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INDUSTRY INSIGHT

Deconstruction of the Value Chain

How will you secure the future of your organisation if your value chain can be dismantled by challengers with the right strategy and the right technology?

Organisations use Digital Transformation as a mechanism to evolve, this is prompted by internal needs or changes in their external environment. As the processing, storage and communications power of technology expands exponentially, the way entire industries operate is also being disrupted. In this article, we will explore how value chains are being eroded and what firms can do to survive.

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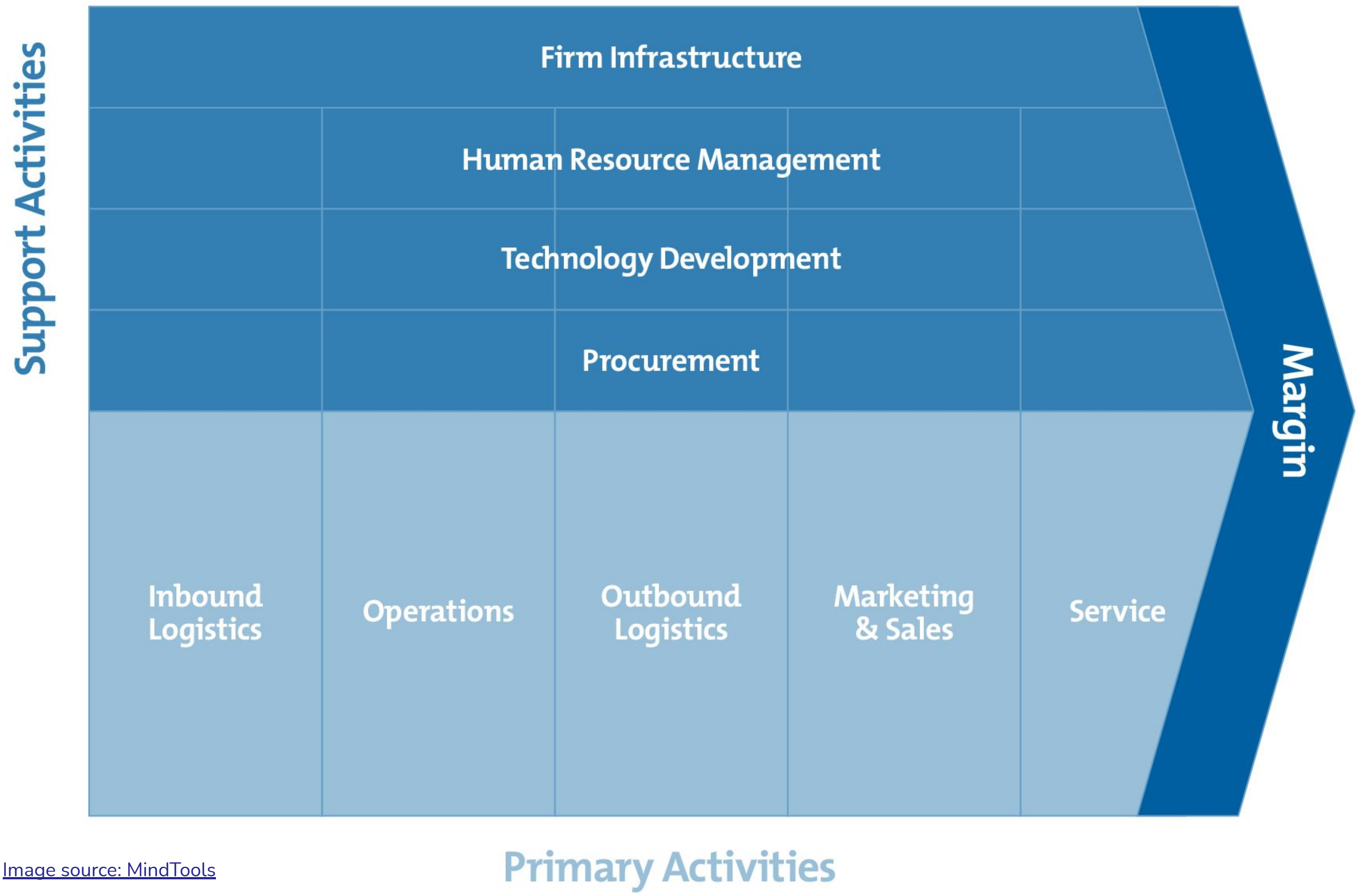
The Value Chain

You may be aware of the value chain; a set of activities that a firm performs to deliver a valuable product or service to the market. The concept was first described by Michael Porter in his 1985 best-seller, Competitive Advantage: Creating and Sustaining Superior Performance.

