European Entrepreneurship Case Study Resource Centre

Sponsored by the European Commission for Industry & Enterprise under CIP
(Competitiveness and Innovation framework Programme 2007 – 2013)

Project Code: ENT/CIP/09/E/N02S001
2011

Joyful Drinks (Romania)

Virginia Maracine

Bucharest University of Economics

Emil Scarlat
Bucharest University of Economics

Camelia Delcea
Bucharest University of Economics

Iulia Maries
Bucharest University of Economics

Luca Iandoli
University of Naples Federico II

This case has been prepared as a basis for class discussion rather than to illustrate either the effective or ineffective handing of a business / administrative situation.

JOYFUL DRINKS

The Problem at a Glance

It was Friday afternoon, and as the rain mixed with the snow in the last days of the harsh winter of 2007, Radu Mincu entered his office with a stack of freshly printed papers in his left hand and a cup of steaming hot tea in the other. He sat on the chair at his desk, put the papers on the desk and slowly he swivelled in his chair and stared out the window. He loved his office, decorated with modern art work, which gave him a 'homely' feeling, but also some inexplicable sense of self-confidence. He was feeling relieved because he had managed to finish writing the two papers he had to developed for two senior managers and had them ready to be presented for the next Board meeting. However, he was far from being relaxed as his reports presented two alternatives which in many respects offered incompatible strategic choices, and Radu felt very uncertain about which one he should embrace and support at the Board meeting. He hoped that a calm moment over a cup of tea would help him make a good decision.

As Radu sipped his tea, he stood up and began to pace across the office. His mind wandered back nine years to when he was appointed to the position of Assistant Marketing Manager after beating the hard competition at Joyful Drinks Srl (JD)[1], the Romanian branch of a foreign company called Joyful Drinks International Ltd (JDI Ltd) which was highly renowned for its long tradition in beer production. But at no time in the subsequent years at JD had Radu ever been faced with a decision so critical for his own career and the future of the company. Eight years had passed since the inauguration of the first production unit in Romania in 1999. In 2007 JD Srl was at a turning point regarding its future development. A meeting of the company's Board had been organised for the following Monday to discuss and define the direction toward which the company development should be oriented. The members of the Board invited Radu as Sales Manager to join the meeting.

[1] Upon a request from the managerial team, the real name of the company, its brand and the people's real names cannot be mentioned in this study. However, the analysis will not suffer in any way from this omission; on the contrary, this 'disguise' allows us to present with more freedom some 'insight' information and facts behind the press releases.

Radu was 39 years old, an engineer with a Masters Degree in Marketing Management. His direct superior on the company's hierarchy was Ioan Ghinea, a 46 year old economist with a Masters Degree in Corporate Finance, the present Marketing Director of JD Srl (since September 2003). The company CEO was Andrei Popescu, 53 years old, with a Degree in Managerial Engineering and a Masters Degree in Strategic Marketing. Throughout his activity at JD Srl, Radu enjoyed working with, and in many occasions, learning both from Mr Ghinea and Mr Popescu. To his surprise, although separated by several hierarchical levels, the contacts, meetings and discussions with the company's CEO were very frequent. Radu had always appreciated Mr. Popescu's availability and his willingness to discuss openly and directly with his subordinates any aspect related to the business activity. This type of collaboration created and maintained a true culture of trust among company's employees and made them consider the CEO as much more than just their employer. Besides, Radu and Mr Popescu were linked in a peculiar way by their common passion for the study of History, in particular Romania's national history. Radu Mincu had worked hard both with Mr. Ghinea and with company's CEO to prepare for the upcoming Board meeting. To his surprise, the two executives had both asked for his help to write the supporting documentation for what appeared to be two very different, almost incompatible, development strategies.

While sipping his flavoured tea and gazing at his profile mirrored in the office's window, all of his attention was focused on the upcoming Board meeting. He felt that this is the most important event in his professional career and he hoped that his performance would repay the top managers trust and expectations. However, it was already Friday and he had not made his decision yet regarding the ideal strategy for the company, and he was beginning to feel uncertain about his next move. Years of experience working with colleagues and members of top management had still not prepared him for this. *"How did I get caught in such a situation?"* he was asking himself. *"After all, am I really expected to make a decision? Couldn't I just build a fair set of arguments for both options? In this way, I would simply be able to answer the questions that the Board members could ask me on Monday."* This idea of creating two sets of arguments made him feel relieved. He now knew what he had to do, to be the lawyer of both strategies. He would try to sketch the future of the company in both situations, engaging in an argument of pros and cons, assuming a neutral stance. He returned to his desk, picked up the phone and informed his wife that he is going to be late. He knew that he was going to have an 'all nighter' and that hard work lay ahead, but he felt once more the adrenalin and enthusiasm of the first years of his career at JD when he would come to work singing and travelled by bus as he was not on a sufficient salary to afford the car he now had.

