Marketing Management

TWELFTH EDITION

Marketing Management

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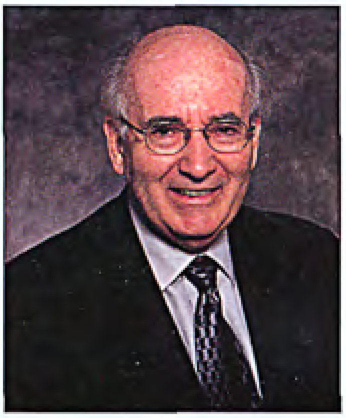
DEDICATION

This book is dedicated to my wife and best friend, Nancy, with love.

This book is dedicated to my wife, Punam, and my two daughters, Carolyn and Allison, with much love and thanks.

ABOUT THE AUTHORS



Philip Kotler *is one of the world's leading authorities on marketing. He is the S. C. Johnson & Son Distinguished Professor of International Marketing at the Kellogg School of Management, Northwestern University. He received his master's degree at the University of Chicago and his Ph.D. at MIT, both in economics. He did post-doctoral work in mathematics at Harvard University and in behavioral science at the University of Chicago.*

Dr. Kotler is the co-author of Principles of Marketing *and* Marketing: An Introduction. *His* Strategic Marketing for Nonprofit Organizations, *now in its sixth edition, is the best seller in that specialized area. Dr. Kotler's other books include* Marketing Models; The New Competition; Marketing Professional Services; Strategic Marketing for Educational Institutions; Marketing for Health Care Organizations; Marketing Congregations; High Visibility; Social Marketing; Marketing Places; The Marketing of Nations; Marketing for Hospitality and Tourism; Standing Room Only—Strategies for Marketing the Performing Arts; Museum Strategy and Marketing; Marketing Moves; Kotler on Marketing; Lateral Marketing: Ten Deadly Marketing Sins; *and* Corporate Social Responsibility.

In addition, he has published more than one hundred articles in leading journals, including the Harvard Business Review, Sloan Management Review, Business Horizons, California Management Review, *the* Journal of Marketing, *the* Journal of Marketing Research, Management Science, *the* Journal of Business Strategy, *and* Futurist. *He is the only three-time winner of the coveted Alpha Kappa Psi award for the best annual article published in the* Journal of Marketing.

Professor Kotler was the first recipient of the American Marketing Association's (AMA) Distinguished Marketing Educator Award (1985). The European Association of Marketing Consultants and Sales Trainers *awarded him their Prize for Marketing Excellence. He was chosen as the Leader in Marketing Thought by the Academic Members of the AMA in a 1975 survey. He also received the 1978 Paul Converse Award of the AMA, honoring his original contribution to marketing. In 1995, the Sales and Marketing Executives International (SMEI) named him Marketer of the Year. In 2002, Professor Kotler received the Distinguished Educator Award from The Academy of Marketing Science. He has* received honorary doctoral degrees from Stockholm University, the University of *Zurich, Athens University of Economics and Business, DePaul University, the Cracow School of Business and Economics, Groupe H.E.C. in Paris, the Budapest School of Economic Science and Public Administration, and the University of Economics and Business Administration in Vienna.*

Professor Kotler has been a consultant to many major U.S. and foreign companies, including IBM, General Electric, AT&T, Honeywell, Bank of America, Merck, SAS Airlines, Michelin, and others in the areas of marketing strategy and *planning, marketing organization, and international marketing.*

He has been Chairman of the College of Marketing of the Institute of Management Sciences, a Director of the American Marketing Association, a Trustee of the Marketing Science Institute, a Director of the MAC Group, a member of the Yankelovich Advisory Board, and a member of the Copernicus Advisory Board. He was a member of the Board of Governors of the School of the Art Institute of

ABOUT THE AUTHORS

Chicago and a member of the Advisory Board of the Drucker Foundation. He has traveled extensively throughout Europe, Asia, and South America, advising and lecturing to many companies about global marketing opportunities.

Kevin Lane Keller *is the E. B. Osborn Professor of Marketing at the Tuck School of Business at Dartmouth College. Professor Keller has degrees from Cornell, Carnegie-Mellon, and Duke universities. At Dartmouth, he teaches an MBA elective on strategic brand management and lectures in executive programs on that topic. Previously, Professor Keller was on the faculty of the Graduate School of Business at Stanford University, where he also served as the head of the marketing group. Additionally, he has been on the marketing faculty at the University of California at Berkeley and the University of North Carolina at Chapel Hill, been a visiting professor at Duke University and the Australian Graduate School of Management, and has two years of industry experience as Marketing Consultant for Bank of America.*

Professor Keller's general area of expertise is in consumer marketing. His specific research interest is in how understanding theories and concepts related to consumer behavior can improve marketing strategies. The research has been published in over fifty papers in three of the major marketing journals—the Journal of Marketing, *the* Journal of Marketing Research, *and the* Journal of Consumer Research. *He also has served on the Editorial Review Boards of those journals. His research has been widely cited and has received numerous awards.*

Professor Keller is acknowledged as one of the international leaders in the study of brands, branding, and strategic brand management. Actively involved with industry, he has worked on a host of different types of marketing projects. He has served as brand confidant to marketers for some of the world's most successful brands, including Accenture, American Express, Disney, Ford, Intel, Levi Strauss, Miller Brewing, Procter & Gamble, and Starbucks. He has done additional brand consulting with other top companies such as Allstate, Beiersdorf (Nivea), Blue Cross Blue Shield, Campbell Soup, General Mills, Goodyear, Kodak, The Mayo Clinic, Nordstrom, Shell Oil, Unilever, and Young & Rubicam. He is also an academic trustee for the Marketing Science Institute. A popular speaker, he has conducted marketing seminars and workshops with top executives in a variety of forums.

Professor Keller is currently conducting studies that address marketing strategies and tactics to build, measure, and manage brand equity. His textbook on those subjects, Strategic Brand Management, *the second edition of which was published September 2002 by Prentice-Hall, has been heralded as the "bible of branding."*

An avid sports, music, and film enthusiast, in his spare time, he helps to manage and market one of Australia's great rock and roll treasures, The Church. *Professor Keller lives in New Hampshire with his wife, Punam (also a Tuck marketing professor), and his two daughters, Carolyn and Allison.*

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PREFACE

Marketing Management is the leading marketing text because its content and organization consistently reflect changes in marketing theory and practice. The very first edition of *Marketing Management*, published in 1967, introduced the concept that companies must be customer-and-market driven. But there was little mention of what have now become fundamental topics such as segmentation, targeting, and positioning. Concepts such as brand equity, customer value analysis, database marketing, e-commerce, value networks, hybrid channels, supply chain management, and integrated marketing communications were not even part of the marketing vocabulary then. Firms now sell goods and services through a variety of direct and indirect channels. Mass advertising is not nearly as effective as it was. Companies are exploring new forms of communication, such as experiential, entertainment, and viral marketing. Customers are increasingly telling companies what types of product or services they want and when, where, and how they want to buy them.

In response, companies have shifted gears from managing product portfolios to managing customer portfolios, compiling databases on individual customers so they can understand them better, and construct individualized offerings and messages. They are doing less product and service standardization and more niching and customization. They are replacing monologues with customer dialogues. They are improving their methods of measuring customer profitability and customer lifetime value. They are intent on measuring the return on their marketing investment and its impact on shareholder value. They are also concerned with the ethical and social implications of their marketing decisions.

As companies change, so does their marketing organization. Marketing is no longer a company department charged with a limited number of tasks—it is a company-wide undertaking. It drives the company's vision, mission, and strategic planning. Marketing includes decisions like who the company wants as its customers; which needs to satisfy; what products and services to offer; what prices to set; what communications to send and receive; what channels of distribution to use; and what partnerships to develop. Marketing succeeds only when all departments work together to achieve goals: when engineering designs the right products, finance furnishes the required funds, purchasing buys quality materials, production makes quality products on time, and accounting measures the profitability of different customers, products, and areas.

