

EDGE STRATEGY

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BUSINESS
REVIEW PRESS

A New
Mindset for
Profitable
Growth

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Special
Sneak Preview

“Edge Strategy® is a powerful concept that previously lacked a name. We wrote this book because we are passionate about teaching the pattern-recognition skills to unlock opportunities that are compelling but not always obvious.”

—Alan Lewis and Dan McKone

ABOUT THE AUTHORS

Alan Lewis and Dan McKone have extensive experience helping companies drive shareholder value and growth through effective corporate strategies, including unlocking value at the edges of their business.



Alan Lewis is a Managing Director and Partner at L.E.K. Consulting. For over a decade he has helped companies identify new growth opportunities and realize the benefits. He started his career as a professional engineer, commercializing new technologies in the chemicals sector.



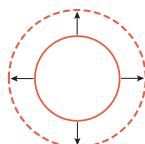
Dan McKone is a Managing Director and Partner at L.E.K. Consulting and a member of L.E.K.’s Global Leadership Team. Over the past two decades he has advised hundreds of clients on corporate strategy and growth, business model evolution, and value-based decision-making.



VIDEO: Hear the authors discuss Edge Strategy at www.edgestrategybook.com/video.

Three Options for Growth

Many firms want to expand their business. However, it's often difficult to see how best to grow while maintaining current successes. Firms generally take one of three paths:

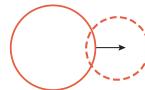


GROW THE EXISTING BUSINESS

Grow revenue by increasing current efforts or trying to improve the core business.

Examples: Market share growth; pricing efforts; international expansion.

Key Considerations: Doing more of the same can often be copied, can have diminishing returns and is often insufficient, particularly in mature businesses.

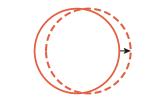


CREATE NEW BUSINESSES

Offer new products and services that may or may not be related to the existing business.

Examples: Search for uncontested market spaces; horizontal or vertical M&A.

Key Considerations: Steps into the unknown and is often high risk. For example, there are nearly 40,000 corporate mergers annually in the United States, but analysis shows that 60 percent of them destroy shareholder value.



IMPLEMENT EDGE STRATEGY FRAMEWORK

Optimize current investment by unlocking value on the periphery of existing businesses. Edge strategy frameworks leverage investments already made and risks already taken.

Examples: Create customer options that better monetize or slightly extend existing products and services; harvest existing assets in new, creative ways.

Key Considerations: Requires deep understanding of how all customers' needs vary. Also requires deep understanding of the value of existing assets.

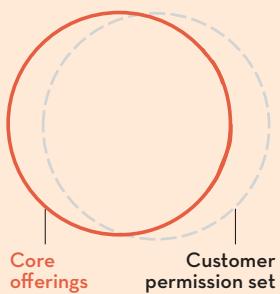
Our findings are a culmination of 30 combined years of working with hundreds of clients around the globe. During the course of three years, we studied nearly 600 companies in 60 industries to validate edge strategy concepts.

Edge Strategy Approaches Defined

An edge strategy mindset is a disciplined methodical approach to growth that focuses on opportunities often hiding in plain sight—at the edge of the core business. There are three main edge strategy approaches, and each examines opportunities outside of the current “customer permission set”—the needs customers would allow your company to address.

Edge strategy approaches are built on top of existing assets to leverage current capabilities and successes, and thus generally offer higher margins with lower risk than do other growth alternatives. Additionally, because new edge offerings are better attuned to individual customer needs, customer satisfaction and core operations often improve.

Challenging the Existing Boundaries: Three Edge Strategy Frameworks



DEFINING THE TERMS

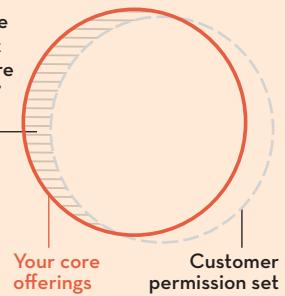
Core offerings

Products and services central to the current strategy of the business.

Customer permission set

The area where customers see value and therefore give a company permission to serve.

