and shape products and services to fit an increasingly fine definition of the customer. This can be expensive, but customer-intimate companies are willing to spend now to build customer loyalty for the long term. They typically look at the customer's lifetime value to the company, not the value of any single transaction. This is why employees in these companies will do almost anything – with little regard for initial cost – to make sure that each customer gets exactly what he or she really wants. Nordstrom is one example of such a company; IBM in its heyday was another; Home Depot is a third.

Home Depot clerks spend whatever time is required with a customer to figure out which product will solve his or her home-repair problem. The company's store personnel are not in a hurry. Their first priority is to make sure the customer gets the right product, whether its retail price comes to $59 or 59 cents.

Individual service is Home Depot's forte. Clerks do not spend time with customers just to be nice. They do so because the company's business strategy is built not just around selling home-repair and improvement items inexpensively but also around the customer's needs for information and service. Consumers whose only concern is price fall outside Home Depot's core market.

Other companies that have embraced a strategy of customer intimacy include Staples in office-supply retailing, Ciba-Geigy in pharmaceuticals, and Kraft and Frito-Lay in consumer packaged goods. These companies have designed operating models that allow them to address each customer or small subsegment of their market individually, as much for the sake of the company's profitability as for the customer's satisfaction. Their infrastructures facilitate multiple modes of producing and delivering products or services. They gladly split hairs when segmenting a market.

Customer intimacy means customers get...

One principle that such companies understand well is the difference between profit or loss on a single transaction and profit over the lifetime of their relationship with a single customer. A leading financial brokerage firm, for instance, knows that not all customers require the same level of service or will generate the same revenues. The company's profitability, then, depends in part on its maintaining a system that can differentiate quickly and accurately among customers based on both the degree of service they require and the revenues their patronage is likely to generate. The company recently installed a telephone-computer system capable of recognizing individual clients by their telephone numbers when they call. The system routes investors with large accounts and frequent transactions to their own senior account representative. Other customers – those who typically place only an occasional buy or sell order, for instance – may be routed to a trainee, junior rep, or whoever is available. In either case, the customer's file appears on the rep's screen before the phone is answered.

The new system, which embodies this company's pursuit of customer intimacy, lets the firm segment its services with great efficiency. If the company has, say, just 400 clients around the country who are interested in trading in a particularly arcane financial instrument, it can group them under the one account rep who specializes in that instrument. It does not have to train every rep in every facet of financial services. Moreover, the company can direct certain value-added services or products to a specific group of clients whose interest it knows to be strong. It could, for instance, search its customer database for affluent retirees interested in minimizing inheritance taxes, customize a service or a product just for them, and train a rep in the new offering's sale and use.

In its move toward customer intimacy, Kraft USA has created the capacity to tailor its advertising, merchandising, and operations in a single store or in several stores within a supermarket chain to the needs of those stores' particular customers. Kraft has the information systems, analytical capability, and educated sales force to allow it to develop as many different so-called micro-merchandising programs for a chain that carries its products as the chain has stores. The program can be different for every neighborhood outlet. But to accomplish this, Kraft had to change itself first. It had to create the organization, build the information systems, and educate and motivate the people required to pursue a strategy of customer intimacy.

Like most companies that choose this strategy, Kraft decentralized its marketing operation in order to empower the people actually dealing with the customer. In Kraft's case, this was the sales force. Instead of pushing one-size-fits-all sales promotion programs, Kraft salespeople now work with individual store managers and regional managers to create customized promotional programs from an extensive computerized menu of program models.

Kraft does not just give its salespeople permission to work with customers, it also is giving them the data they need to make intelligent recommendations that will actually work. To do so, Kraft has assembled a centralized information system that collects and integrates data from three sources. The data it collects from individual stores break out consumer purchases by store, category, and product and indicate how buying behavior is affected by displays, price reductions, and so forth. They also provide profiles of customers who have bought particular products over the past several years and their rates of purchase. A second database contains demographic and buying-habit information on the customers of 30,000 food stores nationwide. A third set of data, purchased from an outside vendor, contains geo-demographic data by nine-digit zip code.