And as marketing techniques and organization have changed, so has this text. The biggest change is the addition of a co-author. Kevin Lane Keller is one of the top marketing academics of his generation. He has conducted ground-breaking research and written a highly successful text, *Strategic Brand Management*. He has also worked with marketing executives from companies around the globe to help them become better marketers. He brings fresh thinking and new perspectives to *Marketing Management*.

The twelfth edition reflects a collaborative effort between the two authors with a goal of creating the best edition of *Marketing Management* ever. Extensive focus groups were conducted to fully understand the course and classroom needs of the instructor. Based on this input, the twelfth edition is designed to preserve the strengths of previous editions while introducing new material and organization to further enhance learning. It is dedicated to helping companies, groups, and individuals adapt their marketing strategies and management to the marketplace realities of the twenty-first century.

::: Revision Strategy for the Twelfth Edition

Marketing is of interest to everyone, whether they are marketing goods, services, properties, persons, places, events, information, ideas, or organizations. As the "ultimate authority" for students and educators, *Marketing Management* must be kept up-to-date and contemporary. Students (and instructors) should feel that the book is talking directly to them in terms of both content and delivery.

PREFACE

The success of *Marketing Management* can be attributed to its ability to maximize three dimensions that characterize the best marketing texts—depth, breadth, and relevance—as reflected by the following questions.

- **Depth.** Does the book have solid academic grounding? Does it contain important theoretical concepts, models, and frameworks? Does it provide conceptual guidance to solve practical problems?
- **Breadth.** Does the book cover all the right topics? Does it provide the proper amount of emphasis on those topics?
- **Relevance.** Does the book engage the reader? Is the book interesting to read? Does it have lots of compelling examples?

The twelfth edition builds on the fundamental strengths of past editions:

- **Managerial Orientation.** The book focuses on the major decisions that marketing managers and top management face in their efforts to harmonize the organization's objectives, capabilities, and resources with marketplace needs and opportunities.
- **Analytical Approach.** This book presents conceptual tools and frameworks for analyzing recurrent problems in marketing management. Cases and examples illustrate effective marketing principles, strategies, and practices.
- **Multidisciplinary Perspective.** This book draws on the rich findings of various scientific disciplines—economics, behavioral science, management theory, and mathematics—for fundamental concepts and tools.
- **Universal Applications.** This book applies strategic thinking to the complete spectrum of marketing: products and services, consumer and business markets, profit and nonprofit organizations, domestic and foreign companies, small and large firms, manufacturing and intermediary businesses, and low- and high-tech industries.
- **Comprehensive and Balanced Coverage.** This book covers all the topics an informed marketing manager needs to understand to execute strategic, tactical, and administrative marketing.

New Themes: Holistic Marketing

One major new theme in this edition is holistic marketing. *Holistic marketing* can be seen as the development, design, and implementation of marketing programs, processes, and activities that recognize the breadth and interdependencies involved today's marketing environment. Holistic marketing recognizes that "everything matters" with marketing and that a broad, integrated perspective is often necessary. Holistic marketing has four key dimensions:

1. **Internal marketing**–ensuring everyone in the organization embraces appropriate marketing principles, especially senior management.
2. **Integrated marketing**–ensuring that multiple means of creating, delivering and communicating value are employed and combined in the optimal manner.
3. **Relationship marketing**–having rich, multi-faceted relationships with customers, channel members and other marketing partners.
4. **Socially responsible marketing**-understanding the ethical, environmental, legal, and social effects of marketing.

These four dimensions are woven throughout the book and at times spelled out explicitly. Two additional themes of this text are *marketing personalization* and *marketing accountability*. The former reflects all the attempts to make marketing more individually relevant; the latter reflects the need to understand and justify the return on marketing investments within organizations.

Organization

The twelfth edition preserves the major topics of the eleventh edition, but reorganizes them into a new modular structure. There are now eight parts as compared to five to allow for greater flexibility in the classroom.

Part 1	Understanding Marketing Management
Part 2	Capturing Marketing Insights
Part 3	Connecting with Customers
Part 4	Building Strong Brands
Part 5	Shaping the Market Offerings
Part 6	Delivering Value
Part 7	Communicating Value
Part 8	Creating Successful Long-Term Growth

The most significant organizational changes are:

- A new part on capturing marketing insights that includes the two research-oriented chapters, placed even earlier in the book (Chapters 3 and 4).
- A new section on creating long-term growth that brings together chapters on new products and new markets (global) as well as a revised concluding chapter, placed at the end of the book (Chapters 20–22)
- Chapters 16 and 17 are now aligned more definitely in terms of mass and personal communications.
- The marketing plan material has been upgraded and moved into Chapter 2 to help students gain concrete marketing skills. We have also created an appendix to Chapter 2 with an illustrative example of an actual company marketing plan and another appendix to the book itself with a series of marketing plan exercises.
- The new Marketing Plan appendix, at the end of the book, provides detailed information on how to develop a marketing plan and includes a series of exercises to help students develop a formal marketing plan using the hypothetical example of Sonic PDA.
- A Glossary containing all the key terms and definitions has been added at the end of the book.

Chapter by Chapter Changes

This edition has been both streamlined and expanded to bring essentials and classic examples into sharper focus, while covering new concepts and ideas in depth. Some chapters received more extensive revisions than others. Here is an overview of the chapter changes:

Chapter 1, *Defining Marketing for the 21st Century*, now consolidates the "big picture" material from the first two chapters of the eleventh edition to introduce key marketing topics, how they have changed and are likely to change in the future.

Chapter 2, *Developing Marketing Strategies and Plans*, provides more discussion on holistic marketing and more detail on marketing plans, including a sample marketing plan.

Chapter 3, *Gathering Information and Scanning the Environment*, is now couched in terms of macro approaches to marketing research.

Chapter 4, *Conducting Marketing Research and Forecasting Demand* , is framed in terms of micro approaches and includes a new section on Marketing Productivity.

Chapter 5, *Creating Customer Value, Satisfaction, and Loyalty*, consolidates material from several chapters related to customers and introduces new material on Customer Equity.

Chapter 6, *Analyzing Consumer Markets*, introduces a new section on Other Theories of Consumer Decision-Making.

Chapter 7, *Analyzing Business Markets*, contains a section on Managing Business-to-Business Customer Relationships.

Chapter 8, *Identifying Market Segments and Targets*, adds new material on local marketing, conversion marketing, experiential marketing and marketing to Generation Y.

Chapter 9, *Creating Brand Equity*, has been completely reworked and expanded to capture more of the important concepts in building, measuring, and managing brand equity.

Chapter 10, *Crafting the Brand Positioning*, introduces a contemporary approach to positioning based on the concepts of points-of-parity and points-of-difference.

Chapter 11, *Dealing with Competition*, includes fresh material on how to increase product consumption.

Chapter 12, *Setting Product Strategy*, has been reorganized to cover material on sources of differentiation.

Chapter 13, *Designing and Managing Services*, introduces a new section on Managing Service Brands.

Chapter 14, *Developing Pricing Strategies and Programs*, contains a new section on understanding pricing with material on consumer psychology and pricing.

Chapter 15, *Designing and Managing Value Networks and Channels*, includes material on e-commerce marketing practices and new material on channel power, conflict and cooperation.

Chapter 16, *Managing Retailing, Wholesaling, and Logistics*, includes relevant material on store activities and experiences and has been reorganized to include private labels.

Chapter 17, *Designing and Managing Integrated Marketing Communications*, introduces a section on the Role of Marketing Communications and information on coordinating media.

Chapter 18, *Managing Mass Communications: Advertising, Sales Promotions, Events, and Public Relations*, includes a new section on Events and Experiences Marketing.

