

## Kodak vs. Fuji

In the fall of 1997, Mr. George Fisher, CEO of Eastman Kodak Company, was meeting his top marketing executives to formulate the strategy to contain Fuji Photo Film Co. from making further inroads in the U.S. film market.

For some years now, Fuji and Kodak have been battling it out in overseas film markets. But in the United States the picture was quite different. Kodak and Fuji treated that market like a cozy, mutually profitable duopoly. Both enjoyed fat margins. Kodak controlled over 80 percent of the American film market, and distant No. 2 Fuji always priced its film just a little bit lower.

Then, in the spring of 1997, Fuji began slashing prices by as much as 25 percent. Fuji's explanation was that Costco, one of its five largest distributors in the United States, ditched Fuji for Kodak and the company got stuck with 2.5 million rolls of film. Fuji unloaded the film at a steep discount to other distributors. When consumers saw that the familiar red, white, and green boxes were a dollar or two cheaper, they snapped them up. Over the past year Fuji increased its share of the U.S. film market to nearly 16 percent from 10 percent, while Kodak's share took an unprecedented tumble from 80 percent to just under 75 percent.

Fuji executives deny that they intended to start a price war. Yet Fuji's prices were still kept low even after the excess inventory had been worked off. Whatever the case, for the first time in its long history, Kodak can no longer take its home market for granted.

### EASTMAN KODAK COMPANY

The Eastman Kodak Company was established in 1884 in Rochester, New York, and still overwhelmingly dominates the \$2.7 billion U.S. amateur film market. Until recently, the Kodak brand remained solid gold, and its quality was never in dispute. But

Fuji's gains in the United States were ominous, especially because the Japanese film company was already poised to surpass Kodak on a global basis, particularly in Asia, where film sales were growing at 20 percent a year or more. (Worldwide, Fuji and Kodak were neck-and-neck, with about a third of the market each.) Alex Henderson, managing director of technology research at Prudential Securities Inc. in New York, who had been watching the two companies for twelve years, believes that if current trends hold, Fuji will overtake Kodak by 1999. "When that happens," says Henderson, "Kodak will go from being Coke to being Pepsi. That's a very damning thing." Worse yet, he expected that in the United States, Fuji would continue to creep up on Kodak by a rate of about 2 percent a year.

### FUJI PHOTO FILM COMPANY

The Fuji Photo Film Company was established in Japan in 1909. In 1997, financially, Fuji was a very strong company, giving it more flexibility to cut prices. Fuji's sales in 1996 were a record \$11 billion, and profits were a near-record \$757 million; at the same time, Fuji had a net cash position of about \$4.5 billion and access to incredibly cheap borrowing—around 2.5 percent interest—thanks to Japan's record-low interest rates. Kodak had more than \$1 billion in short and long-term debt and was in the midst of a sales and profit slide, in addition to impending restructuring write-offs likely to run \$1 billion or more. Also, Kodak could not borrow at much under a 7 percent rate of interest. Fuji could afford a show-down, but Kodak could not.

### MARKETPLACE

Kodak and Fuji have been slugging it out for three equally important parts of the consumer photo

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This case was prepared as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation.

business. Those little yellow and green film boxes are the most obvious to the man in the street, but Fuji and Kodak also manufacture photographic paper, mostly for sale to big photo-processing laboratories and small retail developers. To ensure a market for their paper, both companies have invested heavily in the third line of business—developing—by buying up big film-processing companies across the United States. Fuji's deep pockets had enabled it to make acquisitions like the estimated \$400 million purchase of Wal-Mart's six wholesale photo labs in 1996, a move that in one swoop gave it about 15 percent of the U.S. photo-processing market.

Fuji's long-term strategy was to transplant as much film and paper production as possible onto U.S. soil. That kept costs down, reduced nettlesome trade disputes, and made Fuji's factories more responsive to local market demands. In 1987, just 3.5 percent of Fuji's production was outside Japan; now the figure was 31 percent, and the move offshore was accelerating. In April 1997, Fuji opened a highly automated, \$300 million photographic paper plant in Greenwood, South Carolina, which was already producing about 20 percent of the photo paper consumed in North America. Later that year, Fuji is scheduled to open an equally high-tech, \$200 million film plant in Greenwood. According to industry sources, it would not take much time or investment to double the plants' capacities should Fuji need it.

