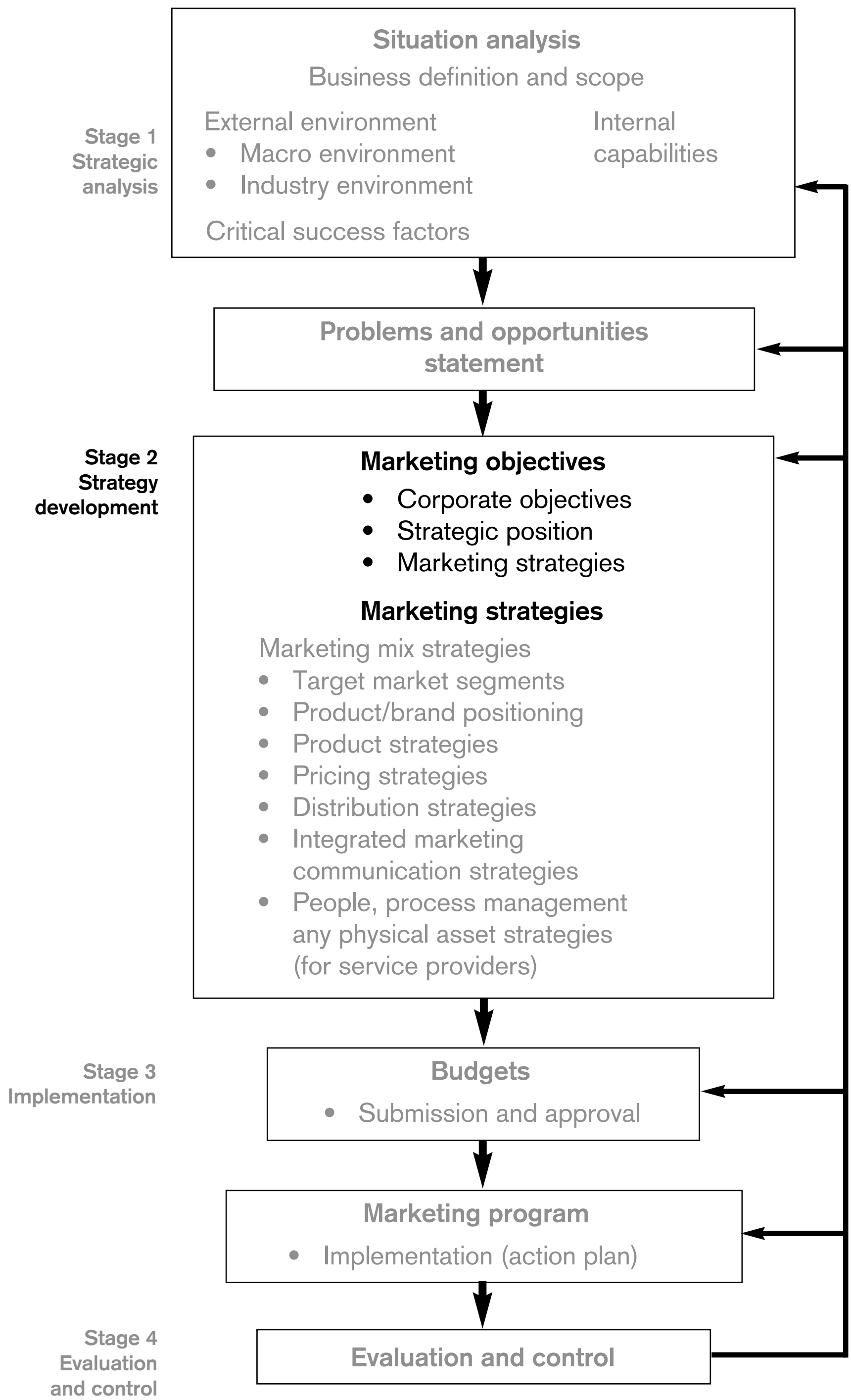
The strategic marketing planning process



4

Strategy development – setting marketing objectives and developing marketing strategies

What's needed in response to the new competition is focus and discipline – to define an unmatched value proposition, build an operating model, and sustain it through constant transformation and improvement.

Treacy and Wiersema[1]

The strategic marketing planning process comprises three main phases of work: the analytical phase described in Chapter 3, the process of strategy development, and the implementation of those strategies. This chapter addresses the second phase – the process of developing, or 'crafting',[2] effective marketing strategies. It is the most critical stage of the entire strategic marketing planning process involving higher level business and marketing decision making, setting marketing objectives and the development of marketing strategies.

As was discussed in Chapter 2, these decisions in market-oriented organisations are made in the first place at the business level of strategy. That is, marketing strategies are developed as a part of the overall strategies developed at the business level of organisation. These strategies focus on how the business unit will compete in its chosen industry – specifically, how it will achieve and sustain a competitive advantage.

At the business level of strategy, the major focus for marketing concerns product-market decisions (market segmentation and targeting to decide which product-markets the SBU should compete in), product-positioning decisions and strategic-alliance decisions (who, when and how to partner). These decisions flow down to the operating level of marketing involving the development of marketing mix strategies and the development of strategies for managing customer and reseller relationships. These strategy decision-making processes are discussed in subsequent chapters of this book. For now, the emphasis in this chapter is towards the development of higher level strategies and the impact of these strategic decisions on the development of marketing mix strategies.

A framework for establishing marketing objectives

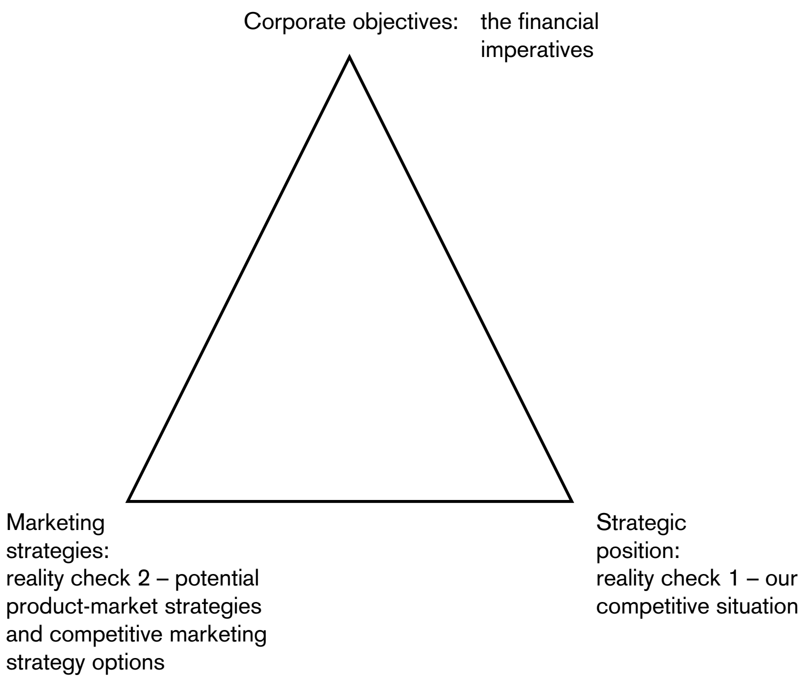
Marketing objectives and marketing strategies can be viewed as being parts of a continuum (a continuous whole or a thing whose parts cannot be separated). Objectives are ends, and strategies are the means for achieving those ends. Under this view objectives and strategies have both a top-down and bottom-up relationship. Strategies are developed in order to achieve desirable objectives, and objectives are developed which can realistically be achieved by available strategies.

Two points need to be made about the objective setting/strategy formation processes. First, decisions concerning the establishment of objectives are predicated on assumptions of what is likely to occur in the future. However, because forecasting is notoriously difficult (as was discussed in Chapter 3) objectives should not be considered to be cast in stone. Long-term objectives need to be regularly reviewed in light of changing environmental circumstances. Second, objectives cannot be set in isolation of consideration of strategic issues, an underlying assumption of many of the strategic planning models of the 1960s and 1970s. Many of these models were based on a 'numbers game' notion that top management, via a process of setting objectives, could summon those below to develop strategies capable of achieving those objectives. Objectives were set in order to motivate and to control performance. As Mintzberg laments: 'What are called strategic planning exercises often reduce to the generation of numbers, not ideas – objectives and budgets but not strategies'.[3]

The iterative process of setting marketing objectives and developing marketing strategies

The operative word here is *iterative*. The process of developing marketing objectives is, essentially, a balancing act between three sets of considerations, which are depicted graphically in Figure 4.1.

FIGURE 4.1 Three sets of considerations in setting marketing objectives and developing marketing strategies



The first consideration in the process of strategy development is to determine *corporate objectives* – the financial imperatives and other performance-related goals that the business unit must achieve, over the period of the strategic marketing plan, in order for it to be judged favourably by its stakeholders. Corporate objectives are essentially top-down goals for the strategic business unit to achieve. However, corporate objectives may simply represent the wishes of top management rather than reflecting marketplace reality. They may set corporate objectives as a motivational device, such as a BHAG (Big Hairy Audacious Goal),[4] or alternatively as a mere extrapolation of past performance.

The second set of considerations, the *strategic position* of the business unit, is the first of two reality checks to be factored into the decision-making mix. This step consists of three main processes: analysis of the business unit's current strategic position, development of competitive strategies, and determination of appropriate marketing objectives and strategies that flow on from the competitive strategies. Strategic position analysis involves consideration of current and future market attractiveness and the competitive position of the business unit in that market (or markets). Based on this analysis a realistic view of the business unit's future growth potential can be developed. For example, a business unit with a high proportion of its products competing in a number of declining markets could hardly be expected to substantially increase its future revenue and profit base unless it could adopt some sort of a transformational strategy.

Consideration of the strategic position of the business unit provides a first-cut view of aligning the top-down corporate objectives with the reality of the business unit's strategic position in the market or markets it competes in. However, neither of these first two steps provides the strategist with a view of marketplace reality. Just how can the business unit achieve its revenue objectives? And, where from? More precisely, what products in what markets will potentially generate this revenue? The third set of considerations, *marketing strategies*, provides this bottom-up input into the decision-making mix. It addresses four product-market strategy options – the revenue that can be achieved from:

- market penetration (existing products in existing markets);
- market development (existing products in new markets);
- new product development (new products in existing markets);
- related diversification (new products in new markets).

Each of these three sets of considerations is discussed in detail in the following sections of this chapter. A summary section providing a practical framework for going about this complex decision-making task follows these discussions.

