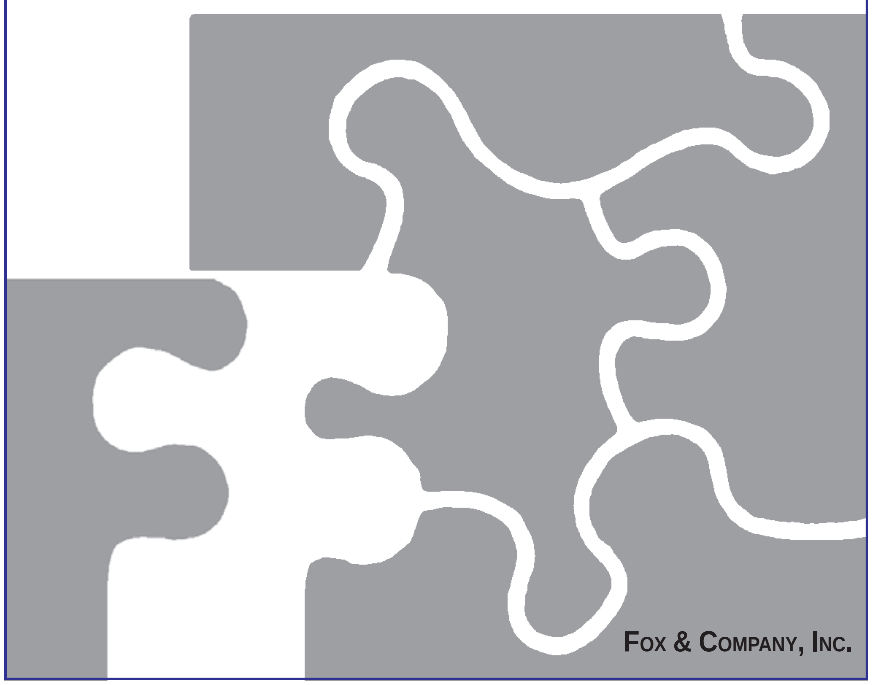
Thoughts on Market Share



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THOUGHTS ON MARKET SHARE AND STRATEGY

These notes on the importance of market share and the necessary interrelationship with sound marketing strategy were collected over time, and are for the thoughtful strategist. Many studies (not the least of which is The Strategic Planning Institute's PIMS findings) empirically demonstrate that for nearly every product and service category, #1 profitability is a function of #1 market share. It is also interesting that products with #1 market share usually enjoy #1 customer awareness, #1 quality status, and the highest prices.

I. THE STRATEGIC IMPORTANCE OF MARKET SHARE LEADERSHIP

Some of the most important missions being written for our companies address market share. Market share is strongly linked to profitability and , therefore, market share is a critical strategic planning issue, as well as an important marketing objective. Separately, the following point was highlighted:

> *"Management must make it very clear to marketing people and sales people that market share is the most worthy of all missions, and without a market share position of #1 or a strong #2, there can be no real lasting success. And over the longer pull, the only secure route to continuous profits is a #1 or a strong #2 market share position. Top management must believe in market share . . . must discuss the subject frequently with marketers, directors, the financial world . . . and must reward financially and generously those who are devoted to market share and are producing exceptional results."*

It is our opinion that market share leadership is vital.

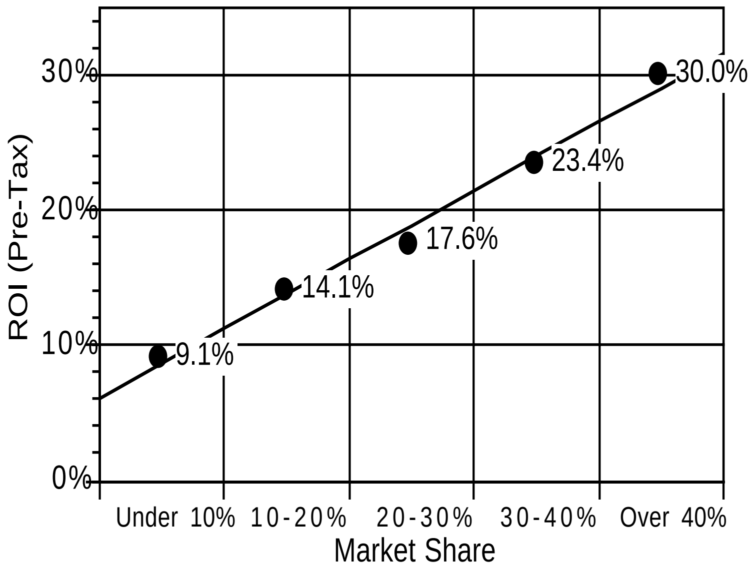
Relationship Between Market Share and ROI

The Marketing Science Institute did a study on the factors contributing to corporate profitability. They looked at several hundred products and found the following relationship between market share and ROI.

