a sliver of the market at first. But Coca-Cola reduced expenses by manufacturing locally, setting up 34 bottling plants and forming partnerships with three bottling groups to create a low-cost, efficient distribution network. With a bottling system that now covered 28 cities across the country, Coke was able to harness system economics to cut production, marketing, and distribution costs. Coca-Cola then added products, selling everything from Modern Tea Workshop herbal tea drinks to Coke Light. It now sells more than 20 different drinks for about 25 cents a can and 12 cents a returnable glass bottle, only slightly more than local brands. Even its marquee Coke brand sells for only 10% to 15% more than the most popular local brands. As a result, Coke sells more than half of all carbonated soft drinks in China and generated more than $2 billion in revenue in 2003.

Bring local brands on board. Perhaps the biggest barrier for most foreign companies is entrenched local competition. Beer makers are up against well-known and inexpensive local brands, as Australia's Foster's, Britain's Bass, and Denmark's Carlsberg learned the hard way. Ditto for dairy producers. China's "big six" dairy companies control well over half the local milk market.

The most successful multinationals are tackling China through a mix of global and local brands. In 2000, Colgate snapped up Jiangsu Sanxiao Group, the leading local player, to control the category. Anheuser-Busch, which leads the market for premium beer with its Budweiser brand, recently purchased a controlling stake in Harbin Brewery, China's fourth-largest brewer. The Harbin acquisition allows Anheuser-Busch to reach the masses, and – along with Anheuser-Busch's minority position in Tsingtao, China's number one brewery – consolidate its position in the market. Similarly, Gillette not only sells premium Duracell batteries but also Nanfu, a local brand it has acquired.

After failing to penetrate the Chinese market on its first try, Danone is now taking a cue from companies like Colgate and Gillette. It recently purchased a stake in Bright Dairy & Food, one of China's largest dairies. The move should improve Danone's cost structure and competitive position, giving it yet another chance to milk the world's fastest-growing dairy market. Reprint F0503D

DEMOGRAPHICS

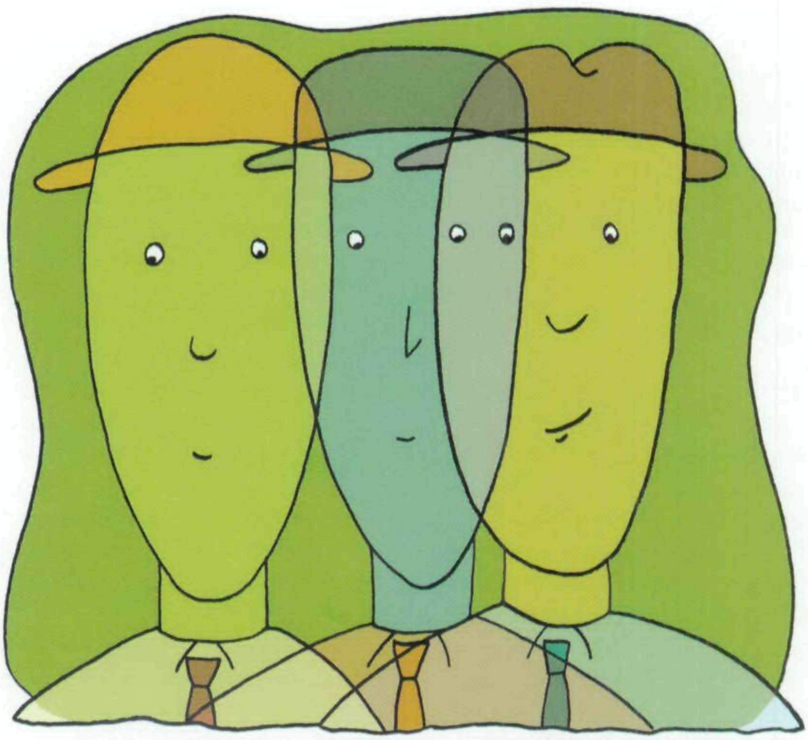
Vanishing Jobs? Blame the Boomers

by PHILLIP LONGMAN

To all the brouhaha over offshoring in America, one rejoinder is that any unemployment is temporary. When the mass of baby boomers starts retiring in the next few years, the argument goes, there will be plenty of work for anyone in the baby bust generation whose job went overseas. That may be a comforting thought for U.S. baby busters, but it's probably wrong. Despite their small numbers, the busters may paradoxically see unemployment get worse, not better.