Corporate objectives and business unit objectives

Objectives are the end results to be achieved. In this context the term 'corporate objectives' has been used broadly to cover the objectives for an organisation as a whole and for each business unit as a part of that whole.

Performance objectives consist of the financial requirements for the organisation and other key result areas, which are critical for the organisation's short-term and long-term success. These include profitability, return on investment (ROI) return on assets (ROA), earnings per share (EPS), dividends and cash flow. They are usually determined on the basis of satisfying the needs of the stakeholders, which includes shareholders and others who might have a 'stake' in the business such as management, employees, customers, suppliers and creditors. The driving force underpinning financial performance in the majority of cases is shareholder value. If the organisation performs well financially, share prices are maintained or increased. If financial performance is below expectations, share prices drop, limiting the organisation's ability to attract equity financing to underwrite future operations and growth while also exposing the organisation to the danger of a takeover. Poor financial performance, particularly cash flow, also limits an organisation's ability to attain debt financing (borrowing).

However, the use of financial performance objectives alone is a dangerous preoccupation for top management. Shareholder value can be enhanced in the short term by cost-reduction strategies such as downsizing and the reduction of product quality. In the long term this might cause customers to become dissatisfied with the organisation's products or services, which in turn could lead to a loss of market share, reduction of profitability and eventual decline in share price.[5] That is, a focus on short-term shareholder value can lead to the diminution of customer value with a resultant loss of competitive advantage and a decrease in long-term financial performance. In order to provide a broader perspective of the organisation's direction a number of non-financial performance objectives should be included as either corporate or business objectives: improvement in innovativeness, improvement in operational efficiency, improvement in product quality, improvement in customer satisfaction, social responsibility and employee welfare. All of these objectives can be translated into specific, achievable and measurable objectives. For example, the 3M Company sets a corporate performance objective based on innovation whereby each business unit is expected to achieve 30 per cent of its revenue from products introduced in the past four years.

Business unit financial performance objectives may be set by the use of sophisticated planning tools such as Du Pont ratio analysis or value-based planning models including economic value added (EVA™) and discounted cash flow methods or **product portfolio models**. (Refer to Appendix 1 at the end of this chapter for a brief outline of the Du Pont and EVA™ methods. Product portfolio models are discussed in the next section.) Alternatively, performance objectives may be developed on a more subjective basis such as to 'double sales in five years'. This was indeed the challenge that Dr Tony O'Reilly issued to the management of Waterford Crystal when he took over as chairman of what was a struggling company. In August 1995, in what was to become known as 'the chairman's challenge', a goal was established to double sales by the end of 1999 while achieving an operating margin of 15 per cent.

Strategic position

The task here is for the strategist to (1) determine the strategic position of the organisation in terms of the attractiveness of the market it competes in and its competitive position within that market; (2) develop competitive strategies for the time horizon of the strategic marketing plan; and (3) set marketing objectives that are in line with the strategic direction of the business unit. There are a number of tools that can assist the strategists in these analytical and decision-making tasks, specifically by providing guidelines that can be drawn on to assist in establishing appropriate objectives and strategies for the strategic position to be taken.

The point needs to be made, however, at the outset of the discussion of these tools that they should be regarded as aids for decision making, not as prescriptive mechanisms. Many of these tools were abused by strategy planners in the 1960s and 1970s and, rightfully so, considerable criticism has been levelled at many of them. However, if some of these tools are completely disregarded, there is also an equal danger of throwing away the baby with the bath-water. A balanced viewpoint is to consider these tools not as immutable prescriptions but as useful aids for strategic decision making. Three main concepts and techniques will be discussed:

- the **product life cycle (PLC)** concept;
- product portfolio models (BCG and GE/McKinsey);
- the concept of sustainable competitive advantage.

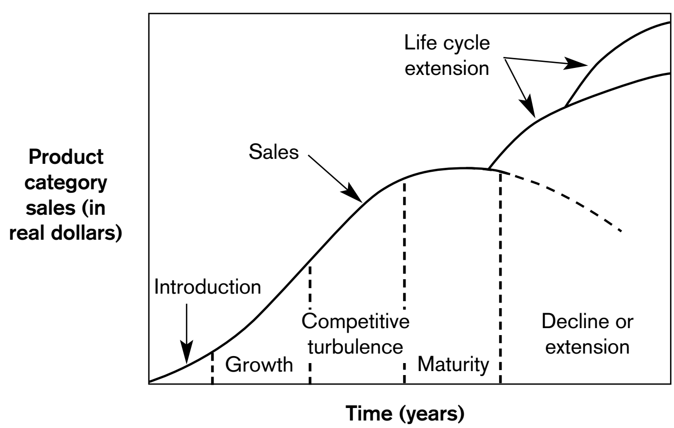
These concepts and techniques provide a means of (1) analysing the current strategic position for the business unit and/or its product lines; (2) determining whether there is a need to change the strategic position; and (3) setting appropriate marketing objectives and higher level marketing strategies in line with the strategic positioning.

The product life cycle concept

The product life cycle concept was developed during the late 1950s[6] and came into prominence during the 1960s. The concept is quite simple as it postulates that products, like human beings, pass through a number of different phases or stages of their life. In the case of products, the stages are described as introduction, growth, maturity and decline. An additional stage described as competitive turbulence or shake-out is also shown in some PLC models as can be seen in Figure 4.2.

There are three levels or dimensions of product life cycles: the brand level, the product category (product subclass) level and the industry (product class) level. The product category level is the most useful for providing guidelines for the development of marketing objectives and strategies.

FIGURE 4.2 A typical product life cycle pattern



The strategic implications of the PLC have been one of the most popular subjects in marketing literature. Box 4.1 provides a summary of the typical characteristics of each of the PLC stages and the marketing strategic implications.

Although there are some variations between the guidelines presented in the various PLC models, Box 4.1 represents what could be described as a typical model. It can be observed that these guidelines are fairly general in nature and that they do not provide for differences in market position (such as different objectives for a leader, a challenger or a follower) or for markets that do not follow the typical S-shaped curve of the PLC

BOX 4.1 TYPICAL CHARACTERISTICS OF THE PLC STAGES AND THE MARKETING STRATEGIC IMPLICATIONS

	Introductory	**Growth**	**Competitive turbulence**	**Maturity**	**Decline**
Characteristic					
Sales	Low	Rapidly	Slowing	Peak sales Cyclically sets in	Declining
Prices	High	Lower than introduction	Low	Low	Falling
Profits (per unit)	Negative	High and rising	Declining	Average	Declining
Customers	Innovators + early adopters	Early majority	Early majority	Late majority	Laggards
Competition	Few	Growing number of imitators	Shake-out begins	Declining numbers	Further decline
Strategic implications – marketing objectives and strategies					
Marketing objective	Encourage trial Establish distribution	Market share penetration Attract new users	Protect and strengthen niches	Protect share Manage for earnings Keep loyal users Extend the PLC	Halt decline or reduce expenditure and milk for profit
Product	Basic	Offer extensions, features, service	Tighten line, improve quality	Diversity of brands and models Reposition brand if necessary	Phase out weak items
Price	Skimming or penetration	Maintain prices	Match or beat competitors	Defensive	Maintain profit margins
Distribution	Selective	Build intensive coverage	Strong dealer support	Intensive and extensive	Selective
Promotion	Create awareness Develop brand loyalty	Stimulate wider trial Emphasise brand loyalty	Maintain customer franchise	Stress brand differences and benefits	Phase out Maintenance weight only

model. It should also be recognised that the concept has been subjected to a good deal of criticism which can be summarised as follows:

- There is a difficulty in defining the appropriate market.
- The length of the various stages differs for different products or industries. It is often not clear what stage the product/brand is at.
- The S-shaped pattern does not always occur. Swan and Rink, for example, contend that there are as many as ten different PLC curves.[7]
- The players can affect the growth curve by extending it in a variety of ways such as repositioning and product innovation.
- Generalised strategic implications are questionable, because of divergent patterns between industries such as competitive structure (may vary during the stages), and the various strategies the competitors use such as price competition, advertising and R&D expenditure.

Porter argues that industry takes many different paths so that the PLC pattern, which describes one pattern, does not always hold. Moreover, he contends that there is nothing in the concept that provides for a prediction of when the S-shaped pattern holds or when it does not.[8] Therefore, it should be noted that care must be taken when developing objectives and strategies based on PLC models. The suggested guidelines are a good starting point for the process of decision making but nothing more than that.

Product portfolio models

During the early 1960s the notion of product portfolio management was introduced as a means for diversified organisations to make decisions concerning the allocation of corporate resources to their various SBUs. These models provided strategists with tools for evaluating the strategic positions of each SBU and appropriate strategic prescriptions. In practice product portfolio models were also used by SBUs to evaluate the strategic positions of their various product lines and to formulate strategies for those product lines.

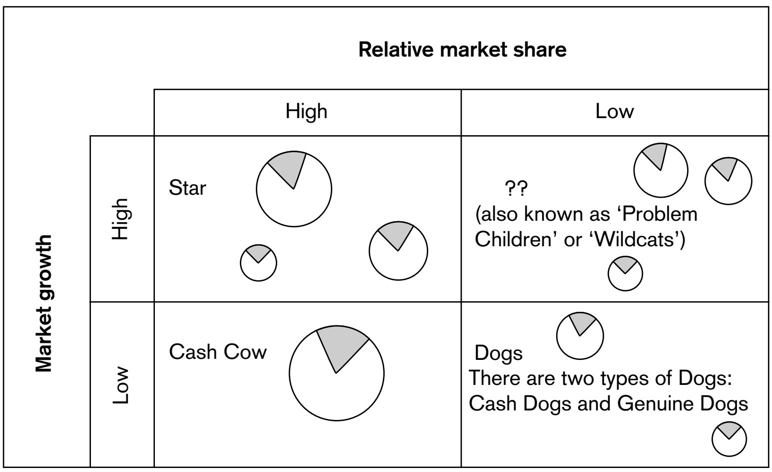
A variety of portfolio models were developed during the 1960s and 1970s with the most publicised being those produced by the Boston Consulting Group, General Electric in consultation with McKinsey & Company and Arthur D. Little. All of these models followed a similar process of evaluating the positions of an organisation's SBUs on a grid or matrix. These positions were plotted on two main dimensions: business strength (an assessment of the strength of each SBU relative to its competitors) and market attractiveness (of the industry the SBU competed in). The first two of these models are summarised in the following section, including a description of the steps to be taken in constructing each model and a summary of the strategic recommendations.[9]

Boston Consulting Group growth/share matrix

The underlying concept of the Boston Consulting Group (BCG) model, developed in the late 1960s, is that strategic business units comprise a corporation's portfolio of investment opportunities. Each SBU's strategic position is plotted on a four-quadrant grid, which is shown in Figure 4.3. It is a two-dimensional model based on *market growth*, which forms the vertical axis of the matrix, and *relative market share*, which forms the horizontal axis. Market growth is essentially a proxy for market attractiveness and the stage the market has reached in its product life cycle. Relative market share is a proxy for the business unit's competitive strength and is computed by dividing the SBU's market share (in value or volume) by that of the largest competitor.

