Case Study: Apple—A Thousand "Nos" and Ten Gutsy "Yeses"

Dan Wood is founder of Karelia Software. His company logo shows two men pumping a handcar—the kind used to maintain rail tracks and resolve other right-of-way issues. The story behind the logo goes back to 2002.

According to *Mac Observer*, "You could see people mouthing the word Watson when Sherlock 3 was demonstrated at MACWORLD New York on July 17. Watson, an Internet services application, was originally released by Karelia Software back in November of 2001 as a complement to Apple's Sherlock search software."[12]

Wood had been called in to Apple prior to MACWORLD and shown Sherlock 3. On his blog he describes his reaction:

> I drove home, gradually realizing what I had just witnessed, and sent off an e-mail to my contact at Apple Developer Relations expressing my unhappy sentiments. An hour later, Steve Jobs called me.
>
> "Here's how I see it," Jobs said—I'm loosely paraphrasing. "You know those handcars, the little machines that people stand on and pump to move along on the train tracks? That's Karelia. Apple is the steam train that owns the tracks." So basically the message was: Get out of the way, kid; this is our market.[13]

Fast-forward to 2011.

Answering a question at the company's shareholder meeting, Apple's leader of iOS development, Scott Forstall, pointed out that Apple has, in the iOS App Store, "created the best economy in software in the history of the planet."[14]

If anything, Apple is now being accused of having allowed too many "handcars on its tracks." Trip Hawkins, once Apple's director of strategy and marketing, left the company in 1982 to found Electronic Arts and other start-ups. He now complains Apple has "overencouraged supply" in its App Store.[15]

The App Store is now considered such a strategic asset that Apple took the unusual step in 2011 of filing "to intervene in the lawsuits

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filed by patent troll Lodsys against iOS developers. If the court accepts Apple's request, then Lodsys is no longer just challenging a bunch of small developers, but will have to fight Apple's formidable legal team and storehouse of patents."[16]

Time and again Apple has shown willingness and ability to change course. It has mastered the art of being a maverick, challenging rules set by others, and defining its own rules.

Saying No to 1,000 Things

In a 2004 *BusinessWeek* interview, Jobs said, "And it comes from saying no to 1,000 things to make sure we don't get on the wrong track or try to do too much. We're always thinking about new markets we could enter, but it's only by saying no that you can concentrate on the things that are really important."[17]

In his biography of Steve Jobs, Walter Isaacson shows many examples of his amazing ability to cut through the clutter and "say no to 1,000 things." Apple's ability to say yes to plenty of gutsy, even maverick, decisions is what really defines its success.

Let's explore 10 (out of many more) high-risk and high-impact decisions Apple has made.

Popularizing MP3 Singles in Spite of the Music Industry

Think about it—our radio stations have long played popular singles. When we were younger many of us created cassettes of our favorite songs and played them on our Sony Walkmans and in our cars. The music industry preferred to sell us complete albums, then CDs.

While Apple did not invent MP3s, it dragged the music industry with iTunes to make it a big business.

Even today, though, many music executives long for the return of albums. They ignore the "long-tail" phenomenon. Consumers buy many more "one-hit wonders" than they would if they were not unbundled.

Here is an example of such music industry thinking:

> "Historically, the price of an album was five times greater than a single," said [Tom] Silverman [a music executive], who believes setting

> the price at a tenth of an album's cost was a mistake and that even $1.29 is too low. "It should've been $1.99, and then we would've seen higher digital album sales because it would've been a bigger discount for buying an album."[18]

Apple persisted. Over 15 billion songs—most of them singles—have been downloaded via iTunes and many more through other channels like Walmart.com.

An Ambitious Phone with Little Previous Phone History

Jobs explained to *Fortune* the rationale behind attempting the iPhone: "We realized that for almost all—maybe all—of future consumer electronics, the primary technology was going to be software. And we were pretty good at software" and "The reason that we were very excited about the phone, beyond that fact that we all hated our phones, was that we didn't see anyone else who could make that kind of contribution. None of the handset manufacturers really are strong in software."[19]

While all that is true, hundreds of other companies could say they are pretty good at software. Was that alone sufficient to make the iPhone so successful? Apple's previous collaboration with Motorola on its ROKR phone just a year prior had not been very successful.

There were many cynics. Verizon President and Chief Operating Officer Dennis Strigl said in 2006, "The iPhone product is something we are happy we aren't the first to market with." Verizon finally started supporting it in 2011.