Chapter 19, *Managing Personal Communications: Direct Marketing and Personal Selling*, introduces new material on interactive marketing.

Chapter 20, *Introducing New Market Offerings*, includes new material on idea generation.

Chapter 21, *Tapping into Global Markets*, covers new material on country-of-origin effects.

Chapter 22, *Managing a Holistic Marketing Organization*, contains new sections on social marketing and the future of marketing.

Additional concepts that have been added or explored in greater detail include: brand management principles, cause-related marketing, consumer decision heuristics, consumer involvement, consumer memory models, events and experiences, innovation and creativity, qualitative research techniques, marketing metrics, mental accounting, reference prices, and sponsorships.

::: Chapter Pedagogy

Each chapter includes:

Chapter Introduction, which includes brief commentary and a short vignette that set the stage for the chapter material to follow. By covering topical brands or companies, the vignettes serve as great discussion starters.

Marketing Insight boxes that delve into important marketing topics, often highlighting current research findings. New and updated Marketing Insight boxes include such topics as "Views on Marketing from Chief Executive Officers," "Progress and Priorities in Customer Equity Management," "Consumer Trends for the Future," and "Small Business, Big Sales: The Burgeoning Small-Midsize Business Market."

Marketing Memo boxes that offer practical advice and directions in dealing with various decisions at all stages of the marketing management process. New and updated Marketing Memo boxes include "Managing Customer Knowledge," "Decision Traps," "Average American Consumer Quiz," and "Guidelines for Selling to Small Businesses."

Text Examples Each chapter also includes 10–15 in-text examples that provide vivid illustrations of chapter concepts using actual companies and situations. Virtually all these examples of good and bad company marketing practices are new to the twelfth edition and cover a variety of products, services, and markets. Many have accompanying illustrations in the form of ads or product shots.

End-of-Chapter Exercises These include Marketing Applications and the Marketing Spotlight.

- The *Marketing Applications* section has two practical exercises to challenge students: *Marketing Debate* suggests opposing points-of-view on an important marketing topic from the chapter and asks student to take a side. *Marketing Discussion* identifies provocative marketing issues and allows for a personal point-of-view.
- The *Marketing Spotlight*, an in-depth examination of one of the world's most successful marketing companies, includes questions for class discussion or student assignments.

::: The Teaching and Learning Package

Marketing Management is an entire package of materials available to students and instructors. This edition includes a number of ancillaries designed to make the marketing management course an exciting, dynamic, interactive experience.

Marketing Management Cases

Prentice Hall Custom Business Resources can provide instructors and students with all of the cases and articles needed to enhance and maximize learning in a marketing course. Instructors can create Custom CoursePacks or Custom CaseBooks. Resources include top-tier cases from Darden, Harvard, Ivey, NACRA, and Thunderbird, plus full access to a database of articles. For details on how to order these value-priced packages, contact your local rep or visit the Prentice Hall Custom Business Resources Web site at www.prenhall.com/custombusiness.

Instructor's Resource Manual

Prepared by Ronald N. Borrieci, the Instructor's Resource Manual includes chapter/summary overviews, key teaching objectives, answers to end-of-chapter materials, Harvard Business School case suggestions, exercises, projects, and detailed lecture outlines. A new feature, "Professors on the Go!", was created with the busy professor in mind. It brings key material upfront, where an instructor who is short on time can find key points and assignments that can be incorporated into the lecture, without having to page through all the material provided for each chapter.

Instructor's Resource Center (IRC)

- **IRC—CD-ROM:** One source for all of your supplement needs. New interface and searchable database makes sorting through and locating specific resources easier than ever before. Includes all the same supplements hosted at our IRC Online; however, the PowerPoint Media Rich set is provided only on this CD-ROM due to its larger file size and embedded video clips. The CD-ROM also contains many images from the textbook, which you may incorporate into your lectures.

- ***IRC—ONLINE:*** *One destination for all of your supplement needs. The Prentice Hall* catalog at www.prenhall.com/marketing is where instructors can access our complete array of teaching materials. Simply go to the catalog page for this text and click on the Instructor link to download the Instructor's Manual, Video Guide, Test Item File, TestGen EQ, PowerPoint slides (Basic only), and more.

NOTE: Prentice Hall manually checks *every* password request and verifies each individual's instructor status before issuing a password.

Test Item File

Prepared by John R. Brooks, Jr. of Houston Baptist University, the Test Item File contains more than 3,000 multiple-choice, true-false, short-answer, and essay questions, with page reference and difficulty level provided for each question. *A new feature is an entire section dedicated to application questions.* These real-life situations take students beyond basic chapter concepts and vocabulary and ask them to apply marketing skills. Prentice Hall's **TestGen EQ** test-generating software is new for this edition. This supplement is available in two places: Download from the *IRC Online* (www.prenhall.com/kotler) or from the *IRC on CD-ROM.*

- PC/Mac compatible and preloaded with all of the Test Item File questions.
- Manually or randomly view test bank questions and drag-and-drop to create a test.
- Add or modify test bank questions using the built-in Question Editor
- Print up to 25 variations of a single test and deliver the test on a local area network using the built-in QuizMaster feature
- Free customer support is available at media.support00 am and 5:00 pm CST.

PowerPoints

When it comes to PowerPoints, Prentice Hall knows one size does not fit all. That's why *Marketing Management 12e* offers instructors more than one option.

- **PowerPoint BASIC:** This simple presentation includes only basic outlines and key points from each chapter. No animation or forms of rich media are integrated, which makes the total file size manageable and easier to share online or via email. BASIC was also designed for instructors who prefer to customize PowerPoints or want to avoid having to strip out animation, embedded files, or other media rich features.
- **PowerPoint MEDIA RICH:** This media rich alternative includes basic outlines and key points from each chapter, plus advertisements and art from the text, images from outside the text, discussion questions, Web links, and embedded video snippets from the accompanying video library. The best option if you want a complete presentation solution. Instructors can further customize this presentation using the image library featured on the IRC on CD-ROM. Both the BASIC and MEDIA RICH version of slides were authored by Mark E. Collins.

Aside from these three PowerPoint options, a select number of slides, based on the MEDIA RICH version, are also available as overhead transparencies.

Marketing Management Video Gallery 2006

Make your classroom "newsworthy." PH has updated the Marketing Management video library for the 12th Edition. Using today's popular newsmagazine format, students are taken on location and behind closed doors. Each news story profiles a well-known or up-and-coming company leading the way in its industry. More than *twenty new video clips* accompany this edition, covering key topics using leading companies such as American Express, Song Airlines, the NFL, Eaton, and Wild Planet. Issue-focused footage includes interviews with top executives, objective reporting by real news anchors, industry research analysts and marketing and advertising campaign experts. A full video guide, including synopses, discussion questions, and teaching suggestions, is available to accompany the video library.

Companion Web Site

at www.prenhall.com/kotler. This FREE site offers students valuable resources. Two quizzes are offered per chapter. The Concept Check Quiz is to be administered prior to reviewing the chapter, in order to assess students' initial understanding. The Concept Challenge Quiz is to be administered after reviewing the chapter. Also featured is the text glossary, plus a link to the new Instructor's Resource Center.

Marketing Plan: A Handbook, 2nd edition with MarketingPlan Pro 6.0

Marketing PlanPro is a highly rated commercial software program that guides students through the entire marketing plan process. The software is totally interactive and features ten sample marketing plans, step-by-step guides, and customizable charts. Customize your marketing plan to fit your marketing needs by following easy-to-use plan wizards. Follow the clearly outlined steps from strategy to implementation. Click to print, and your text, spreadsheet, and charts come together to create a powerful marketing plan. The new *Marketing Plan: A Handbook*, by Marian Burk Wood, supplements the in-text marketing plan material with an in-depth guide to what student marketers really need to know. A structured learning process leads to a complete and actionable marketing plan. Also included are timely, real-world examples that illustrate key points, sample marketing plans, and Internet resources. The Handbook and Marketing PlanPro software are available as value-pack items at a discounted price. Contact your local Prentice Hall representative for more information.

