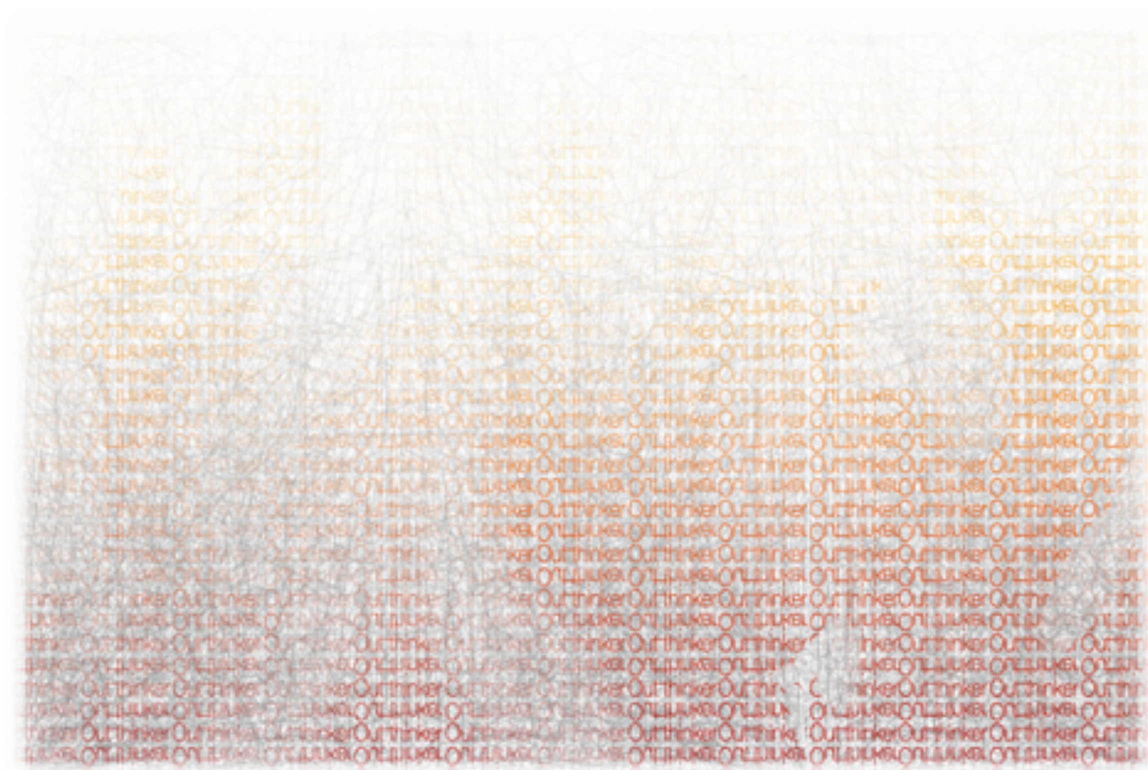
How Outperformers Outthink the Competition

By Kaihan Krippendorff and Nadia Laurinci



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Corporate revolutions

For the past ten years, we have been studying the patterns that lead companies to breakthrough performance. We began by dissecting the strategies of companies like Dell, Southwest Airlines, and Wal-Mart, who over the course of the 1990s radically disrupted their industries, and found some surprising similarities in how these companies engineered breakthrough growth.

Our research showed that the breakthrough companies of the late 1990s and early 2000s shared a unique view of their markets. Because they saw things differently, they acted differently. Because they acted differently, they won. Physicist Thomas Kuhn showed that science does not evolve linearly but rather it periodically undergoes revolutions[i] when paradigms shift. It seemed the turn of the millennium saw the introduction of such a revolution in corporate competition.

We then drilled down further, conducting a rigorous top-down analysis starting with 9,000 publically traded companies from around the world and isolating from these the 100 most competitive companies of the decade. These were 100 companies that for the ten years ending in 2004 consistently outperformed their peers in terms of revenue growth, profit (EBITDA) margin, and shareholder returns. Again, we were struck by the similarities in their approaches. Across industries and geographies, these breakthrough companies adopted surprisingly similar playbooks when engaging their competition.

