Industry Case Studies

Use this information to complete a graphic equation for your industry.

Cereal Industry, 1990s

The breakfast cereal industry has a history of being highly concentrated. In 1999, for example, the four largest firms controlled much of the market share. Kellogg's led the industry with a 32% market share, followed by General Mills at 31%, Post at 16%, and Quaker at 9%. Cereal prices were well above the cost of production. A price hike by one firm was typically matched by price hikes from the others. In fact, the Bureau of Labor Statistics found that the price of cereal increased 90% from 1983 to 1995. This was two times the rate for other foods. This increase was in spite of the fact that the price of other factors of production, such as ingredients, had gone down.

Each year, the big four firms heavily advertised and distributed millions of coupons to promote consumer loyalty. In 1993, the cereal industry aired more than 1.3 million advertisements. These ads cost $762 million dollars a day (second only to the money spent on car ads). Through this advertising, cereal firms and their brands achieved an impressive level of name recognition. Cartoon characters related to the cereals, such as Snap! Crackle! and Pop! and Tony the Tiger, have become embedded in the minds of children and adults.

Firms also used a strategy of product proliferation. They created an enormous number of brands to cover every possible niche in the market. In this way, they were able to squeeze out new, small firms. For example, at one point General Mills's Web site boasted more than 65 varieties of breakfast cereal, Kellogg's had more than 45, and Post listed more than 25. By offering so many brands, cereal firms marketed the same core product but with dozens of small variations as a means to limit competition.

Many consumers complained about inflated cereal prices. They even asked the Federal Trade Commission to investigate alleged collusion in 1972. However, the major cereal firms prevailed, partially by contending that they offer coupons to offset rising prices.

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Fast Food Industry, 2000s

In 2006, fast food was a $142.9 billion industry that included an array of restaurants battling over narrow profit margins. The table shows 2006 sales for the largest firms in the fast food industry.

Fast Food Sales (in billions), 2006

Sandwich Sales	
McDonald's	$27.1
Burger King	8.3
Wendy's	7.8
Subway	7.7
Taco Bell	6.0

Pizza Sales	
Pizza Hut	$5.2
Domino's Pizza	3.2
Papa John's	1.9

Chicken Sales	
KFC	$5.2
Chick-fil-A	2.3
Popeyes	1.5

All **other** fast food firms: $66.7 billion

Many entrepreneurs jumped into the restaurant industry. This was often because of the potential for relatively quick profits. For example, Don Pablo's franchise was a popular Tex-Mex chain restaurant in the central, southeastern, and eastern United States. To open a new Don Pablo's franchise in 1998, start-up costs ran approximately $3 million. However, in that same year, the average Don Pablo's restaurant recorded $4 million in sales.

Franchising was also a popular method of breaking into the fast food industry. Rather than creating a whole new restaurant chain, an individual was given the right to open a store using the parent company's name, product, and management system. Franchises also profited from national advertising for the chain.

Firms often used price discounting to undercut competitors. Indeed, in 2000, 82% of restaurant owners said they used special weekly or monthly price rates. Another 79% said they used bundled "value" meals to boost profits by getting customers to buy more than one item at a time.

Although firms sometimes competed by dropping prices and adding to menus, those practices tended to eat away profits. A more effective method of competition was to spend substantial sums on advertising to emphasize how a company differed from the competition. Firms also differentiated themselves by researching and designing new items. Such items included breakfast foods, premium sandwiches, and "health conscious" selections, such as salads, fruit cups, and baked potatoes.

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Diamond Industry, 1980s

The high demand for diamonds in the late 1980s was driven primarily by the marketing efforts of De Beers Consolidated Mines. This South African company controlled more than 80% of the world diamond market. As an example of its power in the market, De Beers had convinced the Japanese public that giving a diamond ring is a necessary part of an engagement. This idea had already been successfully sold to U.S. consumers decades earlier.

De Beers surprised some economists when it enacted a steep price increase of 15.5% in 1989. This was on the heels of two previous increases—13.5% in 1988 and 10% in 1987. The most remarkable aspect about the ability of De Beers to increase prices at will in the late 1980s was that many believed that De Beers's control of the diamond market had been slipping during the early 1980s. However, De Beers had survived the tough times. It did so by buying diamonds at a high price and stockpiling them to keep world supply levels low. This created an artificial shortage. Their stockpile grew from $360 million worth of diamonds in 1979 to almost $2 billion by 1984.