## COMPETITION

Fuji was one of the leanest and meanest of Japan's big companies. Led for the past 17 years by non-nonsense Chairman and CEO Minoru Ohnishi, Fuji was cutting white-collar overhead long before it started to become fashionable in Japan. In the past ten years the company's sales nearly doubled worldwide, but its staffing in Japan remained almost flat. Ohnishi tried to maintain a sense of crisis by reminding staff that Kodak was still out front. "He likes to constantly cut costs in order to anticipate a rainy day," says a consultant, "so that

there will be less pain down the road." Or, more likely, greater market share.

Fuji's aggressive tactics had sometimes earned it charges of unfair trading practices. In the early 1990s, the U.S. Commerce Department investigated charges that the Japanese company dumped photographic paper in the U.S. market. Fuji managed to dodge import duties by agreeing to raise prices to levels just above the going rate. (Fuji subsequently lost most of its 20 percent market share but bounced back when it opened its paper plant in Greenwood and bought out Wal-Mart's processing labs.) Also, the World Trade Organization is expected to rule soon on U.S. allegations that the government of Japan worked with Fuji to exclude competitors from the Japanese market, which Fuji dominated with a 70 percent market share. A decision is expected in the spring of 1998, though it was not likely to affect either company's business.

Ironically, Fuji got its big break in the American market thanks to Kodak. The company opened its first office in the United States in 1958 in the Empire State Building, but it only began selling film there in 1970, when it was one of several relative minnow—among them GAF, Agfa, and 3M—swimming in Kodak's pond. Then, in 1984, the Olympics came to Los Angeles. Olympic czar Peter Ueberroth believed that Kodak was the natural choice to be the exclusive film sponsor, but Kodak wouldn't bite. Even after Ueberroth visited Rochester to make his pitch, Kodak refused to pay \$1 million, far below the \$4 million floor for sponsorships that Ueberroth had established. So he approached Fuji, which in those days was still barely known in the U.S. market. Ohnishi agreed on the spot and eventually committed around \$7 million. No marketing investment ever brought better returns. Within months of becoming a sponsor, Fuji landed 50,000 new distribution outlets. "Salespeople said that accounts that didn't used to return their calls were suddenly calling them," says Tom Shay, head of corporate communications for Fuji USA and a 26-year Fuji veteran. "The Olympics completely changed the way people looked at us."

Since then, Fuji has built a reputation for price, quality, and sharp marketing. It has won a strong following among professional photographers, some of whom rave over the film's luminous blues and greens. Its acceptance in the professional world has given Fuji a lot of cachet with amateur shutterbugs. Fuji also adopted a hipper, more technologically oriented marketing image to differentiate itself from the sentimental Kodak style. In 1993, Fuji ran a highly successful, award-winning TV campaign obliquely directed at Kodak. The killer line: "Pictures should be nostalgic; your film shouldn't." Fuji's current slogan also painted the company as forward looking: "You can see the future from here."

In technology too, Fuji has shown that it could set the pace by consistently spending about 7 percent of sales on R&D. In 1986, Fuji was the first to introduce the disposable camera, a product that has been a huge boon for both Kodak and Fuji. Fuji also worked with Kodak and other companies to introduce a new 24mm "advanced photo system" film, which uses a new generation camera, a hybrid of digital and traditional systems. In Japan, the launch was a great success, thanks to Fuji's ensuring that the cameras and processing were readily available. Advanced Photo System film already accounts for about 10 percent of the color-negative film market in Japan. "Fuji's greatest strength is that they always make sure that consumers are ready to buy their new products, and they actually get the products to the consumers,"

remarked Toby Williams, an analyst at SBC Warbug in Tokyo. By contrast, Kodak flubbed the U.S. introduction of its advanced photo system, called Advantix.

If Kodak and Fuji have one thing in common, it is their vulnerability as photography moves into the digital age. In 1997 alone, market watchers expect to see 1.8 million digital cameras sold worldwide, and that number will grow sharply as quality improved and prices drop. That poses three big issues for film companies: One was the danger—still much in dispute—that film sales will soften as digital cameras made by companies like Sony, Canon, and Casio take up a bigger share of the market. Another was a challenge on the photographic paper and processing front from Canon, Epson, and Hewlett-Packard. Their latest generation ink-jet printers produce high quality prints of digital images on plain and coated paper. (Fuji just launched a printer of its own.) Both Kodak and Fuji are working on ways to add value to digital photography, such as a service that lets customers order prints directly over the Internet, but those ideas are untested.

Finally, Kodak and Fuji have jumped into the digital camera business themselves. But they are in a mob of nearly two dozen camera, computer, and consumer electronics companies trying to get into the same space. One thing is sure: The companies that win in digital photography will need marketing and product smarts, technology and, not least, money. Fuji, it seems, has them all.