Elements of the core offering that are not universally valued are on the “inside edge”



PRODUCT EDGES

Opportunity to upsell where you are misaligned with customer needs or parsing out elements of the core that are not universally valued.

Example: In addition to their “all-inclusive” core beverage offering, Royal Caribbean Cruises offers passengers seven beverage packages, ranging from unlimited simple soft drinks to unlimited top-shelf spirits and wines.

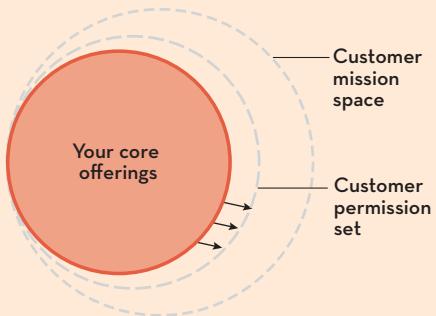
Our research showed that while many firms practice some type of edge strategy mindset, only 10 percent consistently find edges and weave them into their corporate approach.

10%

An edge strategy mindset is a habit of highly successful companies. These “edge achievers” delivered risk-adjusted returns that were 15 percent higher and revenue growth that was 39 percent greater than their peers’ on an indexed basis.

↑
15%

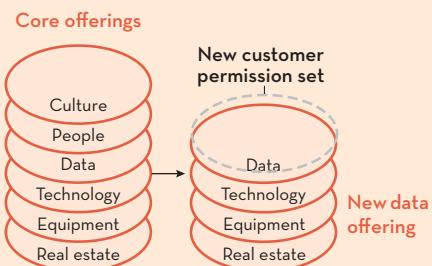
↑
39%



JOURNEY EDGES

Finding ways to create new revenue by extending your involvement in your customers' journey toward their ultimate mission.

Example: Best Buy acquired Geek Squad to help its customers install, learn to use and fix the electronics it sells.



ENTERPRISE EDGES

Finding new revenue streams that are made from existing capabilities, expertise or data that can be restructured to serve new customers.

Example: In Japan, Toyota captures the speed and position of its cars that use its GPS system, and then sells traffic data to municipal planning departments and corporate delivery fleets.

Examples of Edge Strategy Successes

While there are numerous edge strategy variations, many successful edge businesses focus on customer variations to design offerings that leverage existing assets to more completely meet the needs of all customers.

PRODUCT EDGE CASE STUDY: APPLE

Leveraging the Add-On

Apple is an expert at leveraging product edge strategies. Core products like the iPod and iPad are supported by a broad range of optional add-ons for purchase, which generate a high-margin, low-investment and low-risk revenue stream.

- iTunes is an edge platform for Apple's devices, allowing customers to add content to the devices and increase their utility.
- Third-party apps offered on iOS devices through the Apple App Store are also edge offers, allowing Apple to leverage the innovation of others. The apps provide core product functionality enhancements and utility for these devices.

Meeting Customer Demand: Apple offers customers incremental utility for incremental purchase. Optional add-ons continue to improve the original product and allow customers to customize their Apple products based on their changing needs.

How They Did It

- Built platforms allowing optional enhancements, or “add-ons,” to the core product.
- Leveraged foundational assets to build these platforms.
- Supported the add-ons using third parties for low incremental risk and investment.
- Charged separately for the add-ons.

Results: Increased scale of offerings with little investment. This edge strategy introduced the opportunity for an ongoing series of transactions with the consumer, bringing incremental revenues and resulting in expanded profits and more satisfied customers.

JOURNEY EDGE CASE STUDY: WHOLE FOODS

Serving More of the Customer Journey

Today, many think of the upscale grocery store Whole Foods as a leader in ready-to-eat meals. However, the professional chefs, baristas and sit-down dining areas of today started as a deli counter. Whole Foods recognized a journey edge strategy and used value-added services to provide customers more of what they wanted at, or near, the existing core offerings. The company constructed a complementary business that leverages the core business assets to earn outsized margins.

Meeting Customer Demand: By understanding its customers' ultimate missions and by taking a step further down this path with them—going from “I want ingredients to cook my dinner” to “I want my dinner already cooked”—Whole Foods expanded its core offering, capturing more of its customers’ journeys.

