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# COMBINING STRATEGIC ANALYSIS AND CHANGE MANAGEMENT:

## A TOOL FOR IMPROVING THE COMPETITIVENESS OF FIRMS

microREPORT #154

**APRIL 2009**

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# I. INTRODUCTION

*Competitiveness* (www.competitiveness.com) is a boutique consulting company specialized in working with companies, universities and other institutions that are competing in a particular business and are concentrated in a certain geographical area—i.e., a cluster. A cluster is simply a unit of analysis where economies of scale can be attained, thereby contributing to regional economic development.

Over the past 15 years, *Competitiveness* has developed a methodology for working with cluster agents in order to improve their competitiveness; that is, so that they can make more money over the long term. The Competitiveness Reinforcement Initiative (CRI) methodology combines two very important components:

- Thorough ***strategic analysis*** that focuses on the value chain approach to provide a full picture of what is happening in the industry and to enable the right strategies to be devised that capture locally the largest part of the value created globally; and
- An intensive ***change management process***, or "therapy", where tools from the field of psychology are used to convince companies, research centers, government and other relevant institutions to take the necessary actions to make strategies feasible and obtain concrete improvements in companies' competitiveness.

Having tried and tested this methodology in more than 130 CRIs worldwide, *Competitiveness* has standardized the combination of analysis and change management in order to ensure that lessons learned can be assimilated by local teams working on new cluster initiatives elsewhere in the world, in very different socio-economic environments and a wide array of sectors: from Catalonia (Spain) or Rhône Alpes (France), to Atacama (Chile) or Minas Gerais (Brazil), working in clusters related to info-mobility or health services as well as shoe manufacturing, avocados or tourism.

## ANALYZING BUSINESS SEGMENTS

A key aspect when implementing *Competitiveness'* proprietary methodology is to focus on specific business segments, understanding that market forces act differently in each business segment. The methodology uses Michael Porter's Five Forces to determine whether there is money to be made in a particular business segment (whether there are many substitutes and how high are the barriers to entry in that business), who retains the greatest proportion of the margin (clients, suppliers or companies with a certain degree of rivalry between them) and, based on this, recommendations are made concerning changes in business strategy to move into more profitable segments.

Analyzing by business segments allows the CRI team to arrive at precise and concrete recommendations. A more general sectoral approach will find a minimum common denominator that is as general as "improve work force education" or as illusory as "reduce taxes, increase trade barriers and provide cheaper energy"—as was the initial situation in the textile-apparel cluster in the State of Mexico. Focusing on fast fashion, the work carried out through the CRI allowed *Competitiveness* to determine the type of training required, appropriate financial support and infrastructure development adequate for the proposed strategy (see Section II, below).

## BRINGING ABOUT CHANGE

The strategy proposed can be more or less innovative. In some cases, such as with tourism in Bariloche, the strategy centered on better organization of different actors and initiatives and choosing where to focus coordinated efforts (see Section III); in the textile-apparel cluster in the State of Mexico, the strategy was obvious once worldwide trends were analyzed; and in Valparaiso it was innovative for avocado to be considered as "ready to eat" (see Section IV). A great strategy, however, is useless if companies, government, universities and other institutions are not sufficiently convinced to take the necessary actions to implement it. It is not feasible to try to convince everyone (if everyone agrees, then the strategic analysis probably has not added anything new and is therefore flawed), but it is vital to have approximately 20 percent of "believers," that will start taking the right steps—and their success will be imitated by the others in the medium or long term.

Bringing about change in a group of businesspeople is more about psychology than about business analysis. The six-month process of a CRI begins with changing people's ***attitude***. Often businesspeople blame external factors for their woes: the exchange rate, high taxes, government inefficiencies, dumping by competitors abroad, etc., but few take the time to think about what they have done to improve their own competitiveness; often businesses are competing the same way they did 10 or 15 years ago, although the market does not still function the same way today. Changing attitudes—opening people's minds to the problems that are not only external but that are within their own reach—is fundamental to the CRI process.

The second phase in the change process in modifying people's ***belief.*** This is where the thorough analysis is introduced. Hard data helps convince businesspeople that there is more money to be made if they approach their business in a different way. It is always very useful to bring information about the purchasing criteria of the most sophisticated buyers worldwide, and references of how others have done better by following the proposed strategy. The importance of interviewing advanced demand and carrying out a good international benchmarking exercise cannot be underestimated, as this often provides the most convincing arguments that change businesspeople's belief.

Finally, the last part of the change process is to actually engage people so that they alter their ***behavior***. Before the end of the CRI it is necessary to have convinced at least a small group of "believers" that will have worked on the action plan, the budget and the work plan for each action to be undertaken, and will be willing to present these results in front of the entire cluster.

## ABOUT COLLABORATION

It is often perceived that clusters are all about collaboration. This is not necessarily the case. The strategic analysis carried out during a CRI will provide information to companies about the strategic choices they can make at an individual company level, and in that regard companies should and will ***continue to compete*** with other companies in the cluster. The analysis will also include, however, the identification of areas for improvement, where the individual action of each company would not be efficient and only ***coordinated efforts*** will be able to bring about the required changes for companies to be able to fulfill their strategic decisions.