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The twelfth edition bears the imprint of many people.

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PART 1

UNDERSTANDING MARKETING MANAGEMENT

IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. Why is marketing important?
2. What is the scope of marketing?
3. What are some fundamental marketing concepts?
4. How has marketing management changed?
5. What are the tasks necessary for successful marketing management?

CHAPTER 1 ::: DEFINING MARKETING FOR THE 21ST CENTURY

Marketing is everywhere. Formally or informally, people and organizations engage in a vast number of activities that could be called marketing. Good marketing has become an increasingly vital ingredient for business success. And marketing profoundly affects our day-to-day lives. It is embedded in everything we do—from the clothes we wear, to the Web sites we click on, to the ads we see:

Two teenage girls walk into their local Starbucks. One goes to the counter and hands the barista cards for two free peppermint lattes and purchases some pastries. The other sits at a table and opens her Apple PowerBook. Within a few seconds, she connects to the Internet courtesy of Starbucks' deal with T-mobile to create wireless HotSpots at over a thousand Starbucks stores. Once on the Net, the girl "Googles" the name of the band that played the soundtrack of the movie she saw last night. A number of Web sites come up along with two ads—one for tickets to the band's concert tour and another for the soundtrack CD and movie DVD at Amazon.com. When she clicks through to the Amazon ad, search engine giant Google rings up some money. (Through its adwords program, it gets paid whenever someone clicks on an advertiser's ad.) Now her friend has returned with lattes in hand. Teen #2 is eager to show off her parents' Sweet Sixteen gift to her—a ruby-red A220 Samsung cell phone created by a team of young Korean designers after months of market research and >>>

New York's Time Square: a live demonstration of the many faces of marketing today.

focus groups. The phone resembles a cosmetic compact and dispenses dieting tips as well as advice on how to dress for the weather. The two girls are oohing and aahing over the tiny display that doubles as a mirror when they see the reflection of a city bus sporting a giant banner ad for the newest HBO comedy series. . . .

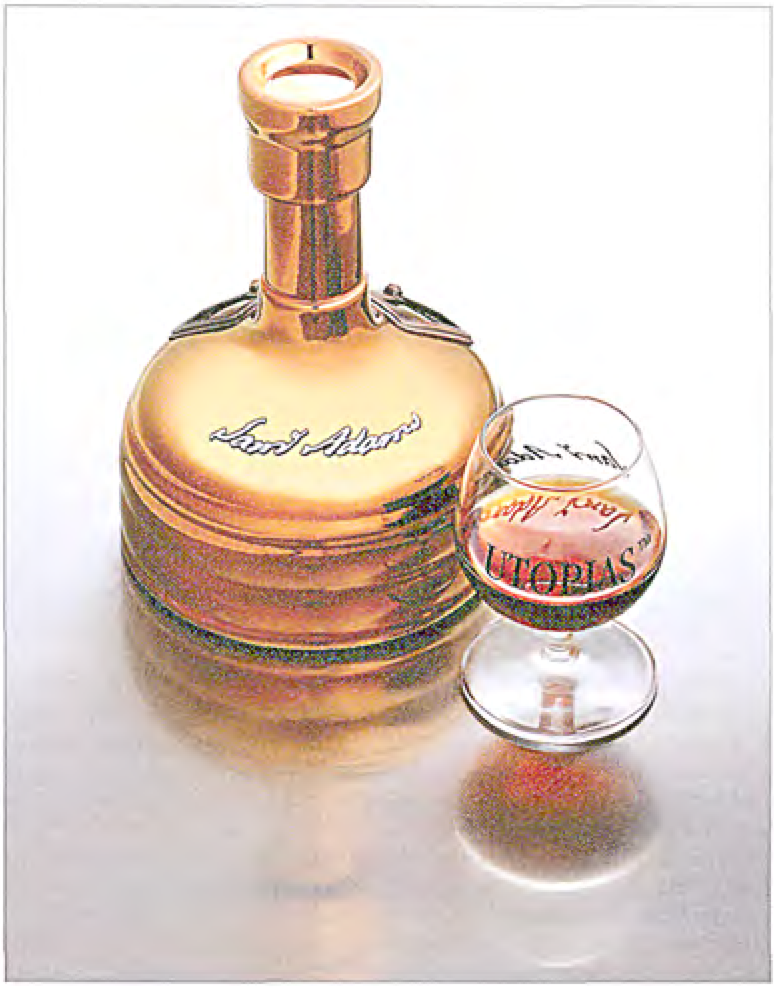
Good marketing is no accident, but a result of careful planning and execution. Marketing practices are continually being refined and reformed in virtually all industries to increase the chances of success. But marketing excellence is rare and difficult to achieve. Marketing is both an "art" and a "science"—there is constant tension between the formulated side of marketing and the creative side. It is easier to learn the formulated side, which will occupy most of our attention in this book; but we will also describe how real creativity and passion operate in many companies. This book will help to improve your understanding of marketing and your ability to make the right marketing decisions. In this chapter, we lay the foundation for our study by reviewing a number of important marketing concepts, tools, frameworks, and issues.

::: The Importance of Marketing

Financial success often depends on marketing ability. Finance, operations, accounting, and other business functions will not really matter if there is not sufficient demand for products and services so the company can make a profit. There must be a top line for there to be a bottom line. Many companies have now created a Chief Marketing Officer, or CMO, position to put marketing on a more equal footing with other C-level executives such as the Chief Executive Officer (CEO) and Chief Financial Officer (CFO). Press releases from organizations of all kinds—from consumer goods makers to health care insurers and from non-profit organizations to industrial product manufacturers—trumpet their latest marketing achievements and can be found on their Web sites. In the business press, countless articles are devoted to marketing strategies and tactics.

Marketing is tricky, however, and it has been the Achilles' heel of many formerly prosperous companies. Large, well-known businesses such as Sears, Levi's, General Motors, Kodak, and Xerox have confronted newly empowered customers and new competitors, and have had to rethink their business models. Even market leaders such as Microsoft, Wal-Mart, Intel, and Nike recognize that they cannot afford to relax. Jack Welch, GE's brilliant former CEO, repeatedly warned his company: "Change or die."

But making the right decisions is not always easy. Marketing managers must make major decisions such as what features to design into a new product, what prices to offer customers, where to sell products, and how much to spend on advertising or sales. They must also make more detailed decisions such as the exact wording or color for new packaging. (The "Marketing Memo: Marketers' Frequently Asked Questions" is a good checklist for the questions marketing managers ask, all of which we examine in this book.) The companies at greatest risk are those that fail to carefully monitor their customers and competitors and to continuously improve their value offerings. They take a short-term, sales-driven view of their business and ultimately, they fail to satisfy their stockholders, their employees, their suppliers, and their channel partners. Skillful marketing is a never-ending pursuit.



A bottle of Utopias, Boston Beer's unique, limited edition "extreme" brew. At 50-proof, it warrants the label "The Strongest Beer in the World."

BOSTON BEER COMPANY

Jim Koch, founder of Boston Beer Company, whose Samuel Adams beer has become a top-selling "craft" or "micro" beer, started out in 1984 carrying bottles of Samuel Adams from bar to bar to persuade bartenders to carry it. For 10 years he couldn't afford an advertising budget; he sold his beer through direct sales and grass-roots public relations. His hard work paid off. Boston Beer found its sales passing the $200 million mark as it became the leader in the craft beer market. As a consequence, it began to spend millions of dollars on TV advertising, employ dozens of salespeople, and carry on sophisticated marketing research. It discovered that continued success required setting up and managing a capable marketing department. But the original passion and desire to move forward remains. In 2002, Boston Beer introduced a unique, limited edition "extreme" brew, Samuel Adams Utopias. The potent 50-proof, $100-a-bottle Utopias claimed the official record as "The Strongest Beer in the World." "At Samuel Adams, we are constantly innovating and creating new ideas that will push the envelope and revolutionize beer drinkers' expectations for beer," said founder Koch.[1]

::: The Scope of Marketing

To prepare to be a marketer, you need to understand what marketing is, how it works, what is marketed, and who does the marketing.

