# Core Objectives:
## Clarity in Designing Strategy

**Sayan Chatterjee**

There are two components for designing successful strategies: choice and clarity. The starting point for developing business models is to consider the outcomes that customers desire.[1] Focusing on outcomes (such as lack of downtime) instead of the means to deliver it (such as a service network) provides for multiple business models. Before embarking on one of these business models, a firm needs to be very clear about what it *capabilities* are. Without this clarity, the firm risks failure.

### Why Outcomes and Not Customer Needs

These days, most practitioners emphasize the necessity for understanding customer needs. For most managers, this implies traditional market research and the use of focus groups. Firms must rephrase these needs as the outcomes that customers really pay for. Consider the following case where the outcome framework was put into action.[2] The Energizer battery company was considering investing in a major research effort for a longer-lasting hearing aid battery. It assembled a focus group of older people to find out about the size or shape of the battery that would most likely appeal to them. The company's real insight did not come from what the focus group told them, but from observing the process by which the participants went about replacing their batteries. The company realized that it was very difficult for older people to replace a small hearing aid battery. Of course, one solution to the problem was spending research dollars to come up with a battery that was longer-lasting. However, the outcome that hearing aid users really wanted was simply to have a hearing aid with a working

The author would like to thank Vasu Ramanujam as well as seminar participants at the Weatherhead School of Management, the Darden School, and the Wharton School.

battery at any time. Energizer decided to develop a package that made replacing the battery foolproof. Not only did the company save the research dollars, but it was selling more batteries in larger packets. By focusing on outcomes, Energizer reshaped the questions that it asked the focus group from what kind of battery they would like to what was the focus group's main frustration with a hearing aid battery. It is this line of questioning that unearthed the difficulty of replacing the battery.

It is a similar line of questioning that enabled Angiotech to develop the stent (a tube or device used to keep a blood vessel or other body part open) coated with the cancer drug Paclitaxel, which prevents tumor growth and thus prevents scar tissue from developing around the stent (which would lead to invasive replacement procedures). William L. Hunter, the CEO of Angiotech, traced the innovation of the coated stent from the manner in which his company asked doctors about their needs regarding stents.[3] As Dr. Hunter notes: "Medical equipment makers typically ask surgeons, 'How can we build a better stent?' and then get the answer, 'You should make it more flexible, easier to see, and stronger. . . . But we've been asking, 'What does the body do to these stents and why do they fail?' When you ask that, you get to the scar-tissue problem." In other words, Angiotech asked about the outcome, while most companies asked about the product.

## Core Objectives

Focusing on outcomes allows firms not only to develop insight into options for new business models, but also allows them to critically evaluate their current business models before they become vulnerable to competitors who can deliver the same customer outcomes. However, outcomes only provide insight into possibilities for satisfying the customer. In order to earn a profit for shareholders, firms need clarity on what they need to do that will simultaneously deliver the outcome that the customer values as well as capture some of this value for the firm's shareholders. Moreover, firms ideally want to capture more of this value than their competitors. The concept of core objectives is the critical first step in developing this clarity. The concept of core objectives helps *recreate* the process by which strategies are developed and not merely *explain* why a strategy succeeded after-the-fact. Such explanations provide little guidance to other firms and are often superficial.

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Southwest Airlines developed a strategy using a methodology similar to the core objective concept. After-the-fact explanations of Southwest's strategy, most notably the activity map used by Porter,[4] do not capture this. The core objective approach also provides clarity about why other airlines failed to imitate Southwest's strategy. Continental's CALite demonstrates this point, and explanations such as straddling[5] that have been offered to explain Continental's failure miss the point. Similar straddling strategies (simultaneously cost cutting and

differentiation[6]) are actually being used by JetBlue Airlines quite successfully. Once again, JetBlue's success is much better understood using the core objective concept, as the company used a similar framework to develop its strategy. The core objective concept allows for recreating a successful strategy even if it was developed serendipitously or in an ad hoc fashion.[7]

## Outcome to Objective

A study by Hackett Benchmarking compared the planning and control practices of world-class companies with non-world-class companies. It found that the average company has 372 line items at the level of budget detail while the world-class company has 21. The process of identifying the few core objectives that drive a top firm's competitive advantage is not easy, but it puts the firm in a much better position to manage the risks of failure than the average company. As a result, the firm does not suffer from information overload, which facilitates better control and communication. Furthermore, focusing resources on the most mission-critical objectives avoids wasted effort and misallocated resources. If something is not performing up to par, it is much easier to spot it from amongst 21 items than 372. However, to cull a large laundry list of objectives down to a handful of critical ones requires the utmost possible clarity as to how your business model is supposed to work. There are two steps to this process. First, the firm must identify the high-level competitive objectives that capture the basic competitive logic of its business model and then, second, develop a more focused set of core objectives that can be calibrated and tracked in real-time.

### *Step 1: Identify Broad Competitive Objectives*

The broad competitive objectives should clearly state how the firm will deliver the outcomes that its customers desire. These broad competitive objectives should also clearly state how the firm can simultaneously capture part of the value for its shareholders.

#### *Competitive Objectives Must Deliver the Core Customer Outcomes*

In analyzing customer outcomes, it is important to note not just the outcomes that customers seek out, but also the ones they *do not care about*.

Southwest has been profitable for decades in an industry where the majors are barely getting by. Southwest flies short hops (on average 375 miles) between city pairs even though it is cheaper to fly longer routes. Whenever possible, Southwest flies out of secondary airports that have easy access to a large metropolitan area, such as Dallas's Love Field (where the company started), Chicago's Midway, and Detroit's City Airport. Southwest fought back many court challenges to remain at Dallas Love Field, which was right next to downtown, and not move to the new Dallas-Fort Worth (DFW) airport. Southwest typically has evenly spaced (usually hourly) flights between a city pair throughout the day as opposed to the morning and evening concentrations favored by

the major hub and spoke airlines. Southwest offers no meals and one class of service with no assigned seats. Southwest encourages direct booking with Southwest's own ticket agents, as the company does not pay commissions to travel agents. Finally, Southwest usually has the lowest fares between a city pairs and does not require a Saturday night stay.