Market growth is subdivided into two categories – *high* and *low*. Determining the cut-off point between these two categories is therefore a critical decision. Similarly, relative market share is divided into *high* and *low* categories and, accordingly, a decision also needs to be made about where this vertical line should be drawn. These two critical decision points are discussed in Appendix 1 at the end of this chapter.

FIGURE 4.3 The BCG product portfolio model



Once the vertical (market growth) and horizontal (relative market share) lines are determined the strategic position of each SBU can then be plotted on the grid. The relative size of the circle for each SBU can be drawn so as to represent sales volume. A segment drawn within this circle can be shown to represent profit contribution.

Categorising each business unit

The BCG product portfolio model provides a means of categorising the strategic position of each business unit into four areas: Stars, Cash Cows, Question Marks and Dogs. Based on these classifications the model is then used by strategists to consider the strategic implications, in terms of future earnings and cash flow, of investing the corporation's resources in each SBU.

- **Stars.** These are SBUs with high relative market share in high-growth markets. Stars are essential for the corporation's long-term success but, paradoxically, they are quite often net users rather than suppliers of cash. High-growth markets are those that are in the introductory or growth stage of the PLC, and business units in these markets are required to invest heavily in market and new product development during these phases of market evolution.
- **Cash Cows.** These are SBUs with high relative market share in low-growth markets. Cash Cows are former Stars that have drifted into this quadrant as their markets have

matured and growth has slowed (or even become negative). Cash Cows are cash generators enjoying economies of scale and reduced investment requirements as the emphasis turns to maintaining rather than establishing market leadership. Profit margins are relatively high.

- **Question Marks.** These are SBUs with low relative market share in high-growth markets. These SBUs are Problem Children as they have been unable to gain a strong position in the market they compete in. They are often new to the market. These business units require large amounts of cash and the objective is to shift them to the left quadrant to become a Star. Otherwise, when the market matures they will slip down into the Dogs category.
- **Dogs.** These are SBUs with low relative market share in low-growth markets. There are two categories of Dogs: *Cash Dogs* and *Genuine Dogs*. Cash Dogs are profitable but Genuine Dogs are either unprofitable or very nearly unprofitable

The aim is to have a balanced portfolio of businesses, which is achieved by following a *success sequence* in which cash generated by Cash Cows is invested in developing Question Marks so that they will become Stars. In turn the Stars will one day change into future Cash Cows as the markets they compete in mature.

It should be noted that the model was originally developed to provide strategists at the corporate level of organisation with an analytical tool for developing strategies for a portfolio of business units. However, it is recommended that the model should be also applied at business unit level in order to review its portfolio of product lines and as an aid for developing strategies for those product lines. It can also be used at a product line level to review the strategic position of individual products and brands within the product line.

Suggested BCG objectives and strategies[10]

Stars: 'Invest for growth'

- Market share objective:
  - Hold/increase; that is, defend leadership or gain if possible. Accept moderate short-term profits and negative cash flow.
- Strategies:
  - Consider geographic expansion, product line expansion and product differentiation.
  - Upgrade product introduction effort.
  - Adopt an aggressive marketing posture, namely selling, advertising, pricing, sales promotion and service levels as appropriate.

Question Marks/Problem Children: 'Opportunistic development'

- Market share objective:
  - Increase or harvest/divest.
- Strategies:
  - Invest in selective products.
  - Identify and target uncontested and/or emerging market segments.
  - Pursue similar strategies as previously stated under 'invest for growth'.

Cash Cows: 'Manage for earnings'

- Market share objective:
  - Hold; that is, maintain market position and manage for earnings.

- Strategies:
  - Maintain market position in most successful product lines, and prune less successful product lines.
  - Differentiate products to maintain share of key segments.
  - Limit discretionary marketing expenditure.
  - Stabilise prices, except where a temporary aggressive stance is necessary to maintain market share.

Dogs[11]

1 Cash Dogs
- Market share objective:
  - Hold. Acknowledge low growth – do not view as a 'marketing problem'.
- Strategies:
  - Identify and exploit growth segments.
  - Emphasise product quality to avoid 'commodity' competition.
  - Systematically improve productivity.
  - Assign talented managers.

2 Genuine Dogs
- Market share objective:
  - Harvest/divest.
- Strategies:
  - Prune product line aggressively.
  - Maximise cash flow.
  - Minimise marketing expenditure.
  - Maintain or raise prices at the expense of volume.

Criticisms of the BCG model

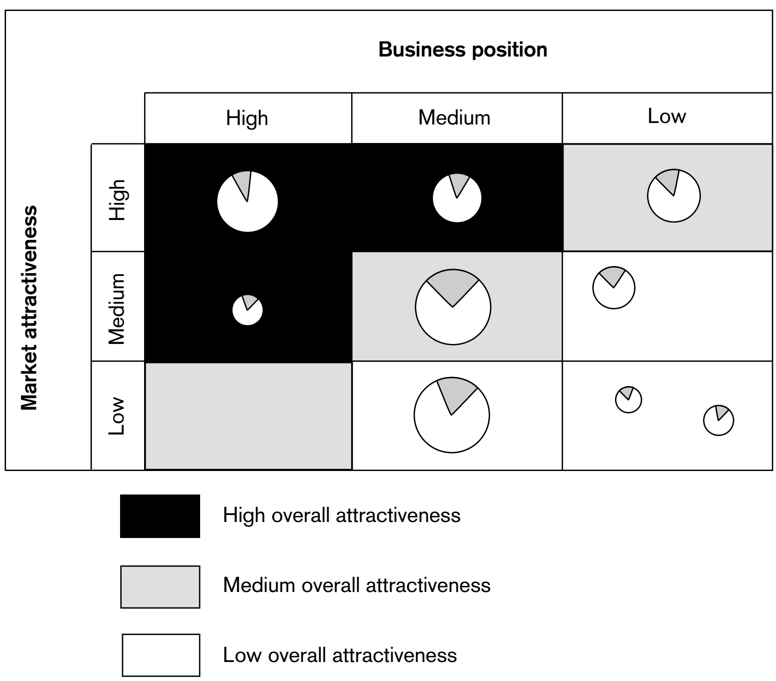
- In many circumstances, factors other than relative market share and market growth influence cash flow.
- The assumption that relative market share is linked to profit, thereby indicating business strength, does not hold as there are many other factors that influence business position including financial resources, marketing expertise and access to distribution channels.
- The assumption that market growth is an adequate indicator of market attractiveness is similarly flawed as there are many other factors that influence market attractiveness. These include the factors identified by Porter in his five-forces model (competitive rivalry, threat of new entrants, bargaining power of suppliers, bargaining power of buyers and threat of substitutes) discussed in Chapter 3. Additionally, legal and technological factors affect market attractiveness.
- Cash flow may be less important than ROI in determining the attractiveness in investing in one business unit or another.
- The model provides little insight into how one business unit might be compared with another in terms of investment opportunity. For example, is every Star better than a Cash Cow?

The General Electric/McKinsey model

In the early 1970s General Electric (GE) became interested in the portfolio management approach. However, General Electric management believed that the BCG approach overlooked a number of important factors that determine market attractiveness and business strength. Accordingly, they commissioned McKinsey & Company to develop an alternative model, which is shown in Figure 4.4. This model has become widely known as the GE/McKinsey market attractiveness / business assessment matrix although it is also alternatively referred to as the GE/McKinsey screening grid. Shell and Arthur D. Little developed a similar model known as the industry maturity/competitive position grid or the directional policy matrix.

The GE/McKinsey model is, like the BCG model, two-dimensional. However, instead of using a single factor as the basis for determining market attractiveness and a single factor for determining business position, the GE/McKinsey model uses a variety of factors. That is, it is a multifactor portfolio model. Additionally the GE/McKinsey model divides each dimension into *high*, *medium* and *low* categories, thereby proving nine strategic positions compared to the four strategic positions in the BCG model.

FIGURE 4.4 The GE/McKinsey market attractiveness / business assessment matrix



The steps to be taken and the factors to be considered in constructing the GE/McKinsey multifactor portfolio model are outlined in Appendix 1 at the end of this chapter. It should be appreciated that this is a more complex model than the BCG model and that it takes a considerable amount of time and effort to construct. It involves judgements about determining factors that make a market attractive and for determining the strength or otherwise of business in that market. Moreover, it requires strategists to rank and to weight the importance of each factor, which means that the model constructs are highly subjective.

The GE/McKinsey model was designed to be used as a tool for corporate level strategists to assign investment priorities in their various business units and to provide a guide for resource allocation. Like the BCG model it is recommended that marketing strategists should develop this model at both the corporate level and business unit level to review the strategic position of the business unit as a whole and the strategic positions of the product lines within the business unit.

