



## How Companies Win

### Profiting From Demand-Driven Business Models No Matter What Business You're In

#### THE SUMMARY IN BRIEF

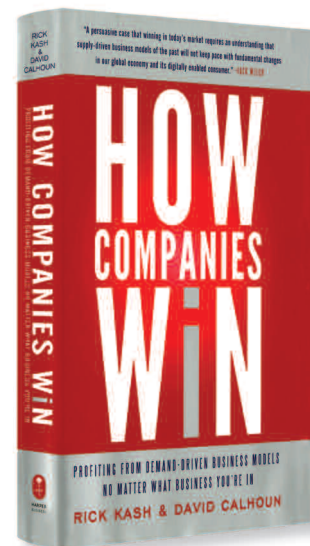
For more than 20 years, the growth formula for business has been to increase revenues by expanding product offerings while simultaneously streamlining supply. But with the recent “Global Recession,” the world economy has changed, in all likelihood forever. The old tools — most notably supply-chain management — are no longer enough. In this Demand Economy, characterized by long-term oversupply and virtually all goods and services flat to contracting demand and diminished pricing power in almost every market, the challenge is to locate and capture the elusive pools of high-profit demand.

The answer is a revolutionary, demand-driven model that has already proved successful for some of the world’s most admired companies. At the heart of this powerful new business model is an achievable vision for a new kind of winning company, one that uses sophisticated new tools and techniques to discover, characterize and then serve these pools of high-profit demand — and, in the process, gain pricing power in that marketplace.

*How Companies Win* shows how organizations can use everything from social networks to more revealing and effective consumer-research techniques, and then introduces the demand chain, the logical new partner to your supply chain. The principles, case histories and insights presented in *How Companies Win* will help your business run faster, cut costs, and become better able to deliver high-quality products and services, even in the tightest economic climate.

#### IN THIS SUMMARY, YOU WILL LEARN:

- How media companies, retailers and manufacturers work together to serve demand with much greater precision.
- What it takes for companies to win in a new era of heightened global competition.
- How to engage every level within a company, small or large, local or global.
- How to find real-world solutions that take advantage of the rise of social networks.



by Rick Kash and David Calhoun

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# THE COMPLETE SUMMARY: HOW COMPANIES WIN

by Rick Kash and David Calhoun

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For additional information on the authors, go to <http://www.summary.com>.

## Introduction: A New Strategy for a New Era

The “big idea” in the air in the 1990s was *disintermediation*: the notion that business systems, empowered by the new information and communications technologies, would strip out the middleman and grow more efficient in the process. The dot-com era was essentially this idea of disintermediation, propelled by the Internet, reaching the retail world — replacing traditional bricks-and-mortar businesses with e-commerce companies.

As we all know, the explosion of thousands of new online retailers that targeted almost every retail business from overstock inventory to groceries to pet food was followed instead by a massive shakeout in the industry that quickly killed the vast majority of those companies. The dot-com bubble was followed by the dot-com bust.

Those companies that did survive the shakeout — Amazon, eBay, Yahoo, Orbitz, Google — have proven to be some of the most important and influential companies of recent years. And they in turn set the pattern for the Web 2.0 social media firms such as Twitter, MySpace, Facebook and YouTube that have redefined modern life. What did those survivors have in common? Their business was based on what customers wanted, rather than what the suppliers already had. They were the harbingers of the demand-driven economy, if only we had noticed.

One of the lessons they taught is that we have now entered an era of oversupply. Oversupply is a situation where significantly more supply exists than there is demand to absorb it. Oversupply is often characterized by a lack of differentiation, with price becoming the pri-

mary factor underlying purchase decisions. As a consequence, pricing power virtually disappears and organic growth and profitability become increasingly difficult to achieve.

### The Concept of ‘Need States’

The second lesson to be learned is that in an era of oversupply it is imperative that you construct a framework in your company that encompasses and aligns everyone toward meeting, not just the current, but also the latent and emerging demand of your highest-profit customers and consumers. And before you can do that, you need to understand who those customers and consumers are, where they are and what “need states” they exhibit as they make their purchasing decisions.

The concept of need states is important for developing an in-depth understanding of demand. Need states are the circumstances or the occasions that cause someone to want something and to take action in its pursuit.