Companies willing to specialize in active corporate tourism in Bariloche will continue competing with each other in devising the most innovative event, the more effective team building outdoors activity or the best facilities for a small corporate meeting, but they all agree to join forces in marketing efforts to re-position Bariloche as the most innovative place for corporate events, and in together negotiating with the airlines to adapt flight schedules to the requirements of their corporate clients.

In the case of the textile-apparel cluster in the State of Mexico, with large foreign players dominating the shopping malls, creating an open-air city center shopping area was not something that cluster companies could carry out on their own. Convinced that in order to move to fast fashion their value chain needed to include adequate retailing, companies were able to work together with government authorities to put in place this ambitious project. Needless to say, competition between cluster companies on design or brand development will continue to be fierce.

In the case of the avocado cluster in Valparaiso, the quality requirements in order to shift to the "ready to eat" business are significantly different from those in the "ingredient" business; improvements in certification standards and precision in the entire logistical process are efforts that need to be undertaken by a large share of cluster companies.

## COMPETITIVENESS WORLDWIDE

A final comment to be made concerns the applicability of this approach and this tried-and-tested methodology to clusters in very different sectors and in diverse economic and political contexts. Although this methodology was initially developed working with clusters in Western Europe, companies today, irrespective of their geography, work in a globalized economy where market forces affect them very similarly. Therefore the strategic analysis must allow them to see how their business is changing and what they can do to better compete worldwide. Changing people's attitudes, beliefs and behavior may take cultural adaptation—whether meetings are long or short; over coffee, water or Argentinean *mate* tea—but it is still necessary to go through the process and convince businesspeople with thorough analysis and by taking the time to listen.

# II. THE TEXTILE-APPAREL CLUSTER REINFORCEMENT INITIATIVE IN THE STATE OF MEXICO (MEXICO)

## BACKGROUND – A TRADITIONAL SECTOR IN CRISIS

The textile and apparel cluster in the State of Mexico is a diverse, highly interdependent and labor intensive sector. It is formed by more than 800 small and medium-sized enterprises and a few large and vertically integrated companies. The cluster produces approximately US$20 billion per annum and employs around 68,000 people.

Historically the textile and apparel sector has been a robust engine for the economy of the State of Mexico. In the 1960s the sector grew in a closed economy, manufacturing for Mexican consumers, and with the signing of NAFTA in 1994, the cluster prospered as a low-cost exporter to the United States. However, in recent years the cluster has suffered from increased competition from China and other Central American countries, resulting in a fall in the cluster's competitiveness, loss of jobs and a drop in companies' profits. As a result, and in order to maintain employment in this traditional cluster, efforts to reinforce the competitiveness of the sector became crucial.

## THE NEED TO REACH THE CONSUMER

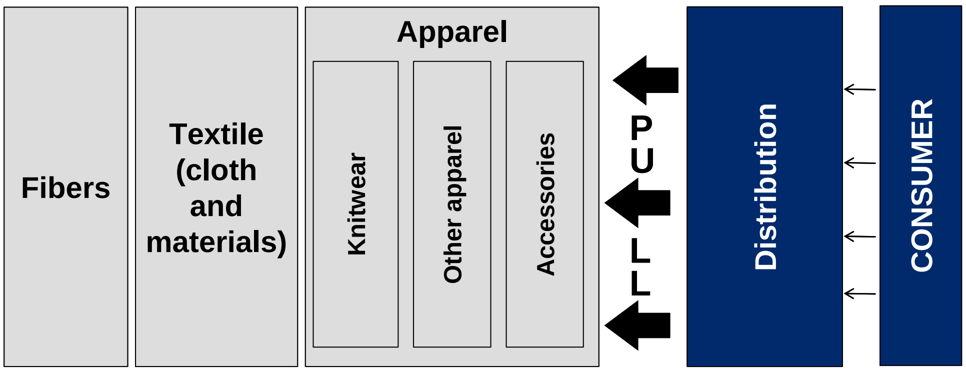
During the CRI, *Competitiveness* conducted a thorough analysis examining the attractiveness of the business segments in which the companies of the cluster were competing, along with the comparative advantage of the cluster in the global economy. It was determined that the underlying weakness of the cluster was that it was competing in a business that was beyond its reach. The cluster could not compete with low-cost countries with an export strategy based on cheap labor and no brand identity. It had previously been able to compete this way due to a protectionist trade policy and then, more recently, Mexico was temporarily attractive as a low-cost manufacturing area for the United States. However, as China grew and the terms of trade improved, a low-cost strategy was no longer an option for Mexico. A smarter alternative was for the apparel manufacturers to create their own direct routes to the consumer. This strategy would allow apparel manufacturers to develop and control their own distribution channels, reducing dependence on other traditional channels such as department stores and clothing retail chains. More importantly, manufacturers' stores would serve as an immediate feedback mechanism, providing direct information on the latest trends and thereby enabling them to manufacture appropriate products.