BOX 4.2 GENERIC STRATEGIC OPTIONS FOR THE GE/MCKINSEY MATRIX[12]

Protect position • Invest to grow at maximum digestible rate. • Concentrate effort on maintaining strength.	**Invest to build** • Challenge for leadership. • Build selectively on strengths. • Reinforce vulnerable areas.	**Build selectively** • Specialise around limited strengths. • Seek ways to overcome weaknesses. • Withdraw if indications of sustainable growth are lacking.
Build selectively • Invest heavily in most attractive segments. • Build up ability to counter competition. • Emphasise profitability by raising productivity.	**Selectivity/ manage for earnings** • Protect existing program. • Concentrate investments in segments where profitability is good and risk is relatively low.	**Limited expansion or harvest** • Look for ways to expand without high risk; otherwise, minimise investment and rationalise operations.
Protect and refocus • Manage for current earnings. • Concentrate on attractive segments. • Defend strengths.	**Manage for earnings** • Protect position in most profitable segments. • Upgrade product line. • Minimise investment.	**Divest** • Sell at a time that will maximise cash value. • Cut fixed costs and avoid investment meanwhile

The concept of sustainable competitive advantage

The concept of competitive advantage was championed by Porter in the 1980s and 1990s.[13] Porter contends that a 'company could only outperform its rivals if it could establish a difference that it could preserve – by delivering greater value to its customers or by creating comparable value at a lower cost, or by doing both'.[14]

Porter's generic 'competitive strategies model' introduced in his 1980 book *Competitive Strategy* and elaborated in his 1985 book *Competitive Advantage* provides a means for managers to (1) evaluate their firm's competitive position, and (2) develop strategies to improve their current position. This model, shown in Figure 4.5, is based on two dimensions: the type of competitive advantage and competitive scope. Porter argues that an organisation must choose between a low-cost or differentiation form of competitive advantage and between a broad (industry-wide) or narrow focus. That is, there are four generic strategies or routes to competitive advantage that an organisation can pursue.

FIGURE 4.5 Porter's concept of generic competitive strategies

		Types of advantage	
Competitive scope	Broad	Broad cost	Broad differentiation
	Narrow	Focus cost	Focus differentiation

Cost leadership

Cost leadership strategies can be employed at a market-wide level (a broad competitive scope) or by market nichers (a focus or narrow competitive scope). With a cost leadership strategy the objective is market share leadership based on a marketing strategy in which cost leadership is the main strategic tool. This strategy needs to be addressed at the business unit level (that is, at an organisation-wide level) and not just at the marketing level. In order for it to be successful, the organisation needs to become the low-cost producer in its industry. This therefore necessitates attention to non-marketing functions, particularly production, supply and R&D in addition to marketing functions. Porter argues that cost leadership is appropriate where an organisation has economies of scale and has been able to reduce costs due to 'the experience curve' effect. As he elaborates:

> Cost leadership requires aggressive construction of efficient-scale facilities, vigorous pursuit of cost reductions from experience, tight cost and overhead control, avoidance of marginal customer accounts, and cost minimisation in areas like R&D, service, sales force, advertising and so on.[15]

Porter contends that achieving a low overall cost position often requires a high relative market share or other advantages such as having favourable access to raw materials or designing products that are easy to manufacture, spreading costs over a wide product line and serving all major customer groups. Having a low-cost position yields a firm above average returns.

These strategies will be discussed in further detail in subsequent chapters, particularly Chapter 7 which is concerned with pricing strategies.

Differentiation

Differentiation strategies can be employed at a market-wide level (a broad competitive scope) or by market nichers (a focus or narrow competitive scope). This strategy calls for differentiating a product or service from the competitor's products or services. Differentiation refers to a customer's perception of difference (uniqueness) and superiority on at least one physical or non-physical product characteristic.[16] The key to a successful differentiation strategy is to identify needs that customers believe to be important and to deliver value to those customers. Differentiators seek to command premium prices; therefore, their customers have to be willing to pay the premium for the perceived value they will receive. The differentiation may be in the product form, brand image, product features, breadth of the product line, technology, customer service, pricing or distribution channels. At the heart of a successful differential strategy is the development of a customer franchise based on brand loyalty. The differentiator can increase margins and avoid the need to compete in the low-cost section of the market. This often implies a lower market share and is a strategy to be pursued when the low-cost leadership position is occupied by a strong competitor.

These strategies will be discussed at greater length in later chapters, particularly product differentiation (Chapter 6), pricing differentiation (Chapter 7) distribution differentiation including customer service (Chapter 8) and image/perception (Chapters 9 and 10).

Porter argues that winners in a chosen industry single mindedly pursue one of the four generic strategies. Each strategy requires a different managerial approach and different skills and assets. He warns that a strategy of being 'stuck in the middle' – where two or more generic strategies are pursued at the same time – will not achieve a competitive advantage:

> The firm in the middle is almost guaranteed low profitability. It either loses the high-volume customers who demand low prices or must bid away its profits to get this business away from low-cost firms. Yet it also loses high-margin business – the cream – to the firms who are focused on high-margin targets or have achieved differentiation overall. The firm stuck in the middle also probably suffers from a blurred corporate culture and a conflicting set of organisational arrangements and motivation system.[17]

Figure 4.6 provides a useful matrix for analysing the cost leadership versus differentiation strategy direction pursued for the organisation's products and for analysing competitive strategies.

FIGURE 4.6 Strategy options based on relative costs and differential alternatives

		Relative costs	
		High	Low
Degree of differentiation	High	1 Market niche	2 High differentiation/high margins
	Low	3 Disaster area	4 Cost leadership

The low relative cost / low degree of differentiation position quadrant no. 4 (Figure 4.6) is where the market leaders would be expected to be found. This is generally a strategy that only the market leader or perhaps a strong no. 2 or no. 3 could successfully pursue. The risk for competitors pursuing this strategy is that as the industry matures their cost leadership advantage could diminish over time. To offset this the organisation must keep abreast of technological innovation, reinvest in modern equipment, scrap obsolete assets and avoid product line proliferation. In some extreme cases the ideal position shown in quadrant no. 2 (Figure 4.6) may be a strategic alternative. If the competitor has a low relative cost and a high degree of differentiation, then it can achieve high margins by pricing either at or just above its competitors (who have higher relative costs). This quadrant may also be occupied by competitors in the low-medium relative cost area who price higher than the cost leader but substantiate the premium price by their medium to high level of differentiation. These competitors must have customers that are willing to pay the additional price to receive the 'added value' for the product. The danger of this strategy is that, as an industry matures, the products tend to be increasingly regarded by the market to be generics or commodities. The value of paying a premium price for the added value (differential) diminishes and customers turn to the lower priced alternatives.

Where neither of these two strategies is available, the competitor can choose to focus on a niche or single segment of the market as shown in quadrant no. 1 (Figure 4.6). Prestige car manufacturers typically pursue this strategy by producing a relatively high-cost product that is highly differentiated. They appeal to a segment that is prepared to pay a high price to acquire a differentiated product. The final quadrant, to be avoided like the plague, is quadrant no. 3 (Figure 4.6): the high relative cost / low degree of differentiation strategy.

In 1996 Porter provided an elaboration of his earlier work on strategy.[18] First, he argues that a company can only outperform its competitors if it establishes a difference that it can preserve. This can be achieved only by delivering greater value to its customers, by creating comparable value at lower cost or by doing both. He argues that it is a mistake to confuse operational effectiveness with strategy. Operational effectiveness means performing similar activities better than competitors perform them. Strategic positioning, on the other hand, means either to perform different activities from that of the competitors or to perform similar activities differently. While operational effectiveness is necessary it can only provide a short-term advantage as competitors will soon catch up on the productivity front.

Second, Porter argues that competitive strategy is all about being different – 'deliberately choosing a different set of activities to deliver a unique mix of value'.[19] He argues that strategic positions emerge from three distinct, but frequently overlapping, sources:

- *variety-based positioning*, which produces a subset of an industry's products or services;
- *needs-based positioning,* which serves most of the needs of a particular group of customers;
- *access-based positioning*, which segments customers who are accessible in different ways (essentially, a distribution-based strategy).

The above three sources of strategic positioning expand the earlier concept of generic strategies by providing three possible sources of strategic positioning for each of the four generic strategies. For example, a low-cost industry-wide competitor can chose a variety-based, needs-based, access-based positioning strategy or a combination of these three sources.

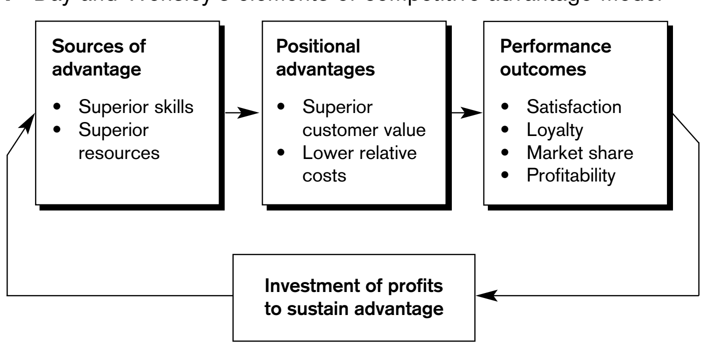
Other dimensions of competitive advantage

Towards the end of the 1980s it became increasingly apparent that strategies based on either low-cost leadership or differentiation were by themselves not enough to provide organisations with a sustainable competitive advantage. Time-to-market or *time compression* [20]– the ability to do things more quickly than the competitors – was discovered as a new source of advantage. Companies increased the speed of getting new products to market (new product realisation), manufactured and distributed on a just-in-time basis, provided quick-response customer service and responded more quickly to market trends and opportunities than their competitors. The new way of thinking or 'new wisdom' as Kanter expressed it, was that organisations need to focus on internal processes.[21] Hamel and Prahalad argue that core competence – the combination of individual technologies and production skills underlying an organisation's product lines – is the essential building block of strategy.[22] The core competence of Sony, they argue, is miniaturisation, which underpins all of their products, from the Sony Walkman to notebook computers. Stalk, Evans and Shulman point out that a focus on core competence is not enough. They argue that the key to success is 'capabilities-based competition'. In an increasingly dynamic business environment, Stalk and his colleagues maintain that 'successful competitors move quickly in and out of products, markets and sometimes even entire businesses'. They argue that 'capabilities-based competitors identify their key business processes, manage them centrally, invest in them heavily, looking for a long-term payback'.[23]

Drawing two views of competitive advantage together

A focus on internal capabilities or core competencies contrasts with the view of competitive advantage proposed by Porter. That is, as Day and Wensley point out, there are two schools of thought as to what the term 'competitive advantage' actually means.[24] The first interpretation is that competitive advantage is analogous to 'distinctive competence' – the possession of superior skills and resources. The second interpretation is that competitive advantage represents the achievement of positional superiority – lower relative costs (cost leadership) or superior customer value (differentiation). Day and Wensley argue that neither of the two views provides a complete picture of competitive advantage and that therefore they need to be integrated in order to describe the state of advantage and how it is gained. Figure 4.7 shows the sequence of how competitive advantage is created and sustained, and the performance outcomes (of achieving a competitive advantage).