When a discovery of considerable diamond deposits in Australia threatened to increase the supply of diamonds, De Beers exercised its power. It convinced the Australian mine to sign a contract with the Central Selling Organization. This organization was owned by De Beers. By agreeing to sell through the CSO, the new mine earned greater profits. If it had instead competed on the open market, it would have lowered everyone's prices. In addition, De Beers was able to continue its dominance of the diamond market.

De Beers connected diamonds to romance and eternal love through advertising campaigns (such as "A Diamond Is Forever") and movie star endorsements. In so doing, De Beers created demand for a unique, sentimental item that could never be resold. The result in the 1980s was that diamonds were kept off the market, and limited supply kept prices elevated.

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Automobile Industry, 1950s

General Motors (GM), Ford, and Chrysler dominated the automobile industry in the 1950s. These three firms were known as the "Big Three." In 1954, they had approximately a 52%, 31%, and 13% market share, respectively, of passenger car production. The remaining four automobile companies fought for no more than a 4% market share. Many of these smaller companies were desperately merging in an attempt to compete with the Big Three.

Why was it so difficult for smaller companies to compete? Auto manufacturing had always involved massive investment in research and development. It had also involved large sums of capital for building factories and buying machinery. The Big Three's substantial bargaining power gave them advantages in buying steel and other inputs of production at lower prices. They also had a strong grip on auto dealers. They were sometimes accused of "forcing dealers to purchase unwanted cars, parts, and accessories." Furthermore, strong labor unions used collective bargaining and strikes to push for higher wages. Ironically, the larger auto companies could absorb higher worker wages by simply increasing their prices and their volume of production. The smaller companies could not compete. They were often forced to go out of business.

In the 1950s, Congress investigated U.S. automobile producers for possible price collusion. In one hearing, the leader of the United Auto Workers union claimed that GM essentially set industry prices. He said, "no other firm [could] price substantially higher, for fear of loss of sales, and none [dared] price substantially lower for fear of retaliation." Indeed, from about 1947 to 1957, Ford saw a 256% increase in profits, GM a 234% increase, and Chrysler a 167% increase. And yet the price of automobiles was not always increasing during this time. In fact, Congress enacted a price freeze during the Korean War (1950–1953). In addition, automakers chose to decrease prices in 1955 to help reduce a surplus of cars.

Reacting to consumer demand, the Big Three furiously competed to develop new technologies. These included automatic transmissions, air conditioning, radios, power seats, and power windows. They also developed numerous brand names and makes of cars. For example, Chevrolet, Cadillac, Buick, Pontiac, and Oldsmobile were all GM brands. Automakers also created a variety of styles, as illustrated by 1954 car sales: 47% of cars sold were four-door sedans, 27% were two-door sedans, 17% were hard tops, 3% were convertibles, and 6% were station wagons.

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Telephone Industry, 1910s–1980s

AT&T proudly claims that the company's history "is in large measure the history of the telephone in the United States." Founded by Alexander Graham Bell, the American Telegraph and Telephone Company was the parent of the Bell System for almost a century. At the time, it was argued that the very nature of telephone technology—that is, the need for physically connected wires—meant that the industry would operate most efficiently with only one provider. Facing the possibility of an antitrust investigation by Congress, AT&T negotiated the Kingsbury Commitment in 1913. In this agreement, AT&T agreed to allow independent telephone companies to connect with the AT&T network. However, AT&T remained the sole long-distance telephone service supplier in the nation.

During the 1910s, AT&T researched several new technologies. These included underground cables, which provided weather protection and could carry more wires in less space. Another technology was carrier-current systems, which allowed multiple calls to travel down one pair of wires. However, the primary goal of AT&T in this decade was to connect the entire nation through a transcontinental telephone line. This feat was impossible in 1910. Telephone signals were too weak to travel such a distance. AT&T hired physicists to study the problem. The company also advertised that it would pay large sums of money if someone could invent a device that would amplify electrical signals. Dr. Lee de Forest and Dr. Harold Arnold successfully invented an electrical amplifier. AT&T bought the patent rights. The Bell System completed the first coast-to-coast telephone line, from New York to San Francisco, in 1915.

