Apple: What's Next?

IN EARLY 2015, Apple's stock market valuation reached $775 billion, making it the most valuable public company of all time.[1] This made Apple twice as large as Exxon, the number two. Not even 20 years earlier, Apple would likely have gone bankrupt if archrival Microsoft (which enjoyed the same position with a valuation of $615 billion in December 1999) had not invested $150 million in Apple. How did Apple become so successful?

Apple became the world's most successful company based on a powerful competitive strategy. That strategy, conceptualized by co-founder Steve Jobs, combines innovation in products, services, and business models. From near-bankruptcy in 1997, Apple's revitalization really took off in 2001 when it introduced the iPod, a portable digital music player, the same year it opened its first retail stores. Apple's stores now earn the highest sales per square foot of any retail outlets, including luxury stores such as Tiffany & Co. jewelry or LVMH, purveyor of fine handbags and other luxury goods.

In 2003, Apple soared even higher when it opened the online store iTunes. Apple didn't stop there. In 2007, the company revolutionized the smartphone market with the introduction of the iPhone. Just three years later, Apple created the tablet computer industry by introducing the iPad, thus beginning to reshape the publishing and media industries. Further, for each of its iPod, iPhone, and iPad lines of businesses, Apple followed up with incremental product innovations extending each product category. By combining tremendous brainpower, intellectual property, and iconic brand value, Apple has enjoyed dramatic increases in revenues.

Apple CEO Tim Cook demos Apple Watch and Apple Pay

A Good Strategy

Why was Apple so successful? Why did Microsoft's once superior market valuation evaporate? Why did Apple's competitors such as Sony, Dell, Hewlett-Packard (HP), Nokia, and BlackBerry struggle or go out of business? The short answer is: Apple had a good strategy. But this begs the question: What is a good strategy?

A good strategy is more than a mere goal or a company slogan. A good strategy defines the competitive challenges facing an organization through a critical

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and honest assessment of the status quo. A good strategy also provides an overarching approach (policy) on how to deal with the competitive challenges identified. Last, a good strategy requires effective implementation through a coherent set of actions. A *good strategy,* therefore, consists of three elements:[2]

1. A *diagnosis* of the competitive challenge.
2. A *guiding policy* to address the competitive challenge.
3. A *set of coherent actions* to implement the firm's guiding policy.

THE COMPETITIVE CHALLENGE. First, consider the diagnosis of the competitive challenge. Above, we briefly trace Apple's renewal from the year 2001, when it hit upon the product and business-model innovations of the iPod/iTunes combination. Prior to that, Apple was merely a niche player in the desktop-computing industry and struggling financially. Steve Jobs turned the sinking company around by focusing on only two computer models (one laptop and one desktop) in each of two market segments (the professional market and the consumer market) as opposed to dozens of non-differentiated products within each segment. This streamlining of its product lineup enhanced Apple's strategic focus. Even so, the outlook for Apple was grim. Jobs believed that Apple, with less than 5 percent market share, could not win in the personal computer industry where desktops and laptops had become commoditized gray boxes. In that world, Microsoft, Intel, and Dell were the star performers. Jobs needed to create the "next big thing."[3]

A GUIDING POLICY. Second, let's consider the guiding policy. Apple shifted its competitive focus away from personal computers to mobile devices. In doing so, Apple disrupted several industries through its product and business-model innovations. Combining hardware (i.e., the iPod) with a complementary service product (i.e., the iTunes Store) enabled Apple to devise a new business model. Users could now download individual songs legally (at 99 cents) rather than buying an entire CD or downloading the songs illegally using Napster and other file-sharing services. The availability of the iTunes Store drove sales of iPods. Along with rising sales for the new iPod and iTunes products, demand rose for iMacs. The new products helped disrupt the existing personal computer market, because people wanted to manage their music and photos on a computer that worked seamlessly with their mobile devices. Apple then leveraged the success of the iPod/iTunes business-model innovation, following up with product-category-defining innovations when launching the iPhone (in 2007) and the iPad (in 2010).

COHERENT ACTIONS. Third, Apple implemented its guiding policy with a set of coherent actions. Apple's coherent actions took a two-pronged approach: It drastically streamlined its product lineup through a simple rule—"we will make only one laptop and one desktop model for each of the two markets we serve, professional and consumer." It also disrupted the industry status quo through a potent combination of product and business model innovations, executed at planned intervals. These actions allowed Apple to create a string of temporary competitive advantages (see Exhibit MC6.1). Taken together, this allowed Apple to sustain its superior performance for over a decade.