FIGURE 4.7 Day and Wensley's elements of competitive advantage model



Source: G.S. Day & R. Wensley, 'Assessing advantage: A framework for diagnosing competitive superiority', *Journal of Marketing*, vol. 52, April, 1988, p. 3

Positional advantages and performance outcomes are a consequence of the sources of advantage an organisation has (relative superior skills and resources). Superior skills and resources together provide an organisation with the ability to do more or do better (or both) than its competitors. Superior skills are the distinctive capabilities of personnel arising from their ability to perform individual functions more effectively than competitors. Superior resources can be found in the scale of operations, location, sales-force breadth, distribution coverage, availability of automated assembly lines and brand name power. Superior skills and resources are the antecedents of positional advantage which are manifested in two forms: superior customer value and lower relative costs. Superior customer value (differentiation) is achieved when an organisation performs some value-adding activity that leads to customer perception of superiority. Lower relative costs are achieved by an organisation performing most of its activities at lower costs than its competitors – while offering a parity product. The achievement of a sustainable competitive advantage is measured in terms of customer satisfaction, customer loyalty, market share and profitability (performance outcomes). Profits are invested in the acquisition or enhancement of the organisation's sources of advantage (superior skills and resources) in order to achieve or maintain a long-term sustainable competitive advantage.

How to use these concepts and techniques

As stated at the beginning of this section the PLC, product portfolio and competitive advantage concepts provide a means of assisting the strategist in analysing the current strategic position of the business unit and, based on this analysis, decisions concerning the future business position and concomitant marketing objectives and higher level marketing strategies. It is suggested that all of these tools should be used and drawn upon for this phase of strategic analysis and decision making. In this way these tools should be used as a starting point, not as an end point, for making these critical decisions.

It should also be pointed out that the emphasis here is to draw on the tools by synthesising the various strategic insights that they provide along with their strategic advice. For example a marketing strategist may write the following: 'XYZ business unit is the market leader in a market that has reached maturity and is anticipated to show very little growth over the next three years. XYZ is categorised as a *Cash Cow* (BCG) and as a business unit in a market of *high overall attractiveness* with a strong business position in a market of medium attractiveness (GE/McKinsey). XYZ's competitive advantage is based on a *market-wide cost leadership strategy* (Porter) because of its economy of scale, high level of brand equity and strong distribution support. Given XYZ's current strategic position and the prospect of a stagnant or declining market, it is recommended that investment should be concentrated in developing and nurturing new products and in developing new markets. The objective for existing products in existing markets is to maintain current market share and to manage for earnings by rasing productivity.'

Marketing strategies

The third step of the decision-making process is a bottom-up process of considering marketplace reality. In what markets and with what products can the business unit achieve its revenue and profitability objectives? There are two main tools that can assist in this area of decision making:

- the Ansoff product-market matrix,[25] and
- marketing competitive strategy options.

The Ansoff product-market matrix,[26] shown below in Figure 4.8, can be used to consider the potential of four strategic options for products and for markets.

FIGURE 4.8 The Ansoff product-market matrix

		Products	
		Existing	New
Markets	Existing	1 Market penetration	2 New product development
	New	3 Market development	4 Diversification

The marketing objectives and strategy options for each of these four product-market strategy options are:

- **Market penetration** (existing products in existing markets). The main objective is to increase market share (or in some cases to maintain market share or to halt a decline). This can be achieved by winning customers from competitors and/or increasing the product-usage rate of existing customers (a typical objective of customer loyalty programs). Efforts to increase the rate of product usage among existing customers can also potentially have the effect of growing the total market. However, the main strategy for the achievement of market growth is via the next option – market development.
- **Market development** (existing products in new markets). Market development or market expansion can be achieved by entering new markets/segments and/or converting non-users to become users. A critical aspect of market development is to identify emerging market segments that have growth potential.
- **New product development** (new products in existing markets). New products may be product-line extensions or new-to-world products for existing market segments. Marketing objectives are to launch successful new products into existing markets.
- **Diversification** (new products in new market segments). The focus here is towards related diversification – where the market segment is closely related to existing market segments; for example, the identification of an emerging subgroup of business travellers seeking no-frills/cheap air travel. If the diversification involves entering an unrelated market, this strategic option may fall outside of the scope of the strategic marketing plan. For example, leveraging a brand such as Waterford into writing instruments (fountain pens and biros) is a completely different product category from Waterford crystal in a significantly different market. Whether the diversification is related or unrelated comes back to the very first stage of the strategic marketing planning process – determination of the business definition and scope.

These four product-market strategic options provide the strategist with a framework for considering the potential revenue and profit that can be achieved for each year of the time frame of the strategic marketing plan. This is essentially a first cut view of a number of higher level marketing strategy options. The model can also be used to provide top-down direction of the strategic emphasis. For example, top management at 3M emphasise the importance of innovation by specifying that 30 per cent of each business unit's annual revenue must come from new products (defined as products introduced within the past four years). Consideration of the proportion of revenue that is expected to be derived from each of the four product-markets is an effective way for marketing strategists to focus on these higher level marketing strategy decisions.

The next step is to consider how these higher objectives and strategies might be achieved. That is, which markets or market segments should be chosen – taking into account the ability of the business unit not only to appeal to the needs of the customers in those markets, but also to compete effectively against other players in those markets.

So just how should the business unit compete in the markets it has chosen to target? Should it take its competitors on head-to-head or would it be better to take a less aggressive approach and try to avoid a marketing warfare type of situation? To help in this decision making a number of competitive options are discussed in the next section.

Competitive marketing strategy options

In this section competitive strategy options are discussed for a market leader, a market challenger/follower and for a competitor pursuing a market niche strategy.[27]

Market leader

There are five competitive strategy options for a market leader to consider:

- *Market expansion* is where the market leader attempts to expand demand for the product category. Apart from stimulating primary demand for the product category a market leader could attempt to broaden the market by expanding into related product or categories or related market segments.
- *Market share protection* is where the market leader attempts to protect its share of the market with strategies such as outspending its competitors in advertising, using consumer and trade sales promotions to maintain customer loyalty, extending the product line to cover all market segments, lowering prices and increasing distribution.
- *Pre-emptive strike* is an offensive strategy which anticipates or discourages competitive entry; for example, tying up the distribution channels by providing attractive trade incentives or by launching a fighting brand designed to offset any competitive product.
- *Counterattack* is attacking a competitor either by taking an individual competitor head on or by mounting a flanking strategy such as by moving into to an emerging market segment that the competitor has not entered.
- *Reactive strategy* is an alternative strategy where the market leader might wait until it is attacked and then react to the competitive challenge by launching a new product to offset the attacker, matching or bettering the price offer, or using advertising or sales promotion.

Market challenger/follower

A market challenger is basically a strong no. 2 or no. 3 in the mainstream market in which it is perceived as an alternative to the leader. Generally these organisations are innovative and aggressive and quite often seek market leadership. Their marketing objective would therefore be to increase their market share. Market followers are smaller and are usually around the midpoint of the market structure. Quite often they compete with value-for-money alternative products (based on being adequate in quality but at a lower price). They may not compete in all of the mainstream markets but would cover the largest segments. In most cases their marketing objective would be to maintain or increase market share. Market challengers and market followers can choose between three proactive strategies of head-to-head competition, flanking strategies and encirclement and one reactive strategy of following the leader.

- *Head-to-head competition* is a dangerous strategy to pursue and the market challenger should be confident that it has a competitive advantage based on product superiority and/or cost. This competitive advantage must not only be real but also be capable of being perceived by the customer to exist and to be significant.
- Because head-to-head competition is so risky, the alternative strategy of *flanking* is often considered to be a preferred option. This strategy involves determining a need that the market leader (or leaders) has overlooked and in response to offer a product that satisfies those needs. That is, a flanking strategy seeks to compete in an uncontested area.
- A third alternative for a proactive strike is *encirclement*. This involves an aggressive move against the market leader on several fronts. This may involve introducing a product range that surrounds the market leader or switching the customer's attention to benefits or attributes that the leader currently does not offer.
- The final strategic alternative for the market challenger/follower is the reactive strategy of *follow the leader*. This minimises the risk of retaliation and is essentially a 'me-too' approach.

Marketing nicher strategies

A marketing nicher specialises in a segment of the market and has a large share of this segment (with a low share of the overall market). Its main marketing objective would be to hold market share for its market niche. Market-niche strategies are those that are intended to avoid competition as the market pursued is either too small or too specialised for the market leaders to be interested. These market segments may be based on customer type, a price segment or a geographic area.

However, while the focus on competitive strategies has a lot to do with a battle for market share leadership, there is a danger of using market share alone as an indicator of an organisation's competitive position. As Porter argues, a goal of becoming the market leader (or to be one of the leaders) can be harmful because market leadership is not a *cause* but an *effect* of competitive advantage: 'The strategic mandate to business units should be to achieve competitive advantage. A goal of leadership *per se* also embroils managers in endless debates over how an industry should be defined to calculate shares, obscuring once more the search for competitive advantage that is the heart of strategy'.[28]

How to do it – a practical framework

The three stages of considerations of the decision-making process for establishing marketing objectives and higher level marketing strategies are complex, encompassing a wide variety of deliberations. So just how should the strategist, or a team of strategists, go about this difficult task?

The objective of this section is to provide the reader with a practical framework for tackling this task.

(*Note:* A worksheet to assist in the organisation of this information is included in Appendix 2 at the end of this chapter. This worksheet provides relevant information to be included in the 'Marketing objectives and higher level marketing strategies' section of the strategic marketing plan.)

There are six steps involved in the process.

Step 1

State the financial goals that the business unit is expected to achieve for each year of the planning period. In most cases these goals will be set in terms of profit objectives, which are stated in a variety of ways such as return on sales, return on equity, return on net assets, return on gross assets and earnings per share.

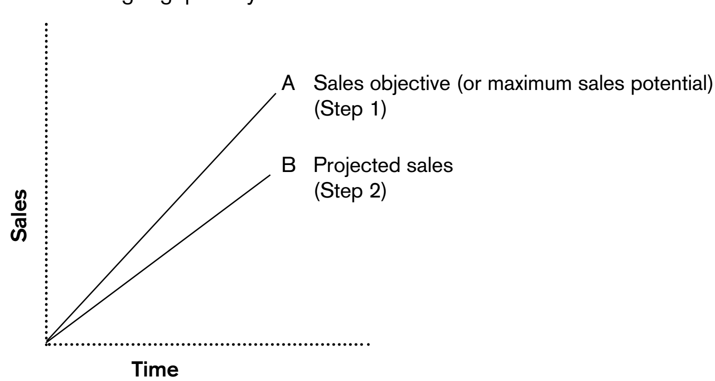
Irrespective of the method that is used it is necessary, for strategic marketing planning purposes, to translate these financial goals into annual revenue (sales) objectives – with accompanying gross margin objectives. Plot this information onto a graph as shown in Figure 4.9 (represented as line A).