How They Did It

- Expanded the core business; ready-to-eat is a natural extension of the grocery store offerings.
- Leveraged existing assets: stores, foot traffic and supply chain relationships.
- Made incremental changes to enable the strategy, mainly around merchandising and some elements of the labor model.

Results:

- In 2014, prepared foods were 20 percent of Whole Foods’ revenue, or \$2.7B.¹
- Industry profit margins for prepared foods are typically 55 percent—1.5 times what the company realized in its overall business.²

¹ Whole Foods Market, 2014 Annual Report.

² “Gross Profit Margin Data From NBJ’s Natural Foods Merchandiser Survey: NBJ Data Chart 124,” *Nutrition Business Journal*, August 2008; and Whole Foods Market, 2014 Annual Report.

ENTERPRISE EDGE CASE STUDY: UNITEDHEALTH

Unlocking Value on the Periphery

UnitedHealth realized that the data assets it had assembled to support its core offering were not uniquely valuable to its core business. In 1996, they established OptumInsight, a business that offers drug companies information from the parent company database. Drug companies use the data to understand how their products (and those of their rivals) are used by customers. This enterprise edge strategy generates incremental cash flow without impacting UnitedHealth’s core business: providing health insurance.

Meeting Customer Demand: While it is typically risky to target new customers in a new sector, UnitedHealth mitigated its risk: the new offering was a pre-existing asset of its core business. The company’s new initiative was to package the data in a way that made it available for new customers. Incremental investment and risk in this strategic move were low.

How They Did It

- Leveraged and monetized existing assets—in this case, data.
- Repurposed a byproduct of core activity for an entirely different customer set.

Results:

- OptumInsight has become a robust profit center, going beyond the original incremental growth opportunity.
- From 2006 to 2014, OptumInsight’s annual growth rate of 16 percent was more than three times the growth rate of UnitedHealth.³
- In 2014, OptumInsight earned:
 - \$5.2B in revenue—up from \$956M in 2006.⁴
 - \$1B in operating income, a 19 percent margin; in contrast, UnitedHealth reported \$10.3B with an 8 percent margin.⁵

³ L.E.K. Consulting, “Analysis of Edge Strategy Prevalence.” Unpublished study, June 2015; growth rates calculated from historical company financial reports, 2006-2014.

⁴ UnitedHealth Group, 2014 Annual Report; and UnitedHealth Group, 2008 Annual Report.

⁵ UnitedHealth Group, 2014 Annual Report.

Edge Strategy Benefits

PROFIT MARGINS

Often greater than those generated by core offerings.

RISK AND INVESTMENT

Leverages investments already made and risks already taken.

CUSTOMER DEMAND

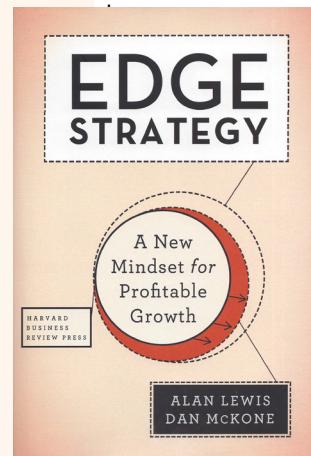
Addressing more fragmented customer needs at more journey points creates a bigger value proposition.

CUSTOMER SATISFACTION

Aligning new offerings with known customer needs increases satisfaction.

UPSIDE

Revenue is incremental to the market rather than captured from competitors and so is more sustainable.



How could an edge strategy mindset benefit your business?

LEARN MORE AT
EDGESTRATEGYBOOK.COM

About L.E.K. Consulting

L.E.K. Consulting is a global management consulting firm that uses deep industry expertise and rigorous analysis to help business leaders achieve practical results with real impact. We are uncompromising in our approach to helping clients consistently make better decisions, deliver improved business performance and create greater shareholder returns. The firm advises and supports global companies that are leaders in their industries – including the largest private and public sector organizations, private equity firms and emerging entrepreneurial businesses. Founded more than 30 years ago, L.E.K. employs more than 1,000 professionals across the Americas, Asia-Pacific and Europe. For more information, go to www.lek.com.

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