Even though Southwest probably attracts more leisure travelers at present, it initially focused on attracting business travelers who would normally drive or take a bus between Dallas, Houston, and San Antonio. Unlike traditional business passengers who would like to have the flexibility of complicated schedules (and are willing to pay for it), Southwest's passengers are looking for low-prices, on-time arrivals, and the ability to fly whenever they choose between a city pair. Clearly, Southwest's fares and schedules accommodate these outcomes. To underscore Southwest's awareness of *its* customer outcomes, consider the decision to stay on at Love Field despite the pressure from American Airlines and the court battles. If Southwest moved to DFW it would mean that the Dallas business person will have to add at least an hour or more for her commute each way, which reduces the attractiveness of flying as opposed to driving. This was one of the key considerations that drove Southwest's dogged fight to stay on at Love Field.

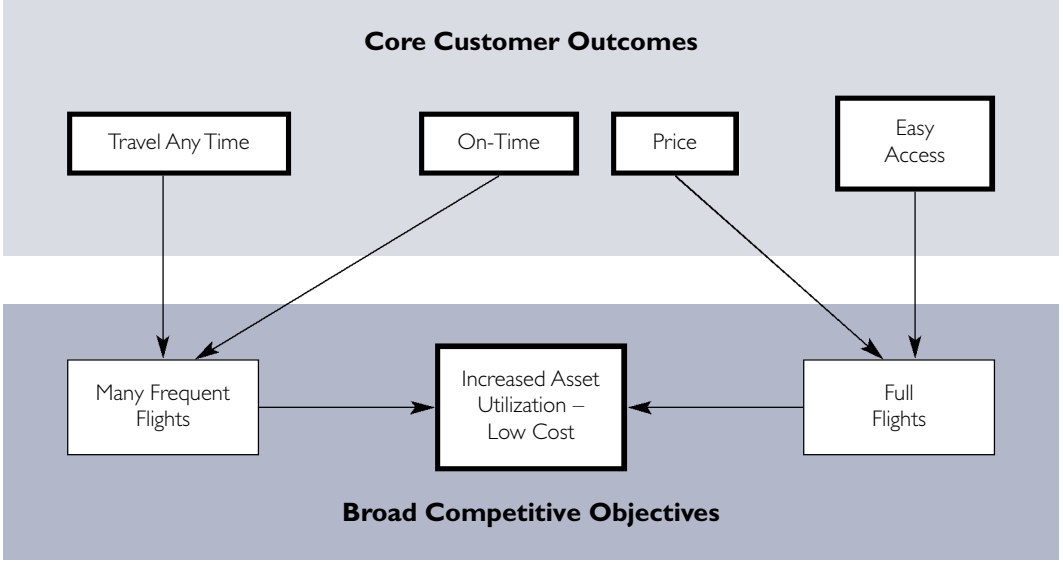
There are several outcomes that Southwest's passengers do not care about. Since they are not looking for a complicated schedule, luggage check-in is not as high a priority for them as it is for traditional business fliers. In the same way, given the short duration of the flight, food service is also not critical. Further, there is probably no need for different classes of service. Finally, consider the fact that there are no assigned seats. What this means is that if a traveler wants a seat in the front of the plane, or to avoid a middle seat, he needs to show up early. For the leisure passenger this is not that much of a problem. For the business passenger the inconvenience of a middle seat is mitigated by the fact that she is traveling when she wants and the flight is short enough to make a poor seat bearable.

*Competitive Objectives Must Capture Some of the Value Customers Pay For*

Obviously, in order to deliver the low price, Southwest has to have a low-cost structure. One way for Southwest to have a low-cost structure is to have higher asset utilization levels than other airlines.[8] Higher asset utilization by itself is not specific to Southwest; all airlines and indeed all companies strive to do this. Most conventional analysis of Southwest's success focuses on its full and frequent flights. The conventional argument is that if Southwest can beat other airlines on these objectives—have more flights between two points as well as fuller flights—it will have a lower-cost structure than other airlines as well as be able to deliver the outcomes that Southwest's customers desire (as noted above). The conventional explanation is described in Figure 1.

The conventional explanations are analogous to "broad competitive objectives." However, while important, identifying the broad competitive objectives is not enough to anticipate the risks of failure. At such a high level of

**FIGURE 1.** The Key to Southwest's Success: The Conventional Explanations




abstraction, these objectives will not provide much insight about the capabilities needed to consistently deliver on these objectives. Capabilities are the main engine of the business model. High-level objectives such as those indicated in Figure 1 do not allow for tracking the performance of a business model in real-time. The components of the broad competitive objectives need to be identified with a degree of specificity that precisely captures what the firm's competitive advantage is. Further, the components must be defined such that their output can be measured in real time, and not ex-post. At the end of this process is the identification of the "core competitive objectives." These core objectives are specific to the business and precisely measurable.

### *Step 2: Identify the Core Competitive Objectives*

*Core Objectives Must Be Leading or Contemporaneous Indicators*

A few years into its operations, Southwest was facing bankruptcy. The very frequency of flights that is heralded these days as Southwest's distinct competitive advantage was bleeding the company dry. This is because Southwest had purchased four planes to offer the frequent flights in order to attract the business passengers. Unfortunately, the notion of substituting planes for cars had not yet caught on and Southwest was facing frequently empty flights. This is of course the flip side of operating leverage that full and frequent flights can benefit from. It is at this point that Southwest identified the kernel of its business model. In order to survive, Southwest had to return one of the four planes that it had purchased from Boeing. However, founder Herb Kelleher was unwilling to

compromise on the frequency of flights that he was convinced was the outcome that other airlines were not providing. Herb got all his employees together and tasked them with this simple problem. How to deliver a four-plane schedule with only three planes? Southwest's solution: focus on minimizing ground time. Moreover, as Southwest would have no margin for error, it had to know on a flight-by-flight basis if anything was not working as designed. This led to the industry-first gate turnaround of 10 minutes. *Everything that Southwest does feeds into delivering this turnaround time*.

