New Balance Athletic Shoe, Inc.

Case Writeup

Individual

Case #1

The George Washington University Executive MBA Program

EMBA 220: Operations Management

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Did New Balance Need To Consider Making Its Own Acquisitions? If New Balance were to make its own acquisitions, it would distract from its own operational problems, and lose the advantage with retailers that the Addidas-Reebok acquisition had given it - especially the unique sales relationships with retailers that it had created.¹

New Balance was undergoing operational problems in 2005, mostly because of operational issues.² "We had a lot of quality problems, late deliveries, and late samples, which inhibited the effectiveness of our salespeople."³ An acquisition when there were already so many problems in its core operational areas would be a mistake for the company.

The "Adidas-Reebok transaction would be felt most by retailers, a fact that that would help New Balance.⁴ Before this deal, the industry had one 800-pound gorilla (Nike); now there are two. Those big guys tend to dictate a little bit, but they don't move as quickly as a smaller company, and they don't really establish the partnerships that we (New Balance) do. We see this as a major opportunity."⁵ "A major New Balance customer had noted that it planned on doing more business with the company after the Addidas-Reebok merger, in part because it knew New Balance and its sales people and managers so well."⁶

Did New Balance Need To Consider Reducing Its Level of Domestic Manufacturing? New Balance should continue its current level of domestic manufacturing. President and COO Jim Tompkins noted: "One thing that sets us apart is that we are manufacturers. But we are mediocre marketers by design. The message that we talk about in the marketplace is different from our competitors' message. And what makes the company unique is that we are manufacturing- and operations-based, not marketing-based."⁷ Jim Davis emphasized this distinction. When New Balance attempted to compete with Nike and Reebok head on we "failed, drastically".⁸ That is when Davis realized that the company was really good at manufacturing and operating and concentrated on doing that, differentiating the company.⁹

While some of the domestic manufacturing costs were higher than for a similar product manufactured in Asia, if they manufactured exclusively in Asia they would lose the ability to learn by doing things domestically and sharing that knowledge with their partners abroad.¹⁰ By sharing information learned with their foreign partners they hope to shorten the time to get foreign manufactured shoes to U.S., increasing their ability to re-stock retailers¹¹

Did New Balance Need To Get Better At The Promotional Tactics Used By Its Competitors? New Balance did not need to change the way it promoted its merchandise. "According to Jim Davis, New Balance already had far greater consumer loyalty than any of its competitors."¹² An analysis of the U.S. Athletic Footwear Sale to U.S. Athletic Footwear Media Expenditure (Exhibit 2), by brand for 2004 showed that New Balance had the most cost effective advertising of any of the top four brands listed.¹³ New Balance yielded $93.76 Million in sales per million expended, more than three times what Nike yielded.¹⁴ The complete chart is in Exhibit A attached to this Case Writeup.

Apparently whatever New Balance is currently doing to promote its merchandise is working. New Balance should strengthen its current promotional tactics.

Should The Company Remain Focused On Scaling Its Current Business Model And Improving Operational Performance Via The NB2E Initiative? New Balance should remain focused on scaling its current business model and improving operational performance via the NB2E initiative. If New Balance could greatly reduce the time between a retailer's order and its delivery, it would build upon it's already strong retailer (and therefore consumer) loyalty.¹⁵ The NB2E initiative, if fully successful would allow New Balance to greatly reduce inventory levels, reducing costs.¹⁶ The results would ideally be stronger relationships with retailers and greater sales.

The NB2E initiative, in order to dramatically reduce manufacturing cycle times, would require "complete realignment of factory operations".¹⁷ This is something that could be difficult to implement in factories that had New Balance's "classic arrangement" (of their manufacturing set up)¹⁸. Since, New Balance's workforce was not unionized and "always pushing us to change things so they can do it better",¹⁹ the New Balance factories were uniquely suited to implement the NB2E initiative.
Conceivably they could then share their knowledge with their Chinese suppliers further decreasing the time it took the Chinese suppliers to get merchandise to the U.S. market.

**Which Option Would Provide New Balance With An Acceptable Level Of Future Growth In Light of Industry Consolidation?** New Balance should continue with the current options to provide an acceptable level of future growth in light of industry consolidation. 1) New Balance should avoid making any acquisitions. Their current size provides them with an advantage over Nike and Addidas-Reebok with retailers as the two larger firms don't establish the type of relationships with retailers that New Balance has.xx 2) New Balance should not change its current level of domestic manufacturing. Manufacturing is New Balance's strength and they should not decrease it.xxi While the manufacture of shoes domestically loses some of the cost advantage of imports, New Balance learns valuable information which they share with their foreign suppliers to shorten the time to get shoes to market.xxx 3) New Balance does not need to get better at the promotional tactics of its competitors. An analysis (See Exhibit A) demonstrates that New Balance's footwear media expenditure produces more sales per dollar than its larger, more marketing savvy, competitors.xxxi New Balance should strengthen its current promotional tactics. 4) New Balance should continue scaling its current business model and improving performance via the NB2E initiative. This would decrease delivery times, reduce inventory levels, and reduce costs. This also would provide them the opportunity (once successfully initiated in their U.S. factories) to share the knowledge with their Chinese suppliers potentially decreasing the time to get product to the U.S. market.