As part of the initiative, a delegation from the government of the State of Mexico traveled to Catalonia to see how a textile cluster could flourish in a region with much higher labor costs than Mexico, producing innovative brands using this alternative strategy. The lessons learned from this reference trip were that, contrary to what other ill-fated textile clusters had done in medium- and high-cost regions, public administration and private sector companies should not attempt to upgrade the value of the products produced by promoting productivity, quality, product design and exports, but rather support manufacturers in creating their own direct routes to market and compete in the business of "fast fashion." The best example of a company following this strategy in the reference cluster is Mango (www.mango.es).

## FROM EXPORTERS TO RETAILERS

Initiating such a dramatic change in strategy was not an easy task for the companies in the State of Mexico. The strategy implied transforming the value chain so that textile producers created small volume and flexible products, while the apparel manufactures had to venture into the retail market. The two main parts of the value chain, textile and apparel, would need to make significant changes in a coordinated manner in order to shift from *supply push* to *demand pull* (see Figure 1). However, the characteristics of the cluster, dominated by two powerful associations representing the textile and apparel manufacturers with competing and incompatible interests[1] and important political connections, and promoting a platform of trade protectionism, made such a transformation a difficult feat to accomplish. The change management process and workgroups were critical in driving change in the right direction.

**Figure 1. Changing the Textile and Apparel Value Chain to Compete in "Fast Fashion"**




Approximately 70 personal interviews were conducted with business people, universities, government agencies and associations in order to better understand the activities of the cluster agents, and more importantly decipher which people could be the drivers of strategic change. This step was crucial, as the largest exporting companies, with some exceptions, were not the ones which could lead the cluster in a different direction: some of them where actually following the new strategy already but were not keen on having local competition develop. After profiling the different actors, a small group of business people were selected to share the vision, with the idea that they could lead future strategic actions. These business people included those from the two powerful associations, but the group sidestepped their leadership and treated them not as industry leaders, but simply as business people with a strategic vision. This group publicly expressed their support for the need to summon workgroups, and encouraged others to participate in order to take actions that would help change the direction of the cluster.

Nine workgroups were convened over a two-month period in order to design specific actions in areas that the value chain needed strengthening. These areas included retailing, logistics and fast and flexible textile production. The business people, together with representatives of public administration, universities and suppliers, worked intensively during these workgroups to create three important projects to help the companies of the cluster make a strategic change and create their own routes to consumers. The projects were:

- An open-air shopping center specialized in brands from local apparel manufacturers that were attempting to enter the retail market for the first time
- A government program aimed at assisting individual apparel manufacturers desiring to open their own stores but lacking the know-how or financial resources

[1] Competing and incompatible interests refers to the trade policy positions of the Canaintex (textile industry association) and the CNIV (apparel industry association). The Canaintex lobbied the government for increased tariffs on imports of textile materials, in order to protect the domestic textile industry. The CNIV, on the other hand, lobbied the government for reducing the tariffs on textile material. For the apparel industry, high tariffs were detrimental to its competitiveness as apparel manufacturers were unable to purchase cheap textile materials from other markets. This issue was a cause of great tension between these two associations.

- A training program in retailing, logistics and fast and flexible production

## THE TEXTILE – APPAREL CLUSTER TODAY

The cluster today has begun to implement all three of these action lines in a cooperative manner. Most importantly, the majority of companies that participated in this initiative are now confronting a new series of challenges. Instead of seeking to lower their production costs—a feat beyond their control—they are succeeding in creating and developing their own brands and stores to have direct access to the consumer for the first time.

It is interesting to note that contrary to what is often expected of "cluster initiatives" the resulting projects or action lines are not only about collaboration amongst cluster companies. Creating retail space where local manufacturers can market their brands, for instance, in fact contributes to an increase in the rivalry between the actors in the cluster, which in the long run will be reflected in the increased competitiveness of those companies: making more money, long term. This result could not have been reached by following the suggestions of the cluster members at the beginning of the project, as they were focused on increasing trade barriers, lowering energy costs or providing tax cuts; none of those measures would make the companies more competitive.

# III. IMPLEMENTING THE VALUE CHAIN APPROACH: THE CASE OF TOURISM IN BARILOCHE, ARGENTINA

## BACKGROUND

Bariloche is a small city in the northern part of the Argentinean Patagonia, long renowned for its legendary ski slopes and breathtaking Swiss Alps-like scenery with beautiful lakes and the backdrop of the imposing Andes. Most of its 120,000 inhabitants make a living directly or indirectly from an extensive tourism industry, which represents approximately 42 percent of the city's economy and brings in approximately 800,000 tourists each year[2].

Tourism started to flourish in Bariloche in the 1970s, when it became the most fashionable destination in Argentina with the largest ski station in Latin America. Since then, there have been good times and bad times, particularly associated to the exchange rate between the US dollar and the Argentine peso. The peso's drastic devaluation at the end of 2002 brought an upsurge of Argentinean tourists that could not travel anywhere else. This provided a comparative advantage that local businesses seized upon opportunistically, cashing in fully booked high seasons, avoiding much-needed upgrades in their facilities, and raising prices 20 percent per year. Slowly but surely, local businesses ate away at their advantage while their main tourists—Argentinean families—were increasingly finding it cheaper and easier to travel abroad again.