Basically, core objectives force a firm to track the few things it must do exceptionally well to succeed. If a firm is hitting the targets set by properly specified core objectives, then it is very likely that it is enjoying the expected returns while managing the risks of failure. Most businesses feel that they already have core objectives. However, when asked what these are, they come back with broad metrics such as return on investments (ROI), market share, or profit margins. *These broad metrics are practically useless in tracking the true risks of the business.* Why? Because these broad measures are at best symptoms of what has already happened within the company—these are *lagging* indicators. The measurement of core objectives must be precise and must use a system of metrics that will unambiguously alert the firm if the business model is working or not working *before* it shows up in broader measures such as profitability. The metric for a core objective has to get the pulse of the business at a glance in real-time. Using this criterion the frequent flights and full flights are not sufficient for Southwest to manage the risks of its business in real time. In order to do this, Southwest has to dig into the processes that allow it to achieve the frequent flights.

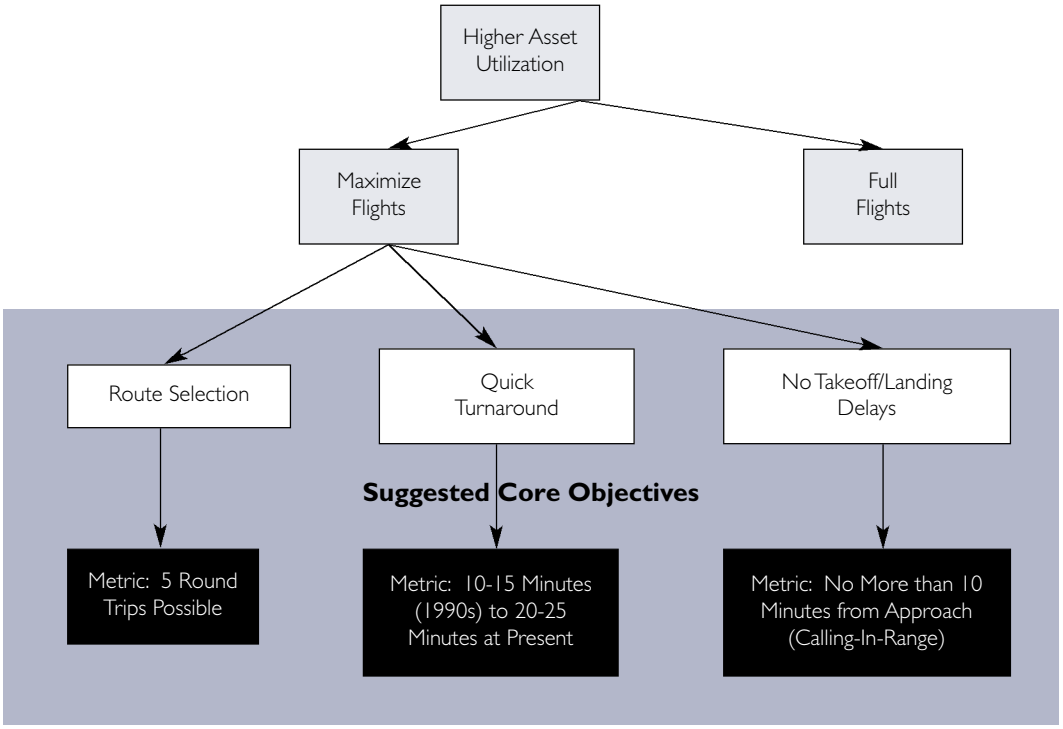
### *Core Objectives Must Be Specific and Measurable*

Consider all the factors that might lead to a flight taking longer than usual. Broadly this can be broken down into delays at the gate, delays in takeoff and landing, and the actual flight itself. The actual flight itself is a function of the aircraft and the weather that is unlikely to be any different from one airline to the next. Southwest, therefore, has focused on minimizing the other two factors. This leads to much more precise objectives that can be observed in *real time* leading to corrective actions if a negative deviation is observed. As described in Figure 2, maximizing flights can be achieved by this set of three specific and measurable core objectives. These are proper route selection, quick turnaround at the gate, and no takeoff or landing delays. Suggested metrics for each of these components are also included in the figure.[9]

### *Core Objectives Provide a Shared Framework for Making Trade-Offs in Business Decisions*

As Porter correctly pointed out all, successful strategies require trade-offs.[10] However, Porter does not provide a framework regarding which trade-offs to make. If you have identified core objectives for your business, then these trade-offs would be almost trivial to make.

**FIGURE 2.** Identifying Specific and Measurable Core Objectives




Southwest uses only Boeing 737 aircraft and keeps them in service longer than most major airlines. Unlike most traditional airlines, Southwest services its planes through its in-house maintenance facility. Southwest is fanatic about maintenance and its mechanics may be the best in the world with the Boeing 737. In fact, once Boeing had to rely on Southwest mechanics to show them an easy way of disassembling the tail section to respond to a FAA mandate. As a result, most Southwest planes rarely fly with a MEL (minimum equipment list; the number of items, such as broken headlamps, that a plane can fly with without violating FAA regulations) of more than 2 or 3, while other airlines sometimes can have close to the limit (15 according to one pilot) allowed by the FAA.

The in-house maintenance facility may not be as cost-effective as outsourcing maintenance, but because of the core objective of quick turnaround the trade-off is clear to everyone. Given the single-minded focus on quick turnaround as the core objective, it is actually more risky for Southwest to try to save money by outsourcing maintenance (or taking a chance on flying with a long MEL that many airlines would do to economize on maintenance) as then it loses control over the immediate *availability of a plane*—a critical activity for delivering the company's core objective. Of course, the availability of the plane will only make sense if all planes are identical. Having a single type of aircraft

(Boeing 737) allows a seamless transfer of passengers in case there is a maintenance problem with a particular airplane. The fact that having only 737s can lead to efficiency in maintenance is an added benefit but is not the main reason for making this choice. Standardizing the boarding process is.[11] Southwest recently made a decision regarding the purchase of a longer (stretch) version of the 737 and chose not to buy the longest version because it would require an additional flight attendant and would disrupt the company's standardized and simplified boarding process.[12] Likewise, having only one type of plane implies that there is always a replacement pilot available to fly the plane. However, the fact that having a single type of plane reduces training costs is incidental and good but not the *primary* reason for this decision.[13] Finally, through in-house simulations, Southwest reached the conclusion that assigned seat numbers lead to increased boarding time. Of course, this is a trade-off because most passengers are conditioned to have assigned seat in most airlines. However, without identifying core objectives a firm is more likely to make the *wrong* trade-offs.[14] The process of mapping out these activities and resources is described in Figure 3.[15]