In 1918, the U.S. government nationalized, or took control of, the telephone, telegraph, and cable networks due to national security issues related to World War I. This turned out to be in AT&T's favor. During nationalization, AT&T worked closely with the government to ensure that the operation worked smoothly. In addition, AT&T convinced federal and state governments to raise rates. By the time AT&T was given back its network, long-distance rates had increased 20%, with the majority of the money going directly to AT&T.

Changes in telecommunications eventually led to another antitrust suit. This suit was settled in 1982. At this point, AT&T agreed to break up the Bell System. AT&T's natural monopoly argument no longer seemed valid. Long-distance service became intensely competitive. AT&T's market share fell from over 90% in 1984 to 50% in 1996. Prices also dropped drastically, as the volume of telephone calls rose steadily.

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Clothing Industry, 1990s

Known as the apparel industry in the business world, the clothing industry was large and extremely fragmented in the 1990s. Broad categories of apparel included clothing for business, sports, and casual wear.

The $169 billion market was divided into two tiers. The first was national brands (about 20 large companies), which accounted for about 30% of sales. The second was other apparel (hundreds of small brands and private-label store goods), which accounted for about 70% of sales. Some of the largest and most well-known apparel companies in 1997 were Liz Claiborne ($2.4 billion in sales), Fruit of the Loom ($2.1 billion), and Polo Ralph Lauren ($1.5 billion).

The clothing industry was characterized by

- simple technologies.
- a low cost of fixed assets (such as machinery and factory space).
- cheap, unskilled labor.
- use of outside contractors to do part of the work.

Getting into the industry was relatively uncomplicated. However, many small start-up companies ended up failing just as quickly. They were generally undercapitalized and faced intense advertising competition.

After holding steady during most of the 1990s, clothing prices began to drop in 1997. This is because apparel manufacturers began to cut labor costs by producing in Mexico, Central America, and Asia (especially China). Consumers also had a substantial influence over clothing prices, as they could easily switch from one brand to another. However, clothing producers that were able to create a strong brand image were rewarded with an ability to somewhat manipulate their prices.

In the 1990s, clothing companies worked to gain a competitive advantage by differentiating their products from competitors. This was often done through creating new product lines that met changing consumer tastes or fashion trends. Apparel companies also increased their marketing and promotional activities to create strong brand names. Once a brand name was solidified (such as Calvin Klein or Tommy Hilfiger), companies could add accessory lines, such as sunglasses, watches, and fragrances.

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Film Production Industry, 2000s

In 2006, consumers around the world spent $43 billion on U.S. movies. In North America, a handful of film production and distribution companies accounted for approximately 70% of domestic box office revenues. For example, the 2006 domestic box office market share broke down as follows: Sony Pictures at 18.6%, Buena Vista (Walt Disney Pictures) at 16.2%, 20th Century Fox at 15.2%, Warner Bros. at 11.6%, and Paramount Pictures at 10.3%. Market shares often fluctuated, depending on the success of the movies produced by each studio.

Many consumers in the early 2000s noticed that movie ticket prices were continually increasing. And yet box office revenues stagnated due to decreasing ticket sales, as shown in the table. Film production companies received about half of these revenues. The other half went to movie theater operators.

U.S. Film Production Industry Profile, 2002–2006

Year	Box Office Revenues (in billions)	Paid Admissions (billions of tickets sold)	Average Ticket Price
2002	$9.52	1.64	$5.81
2004	9.54	1.54	6.21
2006	9.49	1.45	6.55

Source: Motion Picture Association of America, as reported in Standard & Poor's Industry Surveys.

In 2006, the average cost to create a movie was more than $100 million. About one-third of this was marketing costs. Only 4 out of 10 movies actually recouped their initial investments at the box office. Once in a while, a low-budget, independent movie would have a surprise run. *My Big Fat Greek Wedding* (2002) cost only about $5 million to produce but generated $241 million in U.S. box office sales. Independent filmmakers could certainly jump into the business, but the risks were high and success was rare.

Consequently, the industry consisted of a few large, diversified companies. The companies spread their risk by producing thousands of movies. In addition, they used their brand name (such as Warner Bros.) to attract the best creative talent, including actors and directors. These large companies also created a cash flow from TV and DVD sales of older movies. This gave them funds to invest in new projects.