The tourism industry in Bariloche includes more than 600 companies, mainly micro and small enterprises[3] (restaurants, service providers, small lodging facilities, etc.), some medium sized companies (4- and 5-star hotels and more established travel agencies) and even some large companies (mainly related to transport, such as Aerolineas Argentinas and LAN Airlines).

Within this context, a number of efforts had been undertaken by different levels of the public sector, frequently with international donor funding, but no real change had ever resulted from the long list of consultants that had passed by Bariloche. Local businesses were wary of yet another international consultant coming their way and were discouraged by the prospect of a bleak future in the midst of general Argentinean instability and local political inefficiencies.

## IMPLEMENTING THE VALUE CHAIN APPROACH IN A BEATEN TRACK

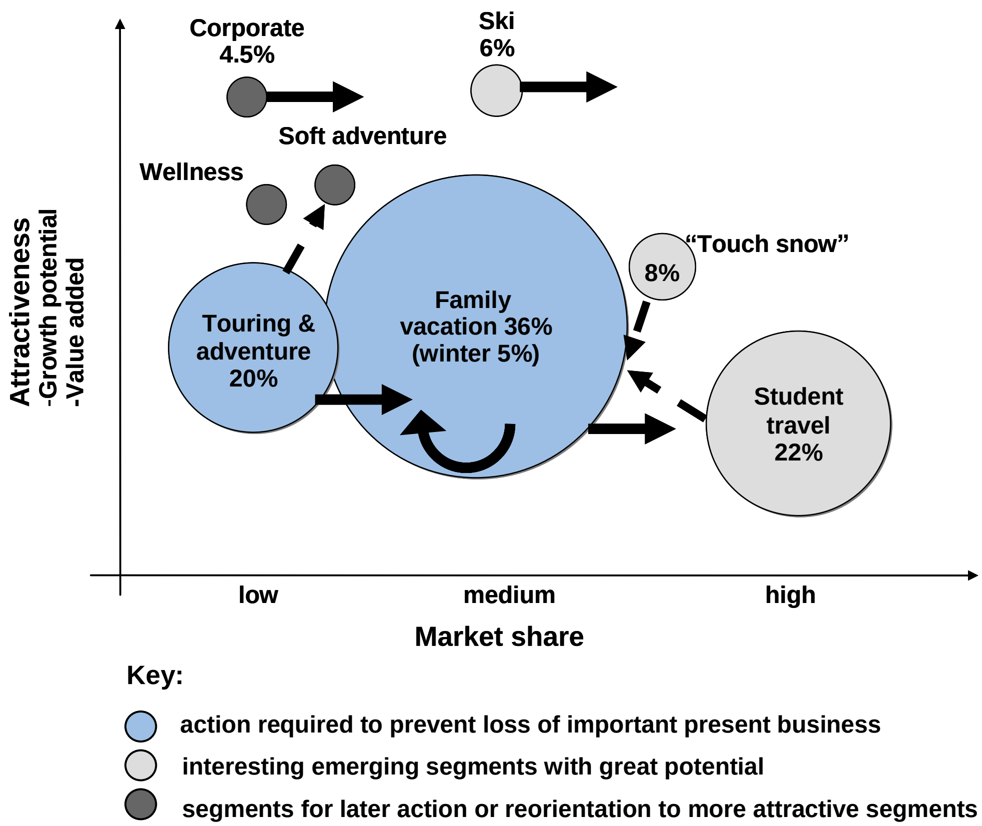
Between November 2006 and June 2007, *Competitiveness'* team applied its proprietary methodology, working intensively in Bariloche with a value chain approach. While it is difficult to draw a clear value chain for "tourism" with a broad definition, segmenting further—grouping businesses associated with various tourist motivations—can facilitate analysis.

[2] Source: FASTA University, 2007

[3] Micro and small enterprises are broadly defined in Argentina as those with less than 40 employees.

By analyzing each segment's contribution to the industry's turnover (represented by the relative size of the circle in Figure 2, below), the market share already attained and each segment's specific attractiveness (both in terms of growth potential and value added), it became much easier to assess the threats faced by businesses in the family vacation segment or those catering to international touring or pure adventure travel, as well as the opportunities that could be harnessed by addressing other niche segments where Bariloche had a competitive advantage.[4]

**Figure 2. Comparison of Various Tourism Segments in Bariloche**




Segmenting by tourist motivation also led to the identification of very different end markets. Student travel, for instance, is dominated by large, specialized agencies in Buenos Aires with strong negotiating power, and international touring is in the hands of large tour operators from Europe or the US. For other segments, it was important to understand the purchasing criteria of small agencies in Buenos Aires specialized in corporate tourism, or the highly specialized channels through which wellness[5] products need to be offered.

A thorough analysis of Bariloche's opportunities enables stakeholders to choose where to focus, and—just as importantly—where not to focus. For example, interviewing Brazil's top travel agency for skiers made it clear that it would be difficult for Bariloche to reposition itself as a top skiers' destination due to a deteriorated image and, more importantly, its poor snow quality as compared to other ski resorts in Latin America (a result of

[4] Source: Own estimation based on official statistics and primary and secondary research. The strategic recommendation included increasing market share in those segments with the highest attractiveness (the horizontal arrows in the graph), and retaining the high market share in family vacation, where most of the income is currently generated.