### *Core Objectives Unify the Organization to a Common Goal*

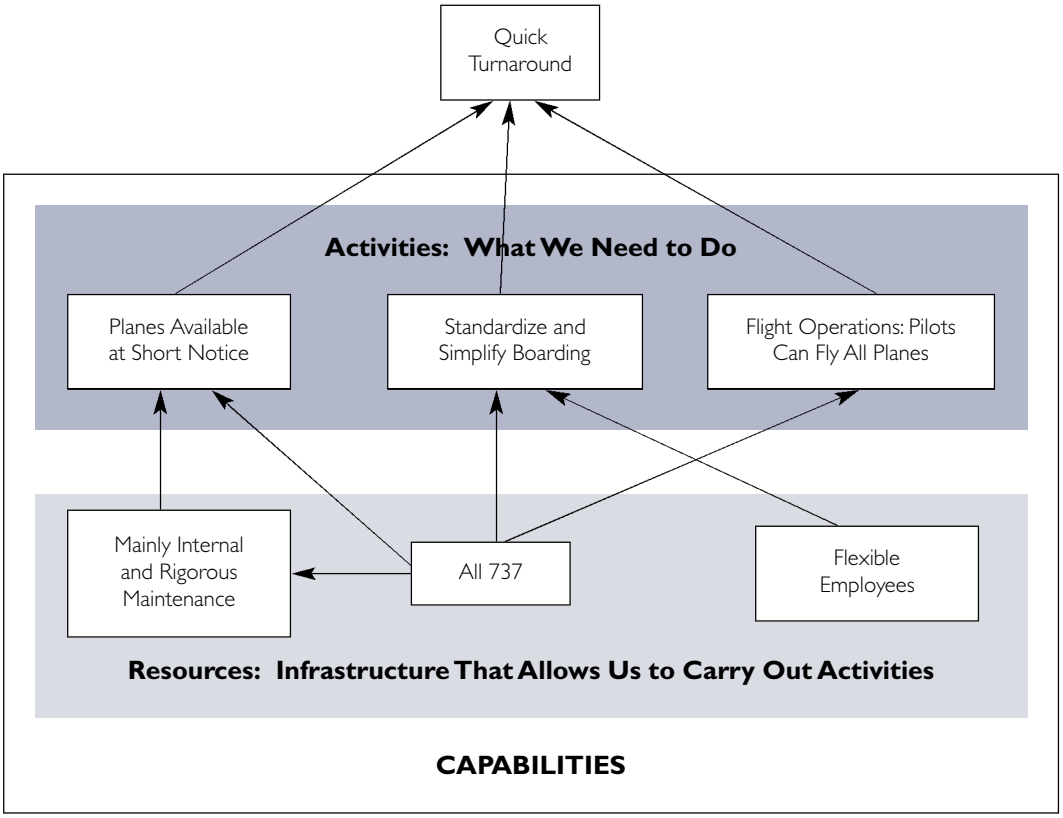
From the moment a plane gets within calling-in-range to the time the plane arrives at the gate, every single Southwest employee knows the role he or she has to play to ensure that the plane leaves the gate within the allotted time. Moreover, if a plane is late, the turnaround time is shortened so that the plane can takeoff on time. If for any reason the turnaround time is not met, a written explanation has to be offered. Much has been written about Southwest's corporate culture that allows everyone to pitch in wherever needed. However, in order to take advantage of the culture, Southwest's employees need to have complete clarity about their roles. Using the core objective lens, the wisdom of the other decisions that Southwest has made begins to become crystal clear to the rank and file.

Without a shared framework (as illustrated in Figure 3), it is extremely difficult for employees to precisely understand their roles in making the company's operations function smoothly. This shared understanding reduces the risk of failure in three important ways. First, the employee knows exactly what he or she has to do. Second, the employee does not feel like a cog in the wheel but an important component of the business—execution risk is much lower with a motivated employee. Third, this shared framework allows the employee to experiment within the bounds set by the core objectives and helps expand the value frontier. This experimentation is possible because the employee knows that the core objectives should drive the trade-offs. The whole process can be captured in what I call "the COAR Model" (Figure 4).

### *The Risks of Not Having a Proper Core Objective*

The risks of not having clarity regarding the core objectives of the company are evident in the case of how Continental tried to copy Southwest.[16] Continental was the first of the major airlines that tried to copy Southwest's

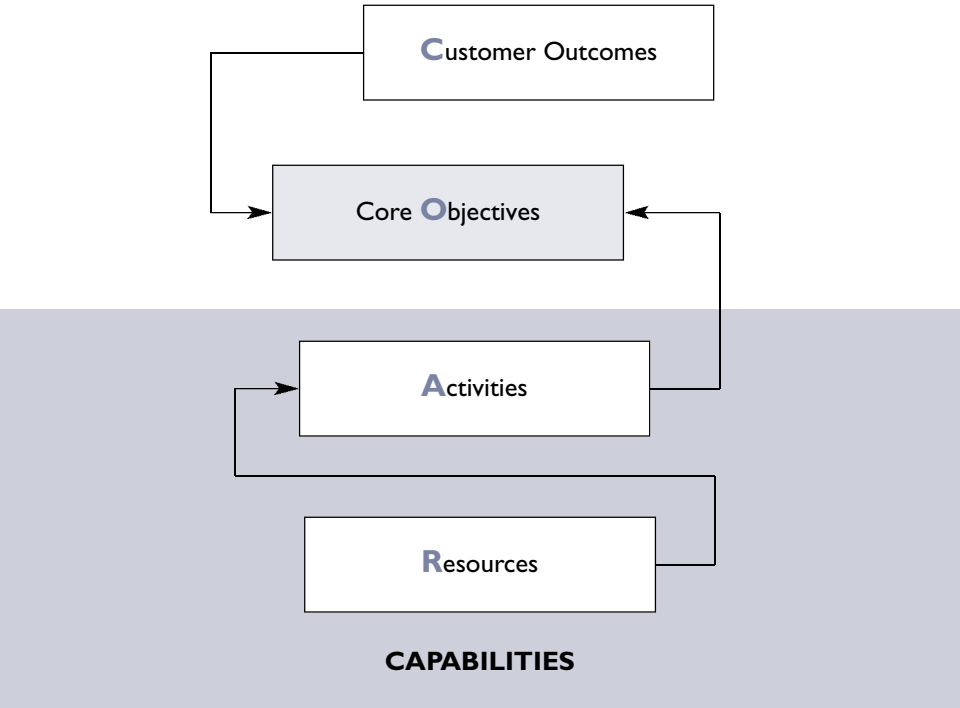
**FIGURE 3.** Capabilities: Activities and Resources Needed to Deliver the Core Objectives