This is not reengineering; this is *rethinking*. This is not reorganizing, it's reshaping manufacturers, retailers and the media into a collaborative network that will work to the benefit of all who participate. For a long time, this new model of organizing and collaborating has been intuitively felt, and now it's real. It's called the “demand chain.” ●

## Part I: Shift

### The Demand-Driven Company

By almost any measure, McDonald's is one of the most successful and influential companies of all time.

But from the mid-1990s until 2002, the company lost



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its way by choosing to focus almost exclusively on supply — in its case, building even more restaurants and acquiring other food chains — rather than on what its millions of customers really wanted. It was only when McDonald's went back to paying attention to those customers — what they liked, what they wanted and what they might like — that the company found its way back to success.

The modern McDonald's story traditionally begins in 1955, when franchisee Ray Kroc opened the ninth store of the 15-year-old company. McDonald's had already pioneered the idea of "fast food," but it was Kroc who systematized the process and, buying the company, turned it into an international corporation and a global symbol of American culture.

By the end of the 20th century, McDonald's was enjoying revenues of almost \$15 billion annually from more than 28,000 stores around the world. Net income was nearly \$2 billion in 2000.

### McDonald's Winning Shift

In 2002, McDonald's suffered its first quarterly loss since 1954, ending a celebrated half-century of continual growth. And the bad news kept coming: Even as profits disappeared and revenues flattened, consumer satisfaction levels fell below that of the company's major competitors. As a further insult, a spate of articles from 1998 to 1999 that eventually became the book *Fast Food Nation* in 2001 singled out McDonald's as contributing to America's health and obesity problems.

And so McDonald's began 2003 by embarking on one of the most remarkable restructurings in modern business history.

What did "doing better" really mean? McDonald's developed a table that showed the components of customer satisfaction and how they related to the company's own values. McDonald's called this its "Plan to Win" and it addressed five components that constituted McDonald's new model for total customer service: people, products, place, price and promotion.

The result? After hitting bottom in 2002, McDonald's revenues and income both returned to their historic upward march, even during a growing recession. Since 2004, McDonald's total sales have increased from \$50.8 billion to \$72.3 billion in 2009, a jump of more than 42 percent.

It hasn't been easy, but McDonald's has transformed itself into a demand-driven corporation.

The single most important lesson to take away from McDonald's remarkable turnaround is this: In a world

## Two Types of Customer Analysis

Several tools are available to enhance precision in a company's operations. Here are two:

- **Demand Gap Analysis.** Demand gaps are the distance between what your customer wants and what it gets from you or your competitors.
- **Customer Demand Analysis.** It is designed to determine first who the most profitable customers are for your business. The second step is to actually contact those customers, who provide valuable insights.

where supply is growing ever more efficient while demand is flattening or even contracting, understanding demand becomes the new imperative for how companies will compete and win.

With the high levels of competition that characterize the present and the foreseeable future, the margin for error has gone down and the need for precision has gone up. In particular, precision in understanding exactly which pools of customers and consumers offer the greatest potential profitability for your company has increased in importance as well as degree. With this knowledge you can align your supply and your resources to better satisfy this demand and thus capture the largest possible share of the most profitable markets. ●

## The Demand-Driven Economy

Just how did McDonald's know that it was time to introduce salads and to keep their stores open 24 hours per day? How did Apple know that consumers wanted to bring the best of mobile phones and PCs together into a device that might ultimately reinvent both industries? How did IBM know that it was time to evolve from the world's largest technology hardware supplier to one of the world's most respected technology services providers?

The simple answer is that each of these companies understood, in a very deep way, the facts, the economics and the content of what their customers and consumers demanded. Companies like these, which win on a continual basis, operate above all by understanding demand at the higher market and sector levels.

By comparison, companies that struggle to compete quarter to quarter operate at lower levels of understanding that encompass only basic customer needs and product attributes. The result is that informed by an under-

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standing that markets evolve at the level of current, latent and emerging demand, demand-driven companies consistently have a larger and longer perspective than their competition.

The demand-driven company not only thinks about today and tomorrow, but next year and the next five years. The supply-driven company only thinks about today, tomorrow and the end of the quarter.

What these great companies do is the result of a business model that operates beyond the simple — and increasingly risky — strategy of “asking customers what they want.”