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Beauty Salon and Barbershop Industry, 1990s

By the end of the 1990s, there were more than 520,000 beauty salons and barbershops in the United States. This was a noticeable 25% increase in just 10 years. The development of no-payroll shops, in which stylists and barbers lease their workstations, made it easier than ever to open a new shop. No-payroll shops are typically small and have lower profit margins (approximately $20,000 annually). They accounted for almost all new salon and barbershops in the 1990s.

Industry leaders had to compete with the onslaught of small shops. To do so, they made significant acquisitions and merged companies so that they could benefit from stronger economies of scale. These industry leaders—such as Regis Corporation, which includes Supercuts, Cost Cutters, and Master-Cuts—saw increased worker productivity and profit margins. However, the top four beauty salon and barbershop chains still held a market share of only 6.3% by 1999. This was up from $4.0% in 1992. Furthermore, the 50 largest companies combined made up only 9.7% of total industry revenues, up from 7.3% in 1992.

Beauty salon and barbershop revenues continued to increase during the 1990s: $16.0 billion in 1992, $20.1 billion in 1997, and $22.1 billion in 1999. This growth occurred in a number of areas, including

- an increasing number of female customers over the age of 40.
- a larger number of male customers.
- an increased reliance on product sales such as shampoos, hair conditioners, and hair sprays.

Salons also attempted to make their stores more male-friendly. They created new chains, such as Sports Clips, that specifically targeted men. As a result, the increase of dollars from men increased the market share of beauty salons to 91.4%, while barbershops fell to 8.6%. In addition, shops—especially larger businesses *with* payroll—increased their reliance on retail merchandise product sales. During 1999, sales of merchandise reached an estimated 9.5% of revenues, up from 4.2% in 1992. Regis Corporation estimated that product sales made up 27.9% of all company revenues that year. This helped the company make up for lower prices of salon services.

Creating a Graphic Equation of Your Industry's Market Structure

Work with your group to create a graphic equation. Your graphic equation must visually explain how your industry illustrates the four main characteristics of market structures. Have your teacher initial each step as you complete it.

Step 1: Assign roles. Review the roles and divide them among the members of your group. Make sure everyone understands his or her responsibilities.

Project Manager Leads the group during Step 2. Makes sure the four written summaries are consistent with their corresponding visuals. Requests teacher initials after each step.

Data Analyst Creates two appropriate graphs for the poster in Step 3.

Graphics Editor Creates two appropriate illustrations for the poster in Step 3.

Writer Writes a one- or two-sentence summary for each of the four visuals in Step 3.

Step 2: Learn about your assigned industry and decide which market structure it exemplifies. Read Student Handout A. Use information from your Reading Notes and the handout to complete these tasks as a group:

- Identify the four characteristics of market structures—number of producers, similarity of products, ease of entry, and control over prices—as they relate to your industry.
- Based on these characteristics, identify your industry's market structure.

Step 3: Brainstorm visuals for your graphic equation and create a rough draft of your poster. On the next page, sketch your graphic equation. Follow these steps:

- Review the sample graphic equation on the Visual.
- Decide the best way to visually demonstrate how the four characteristics of market structures apply to your industry. Include two graphs and two illustrations.
- For *each* characteristic, write a one- or two-sentence summary explaining how it uniquely functions in your industry. Make sure all four summaries relate to their accompanying graphs or illustrations.
- Do not use the name of your industry's market structure anywhere in your summaries. Your classmates will determine the market structure by examining your graphic equation.

Step 4: Create your poster. Draw your final graphic equation on poster paper. Include all the requirements from Step 3 to create a visually appealing poster.

Graphic Equation Layout

Name of Industry, Decade

Visual (graph or illustration)	Written Summary

Number of Producers

+

Visual (graph or illustration)	Written Summary

Similarity of Products

+

Visual (graph or illustration)	Written Summary

Easy of Entry

+

Visual (graph or illustration)	Written Summary

Control over Prices

= ?

Determining Market Structure

For each poster you examine, do the following:

- Record the industry and decade.
- Identify and explain how two of the market characteristics operate in that industry.
- Use information from the graphic equation and your Reading Notes to identify the industry's market structure.

Industry, Decade(s)	Market Characteristic and Evidence for It	Market Characteristic and Evidence for It	Market Structure

Industry, Decade(s)	Market Characteristic and Evidence for It	Market Characteristic and Evidence for It	Market Structure