At Kraft headquarters, its trade marketing team sorts and integrates the information from these three databases and uses the results to supply sales teams with a repertoire of usable programs, products, value-added ideas, and selling tools. For instance, the trade marketing team sorted all shoppers into six distinct groups, with names such as full-margin shoppers, planners and dine-outs, and commodity shoppers. Kraft then determined for its major accounts which shopper groups frequented each of their stores. A Kraft sales team even persuaded one chain to create a drive-through window in stores where planners and dine-outs – people who plan their shopping trips and dine out often – were a large segment, making it more convenient for them to pick up staples between big shopping trips.

Kraft is also able to develop promotion packages for store clusters for special events like the Superbowl. It can design a product mix more likely to succeed in one cluster than another. Pinpointing which store gets which product reduces inventory and delivers the right product to the right place at the right time.

In reinventing itself, Kraft emulates other companies in different industries that also choose to pursue the strategy of customer intimacy. Its business processes stress flexibility and responsiveness. Its information systems collect, integrate, and analyze data from many sources. Its organizational structure emphasizes empowerment of people working close to customers, and its hiring and training programs stress the creative decision-making skills required to respond to individual customer needs. Its management systems recognize and utilize such concepts as customer lifetime value, and the rules and norms that management fosters among employees are consistent with the "have it your way" mind-set that must prevail in a company built on customer intimacy.

Product Leadership

Companies that pursue the third discipline, product leadership, strive to produce a continuous stream of state-of-the-art products and services. Reaching that goal requires them to challenge themselves in three ways. First, they must be creative. More than anything else, being creative means recognizing and embracing ideas that usually originate outside the company. Second, such innovative companies must commercialize their ideas quickly. To do so, all their business and management processes have to be engineered for speed. Third and most important, product leaders must relentlessly pursue new solutions to the problems that their own latest product or service has just solved. If anyone is going to render their technology obsolete, they prefer to do it themselves. Product leaders do not stop for self-congratulation; they are

...exactly what they need.

too busy raising the bar.

Johnson & Johnson, for example, meets all three of these challenges. J&J seems to attract new ideas, but it is not happenstance that brings good ideas in, develops them quickly, and then looks for ways to improve them. In 1983, the president of J&J's Vistakon, Inc., a maker of specialty contact lenses, heard about a Copenhagen ophthalmologist who had conceived of a way of manufacturing disposable contact lenses inexpensively. At the time, the company's Vistakon unit generated only $20 million each year in sales primarily from a single product, a contact lens for people who have astigmatism.

What was unusual was the way Vistakon's president got his tip. It came from a J&J employee whom he had never met who worked in an entirely different subsidiary in Denmark. The employee, an executive for Janssen Pharmaceutica, a J&J European drug subsidiary, telephoned Vistakon's president to pass along the news of the Danish innovation. Instead of dismissing the ophthalmologist as a mere tinkerer, these two executives speedily bought the rights to the technology, assembled a management team to oversee the product's development, and built a state-of-the-art facility in Florida to manufacture disposable contact lenses called Acuvue.

Vistakon's disposable lenses caught rivals off guard – and they never caught up.

By the summer of 1987, Acuvue was ready for test marketing. In less than a year, Vistakon rolled out the product across the United States with a high-visibility ad campaign. Vistakon – and its parent, J&J – were willing to incur high manufacturing and inventory costs even before a single lens was sold. Its high-speed production facility helped give Vistakon a six-month head start over would-be rivals, such as Bausch & Lomb, Inc. and Ciba-Geigy. Taken off guard, the competition never caught up. Vistakon also took advantage of the benefits of decentralization – among them, autonomous management, speed, and flexibility – without having to give up the resources, financial and otherwise, that only a giant corporation could provide. Part of the success resulted from directing much of the marketing effort to eye-care professionals to explain how they would profit if they prescribed the new lenses. In other words, Vistakon did not market just to consumers. It said, in effect, that it's not enough to come up with a new product; you have to come up with a new way to go to market as well.

In 1991 Vistakon's sales topped $225 million worldwide, and it had captured a 25% share of the U.S. contact-lens market. But Vistakon is not resting on its laurels. It continues to investigate new materials that would extend the wearability of the contact lenses and even some technologies that would make the lenses obsolete.