[5] Wellness tourism is understood as travel for the primary purpose of achieving a sense of wellbeing of both body and mind, with activities such as yoga, meditation, massage, etc.

altitude and changing climate patterns) and the significant investments that would be required to expand lodging facilities at the ski resort's base.

Analyzing the corporate tourism segment, it was obvious that Bariloche could not compete in large-scale events as, not only did it lack a convention centre or easy accessibility for large numbers of delegates to a congress, but it did not even have enough four- and five-star accommodation to absorb events above 600 people. For small and medium-scale corporate events, however, the key success factors were varied, and the top reason for specialized corporate event organizers choosing a destination was the innovation factor it could offer. World trends in this segment also showed that these types of events often had an important component of team building, where innovative activities became the differential issue. Bariloche, with some of the best adventure travel operators in the Southern Cone, could certainly have something innovative to offer.

The full project in Bariloche covered niche segments as well as more cross-cutting areas that required strengthening—particularly those associated with the largest group of tourists to the area: families (Argentinean and Chilean) that travel independently. These cross-cutting areas included information coordination amongst different public-sector institutions, quality assurance and promotion. This section explores how the results of the strategic analysis were transmitted to the key stakeholders through an intensive change management process within the specific segment of corporate tourism.

## CHANGE MANAGEMENT BASED ON SOLID ANALYSIS

During the seven months of the intensive phase of the project, *Competitiveness'* team interviewed both large and small players, four- and five-star hotels and various travel agencies. During the first couple of months, whenever companies were questioned about the opportunities in corporate tourism, the only response they gave was that Bariloche needed a large convention center, which had been promised by the local authorities for the past ten years. As with any other area requiring public sector involvement, the private sector's *attitude* was that of disbelief and resignation, cursing a situation that could not be avoided.

As the analysis progressed, it became clear that the conventional wisdom was biased by a crisis setting in the middle of the 1990s when all hotel beds had been empty. Considering the solid data on market trends, buyer purchase criteria, key success factors and the market opportunity that could be seized, a small group of leading companies began to *believe* that something could be done to significantly impact their bottom line if hotels, specialized agencies and active tourism providers came together around a common goal. This small group included agents representative of the value chain, such as the Hotel Llao Llao (part of The Leading Hotels of the World)—a five-star hotel that is an icon in itself; Extremo Sur—the first rafting company set up in Patagonia 15 years ago; and Aukaché—a small start up with less than 10 people that was already catering to this specific niche market based on creativity and the excellence of its service. All of these companies, and 15 others that took part in the workgroup meetings where the specific actions for this niche segment were drawn up, already had an idea of the potential for growth in this market. Some of them had been investing on their own, trying to convince potential clients that Bariloche was the place to look for the type of service they needed, but had had very limited results. Repositioning Bariloche in the eyes of a specialized end market was too costly for one single company to do alone, and even if such an investment could be undertaken by the Llao Llao, for instance, there were other factors that could limit the impact of such efforts, and that needed to be addressed with a combined effort.

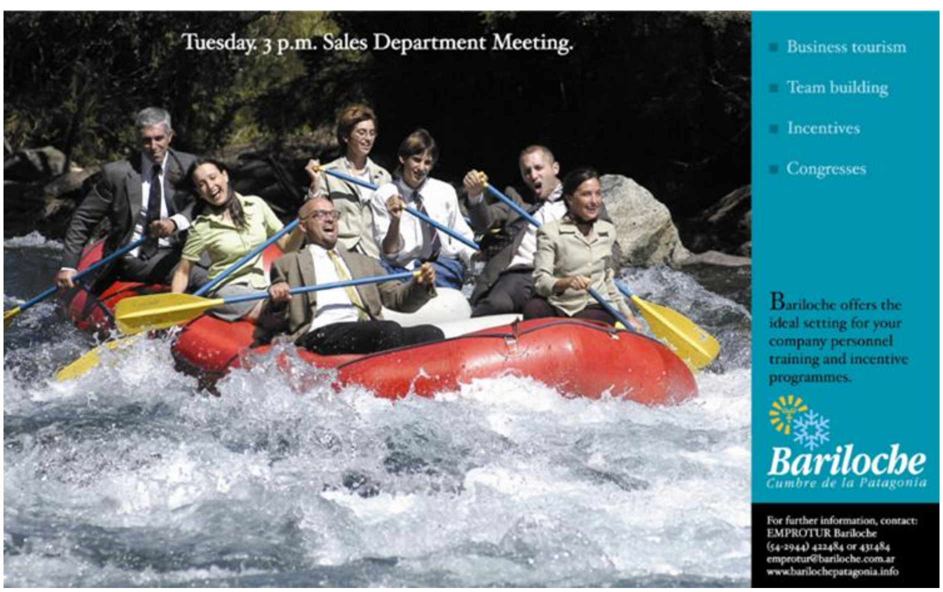
The discussions that took place during intensive workgroup meetings over a three-month period focused on fully taking into consideration the implications of this reality, identifying the main constraints that were hampering the development of this segment and defining very clear actions that needed to be undertaken in order to overcome these constraints. This small group of what could be defined as catalytic firms expressed their full commitment to the action plan that was defined. Companies that had not participated in previous efforts changed their *behavior* and were present at every workgroup meeting speaking up, endorsing the work of the group, and committing to further investment of their time and resources to contribute to the necessary changes.