What Is Marketing?

Marketing deals with identifying and meeting human and social needs. One of the shortest definitions of marketing is "meeting needs profitably." When eBay recognized that people

MARKETING **MEMO** | MARKETERS' FREQUENTLY ASKED QUESTIONS

1. How can we spot and choose the right market segment(s)?
2. How can we differentiate our offerings?
3. How should we respond to customers who buy on price?
4. How can we compete against lower-cost, lower-price competitors?
5. How far can we go in customizing our offering for each customer?
6. How can we grow our business?
7. How can we build stronger brands?
8. How can we reduce the cost of customer acquisition?
9. How can we keep our customers loyal for longer?
10. How can we tell which customers are more important?
11. How can we measure the payback from advertising, sales promotion, and public relations?
12. How can we improve sales force productivity?
13. How can we establish multiple channels and yet manage channel conflict?
14. How can we get the other company departments to be more customer-oriented?

were unable to locate some of the items they desired most and created an online auction clearinghouse or when IKEA noticed that people wanted good furniture at a substantially lower price and created knock-down furniture, they demonstrated marketing savvy and turned a private or social need into a profitable business opportunity.

The American Marketing Association offers the following formal definition: *Marketing is an organizational function and a set of processes for creating, communicating, and delivering value to customers and for managing customer relationships in ways that benefit the organization and its stake holders.*[2] Coping with exchange processes calls for a considerable amount of work and skill. Marketing management takes place when at least one party to a potential exchange thinks about the means of achieving desired responses from other parties. We see **marketing management** as *the art and science of choosing target markets and getting, keeping, and growing customers through creating, delivering, and communicating superior customer value.*

We can distinguish between a social and a managerial definition of marketing. A social definition shows the role marketing plays in society. One marketer said that marketing's role is to "deliver a higher standard of living." Here is a social definition that serves our purpose: *Marketing is a societal process by which individuals and groups obtain what they need and want through creating, offering, and freely exchanging products and services of value with others.* For a managerial definition, marketing has often been described as "the art of selling products," but people are surprised when they hear that the most important part of marketing is not selling! Selling is only the tip of the marketing iceberg. Peter Drucker, a leading management theorist, puts it this way:

> There will always, one can assume, be need for some selling. But the aim of marketing is to make selling superfluous. The aim of marketing is to know and understand the customer so well that the product or service fits him and sells itself. Ideally, marketing should result in a customer who is ready to buy. All that should be needed then is to make the product or service available.[3]

When Sony designed its Play Station, when Gillette launched its Mach III razor, and when Toyota introduced its Lexus automobile, these manufacturers were swamped with orders because they had designed the "right" product based on careful marketing homework.

Exchange and Transactions

A person can obtain a product in one of four ways. One can self-produce the product or service, as when one hunts, fishes, or gathers fruit. One can use force to get a product, as in a holdup or burglary. One can beg, as happens when a homeless person asks for food; or one can offer a product, a service, or money in exchange for something he or she desires.

Exchange, which is the core concept of marketing, is the process of obtaining a desired product from someone by offering something in return. For exchange potential to exist, five conditions must be satisfied:

1. There are at least two parties.
2. Each party has something that might be of value to the other party.

"We could have left well enough alone. But that would hardly be very characteristic. Now would it?" Lexus ads, and its campaign slogan, "The Passionate Pursuit of Perfection," express the company's marketing philosophy: only the best is good enough for its customers.

3. Each party is capable of communication and delivery.
4. Each party is free to accept or reject the exchange offer.
5. Each party believes it is appropriate or desirable to deal with the other party.

Whether exchange actually takes place depends on whether the two parties can agree on terms that will leave them both better off (or at least not worse off) than before. Exchange is a value-creating process because it normally leaves both parties better off.

Two parties are engaged in exchange if they are negotiating—trying to arrive at mutually agreeable terms. When an agreement is reached, we say that a transaction takes place. A **transaction** is a trade of values between two or more parties: A gives X to B and receives Y in return. Smith sells Jones a television set and Jones pays $400 to Smith. This is a classic monetary transaction; but transactions do not require money as one of the traded values. A barter transaction involves trading goods or services for other goods or services, as when lawyer Jones writes a will for physician Smith in return for a medical examination.

A transaction involves several dimensions: at least two things of value, agreed-upon conditions, a time of agreement, and a place of agreement. A legal system supports and enforces compliance on the part of the transactors. Without a law of contracts, people would approach transactions with some distrust, and everyone would lose.

A transaction differs from a transfer. In a **transfer**, A gives X to B but does not receive anything tangible in return. Gifts, subsidies, and charitable contributions are all transfers. Transfer behavior can also be understood through the concept of exchange. Typically, the transferer expects to receive something in exchange for his or her gift—for example, gratitude or seeing changed behavior in the recipient. Professional fund-raisers provide benefits to donors, such as thank-you notes, donor magazines, and invitations to events. Marketers have broadened the concept of marketing to include the study of transfer behavior as well as transaction behavior.

In the most generic sense, marketers seek to elicit a behavioral response from another party. A business firm wants a purchase, a political candidate wants a vote, a church wants an active member, and a social-action group wants the passionate adoption of some cause. Marketing consists of actions undertaken to elicit desired responses from a target audience.

To make successful exchanges, marketers analyze what each party expects from the transaction. Simple exchange situations can be mapped by showing the two actors and the wants and offerings flowing between them. Suppose John Deere, a worldwide leader in agricultural equipment, researches the benefits that a typical large-scale farm enterprise wants when it buys tractors, combines, planters, and sprayers. These benefits include high-quality equipment, a fair price, on-time delivery, good financing terms, and good parts and service. The items on this want list are not equally important and may vary from buyer to buyer. One of John Deere's tasks is to discover the relative importance of these different wants to the buyer.

John Deere also has a want list. It wants a good price for the equipment, on-time payment, and good word of mouth. If there is a sufficient match or overlap in the want lists, a basis for a transaction exists. John Deere's task is to formulate an offer that motivates the farm enterprise to buy John Deere equipment. The farm enterprise might in turn make a counteroffer. This process of negotiation leads to mutually acceptable terms or a decision not to transact.

What Is Marketed?

Marketing people are involved in marketing 10 types of entities: goods, services, experiences, events, persons, places, properties, organizations, information, and ideas.

GOODS Physical goods constitute the bulk of most countries' production and marketing effort. Each year, U.S. companies alone market billions of fresh, canned, bagged, and frozen food products and millions of cars, refrigerators, television sets, machines, and various other mainstays of a modern economy. Not only do companies market their goods, but thanks in part to the Internet, even individuals can effectively market goods.

SERVICES As economies advance, a growing proportion of their activities is focused on the production of services. The U.S. economy today consists of a 70–30 services-to-goods mix. Services include the work of airlines, hotels, car rental firms, barbers and beauticians, maintenance and repair people, as well as professionals working within or for companies, such as accountants, bankers, lawyers, engineers, doctors, software programmers, and management consultants. Many market offerings consist of a variable mix of goods and services. At a fast-food restaurant, for example, the customer consumes both a product and a service.

EVENTS Marketers promote time-based events, such as major trade shows, artistic performances, and company anniversaries. Global sporting events such as the Olympics or World Cup are promoted aggressively to both companies and fans. There is a whole profession of meeting planners who work out the details of an event and make sure it comes off perfectly.

