

# IKEA

CASE

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The name IKEA is a combination of its founder's initials, Ingvar Kamprad, with the first letters of the farm and village where he grew up. At the time of IKEA's founding in 1943, Kamprad could not have guessed that his company would become one of the most popular and iconic brands in the world. From the beginning, IKEA was founded on different principles—namely, frugality and low cost. Most furniture companies offer service and advice in settings where salespeople compete for sales commissions. Kamprad recognized that customers were willing to trade off typical amenities to save money. Today, the no-frills frugality is the cornerstone of the IKEA cachet and the reason for its immense popularity.

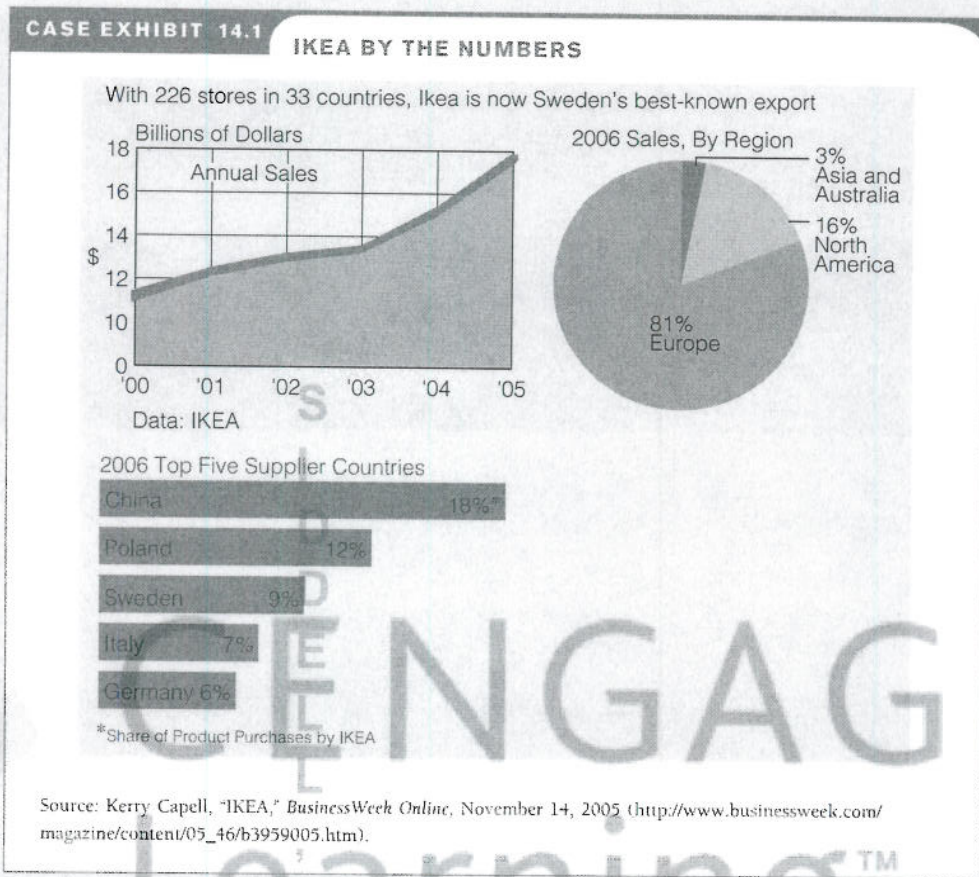
The IKEA concept works to build customer relationships. IKEA's positioning statement reflects this philosophy: "Your partner in better living. We do our part, you do yours. Together we save money." For IKEA's part, the company provides stylish, functional, low-cost home furnishings that customers must assemble themselves. This enables IKEA to save money on manufacturing and distribution, which they then pass on to customers in the form of lower prices at retail. To compensate for the customer having to do-it-themselves, IKEA offers other services that make this proposition a little more attractive. These extra services include in-store child-care and play areas, restaurants, and longer hours of operations. To help visitors prepare for this experience, IKEA provides its customers with pencils, paper, tape measures, store guides, catalogs, strollers, and shopping bags. IKEA even offers delivery for the bulky items that customers cannot carry themselves. For those who want to carry their own bulky furniture home, IKEA rents caravans for convenience. IKEA stores are designed as a circle so that everything is seen, no matter what direction the customer is headed. The aisles are wide to reduce traffic that may occur while stopping to look at different showrooms and displays.