The insights drawn from this 2004 study proved practical. We began applying our findings systematically, helping companies and executives use the same strategies to unlock new growth. We worked with a range of clients, from leading corporations including Microsoft, Wal-Mart, and Johnson & Johnson to mid-market firms. As we incorporated our experience into refining our model, results amplified. One application of the tool-kit led a group of managers to devise a new partner-engagement strategy that tripled top-line revenue in three years. Another client found several simple ways to capture new opportunities that enabled them to reach their three-year growth target in just 18 months.

Since that 2004 study, **we have trained over 3,000 executives and entrepreneurs**—from across the U.S., Latin America, Europe, and Asia—on how to apply the findings. We have helped numerous investors use the findings to make better-educated decisions about how to put their money to better use. By investing in opportunities aligned with proven growth patterns and adjusting the strategies of existing investments so that they better align as well, we believe investors can achieve superior returns.

A new paradigm shift is underway

Each time we apply the research, we update it, seeking out fresher competitors to learn from. Through this refreshing process, we have noticed that winning strategic patterns have started to shift. What most often led to breakthrough performance in the decade ending 2004 may not be as applicable today.

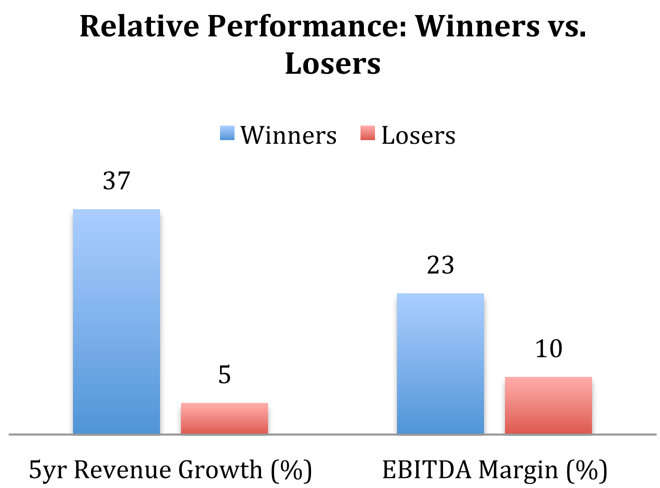
This is surely of no great surprise. The nature of competition has radically changed since 2004. Product life cycles have shortened dramatically, outsourcing has restructured entire business sectors, social media and real-time marketing have become mainstream, and competitors are crossing industry borders faster than ever before. We believe a new paradigm shift is underway. A new crop of business heroes like Apple, Google, and Amazon are displacing once-admired companies like Dell, GE, and Starbucks at an unprecedented rate.

Fortune Magazine's Most Admired Companies		
2000	2005	2010
1. GE 2. Microsoft 3. Dell 4. Cisco 5. Wal-Mart	1. Dell 2. GE 3. Starbucks* 4. Wal-Mart 5. Southwest A.*	1. Apple* 2. Google* 3. Berkshire H.* 4. J&J* 5. Amazon*

* indicates a newcomer to the list

Many well-schooled business strategists argue the success of such companies is unsustainable. Certainly, some of these stars will fall but we believe the inability of traditional analytical tools to satisfactorily explain the success of some of these newcomers should lead us to question our tools, not the quality of their successes. Google's success, for example, cannot be assigned to irrational investor exuberance as some argue. The company has reached $24 billion in annual revenue, generates EBITDA margins in excess of 40%, and has averaged 20% return on equity (ROE) over the past five years. That standard business analysis tools cannot adequately explain this success is a classic indicator that a paradigm shift is underway.

To address the paradigm shift we spent the past six months revisiting our initial analysis. We isolated 20 companies that have delivered extraordinary performance relative to their peers over the past five years to calculate which strategic patterns are working today. These companies—including Apple, Oracle, Research in Motion, and AT&T—produced 40% revenue growth on average over the past five years, seven times that of their peers, and were three times as profitable as their competitors in term of EBITDA margin. See Appendix A for a list of these companies and their comparables.