EXPERIENCES By orchestrating several services and goods, a firm can create, stage, and market experiences. Walt Disney World's Magic Kingdom represents experiential marketing: Customers visit a fairy kingdom, a pirate ship, or a haunted house. So does the Hard Rock Café, where customers can enjoy a meal or see a band in a live concert. There is also a market for customized experiences, such as spending a week at a baseball camp playing with some retired baseball greats, paying to conduct the Chicago Symphony Orchestra for five minutes, or climbing Mount Everest.[4]

PERSONS Celebrity marketing is a major business. Today, every major film star has an agent, a personal manager, and ties to a public relations agency. Artists, musicians, CEOs, physicians, high-profile lawyers and financiers, and other professionals are also getting help from celebrity marketers.[5] Some people have done a masterful job of marketing themselves—think of Madonna, Oprah Winfrey, the Rolling Stones, Aerosmith, and Michael Jordan. Management consultant Tom Peters, himself a master at self-branding, has advised each person to become a "brand."

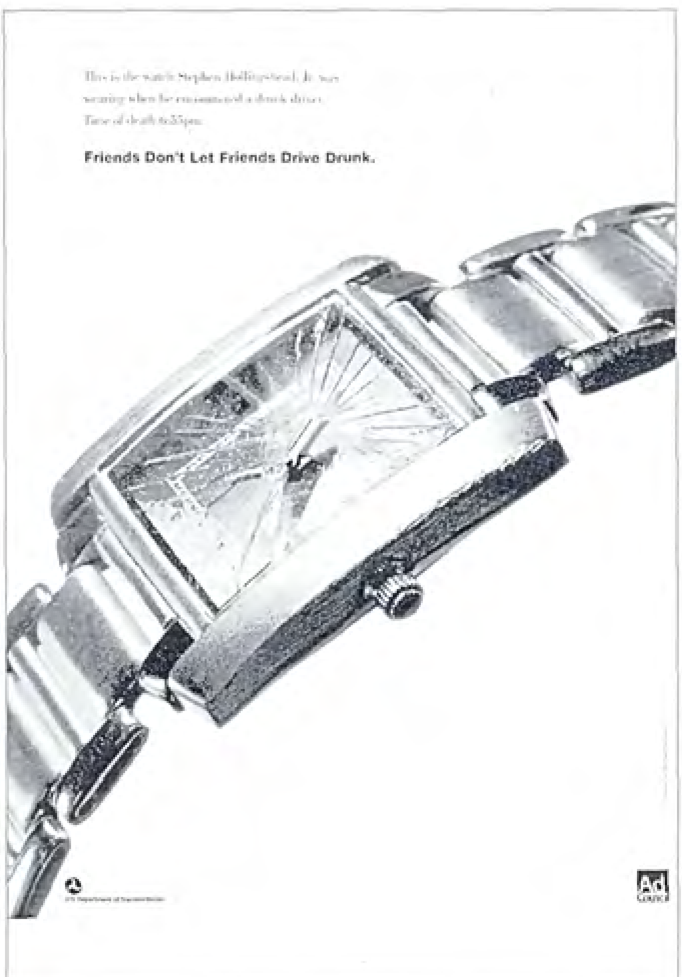
PLACES Cities, states, regions, and whole nations compete actively to attract tourists, factories, company headquarters, and new residents.[6] Place marketers include economic development specialists, real estate agents, commercial banks, local business associations, and advertising and public relations agencies. To fuel their high-tech industries and spawn entrepreneurship, cities such as Indianapolis, Charlotte, and Raleigh-Durham are actively wooing 20- to 29-year-olds through ads, PR, and other communications. Louisville, Kentucky, spends $1 million annually on e-mails, events, and networking approaches to convince 20-somethings of the city's quality of life and other advantages.

PROPERTIES Properties are intangible rights of ownership of either real property (real estate) or financial property (stocks and bonds). Properties are bought and sold, and this requires marketing. Real estate agents work for property owners or sellers or buy residential or commercial real estate. Investment companies and banks are involved in marketing securities to both institutional and individual investors.

ORGANIZATIONS Organizations actively work to build a strong, favorable, and unique image in the minds of their target publics. Companies spend money on corporate identity ads. Philips, the Dutch electronics company, puts out ads with the tag line "Let's Make Things Better." In the United Kingdom, Tesco's "Every Little Bit Helps" marketing program has vaulted it to the top of the supermarket chains in that country. Universities, museums, performing arts organizations, and non-profits all use marketing to boost their public images and to compete for audiences and funds.

INFORMATION Information can be produced and marketed as a product. This is essentially what schools and universities produce and distribute at a price to parents, students, and communities. Encyclopedias and most nonfiction books market information. Magazines such as *Road and Track* and *Byte* supply information about the car and computer worlds, respectively. The production, packaging, and distribution of information is one of our society's major industries.[7] Even companies that sell physical products attempt to add value through the use of information. For example, the CEO of Siemens Medical Systems, Tom McCausland, says, "[our product] is not necessarily an X-ray or an MRI, but information. Our business is really health-care information technology, and our end product is really an electronic patient record: information on lab tests, pathology, and drugs as well as voice dictation."[8]

IDEAS Every market offering includes a basic idea. Charles Revson of Revlon observed: "In the factory, we make cosmetics; in the store we sell hope." Products and services are platforms for delivering some idea or benefit. Social marketers are busy promoting such ideas as "Friends Don't Let Friends Drive Drunk" and "A Mind Is a Terrible Thing to Waste."



This is the watch Stephen Hollingshead Jr., was wearing when he encountered a drunk driver. Time of death 6:55 P.M. Friends Don't Let Friends Drive Drunk. An ad from the "Friends Don't Let Friends Drive Drunk" campaign promotes an idea, not a product.

Who Markets?

MARKETERS AND PROSPECTS A **marketer** is someone who seeks a response (attention, a purchase, a vote, a donation) from another party, called the **prospect**. If two parties are seeking to sell something to each other, we call them both marketers.

Marketers are skilled in stimulating demand for a company's products, but this is too limited a view of the tasks they perform. Just as production and logistics professionals are responsible for supply management, marketers are responsible for demand management. Marketing managers seek to influence the level, timing, and composition of demand to meet the organization's objectives. Eight demand states are possible:

1. ***Negative demand*** – Consumers dislike the product and may even pay a price to avoid it.
2. ***Nonexistent demand*** – Consumers may be unaware or uninterested in the product.
3. ***Latent demand*** – Consumers may share a strong need that cannot be satisfied by an existing product.
4. ***Declining demand*** – Consumers begin to buy the product less frequently or not at all.
5. ***Irregular demand*** – Consumer purchases vary on a seasonal, monthly, weekly, daily, or even hourly basis.
6. ***Full demand*** – Consumers are adequately buying all products put into the marketplace.
7. ***Overfull demand*** – More consumers would like to buy the product than can be satisfied.
8. ***Unwholesome demand*** – Consumers may be attracted to products that have undesirable social consequences.

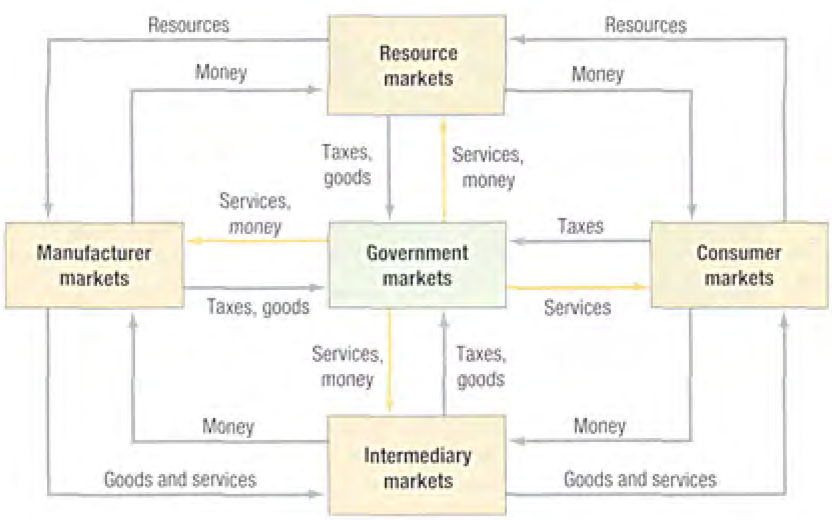
In each case, marketers must identify the underlying cause(s) of the demand state and then determine a plan for action to shift the demand to a more desired state.