The MSI Study concluded that:

1. On average, a difference of 10% in market share is accompanied by a difference of about 5 points in pre-tax ROI.

Exhibit 1



2. Market share contributes to profit leadership in three significant and interdependent ways: economies of scale, market power, and quality of management.

3. Rewards tend to magnify as market share grows. Higher sales can almost always be achieved without proportionate increases in investment so, even at constant margins, ROI's improve. However, almost every category of operating expense declines with increased sales and market share (not just overhead expense, but also ingredient expense and other purchases). Thus, margins also improve and ROI's are magnified.

4. An interesting exception to the rule of declining expense is R&D expense which rises in proportion to sales as market share increases.

5. Product quality is directly related to increased market share and the relationship is extremely dramatic in cases of market dominance (over 40% share of market).

There are a number of other findings that deal with the interrelationship of market share and ROI. The comparisons were generally made comparing low market share companies vs. dominant market share companies (from under 10% up to and over 40%). There are also specific implications influenced by whether the buyer groups are "fragmented" (i.e., no small group of customers accounts for a significant proportion of total sales) vs. "concentrated".

1. Market share is profitable because it is accompanied by economies of scale.

2. Market share is profitable because it is accompanied by market power: i.e., better bargaining position, ability to influence prices, higher barriers to entry.

3. Market share is profitable because the company has good managers (or lucky managers!) who are successful in obtaining high shares, keeping costs down, maximizing productivity, pre-empting competition.

4. Once a business achieves a leadership position — particularly in a new field or product area — it is much easier to retain its lead than for others to catch up. It is five times more costly to get a customer than to keep one.

5. As market share rises, profit margin on sales increases sharply.

6. As market share rises, the company's purchases to sales ratio declines. High share companies tend to be more vertically integrated: they "make" rather than "buy".

7. As market share increases, there is some tendency for marketing costs, as a percentage of sales, to decline.

8. Market share leaders invariable have higher positive customer awareness than competitors. There is, consequently, more bang for the communication buck.

9. Large share (scale) permits a manufacturer to use its own sales force rather than commissioned agents and, at some point, to utilize specialized sales forces for specific product lines or markets.

10. Large share allows the spreading of marketing costs, and the ability to utilize the most efficient advertising and media vehicles.

11. Leading brands benefit from a "bandwagon effect" that results from the brands greater visibility.

12. Market leaders develop unique competitive strategies and have higher prices for their higher quality products than do smaller share businesses.

13. On the other hand, high relative prices reduce ROI for low market share businesses.

14. Market leaders tend to produce and sell significantly higher-quality products and services.

15. It is impossible to determine which variable is more important - the price premiums achieved by market leaders, or the difference in the quality of the competitors' products.

16. Market leaders spend significantly higher amounts (relative to sales) on R&D than do their smaller competitors.

17. R&D spending, plus a quality advantage, suggests market share leaders typically pursue a strategy of product leadership (certainly this is consistent with innovative leaders such as Eastman Kodak, IBM, Procter & Gamble, Merck and Loctite).

18. Market share is more important for infrequently purchased products than for those frequently purchased. ("Frequent" means purchased at least once a month).

19. Market share is more important to businesses when buyers are fragmented rather than concentrated.

20. ROI is greater for large share businesses when they spend more than their major competitors (in relation

to sales) on sales force effort, advertising and promotion, and research and development. These are not mutually exclusive spending areas.

21. High market expenditures hurt profits when product quality is low — and/or when the product does not live up to the claims of the communication.

22. In the long run vertically integrated companies have an advantage in mature businesses.

II. CRITICAL BENCHMARKS FOR BUILDING AND MAINTAINING A STRONG CUSTOMER FRANCHISE

One notion is axiomatic: strategic planning is a marketer's first job. In general, marketing failures in all too many cases come from:

1. Failure of management to make it very clear to marketing people and sales people that market share is the most worthy of all marketing missions, and without a market share position of a #1 or a strong #2, there can be no real lasting success. And over the longer pull, the only secure route to continuous profits is a #1 or a strong #2 market share position. Top management must believe in market share . . . must discuss the subject frequently with marketers, directors, the financial world . . . and must reward financially and generously those who are devoted to market share and are producing exceptional results.

2. Not seeing clearly that market share must be measured in units of sale (vs. dollars). Not understanding the importance of selling new applications.

3. Not having a group of qualified minds who are probing full-time for new products, label and package improvements or refinements, new descriptive names, secret ingredients, new selling concepts, and a shared responsibility for good sound proliferation.

4. Lack of decisive action when market share slippage first appears.

5. Expecting general managers or marketing personnel to maximize market share energies and at the same time to maximize energies in the creative, tedious, high-tension process of developing new and new-type products.