point-to-point low-cost strategy. At that time, Continental had the lowest labor costs amongst the major carriers. Continental felt that it could leverage its low labor cost into a low-priced Southwest imitation in the Southeastern U.S., which had the dual advantage of being a large market with a weak competitor in money-losing USAir. Continental named its newest service CALite.

The impetus for this strategy came from Continental's desire to get out of its money-losing Denver hub and culminated in moving nearly 80 planes and 200 plus flights from Denver to the Southeast in less than nine months. However, once the strategy was explained to the top management, there was considerable doubt amongst the operations people. Instead of sorting through this disagreement, CEO Robert Ferguson fired the airline's president and chief operating officer Lewis Jordan within a few months of the move. Further, Donald Valentine, a Southwest marketing executive with not much operational experience, was hired as the chief marketing officer. Valentine, of course, was aware of the broad competitive objectives of Southwest—frequency and full flights—and was instrumental in making Continental believe that it had found the secret to matching Southwest.

**FIGURE 4.** The COAR Model




Unfortunately, Continental had only a superficial understanding of the Southwest model. For example, Continental did not understand the difference between secondary airports that are close to large cities and smaller airports with not much demand. Thus, Greenville/Spartanburg, S.C. got 17 daily jet flights and Dayton, Ohio, a hub abandoned by other carriers for lack of demand, got 20 extra flights. Further, Continental used its fleet of jets to replace smaller airplanes on routes that simply could not absorb the extra capacity. Basically, Continental did not identify route selection as a core objective.

Likewise, as a result of not understanding the core objective of quick turnaround, Continental failed to get the kind of utilization from its airplanes that led to Southwest's low-cost structures. For example, Continental was unable to replace a canceled flight with another plane because Continental had 16 different types of planes. Further, Continental's maintenance staff did not have the in-depth expertise of Southwest maintenance staff because Continental's maintenance had to understand the mechanical problems and spare parts requirements of those 16 different types of airplane. Further, Continental had its maintenance facilities in its main hubs (for efficiency reasons, which was the *wrong* trade-off) as opposed to Southwest's localized maintenance. Continental also did not keep an inventory of spare parts in its new Greensboro hub. Thus, any maintenance related problems that happened at an airport without a

major maintenance facility had a domino effect leading to delays all through the system. These delays and flight cancellations led to frustrations on the part of passengers and deteriorating employee morale. Continental *simply could not deliver the quick turns* needed to replicate the Southwest model. The largest asset for an airline is its fleet. Any airline that can sell more seats (at the same ticket price) with fewer planes will always win. All the other reasons commonly cited for Continental's failure simply misses this basic point. Oblivious to all of these problems, Continental increased its daily flights to 875 to pursue its goal of frequent flights. This is a classic illustration of focusing on the conventionally accepted broad competitive objectives without understanding the core objective.

Very soon, the losses started mounting and Continental took desperate steps to cut operating costs, such as stopping meals on shorter flights and reneging on its commitment to give credit for its frequent-flyer program to CALite passengers. Travel agents' commissions were cut and overrides ended. In April 1995, CALite was phased out.

Similarly, e-commerce firms such as Value America and eToys failed because they did not clearly identify the core objectives of their business models that they expected would turn the tables on their competitors. Value America's vision was that customers could order anything they want, in any quantity they want, any time they want. Clearly, this is an outcome that customers always desire but can rarely attain through conventional retail channels. For conventional retail channels, the inventory costs would be prohibitive to offer this degree of flexibility to customers. Value America came up with a business model with zero inventory by outsourcing the fulfillment and returns. "It would pick up orders from consumers and immediately transmit them to manufacturers who would ship IBM computers and Knorr soups, Panasonic televisions, and Vicks VapoRub, direct to customers. It featured more than 1,000 brand names, many in multimedia presentations online."[17] In reality, Value America did not set up the communication infrastructure before opening for business. The result was that many orders were transmitted to vendors by fax or e-mail. Further, Value America was totally dependent on vendors for fulfillment but it had no vetting process to make sure that the vendors had the capability to ship single items on time. A core objective for Value America should have been to monitor the vendor's ability to ship items in small quantities and not in pallets. Its vendors needed "pick and pack" capability. Unfortunately, P&G was incapable of shipping a single box of Tide or a bottle of Advil. The end result of all of this was that products were not shipped properly, or on time, computers crashed, and orders took forever to get filled. When Value America came online, just about every retailer from Office Depot to Wal-Mart was concerned. Surprisingly, very few of these conventional retailers tried to imitate Value America in any major fashion. Clearly, Value America had avoided competitive risks. However, it did not anticipate the risks in executing its business model.

Improper core objectives may also have contributed to Ford's trials and tribulations with the Explorer and its Firestone tire problems. Ford chose ride quality and noise and vibration levels as the core objectives when sourcing the

tires for the Ford Explorer. However, if Ford had used avoiding the likelihood of rollover as a core objective (with safety being the broad competitive objective), then it might have been able to avoid the Firestone-related disaster. To accommodate Ford, Firestone compromised on the recommended tire pressures to improve ride quality.