He took a deep breath and looked at the two files on the desk: on the left side, the papers asked by Andrei Popescu, CEO of JD Srl, and on the right side the ones asked by Ioan Ghinea, Marketing Manager for JD Srl. "*The conservative versus the visionary*" he thought, and he decided to start with the Conservative Strategy. However, he decided not to use these terms in the presentation to the Board so as not to create any bias on the decision and on his position, as in management today nobody likes to be labelled as conservative and everybody loves to be defined as a visionary manager, at least in words. No, he is going to stick to more neutral and technical jargon (premium versus diversification), that was how he was going to present the two options. He liked the fact that he has found titles for each proposal, he already felt inspired.

The Company

Joyful Drinks Srl (JD Srl) was the Romanian branch of a foreign company, Joyful Drinks International Ltd (JDI Ltd). JD Srl was established in 1997 in Bucharest, and for two years they distributed the imported brands of beer produced by JDI Ltd in several European countries in East and Central Europe. In 1999 JD Srl started to produce beer in a new production facility built in Romania. Both the JDI Ltd development policy and the CEO of JD Srl were passionate about high quality standards in beer production. As a result, the newly built factory in Romania was a greenfield project[2] that created one of the most contemporary beer factories of Europe at that time, with an initial investment of approximately $56 million USD. Since then, the company had continued to develop its activity and to increase its sales volumes by producing and distributing a large portfolio of products, composed by premium and super-premium brands, designed for Romanian customers with above average incomes. On its entry into the Romanian beer market, JD Srl faced strong competition from both distributors of international brands and producers of local brands which were highly appreciated by the Romanian consumers. However, the market was expanding with further potential for growth, based on one hand, on the Romanian's preference for this drink and, on the other hand, on the insufficient supply available until 1990.

[2] In many disciplines a greenfield project is a project that lacks any constraints imposed by prior work. It is the construction on greenfield land where there is no need to remodel or demolish an existing structure.

In 2007 JD Srl had ten brands in their portfolio which made a significant comparison to 1997, the year of their market entry, when the company held only one brand. The production capacity of the Romanian factory has grown rapidly since its inception, from 0.4 million hectolitres in 1999 to 0.59 million hectolitres in 2001, 0.72 million hectolitres in 2002, 1.08 million hectolitres in 2003 and 2.1 million hectolitres at the end of 2007, due to a total investment of $173 million USD. The growth of sales and volume of activity was accompanied by an expanding employee base, from 310 persons in 1999 to 530 persons in 2003 and 950 people in 2007.

JD Srl's growth rate positioned the company among the top beer producers in Romania, from the 13th place in 1999 to 4th place in 2007. By 2003 JD Srl had become the market leader in the international quality beer segment in Romania. At the end of 2006, JD Srl reached a market share of 8.7 percent of the total beer sales in Romania, but with over 50 percent shares from the overall market for international beers produced in Romania. In 2007, the volume of sales was eight times larger than in 1997 and the market share was five times larger. At present, a fleet five times larger than 10 years ago was transporting the company's brands to quality beer lovers from all over the country. The JD Srl Romanian beer factory was ranked among the 10 most successful factories of the JDI Ltd Group, out of a total number of 55 factories located internationally. Its production capacity allowed the company to reach a sales level of 1.83 million hl, a turnover of $105 million USD (7.5 times larger than in 1997) and a profit of $13.46 million USD (5.4 times larger than in 1997). During this time, the average annual beer consumption in Romania was the same mean of 75-80 litres per capita per year as the European level. Even so, the studies showed that the growth potential for beer consumption still existed, and that in 2008 it could reach a level of 85-90 litres per capita.