**What Are The Company's Production and Marketing Strategies? Are They Compatible? Does The Location Decision Affect These Strategies?** The company's production strategy is to use outsourcers for 75% of its U.S. volume.xxiv The remaining 25% has final product assembly in one of New Balance's five factories in the northeastern U.S.xv New Balance sourced their soles from two Chinese suppliers, which also supplied finished uppers, kits, and a limited amount of finished shoes.xxvi "These firms shipped to New Balance's three material warehouses.xxvii Supplies were shipped from these three warehouses to New Balance's factories.xxxviii In 2004, New Balance adopted the NB2E system to shoe production.xxxix One of the goals of this was to reduce the time between a retailer placing an order and the delivery of the order.xxx 

New Balance's marketing strategy is focused on avoiding the endorsement of athletes.xxxi Instead, they aim to make every one of their shoes a performance product.xxxii They do not make their shoes fashion products.xxxiii 

"We maintain a great percentage of our product in inventory for replenishment, so that dealers can continually get fill-ins when they sell and when they need certain sizes and widths.xxxiv This is in contrast to their competitors who tell retailers to place orders six months in advance, and they don't carry inventory.xxxv New Balance's marketing aims at supporting retailers, especially specialty retailers, with an extensive outside sales force that is committed to New Balance. That sales force is now supported by a "sales force automation system" for smaller retailers that "enables sales representative to place direct orders remotely", and another application that would enable "smaller retailers to do the same without intervention by the sales representative.xxxvi The production and marketing strategies are compatible. New Balance's manufacture of some goods themselves supports their ability to restock inventory to merchants quickly, as they don't have to wait 9-12 weeks after an order is placed for merchandise for it to arrive from China and to be available to merchants.xxxvii This supports their marketing strategy which is focused on supporting retailers and getting merchandise to retailers as quickly as possible.

The location decision is the one incompatible portion of these strategies. While finished shoes are shipped to one of two distribution centers on the east and west coast, imported shoe parts are shipped to factories in the Northeastern U.S., and then manufactured into finished shoes in factories in the Northeastern U.S.xxxviii Finished shoes are then shipped directly to the retailer or to east or west coast distribution centers.xxxix There may be a reason that parts warehouses and factories are all in Northeastern U.S., but it is not stated. Clustering the parts warehouses and the factories closer to the point of entry for the parts would make more sense, reducing shipping, unless New Balance wanted the factories close to its
headquarters, or there was another unstated reason.

**What Is A Reasonable Demand Forecast For New Balance For The Year? For The Next Two Years?** The number of pairs of athletic footwear sold in the United States is estimated to grow by a 6.3% annual growth as provided in the case study, between 2004 and 2009.\[13\] New Balance sold $1,022,000,000 in the United States in 2004, and this should grow by $64,386,000 to a total of $1,086,386,000 in 2005 using this growth rate. New Balance's sales should grow by $68,442,318 to a total of $1,154,828,318 in 2006 using this growth rate. Two year sales (2004-2005) growth totals $132,828,318. No annual growth rate is provided internationally. Without additional information this appears to be a reasonable demand forecast.

**Which Location Option Would You Choose? Why?** I would maintain the current location for warehouse, manufacturing, and distribution. It seems illogical to me to ship parts to parts warehouses in the Northeastern U.S., then to factories in the Northeastern U.S., and then ship finished shoes directly to the retailer or to the east or west coast distribution centers.\[14\] However, there may be a reason for this approach that makes sense, but we have not been provided with information to support it. As for manufacturing, the capability for shoes may only exist in the Northeastern U.S., but more importantly I would want the factories close to the corporate headquarters since the company does pride itself on being a manufacturing firm.

**What Competitive Priorities Are Necessary To Successfully Compete In This Market?** For New Balance, the competitive priorities that allow it to successfully compete in the market are 1) Providing a high quality shoe in a variety of sizes; 2) Having a sales network that works closely with retailers to insure that they have shoes in stock and can easily reorder; 3) Manufacturing shoes both in China, to keep costs down, and domestically, to insure that retailers are supplied quickly and efficiently with the sizes and models that they need; 4) Manufacturing shoes as efficiently as possible (NB2E); 5) Designing a competitive product; and 6) Building loyalty among retailers and its core customer base.

**What Are The Key Success Factors For Competing In The Global Athletic Footwear Industry?** Based on the case study, one key success factor for competing in the global athletic footwear industry has been to avoid endorsements and instead focus on becoming a manufacturer of a quality shoe product; another key is that the quality shoe should be available in a wide variety of sizes/widths since an important part of being a manufacturer is insuring your ability to promptly and efficiently restock your retailers; also to manufacture partially in China to keep costs down and partially domestically to keep in touch with the best techniques; an additional key success factor is to build a sales organization that focuses on serving your retailers and help them to keep your product in stock and to quickly restock it; and finally to design a competitive product to keep your brand image strong, and build customer loyalty.

**Assess New Balance’s Progress In Creating And Sustaining A Competitive Advantage? What Are the Elements Of Its Success To Date? Where Is Greater Attention Needed In The Future?** New Balance has been very successful in creating and sustaining a competitive advantage.

Elements of New Balances's success are: 1) They have created strong loyalty to brand; 2) They have extremely cost effective advertising; 3) They have created a sales organization that successfully serves the company's goals providing excellent service to retailers; 4) They have created a hybrid manufacturing structure that allows them to take advantage of cost effective imports, while manufacturing domestically to quickly supply retailers; and 5) Building strong loyalty amongst their core customer base for New Balance's high-margin shoes.

Elements needing greater attention in the future are: 1) Operational issues which are of greatest importance-quality, deliveries, sample delivery\[15\]; 2) Manufacturing. The NB2E system requires additional attention for success; 3) More efficiency in supply chain; 4) Consider bringing their sales team into the company; and 5) More focus on product design to appeal to broader audience.

**How Would You Advise Jim And Ann Davis, To Proceed?** I would advise the Davis's to stay away from a merger or acquisition. The New Balance brand, evident in its successful and cost effective advertising, shouldn't be diluted. They need to work on the operational issues that caused problems in 2005.\[16\] Also, they should strengthen ties to their retailers, their sales network, their core customer base,
and improve their lean manufacturing initiative (NB2E).

ENDNOTES