These great companies see trends and recognize patterns forming in their markets, their category, among their different customer segments — and even outside their businesses, in adjacent markets and across the entire culture — and develop hypotheses about what those customers *will* want. Only then are they in a position to query customers — and even then, only the right customers — and begin to align current strategies, resource allocation, products and other offers to intercept this demand as it approaches.

This is a far more powerful and multifaceted approach to identifying your *real* customers than was ever before possible.

## About Supply

**Supply is the sum total of what the provider does to satisfy the customer’s demand, both physical and emotional.** It is important to recognize that supply is not just the product itself, but also all the elements that support the product including price, packaging, messaging, the channels of distribution, customer service and the brand. ●

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## Part II: Strategy

Imagine how your business would benefit if you had a single integrated framework to:

- Find the high-profit customers who can raise your margins and revenues.
- Understand current, latent and emerging demand.
- Determine which channels are growing and which channels are slowing.
- Assess where your competitors are strong and where they are weakest.
- Understand the media habits of your most important consumers.
- Identify the best potential opportunities for innovation.
- Build a financial model for resource allocation to

drive faster growth.

- Develop insights about the demand of your most profitable customers that your competitors don’t know.

## Differentiated Demand

When you build an effective demand landscape and understand the demand profit pools within it, all of these questions can be readily answered. Once you have this understanding, you are in a better position to satisfy the demands of the most attractive of these demand profit pools. You can use your knowledge and understanding to align your differentiated brands and products so that you capture a larger percentage of the profitable demand than your competitors. The framework also becomes the basis for how to manage your brands and products as a portfolio. And because it includes information about virtually every function within the company, from finance to manufacturing to marketing and sales, it is the integrated framework through which all can understand, talk about and manage the activities of their operations.

Demand profit pools exist because demand is not homogeneous. Indeed, in the world of demand, no size fits all, which ultimately means that in any given market there are likely to be multiple distinct pools of demand. Mercedes sedans, GMC pickup trucks, Honda Hybrids and Cadillac Escalades can all be successful and profitable car brands while serving very different demand profit pools within the larger vehicle market. Most markets feature at least six different demand profit pools. That’s a lot of opportunity.

Customers within those demand profit pools are attracted to both the rational and emotional benefits of these submarkets. So why the range of products? Because people have different lives, tastes, lifestyles, needs and personal histories. They also live in different environments and are at different points in their lives. The result is a wide spectrum in both rational benefits (quality, performance, safety, comfort, eco-friendliness, mileage, power, price) and emotional rewards (status, “greenness,” hipness, safety).

Demand profit pools are groups of customers who make similar decisions based on the common needs they want satisfied. Any given market, whether in consumer or business-to-business industries, will have several distinct demand profit pools. These should be defined not simply by who these customers are or what they purchase but, most important, by why they make the decisions they make. And beyond understanding the who, what and why of customers by group, businesses that win must fully understand the economics of each demand profit pool. Determining which ones spend the

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most, which are most and least price sensitive, and which offer the highest and lowest profit potential are all critical to determining which demand profit pools to focus on and how to serve them. ●

### The Fifth P

In the new demand economy, the margin for error for all businesses grows smaller and smaller.

In the flagrantly expansionary economy of the past several years, sloppiness in planning and execution were hidden as business sales and profits went up constantly. These days, you are not only competing with ever-growing sources of supply from competitors all over the world, but all of that supply is competing for flattening — even contracting — demand. In this new competitive reality, *any* mistake can have significant consequences.

The solution must go beyond tightening the screws still further on the supply chain. Now the precision must occur on the demand side of the equation.

### Achieving a New Level of Precision

One reason for this is a shift in expectations. Today's customers and consumers expect more precision from business because, thanks to the tech revolution, the world around us has become much more precise. GPS devices will show you within inches how to get from point A to point B. Atomic clocks measure to the billionths of seconds. Twitter can tell you exactly what your friends are up to at any given moment. YouTube, TiVo and iTunes allow you to access the history of recorded entertainment to find exactly the experience you want at that moment. And cellular telephony lets people contact you anywhere on the globe.

In the face of this unprecedented increase in precision, is it any wonder that customers and consumers are increasingly impatient with inaccuracies, delays and imprecision? Precision has become the leitmotif of the lives of your consumers — and if you fail to match that precision, those failings will seem even more amplified.

