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# Countering the Biggest Risk of All

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# Countering the Biggest Risk of All

## The Idea in Brief

You've insured your company against earthquakes, hedged against interest-rate hikes, and created backup data systems. But what about new technologies that may render your products obsolete? Sudden shifts in customer tastes that could redefine your industry? A one-of-a-kind competitor who might seize the lion's share of your market?

These and other forms of **strategic risk** can disrupt and even destroy your business. Over the past 12 years, they've caused more than one-third of *Fortune* 1000 companies to lose 60%-plus of their value in one year.

How to avoid this fate? Apply powerful strategic-risk countermeasures. For example, to insure against technology-shift risk, Microsoft used *double betting:* It invested in the OS/2 *and* Windows operating systems so it could thrive no matter which version prevailed. Recognizing Wal-Mart's threat as a one-of-a-kind rival, Target *changed its business design:* It transformed itself from a conventional discounter into a low-price but style-conscious retailer that attracts different customers than Wal-Mart's.

By countering strategic risk, you protect your company's value, secure your competitive position, and even uncover surprising new growth opportunities. For example, after struggling leather-goods maker Coach began using aggressive in-market testing to anticipate customer-preference shifts, it surpassed rival Gucci in growth rate, profit margin, and market capitalization.

## The Idea in Practice

Technology shifts and one-of-a-kind rivals are just two forms of strategic risk. Watch for these additional forms, and adopt appropriate countermeasures:

### INDUSTRY MARGIN SQUEEZE

Ever costlier R&D, increasingly powerful suppliers, overcapacity, and commoditization erode profit margins for all industry players.

*Countermeasure:* Shift from competition to collaboration. For example, the Visa and MasterCard networks allow member financial institutions to share payment-processing and marketing services that are much more efficient than any bank could create.

### BRAND EROSION

Product defects or a failure to develop appealing new offerings endangers your brand.

*Countermeasure:* Redefine "brand investment" as more than a marketing issue, to account for investments in other factors affecting your brand—such as service and product quality. Reallocate brand investments based on early signs of weakness.

▶ Example:
When American Express began losing market share to rivals, it reduced merchants' transaction fees, accelerated payments, and enhanced its Membership Miles rewards program—paying more to participating airlines and adding hotel chains. These moves arrested the slide, spurring dramatic growth in Amex's market value over the past decade.

### CUSTOMER PRIORITY SHIFT

Customers' preferences shift suddenly and dramatically—or gradually and invisibly.

*Countermeasure:* Gather and analyze proprietary information to detect potential shifts. Conduct fast, cheap experiments to identify attractive offerings for different customer microsegments.

▶ Example:
Known for its conservative styling, Coach wondered whether its customers would remain loyal if it explored trendier styles to expand its customer base. It conducted customer in-store product tests and market experiments to gauge the impact of new pricing, features, and offers by competitive brands. It then used the information to quickly alter product designs, drop unappealing items, and create new lines featuring different fabrics and colors. It also tailored merchandise presentations to fit customer demographics at specific stores. Result? Coach retained its traditional fans *and* attracted new customers.

### MARKET STAGNATION

Growth slows in a mature market. Or prices fall, producing weak earnings.

*Countermeasure:* Expand the value you offer customers—by helping them reduce their costs, cycle time, or risks.

▶ Example:
Industrial-gas supplier Air Liquide developed technology that enabled customers to establish small gas production facilities on-site rather than rely on large centralized plants and tanker shipments for their energy. Air Liquide's new on-site production teams soon identified other customer needs it could address—such as minimizing risk of safety violations. By offering a new set of services, including environmental consulting and chemicals management, the company expanded its potential markets, captured more of its customers' spending, and improved customer profitability and loyalty.