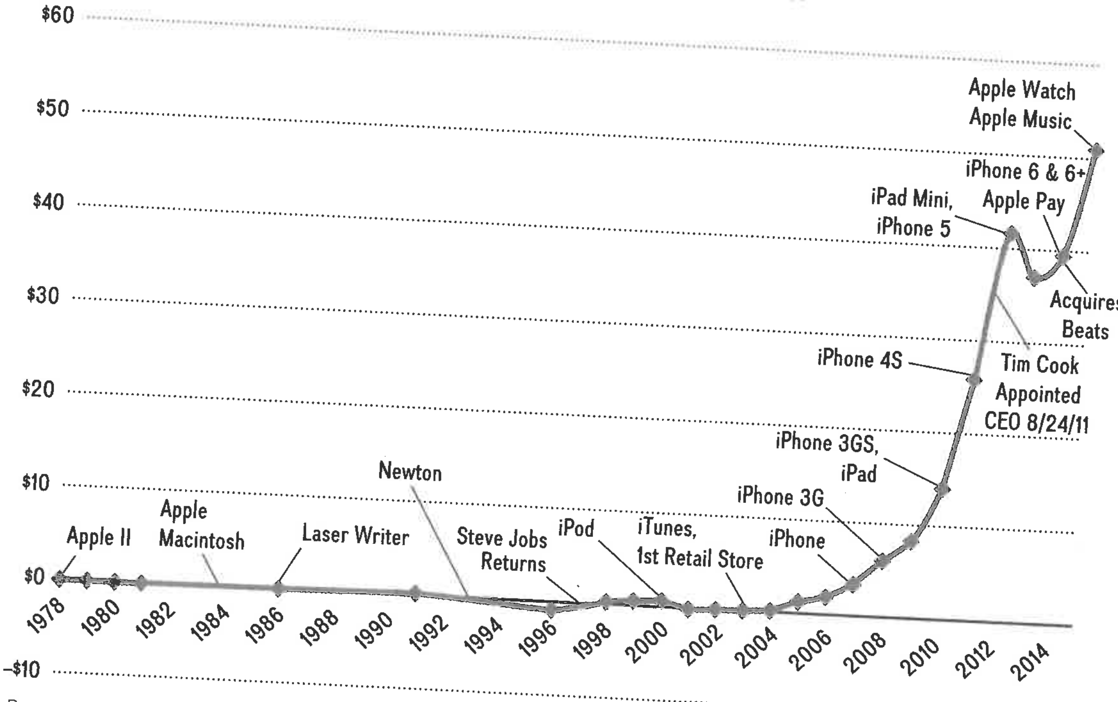
Past performance, however, is no guarantee of future performance. Microsoft was once the most valuable company in the world but has since struggled to keep up with Apple. At the same time, Microsoft, as well as Google, Samsung, Amazon, and others, is working hard to neutralize Apple's competitive advantage.

The trillion-dollar question is whether Apple can continue to maintain a competitive advantage in the face of increasingly strong competition and rapidly changing industry environments. In both mobile payment systems (Apple Pay launched in 2014) and music streaming (Apple Music launched in 2015), Apple was a later mover. The Apple Watch, introduced in 2015, is the first new product category Apple launched since the iPad in 2010. Although Apple has 55 percent market share and captures over 90 percent of profits in the smartphone industry (as of 2015), over 60 percent of Apple's $225 billion revenues come from the iPhone.

DISCUSSION QUESTIONS

1. Explain Apple's success over the last decade. Think about which industries it has disrupted and how. Also look at Apple's main competitors.
2. Is Apple's success attributable to industry effects or firm effects, or a combination of both? Explain.

EXHIBIT MC6.1 / Apple's Net Income ($ billions) and Key Events, 1978–2015



Source: Depiction of publicly available data.

3. What are the greatest challenges Apple is facing? Detail them by internal weaknesses and external threats. How can Apple transform internal weaknesses into strengths, and external threats into opportunities?

4. Apply the three-step process for developing a *good strategy* outlined above (diagnose the competitive challenge, derive a guiding policy, and implement a set of coherent actions) to Apple's situation today. Which recommendations would you have for Apple to outperform its competitors in the future? Be specific.

Endnotes

[1] Apple's valuation is in absolute dollars, not in real (inflation-adjusted) dollars. When adjusted for inflation since 1999, Microsoft's record market valuation would be roughly $850 billion in 2015.

[2] This discussion is based on Rumelt, R. (2011)., *Good Strategy, Bad Strategy* (New York: Crown Business).

[3] Ibid, p. 14.

Sources: This MiniCase is based on: "Apple Earnings Surge 33% on iPhone Sales," *The Wall Street Journal*, April 27, 2015; "Apple, feeling heat from Spotify, to offer streaming music service," *The Wall Street Journal*, June 1, 2015; "Apple's share of smartphone industry's profits soars to 92%," *The Wall Street Journal*, July 12, 2015; "Apple's Market Cap Loses $60 Billion After iPhone Sales Disappoint," *The Wall Street Journal*, July 22, 2015; and Sull, D., K.E. Eisenhardt (2015), *Simple Rules: How to Thrive in a Complex World* (New York: Houghton Mifflin Harcourt); "Apple plans web TV service in fall," *The Wall Street Journal*, March 17, 2015; Kane, I.Y. (2014), *Haunted Empire: Apple After Steve Jobs* (New York: HarperCollins); "An iPopping phenomenon," *The Economist*, March 24, 2012; "From pipsqueak to powerhouse," *The Economist*, August 21, 2012; "iRational?" *The Economist*, March 24, 2012; "Apple market value hits record high," *The Wall Street Journal*, August 20, 2012; "GiantApple," *The Economist*, August 21, 2012; Sull, D., and K.E. Eisenhardt (2012), "Simple rules for a complex world," *Harvard Business Review*, September; Isaacson, W. (2011), *Steve Jobs* (New York: Simon & Schuster); and Rumelt, R. (2011), *Good Strategy, Bad Strategy* (New York: Crown Business).