Prof. Clayton Christensen, who has written treatises on disruptive technologies, was of the view that "Nokia, Samsung, LG, and Sony Ericsson have a lot to lose. You better believe that each of them has a skunk group dedicated to preparing a response to the iPhone. And since the iPhone is a high-end, high-cost product it leaves rivals an opportunity to create a more affordable version that's almost as good."[20]

Turns out the competition was unprepared. "The initial reaction from competitors, or soon-to-be competitors since Apple wasn't really in the game yet, was either shock or laughter. RIM didn't think it was possible to have such a device without it being a power hog. Microsoft's Steve Ballmer laughed at it for not having a physical keyboard."[21]

The iPhone was an audacious move on Apple's part given it was not a telecom insider. The rest, as they say, though, is history.

Signing Exclusive Multi-Year Deals with Carriers

When it introduced the iPhone in 2007, Apple signed exclusive arrangements with Cingular (later rebranded AT&T) for the U.S. market, O2 for the UK market, Orange for France, and other similar deals in other markets. The AT&T arrangement in particular caused Apple significant heartache as that network could not cope with the data demands the iPhone put on a network designed more for voice traffic. There were other customer issues due to outrageous international roaming charges and early termination and upgrade fees.

However, Apple was able to introduce with AT&T innovative features like Visual Voicemail and redefine the customer activation process.

> By allowing users to activate their iPhone from the comfort of their home or office, Apple is redefining the phone-buying experience.
>
> No more waiting at the store while a bumbling employee tries to get your phone registered with the carrier. No more hassling with said bumbling employee to transfer your old phone numbers to your new phone. Apple iTunes will walk you through a step-by-step process to do it all yourself![22]

The AT&T relationship came at a significant price. TechCrunch summarized: "I understand why Apple went exclusively with AT&T at first (though it had first offered the device to Verizon, which turned it down)—it got a pretty sweet deal, and was able to use it to put it in a position of power over the entire industry. And I even understand why they re-upped the first time—to get an even sweeter deal (the subsidy from AT&T for each phone sold). But now AT&T is a liability for Apple that will inhibit its huge potential for growth in the U.S."[23]

To its credit, Apple stuck with AT&T and continued even further, even as it brought Verizon in as an option.

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Contract Manufacturing Arrangement with Foxconn

In the 1990s, Apple made a strategic decision to deemphasize its own manufacturing. Metrics such as inventory turns did not look impressive especially when compared to Dell, which was then a paragon of efficiency. Plants in Ireland, Singapore, and the United States were outsourced. Tim Cook, now Apple's Chief Executive Officer, gets credit for that supply chain transition. Foxconn, the Taiwanese contract manufacturer, benefitted in particular from the outsourcing.

Apple has stayed loyal to Foxconn through multiple releases of iPods, iPhones, and iPads in spite of sweatshop accusations, employee suicides, and explosions in its Chinese facilities. Most companies like to diversify between company-owned and outsourced plants, and certainly across geographies. Apple has been willing to take the risk of putting its eggs in the Foxconn basket and taking plenty of jabs from China bashers (although Foxconn has recently been looking at a significant diversification to Brazil).

Over 200 million iOS devices sold to date, most assembled by Foxconn, justify the loyalty. Its regular audits of the supplier appear to confirm what Joel Johnson wrote in *Wired* magazine. This was after a visit to Foxconn facilities after the spate of employee suicides. "But the work itself isn't inhumane—unless you consider a repetitive, exhausting, and alienating workplace over which you have no influence or authority to be inhumane. And that would pretty much describe every single manufacturing or burger-flipping job ever."[24]

Investing in a Large Retail Operation

When Apple opened its first retail store in 2001, an observer commented, "I give them two years before they're turning out the lights on a very painful and expensive mistake."[25] Apple dealers were not happy. One of them said, "Apple might do just well enough to really hurt our business. They've also done a poor job telling us how sales and service will work when an Apple Store opens nearby."[26] There were others who questioned the timing in 2001 with the tech industry in a severe downturn. They drew parallels to PC maker Gateway's struggling retail effort.

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Apple, of course, has gone from strength to strength with its retail operations, as we describe further in Chapter 12. Over 230 million visitors entered one of Apple's over 300 stores around the world in 2010. In the ultimate compliment, Apple's SVP of Retail, Ron Johnson, was recruited in the summer of 2011 to become CEO of J.C. Penney. A decade after the first store was opened in Virginia, the Genius Bar at the stores really looks like a Genius move.