MARKETS Traditionally, a "market" was a physical place where buyers and sellers gathered to buy and sell goods. Economists describe a market as a collection of buyers and sellers who transact over a particular product or product class (e.g., the housing market or grain market). Modern economies abound in such markets. Five basic markets and their connecting flows are shown in Figure 1.1. Manufacturers go to resource markets (raw material markets, labor markets, money markets), buy resources and turn them into goods and services, and then sell finished products to intermediaries, who sell them to consumers. Consumers sell their labor and receive money with which they pay for goods and services. The government collects tax revenues to buy goods from resource, manufacturer, and intermediary markets and uses these goods and services to provide public services. Each nation's economy and the global economy consist of complex interacting sets of markets linked through exchange processes.

On the other hand, marketers often use the term *market* to cover various groupings of customers. They view the sellers as constituting the industry and the buyers as constituting the market. They talk about need markets (the diet-seeking market), product markets (the shoe market), demographic markets (the youth market), and geographic markets (the French market); or they extend the concept to cover other markets, such as voter markets,

FIG. 1.1

Structure of Flows in a Modern Exchange Economy



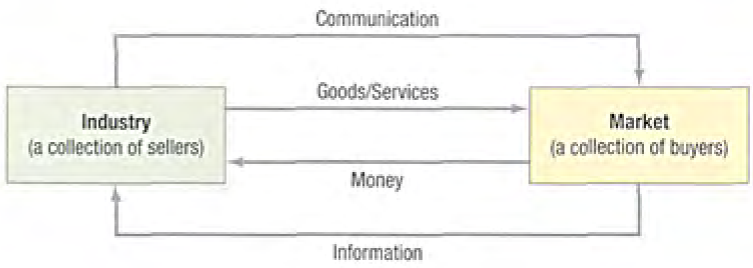


FIG. 1.2

A Simple Marketing System

labor markets, and donor markets. Figure 1.2 shows the relationship between the industry and the market. Sellers and buyers are connected by four flows. The sellers send goods and services and communications (ads, direct mail) to the market; in return they receive money and information (attitudes, sales data). The inner loop shows an exchange of money for goods and services; the outer loop shows an exchange of information.

KEY CUSTOMER MARKETS Consider the following key customer markets: consumer, business, global, and nonprofit.

Consumer Markets Companies selling mass consumer goods and services such as soft drinks, cosmetics, air travel, and athletic shoes and equipment spend a great deal of time trying to establish a superior brand image. Much of a brand's strength depends on developing a superior product and packaging, ensuring its availability, and backing it with engaging communications and reliable service. Complicating this task is the always changing consumer market (see "Marketing Insight: New Consumer Capabilities").

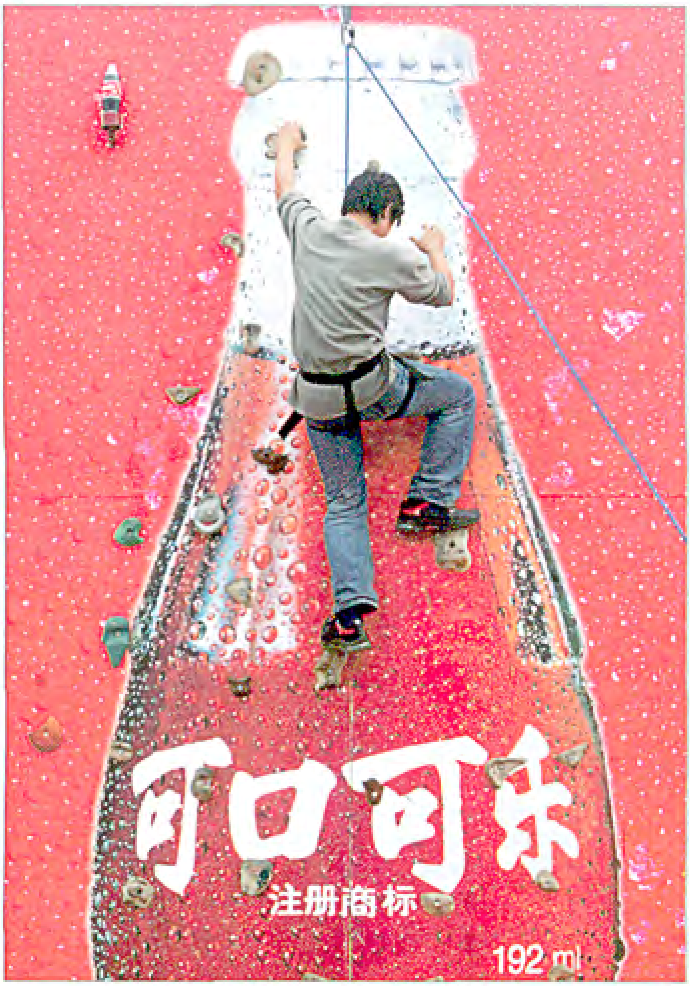
Business Markets Companies selling business goods and services often face well-trained and well-informed professional buyers who are skilled in evaluating competitive offerings. Business buyers buy goods in order to make or resell a product to others at a profit. Business marketers must demonstrate how their products will help these buyers achieve higher revenue or lower costs. Advertising can play a role, but a stronger role may be played by the sales force, price, and the company's reputation for reliability and quality.

Global Markets Companies selling goods and services in the global marketplace face additional decisions and challenges. They must decide which countries to enter; how to

MARKETING INSIGHT | NEW CONSUMER CAPABILITIES

The digital revolution has placed a whole new set of capabilities in the hands of consumers and businesses. Consider what consumers have today that they didn't have yesterday:

- *A substantial increase in buying power.* Buyers today are only a click away from comparing competitor prices and product attributes. They can get answers on the Internet in a matter of seconds. They don't need to drive to stores, park, wait on line, and hold discussions with salespeople. Consumers can even name the price they want to pay for a hotel room, airline ticket, or mortgage, and see if there are any willing suppliers. Business buyers can run a reverse auction where sellers compete to capture the buyer's business. Buyers can join with others to aggregate their purchases to achieve deeper volume discounts.
- *A greater variety of available goods and services.* Today a person can order almost anything over the Internet: furniture (Ethan Allen), washing machines (Sears), management consulting ("Ernie"), medical advice (WebMD). Amazon.com advertises itself as the world's largest bookstore, with over 3 million books; no physical bookstore can match this. Furthermore, buyers can order these goods from anywhere in the world, which helps people living in countries with very limited local offerings to achieve great savings. It also means that buyers in countries with high prices can reduce their costs by ordering in countries with lower prices.
- *A great amount of information about practically anything.* People can read almost any newspaper in any language from anywhere in the world. They can access online encyclopedias, dictionaries, medical information, movie ratings, consumer reports, and countless other information sources.
- *A greater ease in interacting and placing and receiving orders.* Today's buyers can place orders from home, office, or mobile phone 24 hours a day, 7 days a week, and the orders will be delivered to their home or office quickly.
- *An ability to compare notes on products and services.* Today's customers can enter a chat room centered on some area of common interest and exchange information and opinions.



Global marketing: Wall climbing on a Coke ad to attract attention (and customers) at the first China International Beverage Festival in Beijing in 2003.

enter each country (as an exporter, licenser, joint venture partner, contract manufacturer, or solo manufacturer); how to adapt their product and service features to each country; how to price their products in different countries; and how to adapt their communications to fit different cultures. These decisions must be made in the face of different requirements for buying, negotiating, owning, and disposing of property; different culture, language, and legal and political systems; and a currency that might fluctuate in value.

