
Schumpeter

Business and management

How Fujifilm survived

Sharper focus

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THE biggest oddity of Kodak's woes and Fujifilm's revitalisation is that, as we put it in [a story this week](#) (<http://www.economist.com/node/21542796>) , "Kodak acted like a stereotypical change-resistant Japanese firm, while Fujifilm acted like a flexible American one." The article looked mostly at Kodak, since it is the news: an iconic American powerhouse lies at death's door.

But a closer examination of Fujifilm is also warranted to understand how it made the transition away from film—in particular after Kodak filed a lawsuit against the Japanese firm alleging patent infringement on January 13th. Where Kodak is trying to monetize its R&D in its one core business, photography, the digital imaging sector accounts for only about one-fifth of Fujifilm's revenue, down from more than half a decade ago.

How Fujifilm succeeded serves as a warning to American firms about the danger of trying to take the easy way out: competing through one's marketing rather than taking the harder route of developing new products and new businesses. At the same time, it is a reminder to Japanese executives that their constant moroseness and defeatism is misplaced: the country's firms are well placed to succeed if they are willing to reform their businesses.

Shigetaka Komori, Fujifilm's boss (pictured), expresses admiration for Kodak in an interview prior to the lawsuit, calling it "the

strongest company I ever saw." He entered his firm in 1963, when the American firm towered over its Japanese rival in every way. "Its situation fills me with a bit of regret and emotion," he says about Kodak's woes.

Like Kodak, Fujifilm realised in the 1980s that photography would be going digital. Like Kodak, it continued to milk profits from film sales, invested in digital technologies, and tried to diversify into new areas. Like Kodak, the folks in the wildly profitable film division were in control and late to admit that the film business was a lost cause. As late as 2000 Fujifilm counted on a gentle 15 or 20-year decline of film—not the sudden free-fall that took place. Within a decade, film went from 60% of Fujifilm's profits to basically nothing.

If the market forecast, strategy and internal politics were the same, why the divergent outcomes? The big difference was execution.

Fujifilm realised it needed to develop in-house expertise in the new businesses. In contrast, Kodak seemed to believe that its core strength lay in brand and marketing, and that it could simply partner or buy its way into new industries, such as drugs or chemicals. The problem with this approach was that without in-house expertise, Kodak lacked some key skills: the ability to vet acquisition candidates well, to integrate the companies it had purchased and to negotiate profitable partnerships. "Kodak was so confident about their marketing capability and their brand, that they tried to take the easy way out," says Mr Komori.

When sales from film developing and printing were dwindling, for instance, some revenue could still be gained by installing kiosks to print digital photos. Yet whereas Fujifilm had its own system, Kodak needed to partner with another firm—and thus share the income. Moreover, whereas Fujifilm could apply the kiosk technology to other businesses in its digital-imaging division, Kodak could not because it did not own the technology. The Japanese company was also able to strike a deal to place its kiosks in Walmart stores, which gave it scale. Today Fujifilm controls nearly 40% of the photofinishing market in America, whereas Kodak's share is only 15%, according to IBISWorld, a research firm.

Fujifilm's success stems in part from a decision in 2000 to spend around \$1.6 billion for an additional 25% stake in FujiXerox, the firm's joint venture with Xerox, when the struggling American firm was in need of cash. This allowed Fujifilm to control the joint venture's strategy and to consolidate its hefty earnings. When film began its swift decline, the company had a cushion of earnings.

Fujifilm also focused on applying its technologies in new areas. Fujifilm's expertise in nanotechnology for placing chemicals onto film, for instance, was carried over to applying cosmetics to facial skin. Experience with photosensitive materials helped it with

fine chemicals and industrial materials. Today, Fujifilm's medical-imaging equipment business is growing quickly, and it has acquired many firms in the sector, including paying \$1 billion in December for SonoSite, an American ultrasound equipment maker.

(When pressed whether he wants to buy Olympus, the Japanese camera and medical device maker laid low due to a corporate governance scandal, Mr Komori declined to answer. Asked whether the British boss, Michael Woodford, did the right thing by publicly exposing the financial misdeeds or whether he should have handled it internally, Mr Komori adamantly stated: "It was the right way." And the scandal represents a very rare case for Japanese companies, he hastens to add.)

As a result, Fujifilm became a much more diversified company than Kodak. Having a longer-term vision, it invested a lot. This was "damaging" to the firm's short-term profitability, in the words of Mr Komori, but the bet paid off. "We have more 'pockets' and 'drawers' in our company," he explains—a metaphor for different technical areas that bring in revenue.

Although Fujifilm did many things right, its performance has not been unblemished. After the recession hit, the firm has had to restructure again. Sales and profit both fell in the first half of the current fiscal year, and its shares lost one-third of their value in 2011. Still, the company is in a strong position to do well in most of its businesses.

And Kodak? "There was complete and utter denial" about competition from Fujifilm, according to one of the firm's former senior executives, who requested anonymity since his current employer would not want him to speak about previous work. He recalls the reaction at the company's headquarters in Rochester, New York, in 1995 on the day that Consumer Reports, an American magazine, reported that the Japanese company's film was as good as Kodak's. Instead of being alarmed, everyone agreed it simply wasn't true.

"Kodak's monopoly was the problem ... It always believed it had a God-given right to 100% of the market," he says. "It never bothered to look over its shoulder at what was coming up from behind." Instead, Kodak relied on its brand.

The "Kodak moment", he explains, was a way to scare people that unless they bought a little yellow box, their most important memories risked ruin. Adverts at the time depicted schmaltzy images of a toddlers' birthday or a father dancing with his daughter on her wedding day. "The ads were meant to make you cry, and if you cried, that meant you would pay an extra 45 cents for a roll of film."

What are the lessons from the surprising stumble and the equally surprising success? First is the need to cannibalise oneself. Second is the importance of execution in addition to strategy. But most important, firms must resist looking for a magic wand when hard work is needed.

Yet there is an even bigger lesson in this. It is easy to think that companies can compete by outsourcing production and focus on developing and marketing. But many innovations bubble up from the factory floor. Even Apple, a master in outsourcing and orchestrating manufacturing, has in-house expertise and occasionally acquires certain technologies. Today, as debates rage in America over the degree to which returns on capital exceed those from actual business operations, and the relative merits of employment in manufacturing versus the services sector, the history of Kodak is more relevant than ever.