6. Lack of discipline.

7. Lack of understanding.

8. Structural organizational weaknesses.

9. Misunderstood priorities.

10. Too much emphasis on profits today.

11. Inexperienced marketing personnel.

12. Rewarding and promoting, in many cases, highly skilled and above-average performers — marketing or sales specialists — who understand marketing and who are doing outstanding work, into job assignments such as general managers where they become below-average performers.

13. Rewarding and promoting, in many cases, highly skilled accountants, engineers, or other specialists into general manager assignments or marketing assignments where they become average performers.

14. Management's willingness to compromise.

15. Non-recognition or lack of understanding or lack of anticipation of almost certain competitive actions and what is required to minimize competitive actions.

16. Product promotions are essential and constant search must be made for more and more effective promotions.

17. It must be clearly understood that an innovative success today on any product will be challenged tomorrow by a competitive reaction and thus, a time to plan for our next step is now.

18. Product selling failures are what might be termed either weak priorities, lack of discipline, lack of decisive action, lack of urgency, or not really a conviction that you must maintain a #1 or a strong #2 position for any real success.

19. Is it fair to say that a circumstance of the past has been one of wanting growth and market share, but perhaps lack of muscle, lack of discipline, much emphasis on profit today, and not a <u>fierce</u> competitive stance that exists in some companies, notably Michelin Tire and E&J Gallo?

20. A look at our main competitors' market share position, product by product, will clearly determine which companies have total commitment, discipline and nerve to make real the conviction that a #1 or a strong #2 position is absolutely essential long-term to a healthy customer franchise business.

III. DEVELOPING MARKETING STRATEGIES

Because action-oriented marketing plans must be articulated and executed at the operating level, these notes focus on the expectations of good in-depth marketing planning. The line between a tactical and a strategic issue is a thin one. Don't get bogged in semantics.

Missions and strategies are meant to provide the guidelines for broad strategic thrusts. However, it is still necessary to develop product marketing strategies. These are more narrow in scope than the overriding company strategies, but they must be written nonetheless. Marketing strategies are road maps to get from point A to point B and to achieve some pre-determined result. It is not enough to have annual sales forecasts masquerade as marketing planning when the real need is solid strategic planning.

Marketing strategies are written to cover the various elements of the marketing mix: sales, distribution, customer service, advertising, merchandising, publicity, packaging, pricing, market research and so on. Each element of the mix is a deployment of resources, and this deployment should not be implemented without well thought out strategies and objectives.

MARKET SHARE AS A STRATEGIC OBJECTIVE

Market share is strongly linked to profitability and ROI. Therefore, market share is both a critical strategic planning issue, and an important marketing objective. The road to higher and sustained profitability comes not through the maintenance of secondary shares, but rather by driving for and achieving market leadership. Market share leadership can be achieved by:

1. Committing sufficient human and financial resources to effectively execute product/marketing strategies.

2. Developing products with a clear and demonstrable advantage over existing products.

3. Avoiding head-to-head confrontation with large, well-entrenched, low-cost competitors.

4. Effectively communicating product characteristics to target customer-market segments.

A market leadership strategy can be just as applicable to products in established, mature, or stable markets as it is to new products in rapidly changing markets.

PRACTICAL MARKET DEFINITION

Market share leadership need not mean nationwide leadership or leadership in all subsets of the market. Leadership can be achieved on a regional basis or via market segmentation strategies. The key is not to define the market segments so narrowly as to create artificial or impracticably high market shares. Extraordinarily high shares that are a function of very small market definitions are self-deluding and do not inspire aggressive sales and marketing action. In fact, such high shares tend to cause holding strategies instead of building strategies; and results tend to be compared with industry indices, and the like, instead of comparisons to competitors' products' shares, volumes, and growth.

Marketing plans should focus on market share by product and/or by market. A strong market position in a regional market, or a leadership position with certain key customers, is likely to bring higher rewards than a strategy which positions the product weakly across the entire market. This may actually mean passing up some small opportunities in a market in order to concentrate resources to assure market leadership in the areas of big opportunity.

MARKET SHARE GOALS

The basic strategic issue for top management is to set market share goals. These goals depend on several things, including the strength of competitors, the resources available (both financial and <u>managerial</u>), and the willingness of management to forego present earnings for future results (the ROI and profitability rewards of high market share). Big increases in share are rarely achieved quickly, and expanding share is almost always expensive in the short run.
Consider the following in setting market share goals:

1. Often Annual Business Plans are drafted with little or no attention to market share. From a <u>product and/or market</u> perspective, where are you or where can you be #1?

2. Market share leadership which is achieved on the basis of price is less significant than leadership which is achieved by quality, convenience, proprietary technology, exclusivity, nichemanship, or other marketing levers.