What consumers also instinctively understand is that precision has long been a precursor to progress. In high technology, ever smaller chips also have ever more functionality. In medicine, laparoscopic and laser surgery enable doctors to work in small, almost microscopic, spaces instead of using more invasive procedures. Heart stents are implanted with precision to prevent heart attacks and strokes. The Kindle delivers thousands of books to your home on a small device within seconds, and soon tiny chips called RFID (for radio frequency identification) will track individual packages as they trav-

el across America or around the world. Precision is almost always the path into the future.

### The New Marketing Mix

Supply chain management became a science through the creation of more rigorous approaches that increased quality, reduced costs and shrank production cycle time. Every aspect of what before had been the siloed functions of purchasing, manufacturing and distribution was now assessed, optimized and interlinked using several fact-based approaches.

Today, an equally rigorous approach to demand is both necessary and practical. It needs to be done and it can be done.

The marketing mix is best known as the “four P's of marketing”: product, promotion, place and price. If we apply the philosophy of precision to this mix, the potential benefits become enormous.

It is time for the adoption of a fifth P, precision, to make sure that each of the first four P's operate at their maximum efficiency and lowest cost. A lot of companies have already noticed; Coca-Cola, for example, has already declared this “the Age of Precision Marketing.” ●

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## Total Innovation

### Myth-Free Innovation

Of all of the activities that companies engage in, *innovation* may be the one that is most mythologized, misperceived and misunderstood. According to studies, American corporations spend more than \$1 trillion per year on innovation, and only get a fraction of that back in return on their investment, in large part because of this misperception.

The confusion begins right at the start, with the very definition of the word. In everyday usage, “innovation” is perceived as a creative exercise. It is nothing of the sort; in truth, at least in the world of business, *innovation is a disciplined, demand-based process.*

There has never been a successful long-term innovation that did not better satisfy an existing or emerging customer demand. That suggests a definition:

**Innovation is finding unsatisfied profitable demand and then fulfilling it.**

### Total Innovation

You'll note that in defining innovation, no constraints were placed on where that innovation may occur. That was intentional, because a big mistake companies make is to narrow their idea of what innovation should result

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in, typically focusing on new products alone.

It is also worth noting that the word “innovation” itself has a way of freezing people in their tracks. Over and over we’ve heard people say, “I’m just a creative person, so I can’t be very good at innovation.” That’s why, when Jim Kilts was CEO of Gillette, he and his SVP of strategy, Peter Klein, took the pressure off of everyone by reframing the entire topic. They told the company to stop referring to innovation and to just “find a better way.”

### Gillette’s Success

Kilts and Klein applied what they called the “Total Innovation” process at Gillette to great effect. While Gillette had enjoyed a reputation as a highly innovative company, the truth was that its innovation pipeline and innovation successes were running out of steam in the years before Kilts and Klein arrived.

Within six months of putting the Total Innovation process in place, Gillette’s revenues increased by approximately 15 percent and net income jumped by more than 18 percent. While there were arguably other factors at play contributing to Gillette’s financial success during this time, for example favorable exchange rates and a series of hurricanes spurring battery sales, the Total Innovation process was clearly a major contributing factor to Gillette’s success. With the new innovation process and a new confidence throughout the organization — all begun by taking the pressure off the need to be “creative” — Gillette began to post double-digit revenue gains each year after having suffered several years of declining revenues.

Real innovation is total innovation. That is, it begins, like all new products or services, with the idea or market analysis, but it continues all of the way through the manufacturing process, packaging, distribution, retail, consumption and even beyond, through that product’s or service’s entire lifespan. In a world of oversupply and flattening demand, this is the only strategy that ensures that all of the potential profit is realized from the process, and that the product or service itself is precisely aligned with the most important demand pools. ●

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## The Price Is Right

Pricing strategy is often the one area where managers feel least confident about their approach. On the one hand, these managers recognize that if they price their offerings too low, they risk leaving money on the table. And on the other hand, if they set prices too high they risk losing valuable consumers or customers; or just as

bad, risk pricing themselves out of the retail or distribution channels they need to reach those customers. It is a dichotomy that haunts almost every business on the planet: Lose profits or lose customers.

Surely there is a better way, one that ends not with compromise, but with a win.

