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*Original Paper*

# Research on Enterprise Strategy Based on Porter's Five Forces Analysis Model—Taking Dick Smith as an example

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**Executive Summary**

This article firstly provides a brief introduction of Dick Smith. Then, the article analyze the general environment of Dick Smith, including economic trend, technological change and demographic impact. After that, the article identify the industry environment of Dick Smith, followed by analysis of issues in the competitive environment through identifying five forces of which. In addition, this report describes Dick Smith's current strategies. At last, the article explain the reasons why Dick Smith's strategies were unsustainable, and point out the main reason contributes to its strategic failure, loss of competitive advantage and final collapse. Though Dick Smith was one of the most popular retail brands in Australia, it didn't survive owing to its strategic failure, and was acquired by Kogan in 2016. Thus, it is essential to identify and analyze the strategic decision-making in Dick Smith, as which can be taken as a warning, and then help organizations develop effective ones, since only effective strategic plan and implementation can positively impact the performance of the organization (Hanson et al., 2017).

## 1. Introduction

Dick Smith, which was one of the largest electronic retailers in Australia, collapsed in 2016, within several years after the acquisition by Anchorage Capital. This report analyzes the reasons why strategies adopted by Dick Smith are unsustainable during the control of Anchorage Capital, and what are the impacts of general environment, industry and competitor environment, and internal environment on these strategies.

**2. General Environment**

Changes in the general environment have direct and indirect effects on all industries (Gupta, 2013). The Australian electronic retail industry was affected by several elements of the general environment back then, especially by economic, technological and demographic ones.

*2.1 Economic: Lowest Wage Growth Rate and Inflation*

From the perspective of economic impacts, the domestic economy of Australia is in recession during 2016, with the lower wage growth rate accompanied by the rising household spend, it leads to a decline of consumer confidence and a decrease in consumer spending. The wage growth rate has fallen to historical status, and the inflation rate increase to 1.7% at the first quarter of 2016, which illustrated by the following graph. Wage growth could not keep pace with inflation, leading to a drop in real wages, and the pressures on the lives of thousands of employees might continue to mount (Mehra, 1991), which decrease people's ability to purchase of goods as they have less wages relative to the higher cost of goods.

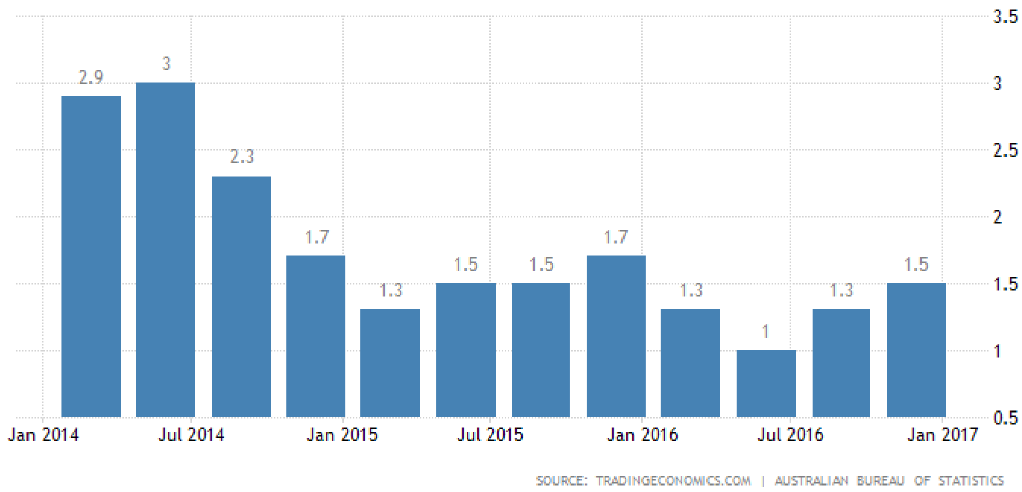



**Figure 1. Australia's Inflation Rate from 2014 to 2017**

The ANZ Bank's Australian Consumer Confidence Index which is provided by the Roy Morgan research and presented in the **Figure 2**, shows that the wage growth rate declined to the lowest level at the late 2015 and early 2016 (David, 2019). Consumer didn't hold the positive attitude about the overall state of the economy and their personal financial situation. Thus, they tend to save more and spend less, which would affect the sale electronic products.