The Premium Strategy

The strategy proposed by Andrei Popescu was based on an analysis of JD Srl business during the period 1999-2007, when the company had been producing beer in the factory in Romania. Radu was delighted when, two months previously, the CEO of the company approached him requesting him to work on such a retrospective analysis. He once more planned to analyse the results of the study that had been developed during the last two months and to mark the most important moments in the establishment of the company. For JDI Ltd the decision of entering the Romanian market was made after consideration of many different aspects of the industry. First of all, market studies highlighted to the international group that Romanian people had a good propensity for the consumption of premium quality beer (Romania holds a top position within the International Group in terms of premium beer sales, after Denmark, Germany, Italy and Turkey). Secondly, they found a competitive market with many active players. And finally, JDI found in Romania all the skills and competencies that were needed to build a modern production facility.

The development strategy of JD Srl was based on three principles - quality, international standards and innovation. Trying to improve the quality of the beer production process, they decided to build their own brewery instead of modernising an old one, for the production of premium and super-premium brands targeting upper-class, high income Romanian consumers. After a decade, the construction of the JD Srl brewery in Romania was worth the large effort to become the most modern in Europe. The realisation of a new production facility was accompanied by many initiatives in corporate social responsibility:

1. Support to Romanian Culture and Art: The production area would host a permanent art gallery for young Romanian artists sponsored by the company.
2. Going Green: An inverted flow for the collection and reuse in agriculture of the organic waste resulted from the beer production process was built. Additionally JD Srl would pursue the active involvement of national and international organisations for elaborating quality standards and research in quality assurance, and environment protection of the natural ecosystems of the Black Sea Region (identifying preservation and rehabilitation methods and technologies for controlling/evaluating the pollution level, and the environment technologies techniques applied in Romania).
3. The design of social, cultural and humanitarian programs which served the purpose of involving JD Srl in growing the community's vitality and also solving the economic problems of some community members (students, young artists, people having economic difficulties from the rural area).

All of these actions were the result of the CEO's vision: *"We cannot sell a product to our consumers and ask them to enjoy it as long as they are unhappy both socially and economically"*. The quality of life and quality of products had to go together in the company vision. The efforts of JD Srl in maintaining the quality level of the products were rewarded through the international certificates for conformance with ISO 14,000 and EN 45,000 groups of standards, and national prizes for excellence in quality were frequently achieved.

It was obvious that the primary objective of JD Srl when entering the Romanian beverages market was that of obtaining the targeted profitability and a good market share. The beer market in Romania in 2003 had a growth rate of 12 percent, while JD Srl had a growth rate of 23 percent, a much highter rate than the market. From this perspective, the company's top management considered that 2003 was the year in which they surpassed their goal, that of becoming leaders on the international quality beer segment in Romania. The next three years came with investments in production capacity, which led to an increase in sales with an average annual percentage of 18 percent. At the end of 2006, the production capacity of JD Srl reached 1.4 million hectolitres per year, with a market share of 8.7 percent of the total beer sales in Romania, but with over 50 percent share from the overall market for international beers produced in Romania.

The objective of the CEO's proposal was to follow the same premium growth strategy. If at the beginning of the year 2007 the total investment that JD Srl made within the Romania market was $115 million USD, the completion of the second factory and a logistics park with a surface of 3.6 ha, would amount to a total investment of $173 million USD at the end of 2007, and a production capacity at 2.1 million hl. This capacity would allow the company to reach a sales level of 1.83 million hl, a turnover of $105 million USD (7.5 times larger than in 1997) and a profit of $13.46 million USD (5.4 times larger than in 1997). However, for this growth to be achieved, a number of things needed to happen:

1. JD Srl had to maintain its current target consumer profile and needed to identify the set of methods for a reasonable increase in the market share up to 12-13 percent of the overall beer production at national level.
2. The product portfolio must remain the same; only premium and super-premium brands would be produced.
3. The super-premium and premium brands returned much larger profits than medium quality brands. Their production and sale would almost assure accomplishing the profit target of the company in the following years and maintaining the quality excellence status of JD Srl.
4. The company's involvement in the socio-cultural life of the community had to be kept and diversified. Other consumers, partners and collaborators may be added or better involved (for example, the academic communities).
5. The consolidation of the 'JD Srl family' spirit amongst the employees would be reinforced by growing their involvement in the adoption and implementation of the decisions regarding the future evolution of the company.

Radu closed the file thinking that these last rows completely reflected the company CEO, Andrei Popescu. He could even hear him saying: *"In order to ensure our consumers pay* *the price of our beer we need to convince them of its quality. And the quality means to know and to fulfil all the expectations of the consumer"*.