### Pricing Power

There really is a rational and systematic way to price products and services in such a way as to escape the lost profits/lost customers dichotomy. Better yet, this kind of intelligent, demand-driven pricing can actually uncover new sources of customers and profits. And that can be a very valuable advantage.

How valuable? The numbers are so compelling and decisive that it is astonishing that every future manager isn’t taught this in business school. A 1 percent price increase has a *50 percent* greater impact on operating income than does a 1 percent decrease in variable cost. More remarkably, that same 1 percent price increase has a *215 percent* greater impact on operating profit than does a 1 percent volume increase in sales.

If you can find a way to raise the price of your product or service by just a few percent — through more targeted marketing, by improving product image, by finding more lucrative profit pools or by adding new features without adding cost — the impact on your bottom line will be so great that almost no realistic amount of cost cutting or increased production will be able to match it. ●

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## Part III: Execution

You need to ask yourself: “Does my company have a simple — and easily understood — plan for how it will succeed?” and “Does everyone in the company understand that plan and their role within it?”

Great companies (the ones that stay on top of their markets for decades) align their internal operations, from the boardroom to the receptionist, to be in total support of that plan. And they regularly communicate that message to their employees.

We call these external/internal strategies the “thesis for winning” and “mental models.”

### The Thesis for Winning

As the years have gone by, it has become absolutely clear that all truly outstanding leaders have a thesis for winning — that is, a set of individual principles, each in itself important, that when taken together represent the strategy to take and the pathway to follow for that busi-

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ness to win. It is what Ed Liddy, former chairman and CEO of Allstate Insurance, calls “The Theory of the Game.”

Liddy speaks with authority and experience, because his own thesis for winning across his eight years at the top of Allstate produced remarkable results. When Liddy became CEO in 1999, company revenues were \$27 billion and net income was \$2.7 billion. When he retired in 2006, revenues had increased to \$36 billion, but profits had skyrocketed to almost \$5 billion.

Liddy credits the success, in part, to giving Allstate a strong thesis for winning. Liddy had three elements in his thesis:

1. *Deliver better service* at all levels of Allstate, starting with their agents.
2. *Deliver better pricing* based on the lifetime value of the customers.
3. *Communicate constantly* to Allstate’s 12,000 agents the importance of good service in attracting and retaining customers and to its millions of insureds that Allstate puts its “good hands” commitment to customer service foremost.

Here is a definition of the thesis for winning:

**Management’s set of beliefs and objectives, which, taken in combination, establishes the basis on which a corporation intends to win versus its competitors.**

### The Mental Model

A mental model is the same picture in every employee’s mind of how their company is going to compete and win — and their own role within that plan.

It is the commitment by the company to the notion that every function in the company — and every person within those functions — must share the same understanding of what they are going to do, and how they are going to do it, to win. And that this message must be shared with the entire company, ratified by employees and made manifest in every move the company makes.

The mental model creates comfort for employees because they understand the larger picture and their important role within it. From that comfort springs confidence, which is the hallmark of high-performing employees and winning companies. ●

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## The Demand Chain

Today, perhaps more than in any time in the past 80 years, manufacturers, retailers and media companies are all finding themselves under assault, not just by a deep

global recession but by a seemingly inexplicable loss in effectiveness of some of their most important and proven business tools and strategies.

These companies watch helplessly as their consumers, now networked, get smarter — and realize, to their dismay, that they aren’t keeping up. The game keeps changing and the rules are evolving quickly. Clearly there’s universal demand by business leaders for a new solution.

This period of economic complexity and turmoil will be a historic opportunity for some companies to gain enormous market share and profit share by participating in a new collaborative business model. This model includes a new level of collaboration and coordination between manufacturers, retailers and media companies that goes beyond traditional data-sharing efforts and approaches such as category management.

This certainty of winning is driven by a truly proprietary understanding of what consumers demand and which of these consumers offer the greatest profitability. With these in hand, a network is formed between manufacturers, retailers and media companies to capture the largest share of profitable demand. The commitment to this network allows all of the participants to grow at faster rates and to higher levels than would be possible without the collaboration of the network.

This new model is the demand chain. It stands as the counterpoint to the traditional supply chain, its information flowing in the opposite direction, with results driving capabilities rather than the other way around.

For manufacturers it means aligning their different brands and products so that they capture the highest share of the most profitable demand.

