Helping Yolanda Break Out of the Commodity Trap

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Yolanda specializes in baked goods. She makes eleven different types of cakes, various kinds of breads, and other baked items. While the business (called Yolanda Bakes) is not registered, she has been running it for five years, initially on a part-time basis but now full-time. She originally also sold arts and crafts, but the baked goods really sold well, especially the cakes, and so she has focused on this. She has been selling at a stall in a local open market, at church socials, and at various community events across town, but would love to have her own shop. She tends to bake enough to serve a given event or venue. She owns basic equipment for use in her baking efforts, including a standard-sized conventional oven. For packaging, she uses cardboard boxes or plastic wrapping, depending the item. With pricing, Yolanda tries to be competitive, and charges differently depending on the venue, but acknowledges that her prices are probably too low. People seem to love her cakes, but she worries they might not buy if she charged more. She buys her ingredients at retail. The business is run from her home in a poor neighborhood in Birmingham, Alabama, which she rents. She has three children who help out with the business when they are not in school. Yolanda took a Quickbooks course and does her own bookkeeping. She has a business Facebook page but no website.

A prevalent reason many ventures started by the poor fail to become sustainable or profitable concerns what we might call **"the commodity trap"** (see figure below). It starts with having a business that is by and large selling something that is not meaningfully different from what many others in the same market are selling. When customers see no difference among competitors, they buy from whomever has the lowest price or is the most convenient to buy from. They have no loyalties, and effectively see the purchase as a commodity. Firms are forced to compete on price rather than on some other basis. Competing on price is almost always a losing proposition.

However, things get worse. Profit margins are squeezed as firms operating in markets with low entry barriers and intense competition attempt to undercut one another in order to retain or gain customers. Meanwhile, operating costs keep rising, further cutting into margins. High unit costs are tied to the fact that the business tends to be labor-intensive, with the entrepreneur doing much of the work in producing a product or delivering a service. Further, the entrepreneur does not have the money to acquire equipment and machinery or incorporate technologies that could reduce unit costs.

Costs are further inflated because the entrepreneur has limited capacity to produce to sell, and keeps relatively low inventories, meaning he or she does not realize economies in production. Small inventories or production quantities translate into (and are the result of) the purchasing materials or supplies in small quantities from suppliers. He or she cannot afford to buy in the larger lot sizes that would qualify the entrepreneur for discounts or lower prices from suppliers. As a result, the entrepreneur has no bargaining power with suppliers. In many cases, the entrepreneur is not able to purchase at the wholesale level, and so must acquire materials, ingredients or supplies at the retail level—and paying retail prices further eliminates any potential profit margins.

The squeeze on margins is exacerbated when operating in more mature or saturated markets, where there is little to no growth in the size or spending levels of the overall customer base. With smaller margins, the entrepreneur has less to reinvest in the business or take home. Lack of reinvestment means the business only becomes more of a **commodity**, especially if other firms are trying new and different things.

A business like Yolanda's can easily be perceived as commodity businesses by customers. Of course, the entrepreneur generally believes their business is different in some way, but this is meaningless if the customer does not see or value the difference.

The goal must be to create meaningful and sustainable differentiation. This means offering something unique that creates real value for enough customers. This can represent a unique challenge for someone who is poor. They first must recognize potential sources of meaningful differentiation, which can require an in-depth understanding of customers, competitors, supplier capabilities, and available technologies. Then they must be able to convey this difference through marketing efforts (which is another area where they cannot afford to spend much).

Your assignment is to come up with a differentiation strategy for Yolanda, ideally an approach that would not be easy for competitors to copy, and a way for her to convey her source of differentiation to customers.