ASN-18-E
Rev. 7/2013

Typhoon Computers GmbH

On November 3, 1995, Mr. Jeff Tsao, managing director of Typhoon Computers in Vienna, was examining the company's list of customers. He was seriously concerned:

> "Our sales manager, Andy Fok, has been with us for almost a year now, but so far he has devoted all his efforts to maintaining the same 30 or 40 accounts that were handed to him on day one. It's very worrying. You can't count on customer loyalty in this industry; computer components are coming to be seen as a commodity. What's more, it's a very price-sensitive market; any company that can supply an item a dollar cheaper can wrestle away an account. The industry is changing so fast and is so competitive that the failure rate among distributors is very high. Annual customer turnover is around thirty to forty percent. It's essential to capture new accounts to make up for those we're bound to lose."

On the same day, during dinner with an old friend, Andy complained:

> "My boss is always pressuring me for new accounts. I understand his concern, and I totally agree with his reasoning, but just maintaining those thirty accounts keeps me busy ten hours a day six days a week. The sales assistants were supposed to help me with the follow-ups, but if they keep changing every six months, how am I ever going to have time to travel, meet potential customers, and capture new accounts? A large chunk of my time is taken up with training new assistants. And I don't even get paid for doing it. I've told Jeff several times that he has to let them do their job as sales assistants and not load them with other responsibilities. The company has reached a size where functions need to be more clearly defined. You can't carry on having polyvalent employees now that the business is so much larger than it was when it started two years ago."

In mid-1995, the company introduced a quarterly bonus system for those employees who did not work on commission, in an attempt to stem the high turnover. Ironically, shortly after the first bonus was paid in the third quarter of 1995, several of the employees affected by it resigned, including the sales assistant who had received the highest bonus.

This case was prepared by Luis Go, MBA 1996, under the supervision of Professor Rafael Fraguas, as the basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. July 1996. Revised in July 2013.

Last edited: 12/21/15

In July 1995, Jeff recruited another sales manager, Paula Fu, and gave her the brief to develop new accounts in the entire sales territory, thus placing her in direct competition with Andy. He thought that this might spur Andy to improve his performance and develop new customers.

Mr. Jirasek, the managing director of H&J Computers in Prague, received a visit from Paula during the Invex Computer Exhibitions in Brno, the largest computer trade fair in the Czech Republic. After a brief meeting, Paula was summarily sent back to Vienna, and Mr. Jirasek got on the phone with Jeff:

> "What are you trying to do? Your new sales manager, Paula, came to see me this morning and showed me a list of the companies she wanted to visit. Ninety percent of them are already buying from me. What's more, she was planning to offer them the same prices that Andy gives me. What's the big idea?"

H&J Computers was Typhoon's largest account in the Czech Republic. It was one of the three main distributors of computer components, supplying around 20% of PC hardware demand in the country. Jeff Tsao was very worried about the damage that Paula might have caused and started to weigh possible solutions via a restructuring of the organization and a new incentive policy.

The PC Computer Industry in Central Europe

Central Europe includes Poland, the Czech Republic, Slovakia, Hungary, Slovenia, Croatia, Serbia, Bosnia, Macedonia, Romania, and Bulgaria. Although Austria is geographically located in central Europe, its political and economic environment is more like that of western Europe. Historically, most of these nations were part of the Austro-Hungarian empire in the nineteenth century. The old empire extended north as far as southern Poland, and south as far as Serbia and Bosnia. Austria has many traditional, cultural and family ties with these countries, and strengthened them during the Cold War by maintaining political neutrality.

After the fall of the Iron Curtain and the disintegration of the communist regime, the entrepreneurial energy of these nations was released almost immediately. Young people, many of them fresh out of university, borrowed from their parents and neighbors, travelled as far afield as Singapore to buy one or two computer systems, brought them back as personal luggage, and resold them for five to ten times the original price. This was how many of the local computer businesses in these regions started. Since then, with the rapid westernization of business practices, many had adapted and turned into larger, more professional organizations.

Although the PC markets of central Europe were generally very price-sensitive and were half a year behind the North American markets in technology, this was not a key success factor for local distributors. The huge inflow of foreign investment stimulated tremendous growth in the economies of central Europe, giving rise to a demand for office automation. The biggest problem facing local suppliers in their efforts to meet the demand was the lack of capital to fund imports. Many of the local distribution companies were start-ups and were thinly capitalized. With annual interest rates at around 14% or 15%, importers were not keen to borrow money to build up inventories. Furthermore, the instability of the local currencies was a considerable risk for local companies. For this reason, local importers and distributors tried to find foreign partners that could provide just-in-time deliveries or offered favorable terms.

Taiwan dominated the manufacturing of key components for the low-price segment of the PC market. In 1994, it produced 83% of the world market's motherboards (the guts of the PC, where all the different processes are coordinated with the central processing unit), 80% of the mice, 51% of the monitors, 49% of the keyboards, 70% of the computer cases, and around 40% of the interface and video cards (source: Dataquest).

Although many Taiwanese companies appreciated the need to be closer to their customers and markets, and had set up foreign subsidiaries, warehousing facilities and service centers' the majority still worked from Taiwan. Taiwanese businessmen were very conservative. Given the very limited knowledge they had of central European markets, they would not ship any goods until they had received payment.

Most central European importers could not afford to invest in 20ft containers of monitors or keyboards for delivery in 60-90 days. A 20ft container could hold up to 300 monitors, or 4000 keyboards, or 800 computer cases, or 10,000 interface cards. Shipment by sea was the cheapest way of importing bulky, low-cost products from Asia. Air transport took only five days, but the cost differential made the price uncompetitive. To illustrate the cost differential: for a monitor costing around US$230 and weighing about 15kg, air transport cost 3 to 4 US dollars per kilogram, whereas a 20ft container cost 4,500-5,000 US dollars. Therefore, even though prices were higher in neighboring Germany or Austria compared to direct import prices from Taiwan, it was still very worthwhile to send a van across the border and pick up only the necessary amount of goods.

Typhoon Computers GmbH

Company History

Typhoon Computers was founded by Mr. Jeff Tsao and his partner, Mr. Dieter Blutsch, in January 1992. Jeff had arrived in Europe eight years before. He had worked as sales manager in the German office of AUVA Computers, a Taiwanese manufacturer of PCs and PC components, and had later been transferred to the Austrian branch, before deciding to start up on his own. He knew the Central European market very well, and had good contacts with several Far Eastern component suppliers.

Mr. Blutsch had been in the industry for around the same number of years as Jeff. Before going into partnership with Jeff, he had been a buyer for EMC Computers, the largest distributor of computer components in Austria at that time. As he was extremely familiar with the local scene, he had been a key person in the company's early stages. And as a management software expert, he had designed the computerization of all the processes from the beginning of the new venture.

Typhoon started out basically with three people: the two partners and one secretary. At first, they did everything themselves, from purchasing to selling, from warehousing of inventories to servicing defective goods. The business went unexpectedly well. By the end of the first year, they had sales of almost 12 million US dollars, with gross margin of almost 8%. By the end of 1993, with the additional help of an international sales manager and four staff, Typhoon reached 26 million dollars in sales (see **Exhibits 1-3**).