For retailers it means organizing and merchandising their stores so that they better meet the demand of the people who shop in their stores versus those of their competitors.

For media companies it means that on the horizon there is a new level of precision that will enable them to reach the specific consumers that the manufacturers and retailers most want to communicate with and motivate.

In the collaborative environment of the demand chain, where information is shared and plans are coordinated, everyone becomes more efficient in what they make, how and where they distribute their products and how they use their marketing and media budgets to motivate consumers and stimulate purchase behavior.

**A demand chain is a collaborative network composed of a manufacturer, retailers and media companies that enables each participant to better**

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understand and more completely and precisely fulfill customer demand. ●

## Supply, Meet Demand

In the years to come, the real power of the supply chain will have less to do with the micromanagement of details regarding cost and performance, or with one's comparative advantage relative to competitors' supply chains. Instead, the true measure of power for one's supply chain will lie in its ability to more precisely target and serve the right demand at the right time at the right place in the right package and in the right environment. Supply chain advantage will now be driven by how closely it is guided by, and responsive to, the demand chain as it enables the supply chain to deliver the right product to the right place at the right time.

Simply put: *Your supply chain can no longer be optimized without a complementary, and equally optimized, demand chain.*

## Going Forward

Going forward, winning supply chains will precisely align demand and supply in ways that have never before been possible. New technologies, combined with the intellectual capital of demand profit pools, will afford companies the ability to align the right supply to precisely the right demand — thus enabling growth in the only way possible in flat markets: taking volume, share and profits from your competitors.

One important implication of this is that managers will need to focus much greater attention on:

1. *Identifying* the target, highly attractive demand profit pools of customers.
2. *Determining* how the supply chain can best respond to, and satisfy, this precise group of consumers.

The strategy of having a demand-led supply chain goes beyond organizational alignment; it is in fact a structural change with enormous implications for organizational efficiency and continual profitability. There are four key benefits:

1. **Start Better.** One of the first benefits of this partnership is the demand chain's ability to get the right product to the right retail outlet at the right time. This essentially converts the supply chain from its current task of replacing what is on the shelf today with more of the same to that of determining what *should* be on the shelf.
2. **Communicate Better.** In the shared network of the demand chain, the communication between retailers and manufacturers improves greatly. The improved communication is the result of shared data, shared inputs

and shared outputs. The result enables better coordination and provides consistent opportunities for high-level supply chain performance.

3. **Align Better.** This balanced approach also drives much greater internal alignment and communication. As the benefits of the partnership between the demand chain and supply chain become apparent, it fosters further collaboration and helps resolve the potential tension between identifying and responding to demand opportunities and the desire to maintain the discipline of the supply chain.

4. **Structure Better.** Over time, this partnership leads to improvements in the overall structure of the supply chain and its ability to serve profitable demand. Fully informed by an understanding of demand on a store-by-store, local market, regional and national level, the flexibility, adaptability and responsiveness of the supply chain can be improved. ●

## Afterword: A Fresh Start

These tools work, as the case studies show, and they can be applied right now.

Evolving from a supply-driven company to a demand-driven company is as much a matter of attitude as it is a process. If your thesis for winning is revised to include the critical challenge of finding your high-profit demand pools and then giving them what they want; if your orientation shifts from asking what your best customers want now to what they want next; and if your company's mental model realigns your organization away from making your supply chain a little more perfect to making it a lot more accurate, then these are not going to be the worst of times, but the best of times.

Your company will enjoy bigger profits, greater market share and higher customer loyalty, even as your competitors struggle and fade. And it all begins with a change of perspective.

Business is always about change, it always has been. The constant companion of change is opportunity. ●

### RECOMMENDED READING LIST

If you liked *How Companies Win*, you'll also like:

1. ***Always a Winner* by Peter Navarro.** Navarro shows how your organization can be a winner over the course of its entire cycle.
2. ***Leading Outside the Lines* by Jon R. Katzenbach and Zia Khan.** Katzenbach and Khan examine how two distinct factions together form the bigger picture for how organizations actually work.
3. ***Overpromise and Overdeliver* by Rick Barrera.** Barrera shows that today's most successful companies master Touchpoint Branding — the art of making sure that every point of contact between a company and its customers is well-executed and fulfills an over-the-top brand promise.