By comparing these breakthrough companies to their closest peers, using a process called "narrative analysis,"[ii] we were able to dissect how their strategic playbooks differ from those of their peers. In all, we analyzed 686 strategic narratives. By isolating their most significant differences, we were able to gain insight into how today's winners see the world, choose strategies, and win.

We then deepened this core analysis by personally interviewing the CEOs of several breakthrough companies,[1] including the CEOs of AFLAC, Rosetta Stone, and Vistaprint. By asking them to walk us through their strategic logic, we were able to further validate the distinguishing patterns of companies who are thriving in the new paradigm.

The new "outthinker" paradigm

What we found is that the winning strategies today are shifting—that companies who hold on to strategies and perspectives that worked at the end of the 1990s and into the early half of the 2000s, risk being left behind. We specifically concluded that:

1. Traditional sources of competitive advantage are expiring
2. A new playbook is emerging
3. Winners are outthinking their competition.

Traditional sources of competitive advantage are expiring

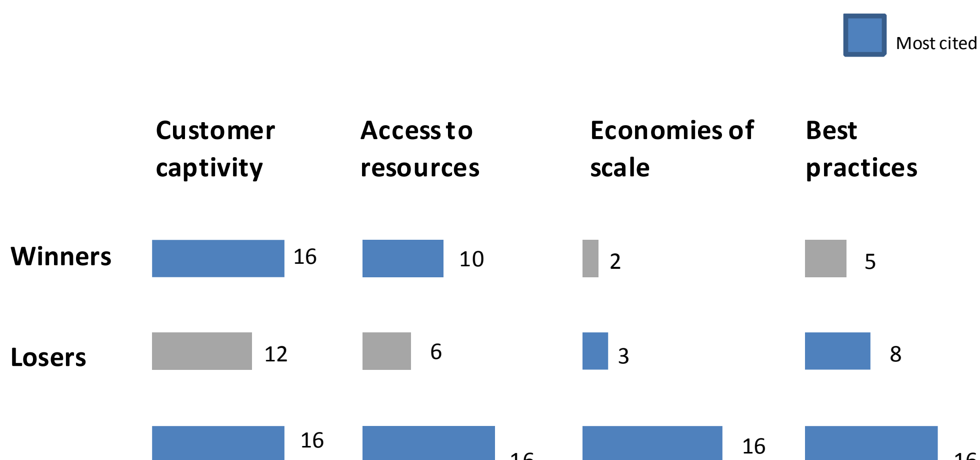
Over the past several decades, companies have primarily built competitive advantage by achieving customer captivity, securing preferential access to

[1] Based on five-year revenue growth and profit margin

resources, building economies of scale, and adopting best practices.[iii] In 2004, we began to see a shift away from these traditional sources of advantage. Today we see this shift accelerating. While today's winners continue to excel at winning customer captivity and preferred access to resources, we actually see two stunning reversals. The winners today actually cite economies of scale and best practices less often than their losing peers.

Given the increasing ease with which smaller companies can "turn on" significant scale (e.g., by outsourcing production and back-office functions) and given the speed with which best practices are now being copied, that these two traditional sources of advantage are expiring is perhaps not surprising. But the implications of this shift are profound for anyone seeking to bet on or grow a firm today.

Frequency with which companies cite traditional sources of advantage
Normalized frequency*



* N = 686 observations

A new playbook is emerging

For the past ten years, we have been working with a specific catalog of 36 strategic narratives. Our CEO has published three books showing the applicability of these strategies to modern business competition.[iv] By analyzing which strategies winning and losing companies utilize most, using this schema of 36 strategies as a tool, we are able provide insight into how each pursues competitive advantage.

We find that today's winners are embracing a radically different approach to building competitive advantage. They are increasingly supplementing traditional sources of competitive advantage with a new set of strategies. They are applying a new playbook.
Three key differences between winners and losers stand out:

1. Winner are more comfortable coordinating outside resources and entities rather than trying to own them

2. Winners create what we call a "two-front battle" by strategically linking unrelated activities and often attacking client needs across multiple industry borders.