Step 2

Consider the business unit's current competitive position. Where is it heading under the current strategy?

Commencing with last year's revenue (and margin) figures project the revenue for each of the following years addressed by the strategic marketing plan. To do this draw on the market forecast work that was previously completed in the situation analysis (in the market review section of the industry environment analysis). Also, draw on the competitive review (in the industry review part of the situation analysis) in order to develop a view of where the business unit is heading in relation to its competitors. (Refer to Chapter 3 for discussions of these topics.) Drawing on these two pieces of information a reasonable view of financial performance expectations – based on the continuation of current strategies – can be formed. Plot this information onto a graph as shown in Figure 4.9 (represented as line B).

FIGURE 4.9 Strategic gap analysis



In Figure 4.9, a gap is shown between projected sales (B) and the sales objective (A). Figure 4.10 shows the strategic options that are available to close the gap.[29]

Step 3

Compare the revenue forecasts determined in Step 2 (based on the continuation of current strategies) to the revenue imperatives determined for the business unit as per Step 1. Is there a gap between what the business unit is required to achieve and what it can be expected to achieve in line with its current competitive strategy?

This comparison is based on a model referred to as **strategic gap analysis** developed originally by Ansoff. It is an extremely powerful illustrative tool that portrays the magnitude of the marketing challenge of achieving the revenue objectives. It also provides a means for crystallising thinking regarding the setting of marketing objectives and product-market strategy decision, which will be discussed in Step 5.

Strategic gap analysis, shown in Figures 4.9, is an important tool for linking the corporate/business financial objectives to marketing performance realities. In this way it is a tool that links the objective setting process to the strategy development process, thereby addressing the criticism, discussed earlier in this chapter, about objectives being set with little or no regard as to how they are to be achieved.

Step 4

Consider whether a shift in the business unit's strategic positioning is desirable or necessary. To do this draw on the tools discussed earlier in this chapter such as the product life cycle concept, product portfolio models (BCG and GE/McKinsey) and models of competitive advantage. These tools provide a means of analysis and for decision making that draws on this analysis. An additional input is the work previously undertaken in the process of developing the situation analysis and the problems and opportunity statement.

The tools also provide suggestions concerning the broad marketing objectives and higher level marketing strategies that are appropriate for the recommended strategic position for the business unit. These decisions now need to be factored into a judgement about how the strategic gap might be closed. These judgements also need to include consideration of just where the revenue can be expected to come from in terms of new and existing products and markets. This is discussed in the next step.

Step 5

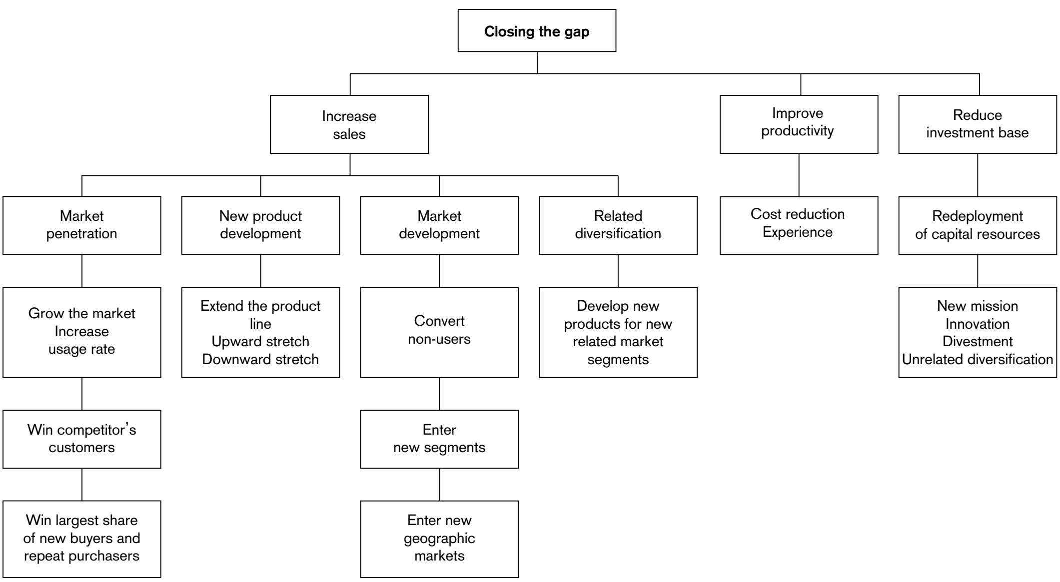
In this step the market realities from a bottom-up perspective are examined. This involves close scrutiny of the potential revenue that could be achieved from four product-market options (as per the Ansoff product-market matrix discussed earlier in this chapter). That is, an estimate needs to be provided of the potential annual revenue from:

- existing products in existing markets (taking into account market growth and market share expectations for the business or strategic planning unit);
- existing products in new markets (the revenue that can be expected from market development including new market segments and/or new geographic markets);

- new products in existing markets (the revenue that can be expected from new product introductions into existing markets);
- new products in new markets (the revenue that can be expected from related diversification).

As can be seen in Figure 4.10 these strategic options are a means for closing what can be described as a revenue or sales gap (that is, strategies for achieving sales growth). However, it should be noted that strategic gap analysis is also used as a tool for analysing strategic options for closing a profitability gap. This involves three main categories of strategy options: strategies for improving productivity, strategies for reducing the investment base and strategies for growing sales.

FIGURE 4.10 Alternatives for closing the strategic gap



Source: Based on the work of D.T. Brownlie & C.K. Bart, *Products and Strategies*, MCB University Press, Bradford, Yorks., vol. 11, no. 1, 1985, p. 14

- *Improved productivity* can be achieved by cost reduction and/or efficiencies achieved from the experience curve effect. This can include non-marketing activity such as production and/or improved marketing productivity such as better distribution cost efficiencies or more effective advertising.
- *Reduction of the investment base* can be achieved by the redeployment of capital resources and/or developing a new mission, innovation, divestment or diversification (new products for new markets). This is, essentially, a business unit level of strategy and therefore beyond the scope of strategic marketing planning considerations.
- *Sales growth* is the main area of interest for strategic marketing planning involving the four product-market strategy options discussed above.

Step 6

Has the strategic (revenue) gap been closed? If it has then the top-down corporate/business objectives (Step 1) have been found to be realistic and achievable. If the gap has not been closed then it is back to the drawing board. Either the corporate/business objectives need to be downgraded to match the market/business position reality or more ambitious strategies need to be developed.

How to write the marketing objectives and strategies section

(*Note:* Refer to Chapter 13, which contains information about writing a strategic marketing plan. A 'Strategic Marketing Planning Template' is also available on the web to assist in this task. The information set out below relates to the 'Marketing objectives and higher level marketing strategies' section in this template. Please also note that Appendix 2 at the end of this chapter is a worksheet that can be used as a means for collecting the relevant information to set out the marketing objectives and product-market strategies.)

The end product of the above decision-making process should be a clear and concise statement of the planning unit's marketing objectives and higher level marketing strategies. To achieve this the following format for writing this section of the strategic marketing plan is recommended.

Marketing objectives

State the marketing objectives in terms of market share, revenue and profitability (or operating margin) for each year of the strategic marketing plan. These objectives, as described in Step 6 above, are the result of the trade-off decision making, taking into account the three sets of considerations discussed in this chapter. That is, they are the end result of the mix of considerations involving corporate/business objectives, strategic position and marketing strategies.

Higher level marketing strategies

Briefly describe the recommended higher level marketing strategies, in terms of the product-market strategies that the planning unit will pursue, in order to achieve the above objectives. State the revenue objectives for each year of the strategic marketing plan to be derived from each of the four product-market categories. Next briefly describe the nature of the competitive conduct that is recommended, such as to adopt a flanking strategy approach, encirclement or a head-to-head strategy.

Justification

Marketing objectives are decisions that are derived from a combination of top-down and bottom-up considerations. The process of setting marketing objectives is essentially a balancing act between consideration of what the business, or planning, unit is required to achieve (corporate/business unit objectives) and what is possible for it to achieve (strategic position and higher level marketing strategies). These critically important strategic recommendations therefore need to be annunciated and supported by well-constructed argumentation. Analytical tools such as the product life cycle, product portfolio and competitive advantage models provide a good starting point for strategists to draw on in order to support this strategic thinking.

The justification (or rationale) should include a brief description of the current strategic position of the business unit (or planning unit) and a rationale for any changes to that position that are being recommended. It should also include a brief description of the strategic position of the planning unit's product line (and products or brands comprising the product line) and a rationale for changes to be made. This rationale should be based on changes that are likely to occur in the market evolution including changes that are likely to occur to existing and emerging (new) market segments. The product-market matrix provides an excellent framework for structuring this part of the rationale.

Supporting evidence for these recommendations should include reference to the market review section contained in the situation analysis. Similarly, the competitive review section in the situation analysis should provide a basis for developing competitive strategies such as whether to defend market share leadership or to challenge a market leader with head-to-head marketing strategies.

Problems and opportunities

Strategies need to be developed that address the problems and opportunities that were identified in the situation analysis and the problems and opportunity statement (as discussed in Chapter 3). By referring back to this work the marketing strategists can now address the most important opportunities and threats confronting the strategic planning unit. For example, a strategic planning unit might have relatively poor distribution coverage despite the fact that achievement of saturation distribution was identified as a critical success factor. A sub-objective to increase the number of distribution outlets during the time horizon of the strategic marketing plan should then be set.

Summary

This chapter has discussed a framework that can be used for the task of setting marketing objectives and the development of higher level marketing strategies. This is the pivotal decision-making process where all of the detailed analytical work (carried out in the situation analysis) forms a foundation for competing successfully in the future.