The Diversification Strategy

Radu Mincu sat further into his chair, closed his eyes for a few moments and poured himself a fresh cup of tea. It had been an interesting read, maybe too dense, so he needed a break before 'jumping' into Ioan Ghinea's document describing the Marketing Manager's alternative proposal. He opened the file and analysed the title for a few moments: *"The development alternative of JD Srl for 2008-2012"*. *"The alternative"*, he repeated this word involuntarily in his mind a few times. This title established right from the beginning the impression that he was dealing with competitive strategies by the two representatives of JD Srl top management.

The first part of the study included mostly the same historical data of JD Srl development, so well known by Radu. But they were phrased different, being organised as an argument. Ioan Ghinea contended that beer production had a marked seasonal profile, explaining this by saying: *"In spite of the spectacular development of the company's activities during the period 1999-2007 (the same data presented in the study for the CEO, Andrei Popescu), the technical, human, IT capital and the company's logistics are hardly used to 60 percent of their full capacity per year, with top sales in the hot season and during the winter holidays (reference Figure One)."* The costs with fixed capital and financial resources (loans) were linear throughout the year, the fixed capital had to be redeemed, the interests for the banking loans paid off, the employees remunerated, both in August when firm's sales are of 160,000 litres, and in February when these decrease to 76,000 litres. *"With an average growth of 9 percent in the last 5 years, the beer market in Romania is close to maturity."* Besides the advantages of being in this development stage, the JD Srl faced the risks normally associated with being present on the market with only one type of product. Any relevant decrease in consumption compromised the firm's profitability. In the beer market in Romania, JD Srl had positioned itself within the niche segment of premium and super-premium brands, leaving unexplored the potential of consumers with lower income, which are much more numerous compared to other European countries.

The multitude of data and information collected and processed over the last months, the studies and simulations provided by Radu to the Marketing Manager had been concluded in short, concise phrases, and finalised with an appendix section. The Marketing Manager also analysed the cost/revenues graph, but this time he included the consumption trends of other drinks like soft drinks, mineral water and even milk. The conclusion was as compact as the whole document itself. Diversification could increase up to 80 percent (from 60 per cent) the degree of use by the company resources, shared between beer and soft drinks products, namely:

1. Labour force,
2. IT&C,
3. Logistics & packaging (transport, warehouses, labelling, palletizing, handling etc.),
4. Economic-financial administration,
5. Clients,
6. Contracts,
7. Auxiliary materials suppliers.

The Marketing Manager envisaged two principal problems which he stated at the end of the study:

1. An evaluation of the investment in the resources strictly needed to produce soft drinks (the technological line for preparing the product and the bottling line);
2. An evaluation of the effort of changing the organisational culture from an exclusively beer producer.

These were serious challenges to diversifying their product range but the rewards were potentially very exciting.

Conclusion

Radu closed the file, and his mind was reeling in an unstoppable whirl of a multitude of thoughts, ideas and feelings. He felt the need to put this swirl in order so he started to produce a structure to the pros and cons for each of the two strategies that he had just read. He admitted to himself that he was biased towards the CEO Andrei Popescu's development strategy. It was so easy for him to identify himself with company elitist attitude accepting no compromise on quality. These were the qualities that had assured the company's success and that brought it amongst the top Romanian beer producers. Even with his friends, he was proud to wear a t-shirt or a cap with the logo of the JD Srl or the slogans of the various advertising companies that were promoting the different brands produced and commercialised by his company. He has full confidence in the company's products and also in the managerial skills of Mr. Andrei Popescu, whose motto "*less, but very good*" became, over time, his own way of being.

Furthermore, in this particular moment, it seemed impossible to see himself in the position of a producer of sweet water or a drink for children, as he used to talk about the soft drinks no matter how natural or artificial they may be. This new mix would mean that they might lose control of the precise, clear objectives that his company had always followed. And at the thought of the time and money investment, and on the necessary effort for launching in a new market, he was almost shivering.

On the other hand, the dependence of the JD Srl business stability on a single product type made him anxious regarding the business growth prospects and/or the effects of a possible reduction of the Romanian consumers' demand. "*Do not ever put all your eggs in one basket*", says an old proverb, and usually those proverbs have much truth to them. However, the decision to enter the soft drinks market seems to him to be too great a leap for JD Srl compared to its actual activity, vision and development policy. But Radu had to stop and think *"Maybe my confidence and attachment to the company's CEO is preventing me from accepting, in a more rational way, the viability of such a diversification strategy. Or maybe, there is even a third strategy for growth on the Romania's beverage market, sort of a middle way?"* Radu needed to think about it over the weekend. He went out of the office and, while he was closing the door, he was thinking about the extent that his opinion and presentation would have on the future development strategy of JD Srl. Radu did not have a solid defined opinion yet regarding the two proposals or the option of a third approach, but he would need to have his mind made-up by Monday morning.