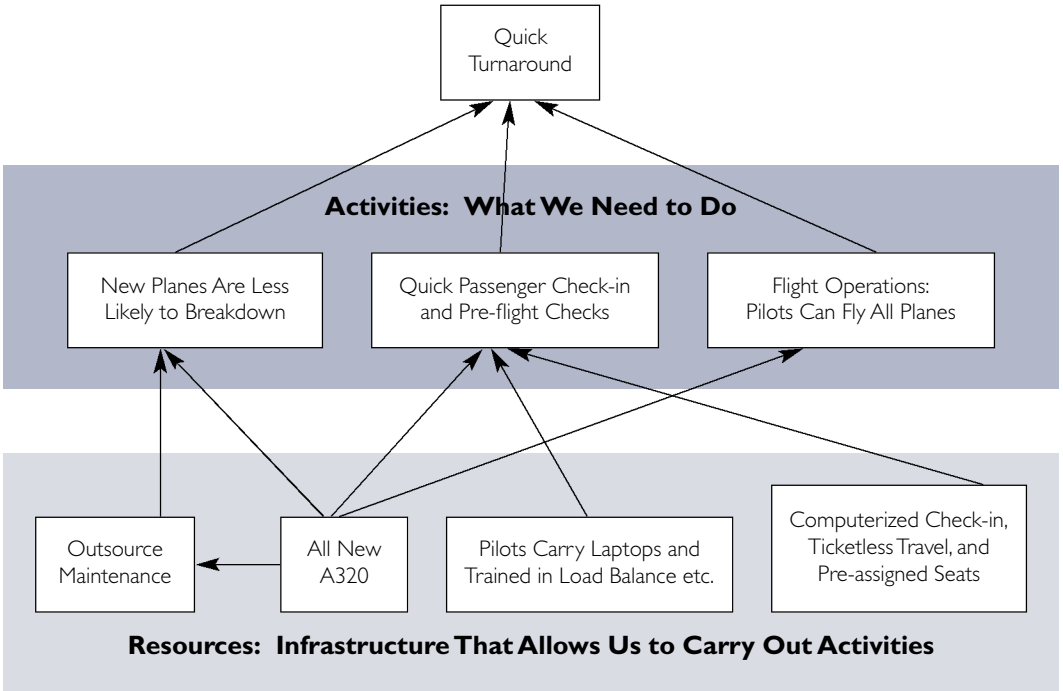
Like Value America, Amazon.com also started with a zero inventory model. However, it focused on books and CDs and did not try to become the Wal-Mart of the Internet—at least initially. Moreover, Amazon made a very critical decision very early. Amazon moved to Seattle to be close to its primary distributor Ingram who would be handling the company's drop shipments. In other words, Amazon correctly identified near-perfect fulfillment as a core objective and developed a business model around being able to monitor this function. Amazon's business model reduced the risk of competitors copying its strategy, but it also executed its strategy without great risks of failure. Amazon did so because of the clarity it had in its core objectives.

*Using Core Objectives to Outwit the Game Changer*

While clarity in core objectives has enabled a firm such as Southwest to change the game on existing players, the same principles can be applied by a new entrant to turn the tables on Southwest. It is not imperative that a new entrant copy the strategies of the incumbent exactly, but it is imperative to have an alternate configuration of core objectives that can deliver the outcomes desired by the customer.

JetBlue commenced operations on February 11, 2000, with two planes out of John F. Kennedy Airport in New York City. Within one year of operations, JetBlue was voted #2 Domestic Airline in the 2001 Zagat survey and posted a profit of $38.5 million in less than two years of operation. All JetBlue pilots are provided with laptop computers to calculate the load and balance of their planes before take-off, eliminating the dependence on dispatchers to crunch the numbers for them (as with other major carriers). This shaves off 15 minutes from their ground time. Ticket reservation is done electronically through its web site or through its reservation agents, who work out of their homes. No paper tickets are issued (all travel is ticketless), all fares are one-way, no Saturday stay is required, and all seats are pre-assigned. It offers only one class of seats and passengers can check-in through electronic touch screens located at flight counters and luggage is tagged electronically. JetBlue has a policy of not over-booking its flights and passengers are encouraged to book tickets in advance as seats are limited. A discount of $5 is awarded for booking tickets online, as a move to promote online ticket reservation. As a result, 63% of the tickets were booked online in 2002, which is also JetBlue's cheapest form of distribution. The ticketless travel system saves paper costs, postage, employee time, and back-office processing expense. Its registration agents work from home using a VoIP line exclusively maintained by JetBlue for ticket reservations. All this contributes to the company's industry-wide lowest CASM (cost per available seat mile) of $6.43.

**FIGURE 5.** How Clarity in Core Objectives Can Allow You to Modify Capabilities




JetBlue currently has 42 technologically advanced Airbus A320s in operation and new aircraft are being added to the fleet at the rate of one every week. These aircraft are also the quietest and most fuel-efficient jets in air. The greater reliability of the new aircraft allows JetBlue to schedule them to fly more hours each day and achieve higher capacity utilization. It also operates a number of "red-eye" flights, which enables a portion of its fleet to remain productive through the night. To avoid weather-related congestion in the Northeast, aircraft are equipped with life rafts, life vests, and high-frequency radios to enable flying farther out over the Atlantic ocean between New York and Florida, thus maintaining on-time performance and completion factors.

JetBlue's strategy is basically similar to that of Southwest in terms of the broad competitive objectives. However, it is different in many of the capabilities needed to deliver the core objective of quick turnaround. JetBlue relies on information technology rather than the flexibility of its workforce (see Figure 5). JetBlue uses brand-new airplanes, which require much less maintenance thus reducing delays due to breakdown—and they can be run for longer hours and are more fuel-efficient. Further, because of its computerized check-in procedure and pre-assigned seats, there is hardly any gate delay for JetBlue's passengers.