Due to technological advancements, business architectures have been transforming in recent years, the business architecture explains how industry players are organized to deliver value to end users. These players include competitors, suppliers and players from adjacent industries, how do they interact together and who do they interact with, you may familiar with Porter's 5 Forces model.

A firm's structure, strategy and overall Digital Transformation are influenced by its industry architecture as the firm positions to add value (though great products and services) and capture value (revenues and profitability) relative other players.



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The game has changed

Historically, business architecture was seen as a vertically integrated value chain whereby a succession of players (suppliers, producers, and distributors) transform raw inputs into market-ready products/service, one step at a time. For example, trees are cut, wood is processed into tables and sold to you by your favourite homewares retailer. Firms used vertical integration to control and reduce transaction costs, gain efficiencies and gain competitive advantage via scale and scope of operations.

With advancements in technology and a little help from Moores law, Butters law and Kryders law, cost reductions and efficiencies are achievable by firms who are unable to achieve vertical integration. It has become cheaper and cheaper to store, process, and communicate information digitally. Additionally, new start-ups or challengers with the foresight to reinvent themselves challenged incumbents by attacking specific parts of the value chain rather, essentially deconstructing the value chain.

Transaction costs declined, for example ERP integration allows firms to check inventory levels in their third party distributors while firms could instantly compare prices between suppliers through online auction portals. As a result, links in the vertically integrated value chain became looser. This independence and inter-operability allowed each layer to evolve with its own key success factors. Some layers were scale sensitive and scaled while other layers needed innovation and agility so they fragmented.

For example, In the early-mid 20th century, telephony was offered as an end-to-end service. A single company would wire your home, manufacture handsets and operate the infrastructure. Overtime, customers purchased handsets from other firms and the telephone infrastructure evolved to provide innovation services. With the emergence of the internet, email, social media and messaging apps, customers could communicate even if they did not have a physical landline/wired telephone. Think about the mobile device in your hand, the efforts of several firms (rather than a single vertically integrated one) allowed you to make that call, send that picture or read this great article.

The convergence of technology creates new opportunities for your customers and competitors. These can be opportunities or threats to your organisation depending on how you choose to respond

Darwin was right

As Darwin said, ‘evolve or die’, firms whose value chain is under attack must adapt how they operate and how they add value. Staying with the telephone example, the telephone providers vertically integrated value chain is crumbling but their infrastructure is still vital in the provision of internet services. Opportunities exist to sell customers larger data plans so they can continue to watch NetFlix, listen to Spotify and order products on Amazon.

There are also opportunities to provide additional services such as cloud storage, cybersecurity protection and other software as a service solutions. Rather than seeing the deconstruction of the value chain as a challenge to one's survival, see it as a call to action to reinvent and provide different products/services that could yield greater returns over time.

This deconstructed teleco value chain can be seen as a stack, layered with different players. The bottom of the stack (the fiber wiring infrastructure) required scale and efficiency among a small number of players. However, the top of the stack required innovation from several players providing hardware, software and services to customers that eat up the data provided from the bottom of the stack. In some ways this can be seen as a symbiosis of different players rather than a competitive scenario where one player vies for total control using scale efficiencies rather than market lead innovation.

How will you secure the future of your firm if part or all of your value chain can be dismantled by new/existing challengers?

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Key Takeaways

- Technological evolution has changed how industries operate, moving from the traditional vertically integrated value chain to a stack-based structure seen below.
- The stack structure reflects how players can compete differently; scale is key at the bottom, while innovation and differentiation can bring success at the top.
- Competitive advantage is not sustained by vertically integrating the whole stack as other players can attack a specific level.
- Incumbents need to think like start-ups and reinvent themselves (from within or acquisition) rather than adopting old models of industry domination through vertical integration.