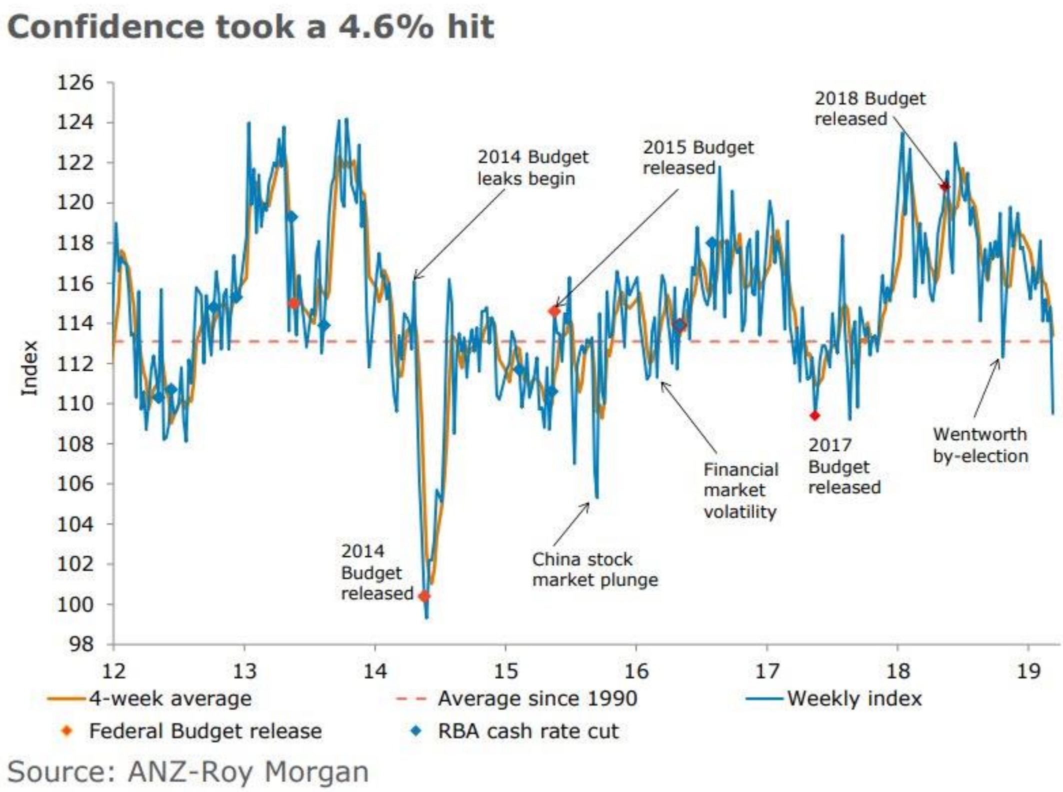
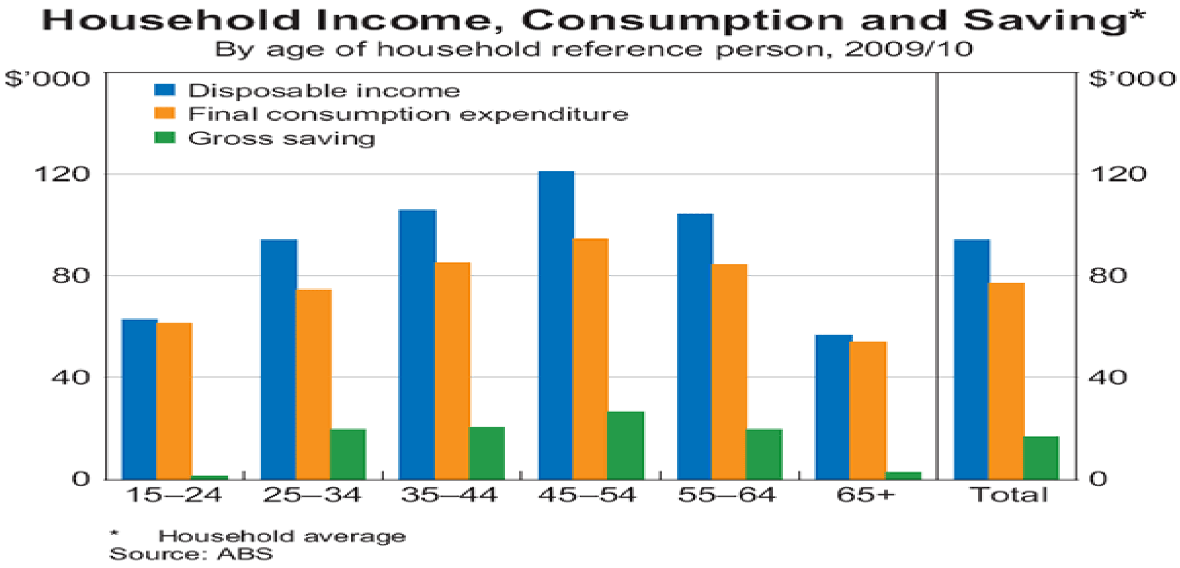
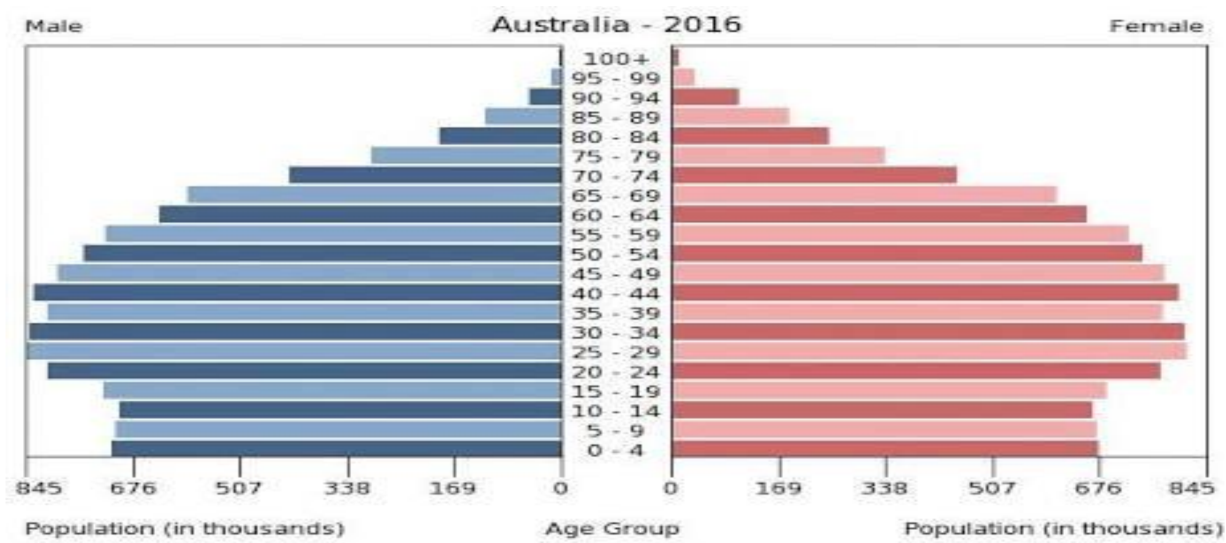