J&J, like other product leaders, works hard at developing an open-mindedness to new ideas. Product leaders create and maintain an environment that encourages employees to bring ideas into the company and, just as important, they listen to and consider these ideas, however unconventional and regardless of the source. "Not invented here" is not a part of their vocabularies. In addition, product leaders continually scan the landscape for new product or service possibilities; where others see glitches in their marketing plans or threats to their product lines, companies that focus on product leadership see opportunity and rush to capitalize on it.

Product leaders avoid bureaucracy at all costs because it slows commercialization of their ideas. Managers make decisions quickly, since in a product leadership company, it is often better to make a wrong decision than to make one late or not all. That is why these companies are prepared to decide today, then implement tomorrow. Moreover, they continually look for new ways – such as concurrent engineering – to shorten their cycle times. Japanese companies, for example, succeed in automobile innovation because they use concurrent development processes to reduce time to market. They do not have to aim better than competitors to score more hits on the target because they can take more shots from a closer distance.

Companies excelling in product leadership do not plan for events that may never happen, nor do they spend much time on detailed analysis. Their strength lies in reacting to situations as they occur. Fast reaction times are an advantage when dealing with the unknown. Johnson & Johnson's Vistakon managers, for example, were quick to order changes to the Acuvue marketing program when early market tests were not as successful as they had expected. They also responded quickly when competitors challenged the safety of Acuvue lenses. They distributed data combating the charges, via Federal Express, to some 17,000 eye-care professionals. Vistakon's speedy response to the concerns raised by its competitors engendered goodwill in the marketplace.

Vistakon can move fast and take risks because it is organized like a small, entrepreneurial company. At the same time, it can call on the resources and capabilities of a multibillion-dollar corporation. This combination makes Vistakon – and J&J – a powerhouse competitor and strong product leader.

Product leaders have a vested interest in protecting the entrepreneurial environment that they have created. To that end, they hire, recruit, and train employees in their own mold. When it is time for Vistakon to hire new salespeople, for example, its managers do not look for people experienced in selling contact lenses; they look for people who will fit in with J&J's culture. That means they do not first ask about a candidate's related experience. Instead, they ask such questions as, "Could you work cooperatively in teams?" and "How open are you to criticism?"

Product leaders are their own fiercest competitors. They continually cross a frontier, then break more new ground. They have to be adept at rendering obsolete the products and services that they have created because they realize that if they do not develop a successor, another company will. J&J and other innovators are willing to take the long view of profitability, recognizing that whether they extract the full profit potential from an existing product or service is less important to the company's future than maintaining its product leadership edge and momentum. These companies are never blinded by their own successes.

One final point about product leaders: they also possess the infrastructure and management systems needed to manage risk well. For example, each time J&J ventures into an untapped area, it risks millions of dollars as well as its reputation. It takes that chance, though, in part because its hybrid structure allows it to combine the economies of scale and resource advantages of a $12 billion corporation with the cultural characteristics of a start-up company. In the case of Acuvue, J&J could manage the tremendous risk associated with developing and launching the lens because it represented only a small portion of the company's outlays.

Sustaining the Lead

Becoming an industry leader requires a company to choose a value discipline that takes into account its capabilities and culture as well as competitors' strengths. (For more on choosing a value discipline, see the insert "Choosing Disciplines or Choosing Customers?") But the greater challenge is to sustain that focus, to drive that strategy relentlessly through the organization, to develop the internal

Product leaders are open to new ideas wherever they can find them.

Choosing Disciplines or Choosing Customers?

When a company chooses to focus on a value discipline, it is at the same time selecting the category of customer that it will serve. In fact, the choice of business discipline and customer category is actually a single choice.

One set of potential customers defines value within a matrix of price, convenience, and quality, with price the dominant factor. These customers are less particular about what they buy than they are about getting it at the lowest possible price and with the least possible hassle. They are unwilling to sacrifice low price or high convenience to acquire a product with a particular label or to obtain a premium service. Whether they are consumers or industrial buyers, they want high-quality goods and services, but even more, they want to get them cheaply or easily or both.

These are the customers who shop for retail goods at discount and membership warehouse stores. They buy PC clones directly from manufacturers. They seek basic transportation when they buy a car and discount com-missions when they buy or sell stocks and other investments. The business that succeeds by serving these customers focuses on operational excellence.

The second set of customers is more concerned with obtaining precisely what they want or need. They are willing to make some sacrifice – in price or delivery time, for instance – if the sacrifice helps them acquire something that meets their unique requirements. The specific characteristics of the product or the way the service is delivered is far more important to them than any reasonable price premium or purchase inconvenience they might incur.