## ONE YEAR ON: HAS THERE BEEN A CHANGE?

Over the past year, work has been progressing in the different action lines that were defined together with key stakeholders and presented to over 200 participants at the last public presentation of the initiative in June 2007. Some of the more notable changes have been in the area of destination coordination: 12 public and private sector institutions have committed to undertake the required efforts to make Bariloche a friendlier place for the independent tourist arriving into town, with better coordination of information, efforts to improve urban areas and the establishment of a tourist bus with eco-friendly technology to tour the main sights in an organized route. In spite of political instability and elections at the different administrative levels (local, provincial and national), the key institutional players are still convinced that they have a great deal to lose if this coordination does not take place.

In the specific area of (active) corporate tourism, 24 companies have signed up to the new "Bariloche Corporate Office", a lean institution established to further the different tasks that had been assigned, with marketing efforts underway to devise a new image for this specific product; negotiations with one of the major airlines to influence air routes, schedules and tariffs; and regular interaction between hoteliers, agencies and active tourism providers to define the most innovative efforts that this unique destination can offer.

**Figure 3. Part of the Marketing Efforts of Bariloche's Corporate Tourism Segment**



# IV. STRATEGY ANALYSIS: THE CASE OF AVOCADOS IN VALPARAÍSO, CHILE

## THE CHALLENGES OF A COMPETITIVENESS REINFORCEMENT INITIATIVE

Valparaiso's project has very ambitious goals: not only does it aim to reinforce the competitiveness of a key sector that is being threatened by a number of factors, it also has to help position the new Regional Development Agency of Valparaiso (RDAV) in the eyes of the region's private and public sectors. This objective is framed in the context of a historical process whereby Chile's traditionally centralized public policy decisions are now being transferred away from Santiago de Chile. When President Michelle Bachelet assumed office in 2006 she created the Regional Development Agencies in order to improve the competitiveness of the Chilean economy because the existing public instruments were not able to adjust to regional needs. *Competitiveness* has supported this process by transferring its proprietary methodology to new teams in seven Regional Development Agencies in Chile.

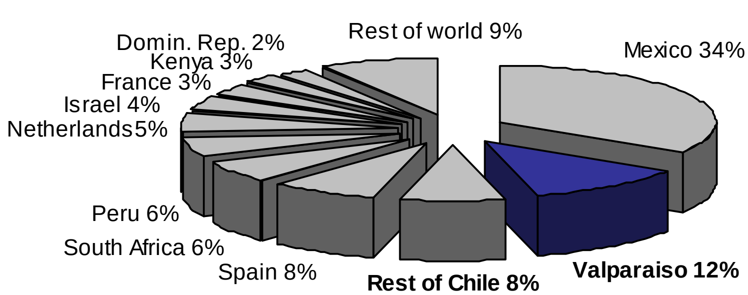
With the assistance of *Competitiveness'* tutors, the RDAV's specialized team began the project by interviewing the individual key actors in the avocado industry and presenting the RDAV as a new type of public-private institution with a well-structured working plan. Through the engagement achieved during the first interviews, the RDAV reached a higher level of dialogue and trust with local companies, breaking away from the traditional demand push of other national-level public services. Companies showed their commitment by supporting this new initiative and taking part of the process.

The RDAV's work, however, was not only different in its approach to companies, but also in the way it analyzed the industry, with *Competitiveness'* support—understanding international trends, end markets and the strategic options available for the companies in Valparaiso, in addition to the implications for the regional value chain.

## AVOCADOS IN VALPARAISO

Chile is well known for its "ecological island" conditions—free of bugs, plagues and diseases. It is also a safe and stable country with very favorable Free Trade Agreements. It is the leading fruit exporter in the southern hemisphere, and fourth worldwide. Valparaiso Region is located in the center of Chile and is known for its agricultural valleys and its port city. Valparaiso, with 60 percent of national production and export of avocados, is the world's second exporter of avocados, after México (see Figure 4, below). In fact, 42 percent of Valparaiso's 324,279 planted hectares are devoted to avocado.

**Figure 4. World Avocado Exports**



There are 4,000 producers in Valparaiso, and 10 exporters are based in the region. Four of the main exporters partner together to rent ships and export 73 percent of the region's avocado production. This concentration of distribution leaves producers in a passive position, accepting exporters' conditions: a 17 percent margin for aggregating production, very limited risk, and payment to producers 6 months after receiving their produce. The exporters' dominant position is reinforced by the Hass Avocado Committee, which is in charge of promotion and is funded on a mandatory fee per ton exported. Export markets are concentrated in the USA (72 percent) and the European Union (24 percent).