Finally, the differentiating features that JetBlue offers actually reduce its profit margin. The A320 has a wider cabin than the Boeing 757 and 737 and

each aircraft is designed to carry 162 passengers in a single class equipped with wide leather seats and live satellite TV at every seat (the first and only airline to offer this service). Some of the other ways that JetBlue differentiates itself from Southwest (and other major airlines) are: more leg room with a 32-inch pitch between rows; change fees of only $25 per passenger (compared to $100 charged by majors); in-flight yoga program to relieve stress; free snacks and drinks provided to delayed customers; self-service kiosks (currently installed at JFK, Oakland, and Ft. Lauderdale); and the CEO works as a flights attendant once a month.

JetBlue is offering features that are very visible and appreciated by its customers, who are quite different than Southwest's. Moreover, the bulk of the cost-savings come from utilizing its most expensive assets—its fleet of aircraft. The expense incurred in offering the visible differentiation has a negligible impact on JetBlue's profits but has a tremendous impact on customer loyalty. JetBlue knows the trade-offs as well as Southwest. If anything, JetBlue improved on the Southwest business model by focusing on its customers' desired outcomes and core objectives. JetBlue also had the luxury of starting with a blank sheet.

*Applying the Core Objectives Model*

The core objective concept can be used by any company to develop better clarity about its strategy and avoid unnecessary risks. Republic Gypsum (based in Dallas, Texas) had 2% of the U.S. wallboard market, compared to U.S. Gypsum with 37% and National with 27%. Yet it had thrived for over 30 years despite periodic recession-induced price wars that decimated the industry's profits. Like most plants in the industry, Republic's plant in Duke, Oklahoma, was located close to a gypsum deposit. From this location, Republic shipped to Dallas and Oklahoma City with good margins despite the freight. When housing and commercial building construction slowed, Republic expanded to cities such as Houston and San Antonio. All in all, Republic kept its plant running at 94% capacity, versus 70% for the rest of the industry.

Freight constituted the largest portion of the cost in the wallboard business. To ship the wallboard to San Antonio or Houston cost $39 a ton, compared to the cost of Gypsum at $4 a ton. Republic found a way to offset the shipping cost by integrating forward into shipping with its own trucking fleet. However, Republic's trucking operation was no more efficient than the contract carriers used by the large competitors. In fact, it cost Republic a bit more to ship to Dallas using its own fleet than what it cost National using a contract carrier. Therefore, in order to justify expanding the selling radius to Houston (during the construction slowdowns), Republic had to offset the cost of the trip back from Houston to Dallas. Republic did this by shipping asphalt shingles and steel from Houston for a wholesale building supplies outfit that Republic operated in Dallas. The trucks were, therefore, filled for most of the backhaul north to Oklahoma. The wholesale building supply company only broke even, but it paid for the freight cost between Dallas and Houston or San Antonio.

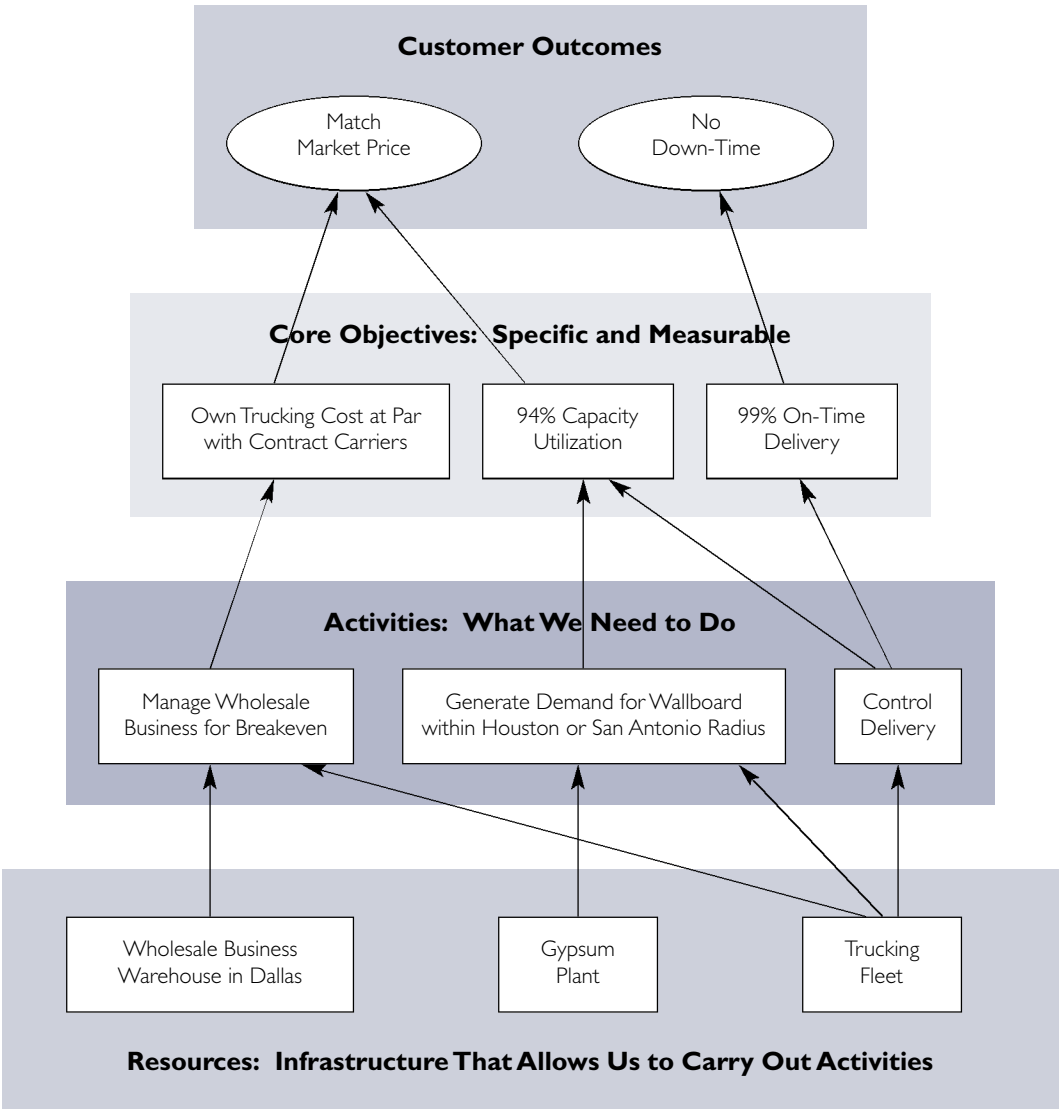
Republic's profitable run in a commodity business earned it a place in the top 100 small businesses. Throughout its 30-year existence, Republic focused on modifying and tweaking the Duke plant in lieu of adding capacity elsewhere. However, in 1999 it increased its capital spending significantly to build a new plant in Lawton, Oklahoma. Using the core objective framework, the capacity expansion decision by Republic can be evaluated by clearly identifying two things: how the firm is delivering the customer outcomes and how it can capture more of the value compared to its competitors. Although freight is the largest part of the cost in the wallboard business, it is simply table stakes for Republic. Where Republic can beat its major competitors is in its capacity utilization—this is its competitive advantage. Given the organizational constraints of the big players, they would have to concede this advantage anywhere in the country. So long as Republic can generate the 20% capacity utilization advantage, it can concede pennies in the freight costs and still match the market price while making a profit. Like Southwest's in-house maintenance strategy, Republic's in-house trucking is critical *not for cutting costs* but for keeping its asset utilization higher than the competition's. Republic's COAR model is described in Figure 6.