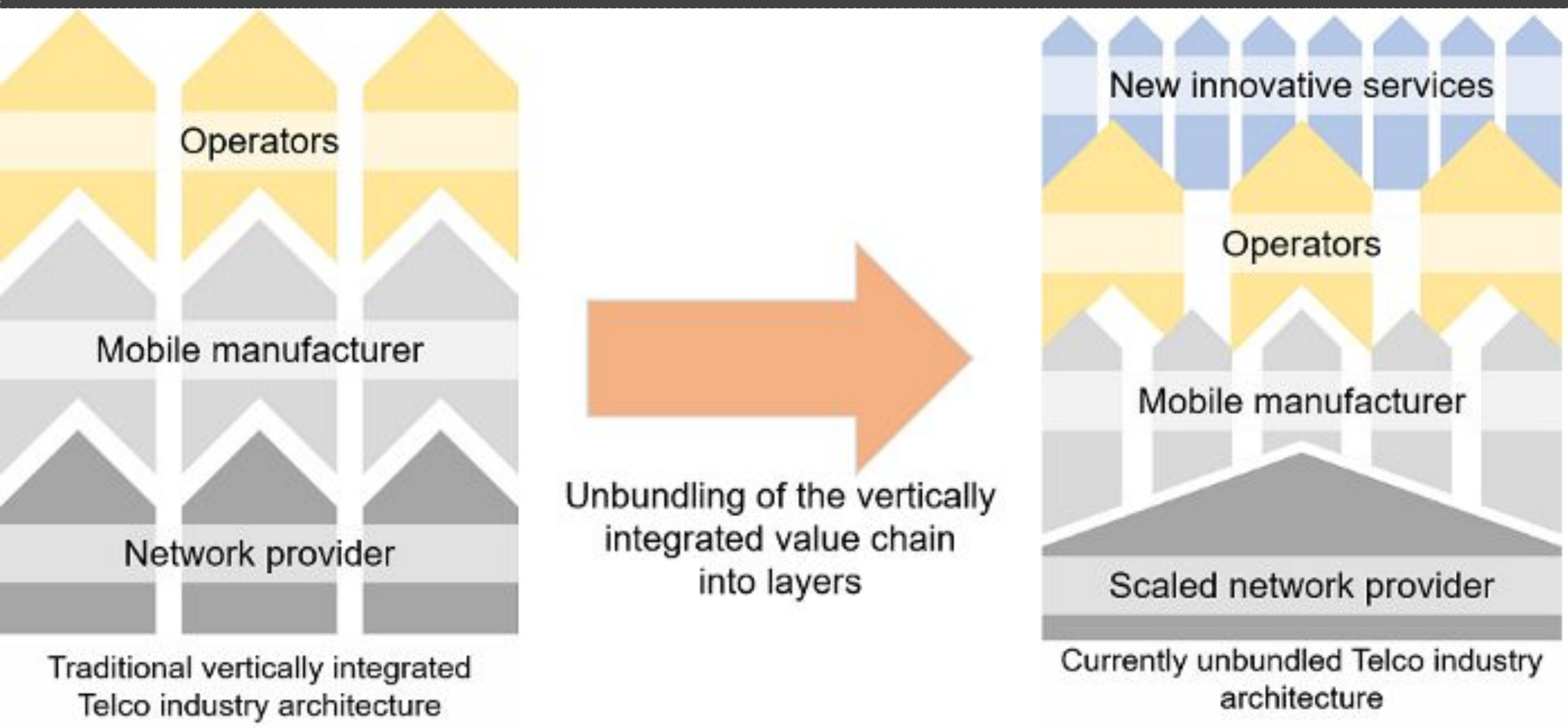

Image Source: Tarabi, N

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Robert is a Digital Transformation & Digital Marketing Lecturer. Robert is available for your webinars, conferences, events & training

With nearly a decades experience, he has worked with Hubspot, Digital Marketing Institute, Irish Times Training and others. He is a judge for several industry awards, he is a regular speaker at conferences and corporate webinars. Robert was even shortlisted for the Net Visionary awards in 2017.

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