IKEA is owned by the IKEA Group, which includes IKEA of Sweden (which designs and develops all IKEA products), Swedwood (which makes all IKEA furniture), the sales companies that operate IKEA stores, and all purchasing and supply chain functions. The IKEA Group is owned by INGKA Holding BV, which itself is owned by the Stichting INGKA Foundation of the Netherlands. Many estimates peg

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Christin Copeland, Florida State University MBA Class of 2006, prepared this case for classroom discussion rather than to illustrate effective or ineffective handling of an administrative situation.





the foundation as one of the world's wealthiest charities—worth an estimated \$36 billion. This type of ownership is unique in that the foundation is a nonprofit organization designed to promote innovation in architectural and interior design. Some criticize IKEA's ownership as an arrangement that leverages the uniqueness of Dutch law to avoid taxes and prevent a hostile takeover attempt.

IKEA is now Sweden's best-known export. This privately-owned company had 2005 sales totaling \$18.1 billion and an enviable yearly growth rate of 17.3 percent. There are more than 226 IKEA stores in 33 countries, with 200 of these stores belonging to the IKEA Group (Case Exhibit 14.1). The remaining stores are owned and operated by franchisees. There are currently 28 U.S. stores with plans to have fifty stores open by 2010. With all of its growth and success, IKEA has a manufacturing challenge: On its current growth trajectory, IKEA will soon have to supply twice the amount of products that it does today.

## IKEA's Functional Divisions

### Production

IKEA's key objective regarding production is to establish and maintain long-term supplier relationships. IKEA works with more than 1,600 suppliers in more than





Clean lines are the hallmark of IKEA's furniture designs.

fifty-five countries. Its oldest suppliers are Swedish; however, other major suppliers are located in China, Poland, Italy, and Germany. IKEA accounts for five to ten percent of the furniture market in each country where its products are manufactured.

One strategy that IKEA has implemented is to place trading offices around the world to localize its operations. This gives IKEA leverage to increase production capacity (that is, labor hours and purchasing materials) when needed. The strategy also allows IKEA to closely monitor manufacturing performance. Producing high-quality products at the lowest possible cost drives IKEA's production mentality. In addition to local trading offices, IKEA also manages production through long-term contractual relationships based on bulk buying. Committing to high-volume purchases over a longer time frame allows IKEA to dramatically cut costs. Additionally, IKEA is in a position to offer its suppliers financial assistance if necessary. This optimization is key to achieving the low-cost business model that IKEA wants to maintain.

Cost consciousness dominates all aspects of IKEA's operations. In land acquisition, IKEA locates stores on property just outside of target cities. In production, the remnants of fabric and wood used for products are used to create more products. IKEA uses natural colors to cut production costs and increase social responsibility to the environment through the manufacturing process. In distribution, flat packages are used to efficiently transport the large bulk of products from suppliers to IKEA stores. The use of flat packages lowers warehousing and distribution costs and the environmental impact throughout the supply chain.

## Marketing

IKEA's marketing program has four focal areas: product design, catalogs, advertising, and public relations/sales promotions. IKEA's product designs are arguably the most important part of its brand image. Customers love the clean lines, frugal styling, and cachet that ownership affords. IKEA admits that creating stylish and inexpensive products is a challenging task. To fulfill its vision, the company's twelve full-time designers and 80 freelancers work closely with in-house production teams to pair the appropriate materials with the least costly suppliers. Though the work is tedious, IKEA is well known for its innovation.

IKEA's main marketing focus is its printed catalog where the company spends 70 percent of its annual marketing budget. The catalog is produced in 38 different



editions in 17 languages for 28 different countries. In 2006, 110 million copies were put into circulation. In addition to the catalog, IKEA also uses television, radio, and Internet-based communication to reach its target customers. The company's advertising is intended to increase both brand awareness and store traffic. Some of the company's advertising is controversial, especially ads that portray gay customers shopping for IKEA products. Advertising, however, is not a major focus of IKEA's promotional efforts. The company prefers to rely on word-of-mouth communication.