Chile was the pioneer in the avocado business in the southern hemisphere. In 1985 there were 71,000 hectares planted with avocado; the last census showed an increase of 89 percent over the past 20 years, and an annual average growth in avocado exports of 17 percent in the last 10 years. For many years, the only southern hemisphere competitor internationally was South Africa, but the battle was not fierce because of a focus on different markets: South Africa on Europe and Chile on the USA. Lately, however, the high profitability of the avocado business has awoken the interest of other countries:

- ***México*** is the world's number one producer (34 percent of the total), with the highest productivity per hectare and has traditionally focused on national consumption. Exports to Europe have been irregular because Mexico's humid climate introduces technical difficulties in transporting the fruit long distances in good condition. Since 2005 Mexico has been allowed to export avocados to all the states in the USA. With such a short travel time, Mexican producers have the flexibility to respond to opportunity windows in the USA in just a few hours.

- ***Peru*** has recently entered the European market competing with Chile in the same season but with lower production costs. Although Peru is new to the business and has poorer sanitary conditions, in the 2007/2008 season they significantly increased their exports to Europe. Peru does not have permission to sell in the USA yet, but this should be obtained by 2010.

With tough competition internationally, Chile's Hass Avocado Committee is making a concerted effort to promote the consumption of avocados in Europe. Avocados are considered by Europeans as an exotic fruit (except by the French and Spanish), and they do not know when or how to eat it. Europeans prefer the Fuerte variety of avocado because the skin is green while Hass avocados have black skin, which is generally associated with an overripe fruit.

In addition to a more competitive international market, Chile is losing profits because of the appreciation of the Chilean peso, an increase in production costs and the impact of the last frost. The situation at the time of the RDAV's project is therefore critical and surely demands creative strategies.

## STRATEGIC ANALYSIS

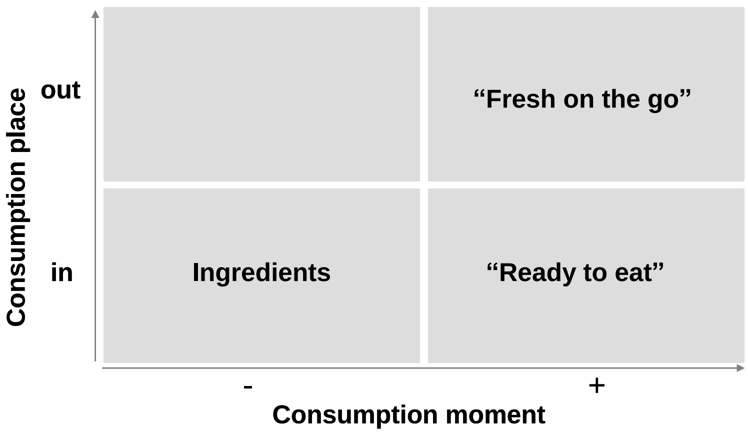
*Competitiveness'* involvement in the project has been vital not only in providing the methodological tools to the RDAV's team, but also because its neutrality provides a view which is not influenced by local conventional wisdom.

As a key part of the strategic analysis, *Competitiveness* organized a reference trip to the Netherlands because of their excellence in logistics and their leadership in related R&D: the Netherlands' food industry invests 2 percent of its turnover in applied research, making it the country with the largest investment per capita. The trip allowed the team to analyze two critical issues:

- ***Imports and logistics***—innovative trends discussed with experts directly in the field.
- ***Added value***—the opportunity for Chile lies in fresh product with ready meals[6]. Mexico is more efficient than Chile for processed avocados, either as food (frozen) or for other applications such as cosmetics, oils, etc.

After meeting experts in post-harvest, logistics, ripening centers and distributors in the Netherlands, the strategic segments in the fresh avocado business were differentiated depending on the place (in or out of the house) and moment of consumption (ripe, unripe).

**Figure 5. Fresh Avocado Market Segments**




- ***Ingredients:*** the fruit is sold to a consumer that does not know the proper time for its consumption (there is no control over the ripening process), or how it can be consumed. The fruit is considered to be an ingredient to have in the kitchen.
- ***Ready to eat:*** the fruit is sold at the right moment for its consumption.
- ***Fresh on the go:*** the fruit is sold ready to be consumed (included, for example, in a salad). It can be considered as a ready meal.

In the "Ingredient" business segment, producers have low bargaining power, there is no differentiation and the market is dominated by the intermediaries, leaving the producers with low profit margins.

The "Ready to Eat" segment provides better margins because the value chain is more complex as it needs ripening at the point of destination. The fruit needs to be of a higher quality and it requires more technology to control ripening. Producers therefore assume a more prominent role and intermediaries need to maintain a stable relationship with them. The market opportunity for this segment today is in Europe, importing through the Netherlands as the center of distribution with ripening facilities. Avocados in Europe are commercialized as "exotic fruits" because they are not part of the traditional diet, so a "Ready to Eat" avocado implies selling the service of knowing when and how to eat it. This product is 30 percent more expensive than the "ingredient".

[6] *Ready meals* are meals that have already been cooked or prepared and are sold ready to eat. In order to compete in this business there are higher requirements in terms of quality control and the lean logistics involved in distribution.