3. Market share and market segmentation should be evaluated on a regional basis and among different customer groups and not exclusively on a national basis or across the total population. A skewed distribution with #1 or #2 position in some markets is a more profitable alternative than being an evenly distributed #3. Again, where are you, or where can you be #1?

4. Effective market segmentation requires that a marketing manager know what differentiates the buyers of his brand from the buyers of competitors' brands. Have you done the basic research to ascertain the differences which already exist vis-a-vis competitors? Why does the aware-user buy, and why does the aware non-user not buy? These are big marketing questions.

5. The importance of market share must be communicated broadly throughout the organization. Every salesperson must learn how to fight for market share.

ASPECTS OF STRATEGIC MARKETING PLANNING

A good marketing plan must be multidimensional. It should address the status of operations, key pressure points in the competitive environment (not "fillers" such as census count growths, GNP rates, etc.), key trends , the customers, the trade, the competition. These diverse dimensions must be factored into the strategic design.

There are many levers available to marketers. In fact, there is a more complex array of variables available to marketers than usually is found in the strategic marketing plan. Some seemingly minor mix levers can be very strategic. To illustrate, some companies protect their product line with patents on the package, as well as patents on the product form and on the processing techniques. Thus, packaging, which is normally thought of as a tactical issue, becomes a key strategic issue and a high barrier to competitive response.

Marketing is the profitable identification, attraction, getting and keeping of customers. Thus, marketing begins by identifying real customer needs and goes on to design products which fill those needs accurately. A partial list of the marketing levers begins with correctly identifying and researching the market, and goes on to include alternative competitive weapons for capitalizing on the marketing opportunity. These are the levers to profitably identify, attract, get and keep customers:

1. **Research** - identify the market, the unmet needs, competitors' weaknesses, segmentation. Deeply understand the aware-user and the aware non-user.

2. **Product Attributes and Design** - use, technology, formulation, smell, color, size, and so on.

3. **Quality** - the most important competitive weapon (defined by the customer).

4. **Positioning** - the highly complex art of establishing a quick positive understanding in the customer's mind, and definitely not doing so in manufacturing techno talk.

5. **Price** - the most important competitive decision.

6. **Brand Name** - the product positioning is the criterion for naming the product.

7. **Packaging** - no longer viewed as a carrier, but often integral with the product itself.

8. **Product Line** - length, new products, size mix, rationale.

9. **Convenience** - including ease of doing business with the company.
10. **Communication** - the total package of brands, labels, audiences, P.R.

11. **Advertising and Sales Promotion** - level, mix, quality, accuracy.

12. **Trademarks** - brand names are often the most valuable intellectual asset.

13. **Technology/Patents/R&D**

14. **Sales Effort** - failure to execute here can doom everything.

15. **Seasonality**

16. **Timing** - when you do something can be as important as what you do.

17. **Legal Action**

18. **Customer Service** - honest, prompt complaint handling creates more loyal customers.

19. **Technical Service** - getting the products to work is critical to customer satisfaction.

20. **Application Engineering** - helping customers get it right upfront is an invaluable sales tool.

21. **Acquisitions** - buying markets or technology is more significant than buying capacity.

22. **Private labeling**

23. **And many others**

Just as advertising messages must be grounded in the product, so must marketing plans be grounded in the market. Writing a decent mission can make the difference between a good plan and an inadequate one. Among other things, it defines where you want to compete. Marketing management must decide if the market definition is broad enough. The mission can determine the definition of competition. It articulates what business we are really in.

Once a good mission is written, there should be a section that accurately describes only the relevant issues impacting the company or product. This may include findings on competitive initiatives, customer changes, regulatory changes, defining meaningful segments in the overall market (geographic, industry groups, seasonality, life style, distribution.)

Part of the planning process is to communicate strategies throughout the organization and get their concurrence from those most involved with the ultimate execution. The strategy must be communicated to manufacturing, technical support areas, and so forth.

It is essential to monitor progress against plan to find out if the plan is any good. So each strategy must be designed with periodic check points or early warning systems.

KEY MARKETING MANAGEMENT QUESTIONS

There are at least twelve key questions that people responsible for sales and marketing should always know about their products.

1. What is the size of the market in dollars and units?

2. Who are the heavy aware-users and aware non-users by geographical location demographics, SIC code? (If you don't know this, for example, media budgets, direct mail budgets, and salesforce allocation can be easily misspent.)

3. What is the unit contribution to overhead and profits of the products and product lines?

4. What was the unit contribution a year ago?

5. Do you know where competitor plants are located, and their capacity?

6. What is the cost picture of the competitor's product line?

7. Have you talked to Purchasing recently, and what is their outlook on your raw material and packaging costs? What are you doing to Purchasing to motivate them to cut product costs... without sacrificing quality, service, or customer responsiveness.

8. When was the last time you visited end users, customers, distributor branches, stores — and what is really going on in the marketplace?