There were several growth options that Republic could consider that leveraged its unique competitive advantage. Building a plant close to its existing plant would take advantage of synergies. Alternately, it could clone its Duke plant in a different part of the country where the major players would face similar constraints. By building a plant close to its existing facilities, Republic ran into the same constraints as the big players. Republic had assured sales of 50% of its new capacity. However, for the balance it would have to create the demand from the same market that it was currently selling to. By July 2000, Republic found that the new plant could only operate at 60% capacity and it hired J.P. Morgan to investigate opportunities to sell the company.

## Concluding Comments

In order to develop clarity about a business model, a firm needs to develop metrics to track its competitive advantage in real-time. Unfortunately, most companies' control systems actually hinder instead of help because they try to track everything. The most successful companies are able to focus on a few critical items because they *control what they must, not what they can.* The core objectives of the best companies guide them to the few metrics that will give them immediate feedback on how they are doing. They reduce the amount of time—and the number of intermediaries—between measurement and action. Southwest is immediately aware when a plane is on the ground longer than twenty-five minutes. Dell Computer is immediately aware when a computer has taken more than four days to be ready for shipping. Thus, control systems should be set up to monitor core objectives at all levels in the organization.

**FIGURE 6.** Republic Gypsum COAR Model




## Notes

1. Sayan Chatterjee, "Delivering Desired Outcomes Efficiently: The Creative Key to Competitive Strategy," 40/2 (Winter 1998): 78-95.
2. The material in this article extends concepts developed by Sayan Chatterjee in *Failsafe Strategies* (Upper Saddle River, NJ: Wharton School Publishing, 2004).
3. Carol Hymowitz, "The Best Innovations Are Those That Come From Smart Questions." *The Wall Street Journal*, April 13, 2004, p. B1.
4. Michael E. Porter, "What is Strategy?" *Harvard Business Review*, 74/6 (November/December 1996): 61-78.

5. Ibid. Porter uses the term "straddle" to identify a strategy that is simultaneously one of low cost and of differentiation. To quote directly from Porter's article, "while maintaining its position as a full-service airline, Continental also set out the match Southwest on a number of point-to-point routes. . . . It eliminated meals and first-class service, increased departure frequency, lowered fares, and *shortened turnaround time at the gate*."[emphasis added] Continental did not fail because it also maintained its identity as a full-service airline but because it failed to do what Porter claims it did. It *failed* to shorten the turnaround time—the core objective of Southwest. In fact, it was precisely this failure to understand the core objective that doomed Continental.
6. JetBlue offers many more differentiating features than Southwest and yet it has been extremely successful because it can deliver the core objective of short turnaround time with a very different set of capabilities than Southwest.
7. Many famous strategies from Microsoft to Wal-Mart to Timex resulted from good fortune that their founders capitalized on. However, in *explaining* these strategies we often give the founders credit for foresight that they did not necessarily display.
8. There may be other ways of reducing costs, such as having airplanes that are more efficient to run. This is the strategy that JetBlue adopted.
9. Some of these are for illustration only. Turnaround time is used by Southwest.
10. Porter, op. cit., p. 68.
11. When Southwest first started its operations and had a 10-minute turnaround time, it would literally board departing passengers through the front door while arriving passengers exited the back door.
12. Once again the primary reason for not offering meals is not cost but the reduction of boarding time. Loading food takes time during departure.
13. According to twin brothers who pilot for Southwest and for United the training times are 30% and 60% respectively.
14. Porter [op. cit., p. 64] suggests that "a standardized fleet of 737 aircraft boosts the efficiency of maintenance." The efficiency of maintenance helps to reduce the cost—one key factor for the low-cost strategy of Southwest. This conclusion completely misses the point of having a standardized fleet. The primary reason for the standardized fleet is to facilitate the core objective of quick turnaround. From my conversations with Southwest operations, its maintenance costs are on par with other airlines. However, Southwest will never consider outsourcing maintenance even if it is cheaper than doing it in-house. However, this decision will not help meet its core objective of quick turnaround.
15. Compare the COAR methodology to that of the activity maps that Porter [op. cit., p. 71] drew to explain Southwest's strategy. Activity maps do not allow a firm to understand how the activities help a firm to deliver the core objectives ("internal outcomes" [Chatterjee, op. cit.]) and how the core objectives deliver the outcomes desired by customers. Further, separating resources from activities (Porter combines the two) allows us to develop the insight of how different resources can be used to deliver the same core objective, as illustrated by JetBlue. Southwest relies on its culture for quick boarding, JetBlue uses IT.
16. This case is based on Bridget O'Brian, "CALite's Pursuit of Southwest Reverses Engines," *The Denver Post*, January 15, 1995, p. G-1; "Continental Phasing Out CALite Service," *Chicago Sun-Times*, April 14, 1995, p. 39.
17. John A. Byrne, "The Fall of a Dot-Com," *BusinessWeek* Online, May 1, 2000.