**Figure 2. The ANZ Bank's Australian Consumer Confidence Index**

*2.2 Technological and Demographic: Short Life Cycle and Innovation*

Technology change frequently, accordingly the electronic products have shorter life cycle. With the continuous improvement of technology, consumers' needs tend to be diversified. Their needs for electronic products can be described as multifarious. Moreover, the main consumer for electronic products is the younger generation, the age range of whom is between 15 and 34 as they have a comparatively high demand for new electronic products though with a relatively low income compared with the older generation, which is illustrated by the graphs below.




*2.3 Industry and Competitor Environment*

Dick Smith is an Australian electronics retail chain that specializes in all electronic items and belongs to the bricks-and-mortar electronics retailing in Australia. Since such an industry is unattractive, it is of vital importance for Dick Smith to understand the impacts of the industry and competitor environment on strategic planning and implementing (Porter, 2008). Through identifying its position in the retail industry and its competitors by Porter's five forces, Dick Smith could have been able to appropriately use its competitive advantages if any.

Buyers in the electronic retail industry have high bargaining power as this industry offers homogeneous products and the switching costs between the different sellers are not high. This a very strong force as the bargain hunting customers switch to other stores if they do not get what they desire at lowest prices (Legget 2016). From this way, the buying power of buyers in the industry ranges from moderate to high.