This decision-making process involves a combination of top-down and bottom-up thinking consisting of three sets of interrelated considerations: corporate objectives, strategic position and marketing strategies. Marketing strategists need to take all three sets of these considerations into account when determining marketing objectives and strategies in order to arrive at objectives that are realistic, achievable and measurable.

One of the most common mistakes found in many strategic marketing plans is the absence of support argumentation for these strategic decisions. Marketing objectives should not be 'plucked out of the air' and it is essential that a rationale is included in this section of the strategic marketing plan. Draw on the analytical work conducted in the situation analysis and the various tools discussed in this chapter (and elaborated in Appendix 1 to this chapter) to not only assist in the strategy decision-making processes, but also provide support argumentation for those decisions.

Endnotes

1 M. Treacy & F. Wiersema, *The Discipline of Market Leaders*, HarperCollins Publishers, London, 1995, p. 13.
2 The term 'crafting' draws on a proposition put forward by Mintzberg of emergent strategies discussed in Chapter 2. Refer to H. Mintzberg, *The Rise and Fall of Strategic Planning*, Prentice-Hall International, Hemel Hempstead, Herts, 1994, in particular pp. 23–7; and 'Crafting strategy', *Harvard Business Review*, July–August, 1987.
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11 *Note:* BCG introduced the concept of 'cash dogs' in the 1980s in response to criticisms that not all dogs were disasters – as had previously been suggested.
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13 Refer M.E. Porter, 'How competitive forces shape industry', *Harvard Business Review*, vol. 57, March–April, 1979, pp. 137–45; M.E. Porter, *Competitive Strategy: Techniques for Analyzing Industries and Competitors*, The Free Press, New York, 1980; M.E. Porter, *Competitive Advantage: Creating and Sustaining a Competitive Advantage*, The Free Press, New York, 1985; and M.E. Porter, 'What is strategy?', *Harvard Business Review*, November–December, 1996, pp. 61–78.
14 M.E. Porter, 'What is strategy?', *Harvard Business Review*, November–December, 1996, pp. 61–78.
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17 M.E. Porter, *Competitive Strategy*, pp. 41, 42. This is one of the most controversial notions of Porter's. The following are examples of articles criticising this aspect of Porter's work: A. Karnani, 'Generic competitive strategies – an analytical approach', *Strategic Management Journal*, vol. 7, 1984; A.I. Murray, 'A contingency view of Porter's generic strategies', *Academy of Management Review*, vol. 13, 1988; C.W. Hill, 'Differentiation versus low cost or differentiation and low cost: A contingency framework', *Academy of Management Review*, vol. 13, 1988; J. Hendry, 'The problem with Porter's generic strategies', *European Management Journal*, vol. 8, 1990; M. Cronshaw, E. Davis & J. Kay, 'On being stuck in the middle, or good food costs less at Sainsbury's', Centre

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21 R.M. Kanter, 'How to compete', *Harvard Business Review*, July–August, 1990, pp. 7–8.

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25 H.I. Ansoff, *Corporate Strategy*, McGraw-Hill, New York, 1965, Table 6.1, p. 109.

26 The concept of categorising products and markets into new and existing dimensions was pioneered by Drucker but incorporated later into a matrix format by Ansoff. Refer to P.F. Drucker, *The Practice of Management*, Harper & Row, New York, 1954; and H.I. Ansoff, *Corporate Strategy,* McGraw-Hill, New York, 1965.

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Appendix 1 to Chapter 4: Financial performance objectives and product portfolio models

In this appendix a brief summary is provided of some of the most popular techniques used by financial managers and strategy planners for the task of determining financial performance objectives.

The appendix also contains useful information about how marketing strategists can construct a BCG and a GE/McKinsey product portfolio model.

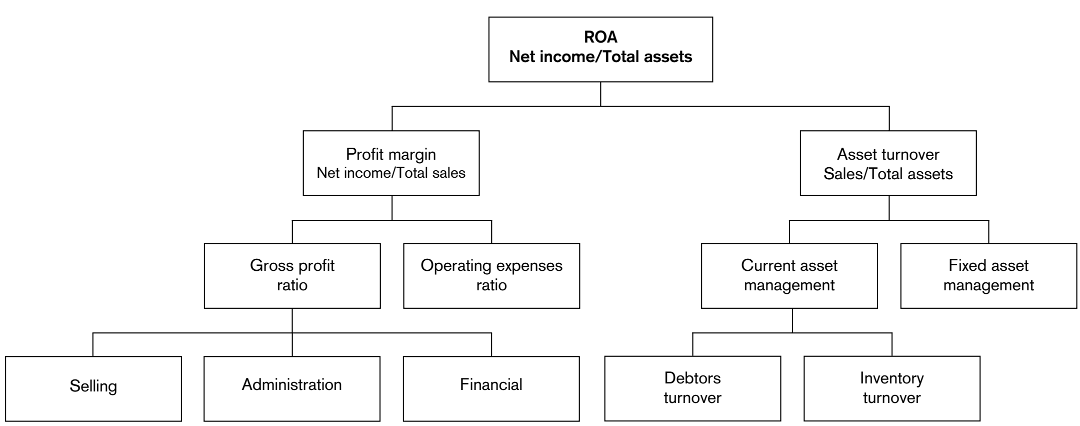
Financial performance objectives

Financial managers draw on a range of techniques ranging from ratio analyses to more complex **value-based planning** models for determining future earnings. In this section the Du Pont ratio analysis model and three value-based planning models are briefly summarised.

Du Pont ratio analysis

The Du Pont model is one of the most popular techniques used for the assessment of current and past financial performance. Financial managers use this model, originally developed by Du Pont, to forecast their organisation's future value by determining the growth rate of earnings in terms of return on assets (ROA). The model decomposes ROA into a series of constituent ratios that show how changes in a planned activity, such as an expense item of profit margin, will potentially impact on the organisation's ROA. There is also another version for arriving at return on equity (ROE).[1]

FIGURE 4.11 Du Pont ratio analysis



Value-based planning

Value-based planning techniques are designed to forecast the economic value to an organisation that a specific strategy or operating program will yield. There are several methods used including shareholder value analysis (SVA), market value added (MVA) and economic value added (EVA™).

Shareholder value analysis is a discounted cash flow approach. The most well-known approach to SVA is that proposed by Rappaport.[2] In this model, shareholder value is derived by taking into account cash flow that would be generated by a proposed strategy, the cost incurred as cost of capital and the market value of the debt assigned to the organisation. Shareholder value is estimated by consideration of seven value drivers: sales growth rate, operating profit margin, income tax rate, fixed capital needs, working capital needs, the cost of capital and the planning period.

Market value added (MVA) is a method of evaluating the extent to which an organisation performs its basic mission of creating wealth for its shareholders. MVA, as proposed by the New York consulting company Stern Stewart, is the difference between total market value (the value of an organisation's stock and debt) and invested capital (the capital an organisation has collected over its life from equity and debt offerings, bank loans and retained earnings).[3] A closely related concept to MVA is economic value added (EVA™) which sets out to measure the wealth created by an organisation each year. EVA™ estimates the amount of return a specific strategy or operating program will generate for an organisation that is in excess of its cost of capital. EVA™ is calculated by deducting from net dollar income (derived from operations) the cost of capital required to produce that income.

EVA™ = Net operating profit after taxes – (capital in place x cost of capital)[4]

Product portfolio models

The following are guidelines to assist marketing strategists in constructing the BCG and GE/McKinsey product portfolio models.

BCG model

The model is based on the underlying assumption of the *learning* or *experience curve*. That is, the unit cost of production declines as the firm gains more cumulative experience in production, distribution and marketing.

Relative market share

This is the ratio of the firm's unit sales (or actual market share) to that of its largest competitor. To compute, divide your market share by the largest competitor's market share. For example:

	Your share	*Largest competitor*	*Ratio*
Example 1	10	20	0.5
Example 2	10	10	1.0
Example 3	30	20	1.5

A ratio less than 1.0 means that you are not the market leader; a ratio of precisely 1.0 means that you are tied for the lead; and a ratio greater than 1.0 means that you are the market leader.

The relevance of relative market share is based on the experience curve concept: the greater the market share, the greater the cost efficiency. Profit impact of market strategy (PIMS) studies show (generally) a strong relationship between market share and ROI, although there are several other factors that impact on ROI.

A log scale is normally used for the (vertical) relative market share axis. Relative market share is usually divided at the 1.0 (vertical) line so that 'high' signifies market leadership. However, this is not a fixed rule and the line could be drawn at a lesser value so that strong no. 2s and no. 3s in a good market position can be placed on the 'high' side.

Market growth rate

This is a rough proxy for the PLC stages separating *growth* from *maturity*. The placement of the horizontal line is an arbitrary decision (although most examples illustrate it at 10 per cent). As a guide the line should be placed to show:

Growth – sustained growth above GDP

Maturity – approximately equal to GDP

As a further consideration the cash flow situation for a product placed in each of the four quadrants (assuming that the product holds its market share) should equate to the following:

FIGURE 4.12 Cash flow guidelines for the BCG matrix

Market growth	In balance	Cash users
	Cash generators	In balance

The GE/McKinsey market attractiveness / business assessment matrix expands the two-dimensional approach of the BCG model. It uses a multifactor assessment of 'industry attractiveness' and 'business strengths' as the two main factors and expands the 'high' and 'low' dimensions into 'high', 'medium' and 'low', thereby creating nine strategic positions.

Constructing a GE screening grid

Constructing a GE screening grid consists of two main steps: developing criteria for the assessment of market attractiveness and business strength, and the assessment of individual products against those criteria.

Constructing the matrix and developing the criteria for the assessment of market attractiveness and business strength

1 Determine the factors that would make any market attractive. There are a number of factors that determine the degree of market attractiveness. These would be drawn from the external environment factors contained in the situation analysis and, for example, might include:

(a) market factors;

(b) competition;

(c) financial and economic factors;

(d) technological factors;

(e) sociopolitical factors (in the SBUs) environment.

Note: There are a number of subfactors which need to be considered to expand each of these areas. For example, market factors would include the size of the market, growth rate, diversity of the market, sensitivity to price and several other factors. Box 4.3 provides a check list of subfactors to consider for each of these main areas. This check list was developed by William Rothschild, a specialist in strategic planning at General Electric. The check list groups the factors for both market attractiveness and business strength into five categories: market, competitive, financial and economic, technological and sociopolitical.

