Dell's problem in china

In recent years, the Texas-based manufacturer of computers and other related peripheral computing devices known as Dell has begun to experience significant success in China, but not without overcoming significant challenges specific to the Chinese markets. Some analysts have been quick to celebrate the company’s success as principal evidence that Dell has not only learned from its lessons, but that the market for personal computers in China is undergoing a maturation of sort. (Zhang, 2005)

However, the most critical insight to be gathered from Dell’s experience in China is not merely a general understanding of the peculiarities of a foreign country, but the heterogeneity of its markets.

The successful emergence of Dell in the mid-1980s is largely attributed to its direct sales model, which arose more out of necessity rather than out of any broad designs for the company’s direction. The direct sales model’s principalmotivationis efficiency, which was a critical issue for the company, then called PC Limited, and is achieved through the elimination of intermediaries between it and the customer. (Pletz, 2004) Rather than dealing with resellers to determine the needs of customers or accumulate a large inventory of products, Dell chose to place itself directly between the market and the suppliers. Effectively speaking, this means that products are built by the company and their product line is kept up to date.

Furthermore, the company did not maintain retail outlets to showcase their products, relying instead on direct sales to PC customers, removing many of the costs that are associated with maintaining a retail chain. Pletz (2004) also notes that the Internet proved to be a great boon to Dell because it significantly improved the company’s ability to gather customer data and effectively acquire pricing feedback and predict future trends, as well as tighten its link with supplier databases.

However, in recent years, the direct model has come under intense scrutiny in the wake of a receding market position and a diminishing stock value for Dell. This is because the direct sales model is mostly effective in the business and government markets, and Dell’s incarnation of it does not apply well to consumers and small-to-medium businesses (SMBs), most specifically in its attempts to expand its business outside of the U. S. and towards China, now seen as a lucrative site for business and commerce following the liberalization of its markets. Lee (2005) notes that a practical reason behind thefailureof Dell’s business model of direct sales is that it simply does not play well outside of the major cities, which is where the large-scale customers it appeals to the most are.

[Dell] is out of sync with shifting market conditions in fast-growing China. … demand is emerging elsewhere -- in hundreds of smaller cities, […] where even some business customers want to see products before they buy. That's where competitors … have been selling briskly through retail shops. Says HP Executive Vice-President Ann Livermore: " You have to wonder, how well does the direct model work in the hinterland?" (Lee, 2005)

As a result, Dell is unable to replicate the success it has in China’s urban centers within the conditions of the semi-urban and rural markets. Not only are many Chinese customers wary about purchasing products sight unseen, but they are also far less enthusiastic about owning credit cards and using them religiously like their American counterparts.

Additionally, there is a certain degree of cultural hesitation towards making purchases over the phone or the Internet.

The success of its competitors in these markets is no mere chance. Its archrival Hewlett Packard has invested heavily into local retail infrastructure and support, which effectively holds the hands of its customers in making their purchases. On the other hand, the homegrown powerhouse Lenovo Group and Taiwan-based Acer present more conservatively priced options.

These are strengths should not be discounted, as they are critical to winning customers over. Sheff (2002) notes that while demand for personal computers may be spiraling upwards in China, personal computers remain unaffordable for most Chinese. To be blunt about it, personal computers are a major investment and it is not only important for consumers to feel secure throughout the process of purchasing one, but it would be presumptuous for companies, not just Dell, to think otherwise. Dell’s business model is inappropriate in this aspect, because it ignores this deep-seated need of customers.

To this end, Dell has not only begun investing in a physical presence in the form of kiosks and retail outlets inside and outside of China, but it has also begun outsourcing its consumer product design in order to tailor its products more specifically for the Chinese market. Because the market of China is currently moving at a rapid rate, this is a promising strategy as it allows the company to recognize the detrimental effect of generalizing the product forecasting it conducts in its home turf across the international markets.

A more controversial move however, has been Dell’s decision to partner with retail chains such asCostcoand Wal-Mart in an attempt to distance itself from the direct sales model. As CEO Michael Dell has opined repeatedly in numerous press statements, “ The direct model has been a revolution, but it is not a religion.” This is not an entirely new enterprise for Dell, as it used to sell through such chains in the early 90s in the United States. However, those operations ceased in its attempt to concentrate on the direct model in the face of disappointing profit margins in that area. A return to retail holds the promise of augmenting its present direct sales strategy with additional profits and a more comprehensive coverage of the market for personal computers.

Additionally, Sanders (2007) opines that a successful expansion into the retail market can help “ polish up the company’s tarnished customer service image by serving as a drop-off point for products that need servicing.”

However, there is some concern from analysts that such an exploration of alternative channels risks compromising its strength in the direct model, simply by diluting the focus of its operations. Furthermore, there is the risk that shareholders could restrict the growth of these alternative channels for the short-sighted reason that retail requires significant costs and investments that may not see a return until some years later.

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