As per Porters theory, the larger or stronger the supplier is, the stronger is its bargaining power. So for retail industry the bargaining power of suppliers may range from moderate to high. As for electronic industry, the dependence on suppliers is less, resulting in very moderate bargaining power of suppliers in the industry. The prime reason for moderate bargaining power of suppliers in the Australian retailing industry is that there’s a large percentage of market share of retailers in Australia and large number of products are being sold by them in the industry.

In terms of the industry rivalry, Dick Smith faced with high threat of industry substitutes from Woolworths, Harvey Norman and JB Hi-Fi. The high industry substitutes are due to high competition that retail industry of Australia faces (Davidson, 2016). Since there are a large number of industry substitutes, they tend to restrict the market share usurped by Dick Smith in totality. Thus, within the electronic retail industry there’s an intense competition, leaving barely no competitive advantage in charging low prices. Thus the availability of substitutes ranges from moderate to high. Such intense rivalry compels the firm to continuously engage in effective and competitive strategies so as to differentiate themselves from other rivals in the industry.

The electronic retail industry of Australia has comparatively low barriers to entry as the market is flooded with many industry substitutes. Also, since the price offered in the industry is not that high, it is not considered as an attractive industry as there’s low profit margin. However, government regulations and restrictions and scarce availability of land may act as barriers to entry into the industry. Also, the relationship already established between the known brands and the customers may also deter entry into the industry. Thus, the threat of new entrants is moderate to low.

Taking into consideration Porter’s five forces mentioned above, it can be seen that electronics retailing is an unattractive industry due to fierce competition, large number of suppliers opening their own stores, low barriers to entry and high amount of rent charged by land lords of the bricks-and-mortar retailing. Besides, the customers in such industry want latest products at least prices.

*2.4 Internal Environment*

The brand of Disk Smith has been established for more than 50 years (Dick Smith From Wikipedia, 2019). Goodwill and brand value can be seen the most important intangible assets for Disk Smith. Besides, the numerous stores and their wide distribution could be seen as a valuable strategy arrangement if with attractive products to sell. These resources could be considered as strengths of Dick Smith, and used as its the core competence.

However, due to electronic products update rapidly, the price and value of remaining outdated inventory would be compromised. Prior to its acquisition in 2016, Disk Smith stuck to an expansion policy, piling up inventory and devaluing products (Disk Smith, 2015), eating up most of the company’s earnings, which directly led to the company’s capital chain rupture. In order to ensure daily operations, Dick Smith had to borrow loan from banks. Total borrowing nearly doubled in 2015 from a $71m to a $127m in just six months (Disk Smith, 2015). The huge borrowing led to higher interest payments, and the company lost money as its surplus was wiped out by the depreciation of inventory. The huge losses made it difficult for Dick Smith to resume business. A large amount of debt broke its capital chain and increased its financial risks. These weaknesses of Dick Smith finally led itself to collapse.

When Disk Smith was bought by Anchorage Capital Partners in 2016, it canceled all its physical stores and focused on Disk Smith online. This allows Disk Smith to reduce payroll costs and reduce inventory. This gives Disk Smith new life and opportunities.

There are also potential threats. The business model of online mall adds difficulty to after-sales service. Customers can only communicate with Disk Smith by phone and over the network, making it impossible for customers to communicate directly with Disk Smith.

*2.5 Current Strategic Priorities or Direction*

After acquired by Kogan in 2016, new strategy has been adopted that only online business of Dick Smith is run under Kogan's stewardship. Although Dick Smith's online business accounts for only 8% of total sales (Sue, 2016), its website, customer database and intellectual property is a big database for the retail industry

Ruinous power of the online sales activities impacts the retail industry significantly in how to sale and what to sale. Compared with other retail commodities, electronic products are especially affected, and accordingly, the electronic retailers face a severer situation, as prices fall and life circle reduces. Thus, strategies like promoting sales based on fixed costs and operating leverage, such as aggressive store expansion and mass inventory storage, are not applicable and should be avoided.