The iPad Decision after Many Industry Tablet Failures

When Apple introduced the iPad in 2010, it tried to reverse "more than two decades of (industry) attempts to get tablets right—none of which really succeeded, and some of which failed on a monumental scale."[27]

John Dean, former CIO of Steelcase and a big user of tablets himself for almost a decade, explained the challenge: "If I could get 15 minutes to spend with anyone, I could convert them to using a tablet. But I would only target those that were doing things where a tablet offered a better way." "When you mess with the physical interaction aspect of a technology, the change can be traumatic. We are stuck in a keyboard/text/formal content world with fingers (or thumbs) as the means of interaction."[28]

Others were harsher. A Dell executive said, "Apple (iPad) is great if you've got a lot of money and live on an island. It's not so great if you have to exist in a diverse, open, connected enterprise; simple things become quite complex."[29]

By June 2011, just 14 months after the iPad was introduced, Apple announced it had sold 25 million units and it had pretty much locked out competition from over 100 tablets that were launched in the wake of the iPad success.

Challenging Amazon in eBooks

Amazon has over the past decade become a dominant player in the book market. As eBooks started to grow in popularity over several years, Amazon had driven the market toward a $9.99 price point. At the iPad

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launch, Walt Mossberg of the *Wall Street Journal* asked Steve Jobs why people would pay more for the same book on an iPad. Jobs' response was "The prices will be the same."[30]

Apple had no intention of keeping prices that low, even though it was a trivial player in the book market compared to Amazon. Instead, it signaled to publishers it would accept an agency model that would give them more control over pricing. That precipitated a showdown between publishers and Amazon. Amazon ended up ceding price control to the publishers.

Venturebeat wrote, "The ten-dollar e-book may soon be gone, replaced by the fifteen-dollar eBook."

The Mind Games with Microsoft and Adobe

Starting in 2006, Apple ran the Mac versus PC commercial series.[31] It was a series that humiliated Microsoft across 66 commercials. Given the earlier statement that Apple is good at software, it could have tried to develop its own version of Microsoft Office. Its repeated badgering in that series could have annoyed Microsoft to give up on the Apple market.

The reality is Microsoft's continued development of Office products for the Mac has actually made transitions away from the PC easier for many. Phil Fersht, founder of the analyst firm Horses for Sources, says, "We have our whole firm on Macs now—we would likely have never considered that scenario if the Office suite wasn't available."

The attack on Adobe was even less subtle. Wrote Jobs: "Flash was created during the PC era—for PCs and mice. Flash is a successful business for Adobe, and we can understand why they want to push it beyond PCs. But the mobile era is about low power devices, touch interfaces, and open web standards—all areas where Flash falls short." And "New open standards created in the mobile era, such as HTML5, will win on mobile devices (and PCs too). Perhaps Adobe should focus more on creating great HTML5 tools for the future, and less on criticizing Apple for leaving the past behind."[32]

In November 2011, Adobe took his advice to heart and announced they would deemphasize Flash for mobile platforms. Apple, long called

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a "closed vendor," had actually driven the market toward HTML5, an open standard. How maverick is that?

Large-Scale Sourcing of Strategic Components

While many technology companies use cash reserves to make acquisitions, Apple has on many occasions used large sums of money to secure strategic components. In 2005, "Apple reached long-term supply agreements with a number of memory supply companies including Hynix, Intel, Micro, Samsung Electronics, and Toshiba. Apple will prepay up to $1.25 billion for flash memory over the next three months. The agreements secure a supply of NAND flash memory through 2010."[33]

In 2011 Apple announced, "During the September and December quarters, we executed long-term supply agreements with three vendors through which we expect to spend a total of approximately $3.9 billion in inventory component prepayment and capital expenditures over a two-year period."

Apple would not reveal the components or the suppliers, but such large commitments not only get them priority in tight markets but also freeze out competitors.

Doubling Down on the MobileMe Failure

At Apple's developer conference in June 2011, Jobs showed his sense of humor as he announced the iCloud service with this quip, "You might ask, why should I believe them? They are the ones who brought me MobileMe."

MobileMe was not one of Apple's best products. *Wired* magazine wrote: "Tech observers agree that MobileMe has been one of Apple's most embarrassingly flawed products, thanks to its extremely buggy launch and limited functionality. MobileMe was itself a 2008 rebranding of .Mac, which began its life in 2000 as iDisk."[34]

In fact, the industry view was that if Apple had a chink in its armor it was in web services—Amazon, Google, Facebook, and several others were far superior. In the months prior to the iCloud announcement,