Alternatively, market attractiveness can be determined by drawing on Porter's five-forces model – that is, the intensity of competition, buyer power, threat of new entrants, supplier power and the threat of substitutes.

2 Weight the relative importance of each of these factors, by assigning values to add up to 100. The following example, for a hypothetical manufacturing company in the business-to-business area, shows the external factors that top management considered to be significant and the relative weighting they assigned each factor:

	Market attractiveness weighting
Market factors	15
Competition	15
Financial and economic factors	30
Technological factors	25
Sociopolitical factors	15
Total	100

3 The next stage is to determine the criteria for assessing the *current* business strength for *any* product. The starting point for this assessment is to identify the business strengths that are necessary for any product to be successful. That is, what are the critical success factors for a product to succeed in its market?

One way of doing this is to use the same factors that were used to determine market attractiveness. However, a preferable alternative is to use the critical success factors that were identified in the problems and opportunity stage of the marketing planning process. This was discussed in Chapter 3 and a list of potential CSFs was identified: financial capabilities, production/manufacturing capabilities, supply, human resources, management, R&D (technological leadership), competitive position, marketing, uniqueness of product/service, product/service quality superiority, product range, strength of brand name, superior customer service, distribution availability, price, image/reputation, sales-force superiority or advertising effectiveness. In most cases around five to eight CSFs would be identified to be the most significant.

4 After identifying the CSFs, the next stage is to weight their relative importance in a similar fashion to the process described for Step 2 to weight the external factors. Turning to our hypothetical manufacturing company, top management identified and assigned relative weightings of the following CSFs:

CSF	*Business strength weighting*
Manufacturing	20
R&D	20
Financial resources	10
Management	10
Distribution	10
Product Quality	10
Sales Force	10
Image	10
Total	100

5 It is important that agreement is reached regarding the above assessment criteria before proceeding to the next stage. Otherwise, an endless round of arguments will ensue and the criteria will become a moving target.

The next stage is to construct the screening grid. The usual way of doing this is to divide the matrix into equal (one-third) shares for both market attractiveness (the vertical lines) and business strength (the horizontal lines). Once this has been developed the next stage of the process is to assess the position of each product.

Judging individual products against assessment criteria

6 To judge the market attractiveness of each product it is suggested that a scoring system ranging from 1.0 for high attractiveness to 0.5 for medium attractiveness to 0.0 for no attractiveness be used.

Some organisations predetermine the potential score to be assigned. For example, for market factors it may be predetermined that size and growth will be the key determinants. Moreover, if a market has a turnover of \$10m or less it is 'low', \$11–25m 'medium' and \$25m+ is 'high'. Growth may range, for example 3 per cent or lower may be 'low', 4–6 per cent 'medium' and 7+ per cent 'high'. The use of such a scoring system can add an objective element to the process of evaluation.

Using the example of the hypothetical manufacturing company, Product A's market attractiveness was judged:

	Score for Product A
Market factors	0.5
Competition	0.1
Financial and economic factors	1.0
Technological factors	0.7
Sociopolitical factors	0.4

7 The next step is to combine the market attractiveness weighting determinants with the assessed score for the particular product. This can be computed as follows for Product A:

Factor	*Weighting*	*Score**	*Rating*
Markets	15	0.5	7.5
Competition	15	0.1	1.5
Financial and economic	30	1.0	30.0
Technological	25	0.7	17.5
Sociopolitical	15	0.4	6.0
Total	100		62.5

*Scored: high = 1.0, medium = 0.5, low = 0

In this example, Product A has been assessed to be of medium market attractiveness.

8 The next step is to judge the business position for the product to determine the product's business strength *vis-à-vis* that of its competitors. Market research may be used to assist in the assessment of the marketing-related factors such as product quality, distribution (availability and customer service) and image.

CSF	*Score for Product A*
Manufacturing	0.2
R&D	0.5
Financial resources	0.6
Management	0.7
Distribution	0.3
Product quality	0.5
Sales force	0.8
Image	0.4

9 The next stage is to compute the rating for the product:

Business Position Factor	*Weighting*	*Score**	*Rating*
Manufacturing	20	0.2	4.0
R&D	20	0.5	10.0
Financial resources	10	0.6	6.0
Management	10	0.7	7.0
Distribution	10	0.3	3.0
Product quality	10	0.5	5.0
Sales force	~~10~~	0.8	~~8.0~~
Image	~~10~~	0.4	~~4.0~~
Total	100		47.0

*Scored: high = 1.0, medium = 0.5, low = 0

Product A's business strength of 47.0 places it in the medium business strength box. Thus product A has been found to be in a market of medium attractiveness and it has a medium business strength.

Note: When developing the grid it is suggested that a circle is used to show each product's position. The size of the circle should represent the relative size of the current market that the product competes in. It is also useful to draw a segment within the circle to represent the product's current market share.

10 Finally the generic strategic option for the product can be considered. Box 4.2 (presented earlier in this chapter) provides a summary of generic strategic options that have been recommended by Day.[5]

Reference to this table shows that the product evaluated in the above example should pursue a strategy of selectivity/management for earnings.

The above steps should have been followed for determining the current position for each product. In order to determine the trend the entire procedure outlined in Steps 1–10 should now be repeated projecting the information criteria three to five years into the future (i.e. for the planning horizon of the marketing strategic plan). This will enable the *future* position to be plotted on the grid. This is usually achieved by drawing an arrow pointing to the projected position.

Identifying the relevant factors

Different industries will have different emphasis on what factors are important. As a guideline the *nature of the product* and *customer behaviour* should determine the emphasis. For example, for highly differentiated products for which customers seek technical innovation or other special benefits, relative technological position may be the key to a strong business position. Patent protection may be the key to market attractiveness.

For commodity products, low manufacturing costs and entry barriers may be the prime contributors to business position and market attractiveness.

BOX 4.3 A CHECK LIST OF FACTORS TO CONSIDER FOR DETERMINING MARKET ATTRACTIVENESS AND BUSINESS STRENGTHS[6]

Factors contributing to market attractiveness

Market factors

- Size (dollars, units or both)
- Size of key segments
- Growth rate per year:
  - Total
  - Segments
- Diversity of market
- Sensitivity to price, service features and external factors
- Cyclicality
- Seasonality
- Bargaining power of upstream suppliers
- Bargaining power of downstream suppliers

Factors contributing to business position status / position of your business

Market factors

- Your share (in equivalent terms)
- Your share of key segments
- Your annual growth rate:
  - Total
  - Segments
- Diversity of your participation
- Your influence on the market
- Lags or leads in your sales
- Bargaining power of your suppliers
- Bargaining power of your customers

Competition • Types of competitors • Degree of concentration • Changes in type and mix • Entries and exits • Changes in share • Substitution by new technology • Degrees and types of integration	*Competition* • Where you fit, how you compare in terms of products, marketing capability, service, production strength, financial strength and management • Segments you have entered or left • Your relative share change • Your vulnerability to new technology • Your own level of integration
Financial and economic factors • Contribution margins • Leveraging factors, such as economies of scale and experience • Barriers to entry or exit (both financial and non-financial) • Capacity utilisation	*Financial and economic factors* • Your margins • Your scale and experience • Barriers to your entry or exit (both financial and non-financial) • Your capacity utilisation
Technological factors • Maturity and volatility • Complexity • Differentiation • Patents and copyrights • Manufacturing process technology required	*Technological factors* • Your ability to cope with change • Depths of your skills • Types of your technological skills • Your patent protection • Your manufacturing technology
Sociopolitical factors in your environment • Social attitudes and trends • Laws and government agency regulations • Influence with pressure groups and government representatives • Human factors, such as unionisation and community acceptance	*Sociopolitical factors in your environment* • Your company's responsiveness and flexibility • Your company's ability to cope • Your company's aggressiveness • Your company's relationship with the broader community, external bodies, employees and unions

Appendix endnotes

1 For further information concerning the Du Pont model based on ROE refer to Z. Bodie, A. Kane & A.J. Marcus, *Investments*, Irwin/McGraw-Hill, Boston, Mass., 1996, pp. 570–3.
2 A. Rappaport, *Creating Shareholder Value: The New Standard for Business Performance*, The Free Press, New York, 1986.
3 Refer to S. Tully, 'America's best wealth creators', *Fortune*, 28 November, 1994, pp. 143–62.
4 For further information concerning EVA™ refer to J. Brown, 'Value+: Looking at EVA™', *Australian CPA*, April, 1999, pp. 44–6.
5 Refer to G.S. Day, *Analysis for Strategic Market Decisions*, West Publishing Company, New York, 1986, p. 204.
6 Based on a table presented by D.F. Abell & J.S. Hammond, *Strategic Marketing Planning: Problems and Analytical Approaches*, Prentice-Hall, Englewood Cliffs, NJ, 1979, p. 214.

Appendix 2 to Chapter 4: Worksheet for developing marketing objectives and higher level marketing strategies

Strategic gap analysis	**At end of planning periods**		
	Year 1	**Year 2**	**Year 3**
Corporate revenue objectives	_______	_______	_______
Projected revenue from current strategies	_______	_______	_______
Revenue gap	_______	_______	_______

Competitive position		*Marketing objectives*
PLC	[____________________]	______________________________
BCG	[____________________]	______________________________
GE/McKinsey	[____________________]	______________________________
Porter CA strategy	[____________________]	______________________________

Summary of current competitive position

Describe our current competitive position.

What should our competitive position be in 3 years time?

What are the strategic implications – in terms of our existing and potential new products and markets? That is, how will we grow the business?

Estimated revenue from existing products in existing markets (market penetration)

Market size (value): Current size: $________________

Market projections	Year 1	Year 2	Year 3
	________	________	________

Current market share ________

Projected market share (via new strategies)	Year 1	Year 2	Year 3
	________	________	________

Estimated value of existing products in existing markets (market projection x market share)	Year 1	Year 2	Year 3
	________	________	________

Estimated potential revenue from existing products in new markets (market development)*

Year 1	Year 2	Year 3
________	________	________

* Identify the specific market development opportunities and the time frame when these initiatives could come on stream.

Estimated potential revenue from new products in existing markets (new product development)*

Year 1	Year 2	Year 3
________	________	________

* Identify the specific NPD opportunities and the time frame when these initiatives could come on stream.

Estimated potential revenue from new products in new market segments (related diversification)*

Year 1	Year 2	Year 3
________	________	________

* Identify the related diversification opportunities and the time frame when these initiatives could come on stream.