*2.6 Reasons Contribute to the Unsustainable Strategies*

After the acquisition by Anchorage Capital in 2012, several strategies were adopted for Dick Smith, including aggressive store expansion, increase in private label inventory (Talevski, 2016), and rebate-driven inventory purchase (Mitchell, 2017), by which the collapse of Dick Smith in 2016 was caused. These unsustainable strategies can be attributed by Dick Smith's failed analysis and response of changes and impacts of external environment as well as internal environment.

*2.7 Inappropriate Analysis and Response of External Environment*

The external environment directly and indirectly influences the organizations' strategic planning and implementing, as the components of which are of complexity, numerousness, dynamic, and unpredictability (Muscalu, Iancu, & Halmaghi, 2016). The strategies adopted by Dick Smith turns out to be inaccurate and unsustainable due to its failure in thoroughly understanding and effectively responding to impacts of the three segments of the external environment, which are general, industry and competitor (Hanson et al., 2017).

In terms of the changes and impacts of the general environment, despite the economic sluggish might tighten consumers' spending (Davidson, 2016), the main impact comes from the technological advancement which influences the way people shop and the product people willing to buy (Mun & Yazdanifard, 2014). Being obsessed with the idea that revenue growth is positively with store network growth, Dick Smith gradually expanded its store network. The chain reaction of Dick Smith's store expansion strategy is the increase in inventory storage. However, the product mix is undesirable (Candler, 2016), resulting a poor store presentation. Owing to improper general environment scanning, monitoring, forecasting and assessing, Dick Smith didn't thoroughly detect the potential changes in the rapid technological development trend, nor did it response feasibly or change strategies accordingly. The availability of technology does not hold back Dick Smith, but instead, it is the inability to understand the trend and the inflexibility to adopt the change that foreshadow the strategic failure of Dick Smith.

As for the changes and impacts of the industry environment, low barriers to entry the electronic retail industry, high bargaining power of buyers, moderate bargaining power of suppliers, strong threats of substitute products, and intense rivalry indicate that the electronic retail industry is of fierce competitiveness, which stresses the significance of competitive strategies one has. Owing to the homogeneous nature of electronic product supply to retailers, the strategy implemented to differentiate oneself to others is limited. As other electronic retailers also chase the same customers, they can provide lower price for same products (Candler, 2016), thus differentiating from other competitors through lower price becomes impractical. Unfortunately, differentiating product by increasing in private label inventory did not bring Dick Smith any competitive advantages (Bartholomeusz, 2016). High level of private label inventory, instead, strained the cash flow of Dick Smith, resulting a gap between what Dick Smith can provide and what customers actually wanted, which could also be explained by its chaotic product mix. The inconsistency with customer demand and the inappropriate strategy affect each other reciprocally, together contributing to the strategic failure of Dick Smith.

In terms of the changes and impacts of the competitor environment, the current strategies, capabilities, assumptions about the industry, and future objectives (Hanson et al., 2017) of competitors as well as the intensity of rivalry are correlated to the according responses of an organization. The competition of electronic retail industry is intense, as there exists many competitors including JB Hi-Fi, Harvey Norman, Kogan and eBay. Taking JB Hi-Fi as an example, the strategy adopted by JB Hi-Fi was different, as its products remained a diverse range and it did not heavily invest in private label product (Hatch, 2016). On the contrary, Dick Smith allocated its limited capital inefficiently, failed to spread the potential risks, and lost the feasibility owing to the chain effects of its strategies of aggressive store expansion and high level of private label inventory storage, and as a consequence, its market share shrunk.

Misjudgement and inappropriate response to issues in the three parts of external environment compromised the strategic sustainability that Dick Smith should have, inevitably contributing to the failed strategies.

### *2.8 Inappropriate Analysis and Response of Internal Environment*

The internal environment of an organization lays the foundation for strategic planning and implementing, the analysis of which enables an organization to know what resources, capabilities, strengths and weaknesses, and accordingly core competences one has (Hanson et al., 2017), thus helps one cope with issues in external environment. Coherently, altogether affects the strategic planning and implementing.

