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Design of value chains in volume-intensive market segments – exploiting economies of scale, scope and integration

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The wood value chain is facing further consolidation with fewer and larger actors along the various positions in the vertical marketing system, from raw material to finished products and systems. Increasingly, finished products and systems are sold directly to end customers or via large retail chains (so called mega-retailers). This tendency is apparent even accounting for competition enhanced by increased globalization.

Large suppliers of wood products and large industrial customers and mega-retailers experience situations, where there are fewer potential partners for large-scale business agreements. The customer-supplier relationships are moving in the direction of bilateral relationships between large and resourceful suppliers and customers, with fewer options to play “the competitive game”. Traditionally, the wood value chain has been characterized by aiming for economies of scale. Wood products manufacturers have focused on high raw material recovery thus moving towards larger and more efficient production units. The retailing business has moved in the same direction as a consequence of the competitiveness on the end-user market with its focus on price. Consequently, there are actors adopting a scope strategy aiming at differentiation in some dimensions. There has thus been a build-up of large suppliers and retailers.

In this new competitive landscape, both suppliers and customers have to rethink their traditional strategies and to design more complex value chains (and business models), often with more than two partners involved. We describe a business case of a co-operation between one large sawmilling company and one smaller wooden component manufacturer on the supplier side, and a large mega-retailer on the customer side. The sawmilling company and mega-retailer have strong large scale orientations, with solid finances and a focus on large volumes. The manufacturer of wooden components is small-scale and not able to operate on its own as a partner to the large customer.

The result of the study indicates the possibilities for large scale professional actors to opt for economies of integration by introducing a third party. Agreements are negotiated and secured by the large actors’ professionalism and size, and control of input material and market knowledge. The flexibility and efficiency of producing and delivering adapted products are created by the innovativeness of the small-scale component manufacturer, investing in niche markets. The study therefore indicates a possible business option for actors in the presently scale-dominated value chain.

Keywords: wood value chain, mega-retailer, economies of scale, scope and integration