IKEA does use promotional stunts and games to attract customers into its stores. For instance, IKEA managers invited Atlanta locals to apply for the post of Ambassador of Kul (Swedish for "fun"). The five winners of an essay contest received \$2,000 in vouchers, had to live in the store for three days, sleep in the bedding department, and participate in contests. Prior to the opening of the Atlanta store, IKEA offered \$4,000 in gift certificates to the first person in line. By the time the store opened, there were more than 2,000 customers waiting. IKEA also holds "Antibureaucracy Weeks" on a regular basis. These are times when executives work on the shop floor or stockroom, operate cash registers, and even load trucks and cars for IKEA customers. This simple step goes a long way in upholding the IKEA culture and maintaining employee morale.

IKEA's marketing program is designed to be thrifty but still effective. In fact, all of IKEA's operations are designed to maintain a downward pressure on operating expenses. For example, in most stores, IKEA does not accept checks—only cash or credit cards. This reduces IKEA's accounts receivable and minimizes losses. It also eliminates the need to maintain an expensive collections operation. With policies like these, it is not surprising that IKEA's pretax operating profit for 2005 was an estimated \$1.7 billion. The company's operating margin of ten percent is among the best in the home-furnishings industry. And, despite its low cost and price model, IKEA aims to cut prices by an average of two to three percent every year.

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## SWOT Analysis

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### Strengths

*Low-Cost Structure* IKEA's low-cost structure has been the very essence of its success. Being that low-cost measures are ingrained into IKEA's corporate DNA, the company does not have a hard time tailoring its operations around this business model. This model also pairs nicely with customers who appreciate IKEA's operating style.

*Antibureaucracy* IKEA treats all of its employees the same. The company's anti-bureaucracy weeks help maintain a strong corporate culture and its low-cost business model.

*Do-It-Yourself Approach* IKEA can maintain its low-cost business model by creating a different furniture-shopping experience. IKEA supplies customers with all possible materials needed to complete their furniture shopping when they enter the store



(that is, measuring tape, paper, and pencils). The floor has showrooms displaying IKEA furniture with multiple accessories that will accentuate the style. With this approach, customers do not have to be bothered with salespeople who work on commission. Customers can pick and choose among the different options of accessories that they would like to use with furniture.

**Added Amenities** Although IKEA is not set up as a traditional furniture store, IKEA does provide delivery for customers who cannot fit all their items into their vehicles. If the item can be carried on top of the customer's car, IKEA rents carracks that the customer can use to get the items home. IKEA also provides child-care services to give parents time to shop. Once the children are in a safe place, parents will delegate more time to browsing and purchasing IKEA furniture and accessories. As another amenity, IKEA places restaurants in its stores to urge consumers to stay a little longer. At this point, customers can choose to have lunch or dinner with their children or another shopping partner. IKEA wants the customer to feel as if there is not a rush to leave the store and customers can do more than just shop for furniture.

### Weaknesses

**Do-It-Yourself Approach** Some customers may not appreciate the do-it-yourself approach. IKEA targets young, cost-conscious customers who want stylish furniture. High salary-earning individuals may not want to indulge in shopping and picking out their furniture from a warehouselike environment. Some individuals may actually enjoy having a conversation with a salesperson and getting individual ideas and input from an employee. These same customers may not have the time to wrestle with assembly of their furniture once they get it home. Customers who feel that this is an unnecessary step may continue to buy furniture from traditional retailers.

**Service Trade-offs** IKEA's business model trades service for cost. This trade-off may not be appealing to some customers who are accustomed to traditional furniture shopping and may feel that IKEA does not care about its customers and what they buy. With IKEA operating as numerous franchises, this lack of customer service may begin to taint the IKEA brand. This trade-off could present a future brand-loyalty problem for IKEA.

**Limited Promotional Expenditures** IKEA does not spend an enormous amount of money on promotion. Instead, the company depends on word of mouth and catalogs to generate a buzz among customers. Most of IKEA's television commercials are unknown outside of the United Kingdom. Further, many of the company's ads are controversial. Overall, this is a weakness in the United States where consumers watch much more television than in any other nation. As a result, IKEA may be missing out on a larger potential customer base.

### Opportunities

**Urban Sprawl** In most major metropolitan areas, residents continue to move away from the city center into outlying areas. Many of these residents are young, educated, and value conscious. IKEA's strategy ties well into this geographic/demographic trend.