Without a crystal ball, we can't say definitely what will happen as baby boomers start retiring. But we can find clues in two places. Japan's birthrate fell below replacement levels long before that of any other industrialized nation. As a result, workers have been a shrinking proportion of the country's population since 1989. Yet the jobless rate has actually gone up. Similarly, in the United States, the number of people between the ages of 15 and 24 has been declining in relative terms since 1990. But the smaller supply has not made younger workers more valuable; their unemployment rate has increased relative to that of their older counterparts. The situation is even worse for young men: Their median inflation-adjusted income in the booming economy of the late 1990s was actually below what the legions of young baby boomer men earned when they hit the workforce during the stagflation of the late 1970s. A similar story can be told about young workers in most European economies.

Why doesn't a declining labor supply bring more opportunities for those seeking jobs? First, an aging population often increases the cost of hiring. All those elder baby boomers are already helping to drive up the cost of employer-provided health care, and as they start to retire, payroll taxes will be likely to rise to make up for shortfalls in public health and pension



systems. Such a jump in taxes could discourage hiring in the United States, as it has in nations that have already experienced large jumps in their elderly populations, like Germany. Payroll taxes there exceed 40%.

Second, as their populations age, societies become more risk averse and resistant to change. One reason Japan is still struggling to fix its sclerotic banking system and France can barely raise its absurdly low retirement age is that older voters have nothing to gain, and much to lose, from fundamental changes that pay off only in the long term. The U.S. population may not be as old as those of other rich countries, but just look at how hard it is for Americans to face up to obvious threats to their country's long-term prosperity, such as the unsustainable cost of entitlement programs, looming future deficits, and overdependence on foreign energy sources. Studies worldwide also show that older populations are less likely to be entrepreneurial and so may create fewer new jobs.

Finally, businesses have other, potentially less costly, options besides replacing retirees with the next generation. They can move even more work offshore, and for those jobs that can't be sent overseas, they can lobby the government to allow more immigration. Or, as some hard-nosed firms are already doing, they can reduce their operations, either directly or by cutting plans for future investment. A shrinking workforce could give us merely a shrinking economy.

Reprint F0503G

COMPETITION

The Faster They Fall

by S. PATRICK VIGUERIE AND CAROLINE THOMPSON

As the economy strengthens, industry leadership is more contestable and fleeting than ever. Globalization, changes in technology, and deregulation not only drive strong supply-side growth in the broader economy but also create new sources of supply, new competitors, a flood of new innovations (and knockoffs), and dramatically higher productivity. Today's industry leaders will face increasing risk as growth emboldens attackers – many of whom will have lower costs, lower return requirements, or both.

We have powerful evidence that attackers have gained greater traction in recent decades. We analyzed industry leaders in 1,300 companies from 35 industries over some 30 years. The results were stark when we tracked the "topple rate" for the entire group of companies. That's the probability that a top company (a firm with revenues in the top 20% of its industry) will lose its revenue leadership position in the ensuing five years. Our data show that the rate doubled between 1972 and 2002.

Our analysis does not count companies that are acquired as topples. When these are taken into account, the rate has actually tripled. And the loss in revenue leadership is accompanied by an average 30% decline in profitability. Perhaps more important, toppled leaders are far more likely to exit their industry through acquisition or bankruptcy than those that sustain their position (no matter what quintile they're in); more than one-third of toppled companies no longer existed as independent companies after five years. That exit rate is twice as high as it is for leaders that are not toppled and a third higher than for the average company in the data sample.

Strikingly, many of the successful attackers that topple incumbents come abruptly (and unexpectedly) from far behind. Companies are traveling through the ranks about 40% faster than they did in the 1970s or 1980s, and the average new leader was in the middle of the pack just five years before ascending to the top quintile.

Why do companies topple? Each case is unique, but three factors figure most often: First, shifts in demand or superior offerings from competitors undercut the leader's value proposition. Second, competitors come along with acceptable substitutes or prices so much lower that the leader's productivity or cost position is undermined. Third, the leader makes some radically mistimed or otherwise unsuccessful big bets. Growth only exacerbates these strategic risks.

Growth, and the three supply-side forces that will help drive it over the next five to ten years, will almost certainly create a new generation of industry leaders. How well companies manage this risk – or capitalize on this opportunity – will determine which ones topple and which rise to the top.

Reprint F0503H

MARKETING

Outsourcing Marketing

by GAIL McGOVERN AND JOHN QUELCH

Companies have long outsourced creative, right-brain marketing activities, such as advertising and promotion campaigns. But a fundamental change is under way: Increasingly, firms are farming out marketing operations and analytics as well. A Forrester Research survey of 650 B2B marketing executives found that 53% aimed to outsource more than half their marketing activities in 2004. Forrester projects that CRM outsourcing in the United States will quadruple to $4.6 billion by 2008. And the British firm Astron Group forecasts that customer

continued on page 26