Customers in this group ascribe value to a product or service according to how closely it appears to be designed just for them. Chain stores – whether in the food, book, or music business – that customize their inventories to match regional or even neighborhood tastes serve this category of customer. Other retailers and catalogers attract this customer type by offering the largest imaginable range of products. They won't carry just standard Scrabble, for instance, but every version of the game. An industrial distributor we know carries 12 pages of water heaters in its catalog. Its breadth of inventory is a strategic asset in appealing to this second customer category. These customers require a company to focus on customer intimacy.

To the third category of customers, new, different, and unusual products count most. These are customers who, as clothing buyers, are primarily interested in fashion and trends. In an industrial context, they are buyers who value state-of-the-art products or components because their own customers demand the latest technology from them. If they are service companies, they want suppliers that help them seize breakthrough opportunities in their own markets. For a company to succeed in serving these customers, it has to focus on product leadership.

One point to bear in mind: the same people can be found in all three customer categories, depending on what they are buying. An individual might buy office supplies primarily on price, groceries strictly on the basis of personal taste, and clothes as fashion dictates. The same people will define value differently as it applies to different goods and services.

consistency, and to confront radical change.

Many companies falter simply because they lose sight of their value discipline. Reacting to marketplace and competitive pressures, they pursue initiatives that have merit on their own but are inconsistent with the company's value discipline. These companies often appear to be aggressively responding to change. In reality, however, they are diverting energy and resources away from advancing their operating model.

Sears is a good example. Under enormous pressure from Wal-Mart and other competitors, Sears's retailing division in the late 1980s launched a number of initiatives aimed at winning back customers and boosting its sagging bottom line. First came "everyday low prices," a component of an operational excellence discipline. For that gambit to pay off, Sears needed to cut costs – which it did to some extent by eliminating many in-store employees and slashing front-office expenses. But the cost cutting did not go nearly far enough, in part because Sears had not consciously focused on the discipline of operational excellence. Had it done so, it would have scrutinized each part of its organization, including the order-fulfillment process, to see where it could realize savings. The consequence of not focusing meant, among other things, that Sears failed to restructure its end-to-end distribution costs, as Wal-Mart, for instance, has done.

In another attempt to regain market share, Sears inaugurated "Brand Central," whereby the retailer would carry branded products in addition to its house brands, Kenmore and Craftsman. Creating more product variety in an attempt to meet the needs of different market segments is a component of a customer intimacy discipline. But again, Sears did not go far enough. By just plucking Brand Central from a quiver of random ideas, Sears shot wide of the target. Brand Central only confused existing customers, who did not know which brand to buy. Sears's strategy also cut into sales of its own brands. And since the move did not give Sears any more product variety than competitors had, it did little to boost sales.

Sears's third initiative, meant to give the retailer a trendy image, was to have models and actresses endorse its fashion line. This tack, which corresponds to a product leadership discipline, also had little impact on profits. One problem was that Sears struck just one deal, with model Cheryl Tiegs. The second problem: J.C. Penney was following the same strategy but was outdoing Sears with more endorsements, slicker advertising, better catalogs, more sophisticated marketing, and better product design. In trying to be all things to all people, Sears pursued strategies that steered it away from its chosen value discipline and into unproductive dead ends. It tried to fuse together incompatible philosophies and practices and got predictable results. In its time, Sears was a value leader, but to regain that distinction in today's competitive market, the company will have to pick one value discipline and vigorously pursue it while meeting industry standards in the other two.

The key to gaining and sustaining value leadership is focus, but the management of a company that's a value leader must stay alert. The operating model that elevated a company to value leadership – Compaq's model, for instance – is superior and worth exploiting only until a better one – Dell's distribution model, say – comes along.

Companies that sustain value leadership within their industries will be run by executives who not only understand the importance of focusing the business on its value discipline but also push relentlessly to advance the organization's operating model. They will personally lead the company's drive to develop new capabilities and to change the imbedded work habits, processes, and attitudes that prevent them from achieving excellence in the discipline they have chosen. By leading the effort to transform their organizations, these individuals will be preparing their companies to set new industry standards, to redefine what is possible, and to forever change the terms of competition.

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