Understanding itself inaccurately, Dick Smith failed to allocate its resources properly though claimed in its 2015 annual report that a dividend payout ratio of 60% to 70% could still balance the resources required for business growth with rewarding directors (Dick Smith, 2015, p. 2). In fact, the dividend paid did erode the sustainability of strategies that Dick Smith ought to have, as the initial purpose of its strategic planning was not to obtain competitive advantages, outperform its competitors nor achieve sustainable development, but to increase the dividend paid. In doing so, the rebate-driven inventory purchase strategy was adopted since at least May 2014 (Mitchell, 2017), and Dick Smith banked the rebate as revenues (Candler, 2016) to boost short-term book profit thereafter to gain rewards, squeezing as much money as possible from suppliers and maximizing directors' own profits. The rebate-driven strategy failed to be consistent with customers' demand, causing its products to be unattractive. Though the reputation of Dick Smith should have helped to gain some advantages, the bizarre product mix disappointed potential customers. Being unable to sell old inventories, cash flow in Dick Smith was negatively affected, which hinders Dick Smith from paying both suppliers and the bank loan. Simultaneously, the aggressive store expansion strategy and high level investment in private label inventory strategy, altogether forming a vicious circle, enlarged the inflexibility and unsustainability of Dick Smith.

Incapable of understanding internal environment, ignoring the organizational capacity, relying on poor products and blindly expansion to gain competitive advantage, and self-interest driven decision making erode Dick Smith's strategic planning and implementing, making its strategic failure unavoidable.

*2.9 Main Eason of the Strategic Failure*

Dick Smith with u *R*nsustainable developments losing its competitive advantage in the market is attributed to the external and internal environmental aspects, but the fundamental cause of its collapse is related to ineffective strategic leadership and management issue. Hanson et al. (2017) stated that effective strategic leader plays an essential role in energizing the human capital of the firm and guiding the organization to achieve positive outcomes. However, during the strategic management process of Dick Smith, the leaders and managers represented the insufficient capacity of developing appropriate strategies to implement.

In December 2013, with floating on the Australian Securities Exchange by Anchorage Capital Partners in Australia which purchased Dick Smith in September 2012 (Intelligent Investor, 2016), Dick Smith continually concentrated on significantly increasing revenue and generating profitability, such as an aggressive expansion strategy (Chung, 2016). This inappropriate decision-making resulted in considerable costs of expanding stores reaching a peak of approximately 381 stores during 2014 (Anchorage Capital, 2014), which ultimately led to purchasing excessive amount of inventory with completely outdated electronic products (Mitchell, 2016). According to the annual reports of Dick

Smith, the inventories increased from $171 million to $293 million between 2013 and 2015, this is mainly because Dick Smith did not consider the rapid technological innovation, and purchasing products were determined by the rebates-driven buying inventory from suppliers rather than customers' demands and needs (Mitchell, 2016).

In addition, under the high cash flow pressure and inadequate profits, one of the main management issues is relevant to the failure of management control such as manipulating sales for increasing profits. The management breached duties and failed to conduct adequate procedures to monitor stock including overstating inventory and impairment for inventory. For instance, from 2013 to 2015, the amount of accounts receivables dramatically increased from $10.4 million to $53 million because of maximizing rebates from suppliers, while the amount of accounts payable grown from $153 million to $220 million by reason of gaining extra credit from suppliers (Mitchell, 2017). Consequently, Dick Smith was not successful to ensure the proper financial statements, especially for inventory and earnings. The management also breached banking covenants in order to extend the payment of debts as a result of insufficient positive funds (Mitchell, 2016).

Hanson et al. (2017) dedicated that corporate management is essential for making and implementing strategic decisions effectively, and conducting appropriate decision-making is beneficial for promoting stakeholders' interests in organizations. Overall, without the quality of leadership and management decision-making as a fundamental component of strategic management, Dick Smith did not create and implement appropriate and valuable business strategies to achieve sustainable competitive advantage by integrating the analysis of external and internal factors, Dick Smith, therefore, eventually failed to compete in the electronic retail market.

## 3. Conclusion

Dick Smith as the electronics retailer since 1968, creating such great customer experience for Australian and New Zealander, however, the firm failed to deliver unique products and services to customers. Hanson et al. (2017) indicated that strategic management is crucial for organizations to set a direction for organizational development and to avoid failure in the market (Hanson et al. 2017). Organizations need to adopt suitable management approaches and actions for conducting and operating their business, which can improve corporate performance, enhance enterprise investment and strengthen business growth (Tapera, 2014). Thus, only with appropriate strategies and effective management practice could Dick Smith have been able to obtain competitive advantages and then ensure sustainable development in a dynamic business environment.

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