3. Winners think longer term about strategic relationships (e.g., with clients and partners), often entering as a guest and gradually establishing a trusted position and power.

Top strategies used by winners and losers

Normalized frequency*

☐ Non-traditional strategies

Top winner strategies

Play	Frequency
Customer captivity	*16*
Access to resources	*10*
Next battleground	**6**
Best practices	*5*
Coordinate uncoordinated	**3**
Two-front battle	**2**
Guest for host	**2**
Economies of scale	*2*

Top loser strategies

Play	Frequency
Customer captivity	*12*
Next battleground	**9**
Best practices	*8*
Access to resources	*7*
Economies of scale	*3*

* N = 686, only included narratives with greater than 10 observations and with frequency greater than 1

Winners are outthinking their competition

We believe these key differences in playbook, and some other strategic plays emerging, point to a broad shift in paradigm. This shift extends beyond the competitive tactics of a few firms. Trying to guess Steve Job's or Sergey Brin's next move is to miss the broader phenomenon underway right now. At its core, it is about relying less on physical, permanent sources of advantage and instead adopting a mindset focused on answering the following key question: **What it is that my competitors will choose not to do or copy even though they can?**

- How was Apple able to reach $65 billion in revenues in an industry dominated by players with far deeper pockets and broader reach? The company has intelligently played on numerous industry dogmas—by, for example, launching a retail store concept or reinventing the "tablet computer"—and thereby preempted competitive response.

- How was Vistaprint able to become the most well-known printing brand among small businesses without a sales force or marketing budget? They owe part of their success to playing on the fact that the printing industry had decided that to be profitable, a printing business had to deliver bulk orders to large customers.

- How was Blue Nile, a newcomer, able to beat Tiffany's, with over a century of experience and expertise, to become the dominant player in online diamond retailing? Because they recognized that Tiffany's wouldn't put their high margin retail business at risk.

Winners recognize that business competition is experiencing a paradigm shift and are stepping firmly onto the winning side of the revolution. They see which parts of the playbook are expiring, understand which plays to add, and capitalize on the tendency of tomorrow's losers to hold on to outdated perspectives. They are winning the mental game of business. They are "outthinkers."

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About the authors

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About Outthinker

Outthinker is a New York City-based business and capital advisory firm that helps companies, investors, and entrepreneurs win by outthinking the competition.

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Appendix A: Companies subject to our study and their peers

Winners	**Losers (Peers)**
Research in Motion	Nokia
Apple	Microsoft
AT&T	Sprint
Oracle	SAP
Aflack	UNUM
Urban Outfitters, Inc.	American Eagle Outfitters
Blue Nile	Tiffany's
Priceline.com Incorporated	Expedia, Inc.
inVentiv Health	PDI
WMS Industries Inc.	International Gaming Technologies
Community Health Systems	Universal Health Services, Inc.
Concur Technologies, Inc.	Ariba, Inc.
Green Mountain Coffee Roasters Inc.	Caribou Coffee Company
VistaPrint NV	Consolidated Graphics, Inc.
Hansen Natural Corporation	Dr. Pepper Snapple Group
Illumina, Inc.	Beckman Coulter, Inc.

[i] See Kuhn, Thomas, "The Structure of Scientific Revolutions" (*International Encyclopedia of Unified Science*, 1961).
[ii] For more in Narrative Analysis, see Riesman, Catherine K. (1993). *Narrative Analysis*. Thousand Oaks, CA: Sage Publications; see Gabriel, Y. 2004. Narratives, stories and texts. In D. Grant, C. Hardy, C. Oswick, & L. Putnam (Eds.) *The Sage Handbook of Organizational Discourse*: 61-77. London: Sage.
[iii] See Greenwald, Bruce, *Competition Demystified* (New York, Penguin Group 2005).
[iv] See Krippendorff, Kaihan, *The Art of Advantage* (Thomson, 2003), *The Art of the Advantage* (Adams Media, 2008), and *The Way of Innovation* (Adams Media, 2008).