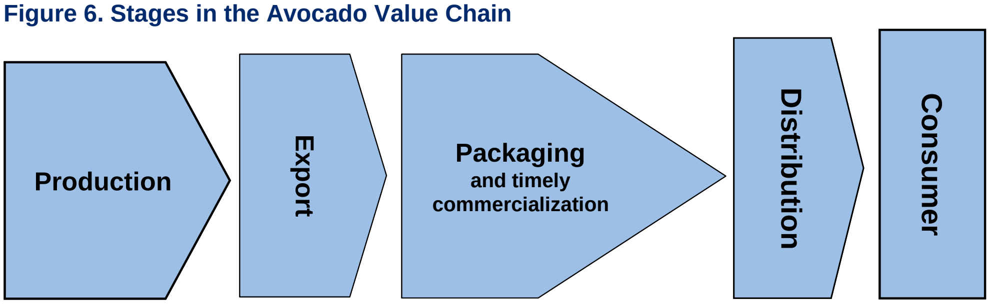
The "Fresh on the go" segment is even more complex, adapting the products, processed and with a convenience format to eat outside of the house. This segment requires a specialized distribution that is adjusted to retail or small markets.

The strategic recommendation for the companies involved in the avocado value chain in Valparaiso is to shift from selling an "Ingredient" to providing avocados that are "Ready to Eat". Once they can get closer to the European market through the "Ready to eat" segment, Valparaiso will be able to focus on more attractive segments such as "fresh on the go".

## IMPLICATIONS OF THE STRATEGY THROUGHOUT THE VALUE CHAIN

Following this strategic recommendation requires significant adjustments in the existing value chain. The explanation below compares the characteristics of the value chain for the "Ready to Eat" segment (in italics) with those of the current value chain in Valparaiso, for the "ingredient" segment.

**Figure 6. Stages in the Avocado Value Chain**




**Production**

*In order to compete in the "Ready to Eat" segment, producers need to improve fruit quality standards by controlling harvest and post-harvest procedures with upmost precision, to obtain a homogenous ripening and control of the ready ripening stage.*

Valparaiso presently grows heterogeneous fruits, the production process is not precise and producers do not have stable relationships with exporters. Fruits are not necessarily harvested at the best ripening stage; they are collected when it is most convenient for the exporter, who is more concerned about shipping schedules than about the quality of the exported products.

**Export**

*In the "Ready to Eat" business it is very important to control with precision the ripening process; a quality management system is therefore required.*

Valparaiso's avocado business today does not have accurate information about the ripening process of the fruit: 30 percent of the fruit is being exported without certification, while the other 70 percent is verified by the Hass Avocado Committee, which analyzes the fruit but cannot stop an exporter from selling it. Unfortunately the Committee is not a neutral evaluator, as it is both judge and part of the business. The logistics process is not adequately managed: a shift would be needed from counting the process in terms of weeks to a process in terms of days in order to maintain strict control of the ripening process.

**Ripening Center and Packaging**

*The "Ready to Eat" avocado value chain adds a new component: the Ripening Center at destination, where the fruit can be artificially ripened. The packaging also changes because this product is commercialized by unit instead of by loose kilo. The "Ready* *to Eat" avocado does not require the consumer to touch the fruit in order to verify the ripening, and the packaging format should be simple as it will not be stocked for long.*

Valparaiso companies presently do not even consider ripening at destination because avocados are commercialized in bulk with an unspecified ripening stage.

### Distribution

*The distribution also changes in the "Ready to Eat" segment, where deliveries are smaller and must be carried out at the exact time of ripening for each final destination.*

Currently Valparaíso is distributing through traditional logistic and distribution channels.

### Consumer

*The consumer of the ¨Ready to Eat¨ avocado buys a fruit with assured quality, exact ripening and convenient format. The consumer does not need to know when to eat it, so it is ideal for attracting new consumers. The packaging could also include a legend with recipes and the nutritional aspects of the avocado.*

The consumer of the ¨Ingredient¨ avocado needs to know the right moment of ripening, and a new consumer will have to guess it, having a high probability of error, leading to a negative experience.

### Areas for improvement

Through the thorough strategic analysis and intensive change management process, the RDAV, assisted by *Competitiveness*, leads the private and public sector workgroups that were set up to improve the key areas that are required in order to allow companies to follow the right strategies and upgrade the value chain.

- ***Quality:*** The objective of this workgroup is to assure fruit quality in line with European market requirements for the "Ready to Eat" segment. This group includes producers, certification companies and support institutions.
- ***Logistics and ripening:*** The objective of this group is to ensure and control the ripening at destination, by analyzing the logistic process and designing and implementing the management system.
- ***New consumers:*** The objective of this group is to design a focused promotion plan for this specific segment in order to educate new consumers as to when and how to consume "Ready to Eat" avocados.

This project is presently under finalization, fine-tuning action lines, but to date there has been an excellent response from the companies and institutions involved. Ten of the more innovative producers are willing to join together in an export consortium to develop the "Ready to Eat" segment. The most important university of Valparaiso has engaged in the R&D for assuring the quality of the fruit, and conversations are underway with a Belgian ripening agent and distributor.