Figure One: Beer Consumption vs Fixed Costs Profile over the Year

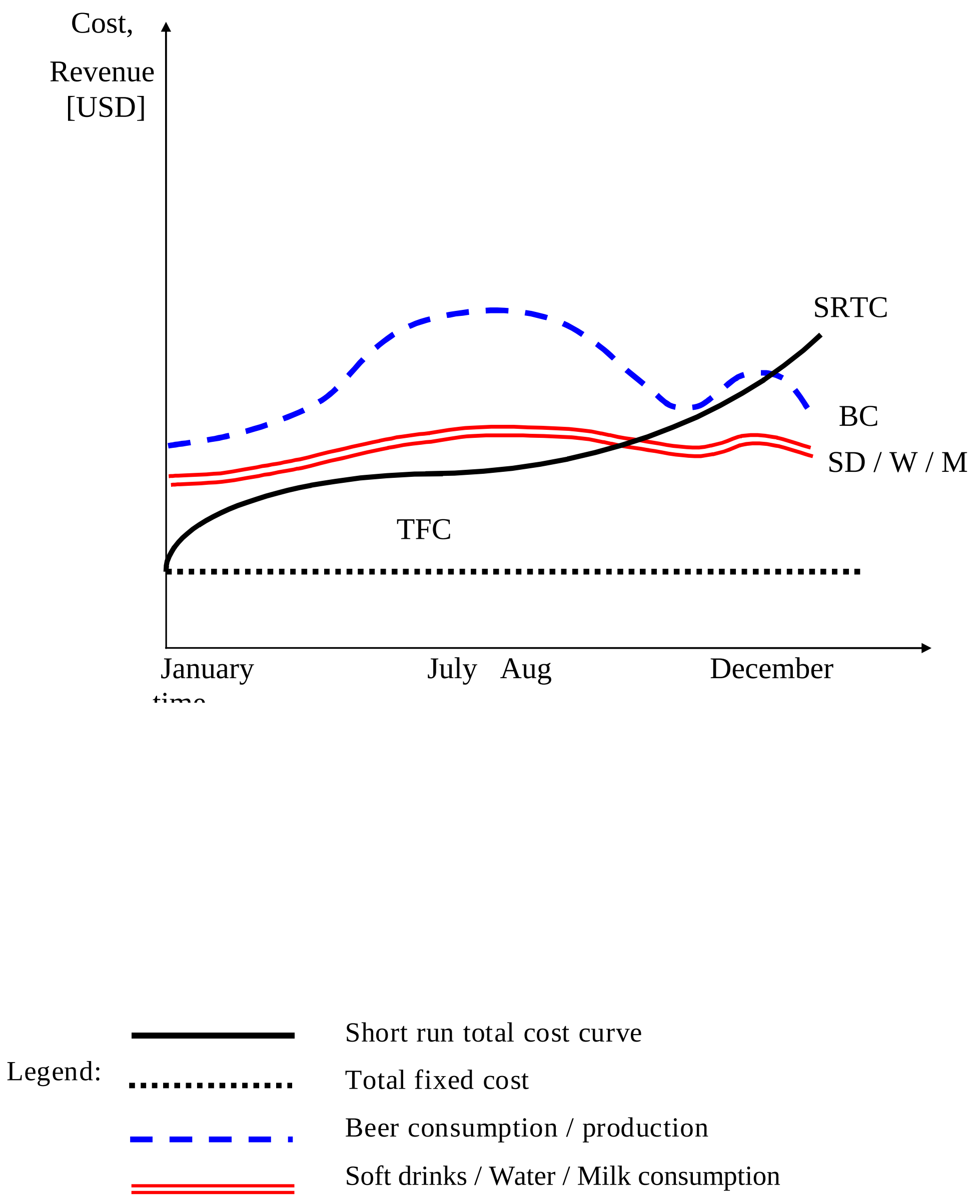

Figure Two: Diversified Consumption vs Fixed Costs Profile over the Year