Nonprofit and Governmental Markets Companies selling their goods to nonprofit organizations such as churches, universities, charitable organizations, or government agencies need to price carefully because these organizations have limited purchasing power. Lower prices affect the features and quality that the seller can build into the offering. Much government purchasing calls for bids, with the lowest bid being favored, in the absence of extenuating factors.

MARKETPLACES, MARKETSPACES, AND METAMARKETS Today we can distinguish between a *marketplace* and *marketspace*. The marketplace is physical, as when you shop in a store; marketspace is digital, as when you shop on the Internet.[9]

Mohan Sawhney has proposed the concept of a *metamarket* to describe a cluster of complementary products and services that are closely related in the minds of consumers but are spread across a diverse set of industries. The automobile metamarket consists of automobile manufacturers, new car and used car dealers, financing companies, insurance companies, mechanics, spare parts dealers, service shops, auto magazines, classified auto ads in newspapers, and auto sites on the Internet. In purchasing a car, a buyer will get involved in many parts of this metamarket, and this has created an opportunity for metamediaries to assist buyers to move seamlessly through these groups, although they are disconnected in physical space. One example is Edmund's (www.edmunds.com), a Web site where a car buyer can find the stated features and prices of different automobiles and easily click to other sites to search for the lowest-price dealer, for financing, for car accessories, and for used cars at bargain prices. Metamediaries can also serve other metamarkets such as the home ownership market, the parenting and baby care market, and the wedding market.[10]

How Business and Marketing Are Changing

A recent book entitled *Beyond Disruption* praises companies such as Apple, Sony, and TAG Heuer for achieving exponential sales growth despite being in established, but stagnant, markets.[11] The explanation offered for these success stories was that these companies adopted a clear vision of the proper direction in which to take their brands and challenged marketing convention through product innovation, advertising, or some other aspect of marketing. Another recent book entitled *Radical Marketing* spotlights companies such as Harley-Davidson, Virgin Atlantic Airways, and Boston Beer for adopting a different approach to marketing that focuses on stretching limited resources, staying in close contact with customers, and creating more satisfying solutions to customer needs. (See "Marketing Memo: The Ten Rules of Radical Marketing.")

We can say with some confidence that "the marketplace isn't what it used to be." It is radically different as a result of major, sometimes interlinking societal forces that have created new behaviors, new opportunities, and new challenges:

- ***Changing technology.*** The digital revolution has created an Information Age. The Industrial Age was characterized by mass production and mass consumption, stores stuffed with inventory, ads everywhere, and rampant discounting. The Information Age promises to lead to more accurate levels of production, more targeted communications, and more relevant pricing. Moreover, much of today's business is carried on over electronic networks: intranet, extranets, and the Internet.
- ***Globalization.*** Technological advances in transportation, shipping, and communication have made it easier for companies to market in other countries and easier for consumers to buy products and services from marketers in other countries.
- ***Deregulation.*** Many countries have deregulated industries to create greater competition and growth opportunities. In the United States, long-distance telephone companies can now compete in local markets and local phone companies can now offer long distance. Similarly, electrical utilities can now enter other local markets.

MARKETING **MEMO** | THE TEN RULES OF RADICAL MARKETING

In their book *Radical Marketing*, Sam Hill and Glenn Rifkin lay out a set of guidelines that can help other companies emulate the radical marketers.

1. ***The CEO must own the marketing function.*** CEOs of radical marketers never delegate marketing responsibility.
2. ***The marketing department must start small and flat and stay small and flat.*** CEOs of radical marketers must not allow layers of management to grow between them and the market.
3. ***Get face-to-face with the people who matter most—the customers.*** Radical marketers know the advantages of direct interaction with customers.
4. ***Use market research cautiously.*** Radical marketers prefer grassroots techniques.
5. ***Hire only passionate missionaries, not marketers.*** Radical marketers "don't have marketers, they have missionaries."
6. ***Love and respect customers as individuals, not as numbers on a spreadsheet.*** Radical marketers recognize that the core customers are responsible for the bulk of their companies' successes.
7. ***Create a community of consumers.*** Radical marketers "encourage their customers to think of themselves as a community, and of the brand as a unifier of that community."
8. ***Rethink the marketing mix.*** For example, radical marketers use "surgical strike advertising" characterized by short, targeted ad campaigns.
9. ***Celebrate common sense and compete with larger competitors through fresh and different marketing ideas.*** Radical marketers, for example, limit distribution in order to create loyalty and commitment among distributors and customers.
10. ***Be true to the brand.*** Radical marketers "are obsessive about brand integrity, and they are fixated on quality."

Source: Sam Hill and Glenn Rifkin, *Radical Marketing* (New York: HarperCollins, 1999), pp. 19–31.

- ***Privatization.*** Many countries have converted public companies to private ownership and management to increase their efficiency, such as British Airways and British Telecom in the United Kingdom.
- ***Customer empowerment.*** Customers increasingly expect higher quality and service and some customization. They are more and more time-starved and want more convenience. They perceive fewer real product differences and show less brand loyalty. They can obtain extensive product information from the Internet and other sources, which permits them to shop more intelligently. They are showing greater price sensitivity in their search for value.
- ***Customization.*** The company is able to produce individually differentiated goods whether ordered in person, on the phone, or online. By going online, companies essentially enable consumers to design their own goods. The company also has the capacity to interact with each customer personally, to *personalize* messages, services, and the relationship. Using smart software and new manufacturing equipment, catalog house Lands' End put customized chinos up for sale in 2001 and is now expanding its number of customized products. Because items are cut to order, the company doesn't have to keep as much inventory around.[12]
- ***Heightened competition.*** Brand manufacturers are facing intense competition from domestic and foreign brands, which is resulting in rising promotion costs and shrinking profit margins. They are being further buffeted by powerful retailers who command limited shelf space and are putting out their own store brands in competition with national brands.
- ***Industry convergence.*** Industry boundaries are blurring at an incredible rate as companies are recognizing that new opportunities lie at the intersection of two or more industries. Pharmaceutical companies, at one time essentially chemical companies, are now adding biogenetic research capacities in order to formulate new drugs, new cosmetics (cosmoneu-

Cosmoneuticals: An ad for dermatology drugs marketed by Shiseido, the Japanese cosmetics firm. The WH/SIS product line targets spots and freckles, and includes cleanser, lotion, emulsion, day/night whitening beauty essence, and medication to be taken orally. It is sold only in Japan, mainly in drugstores.

ticals), and new foods (nutriceuticals). Shiseido, the Japanese cosmetics firm, now markets a portfolio of dermatology drugs. Christmas 2003 saw the convergence of the computing and consumer electronics industries as the giants of the computer world such as Dell, Gateway, and Hewlett-Packard released a stream of entertainment devices—from MP3 players to plasma TVs and camcorders. The shift to digital technology, in which devices needed to play entertainment content are more and more like PCs, is fueling this massive convergence.[13]

- ***Retail transformation.*** Small retailers are succumbing to the growing power of giant retailers and "category killers." Store-based retailers are facing growing competition from catalog houses; direct-mail firms; newspaper, magazine, and TV direct-to-customer ads; home shopping TV; and e-commerce on the Internet. In response, entrepreneurial retailers are building entertainment into stores with coffee bars, lectures, demonstrations, and performances. They are marketing an "experience" rather than a product assortment.

- ***Disintermediation.*** The amazing success of early online dot-coms such as AOL, Amazon, Yahoo, eBay, E'TRADE, and dozens of others who created *disintermediation* in the delivery of products and services, struck terror in the hearts of many established manufacturers and retailers. In response to disintermediation, many traditional companies engaged in *reintermediation* and became "brick-and-click," adding online services to their existing offerings. Many brick-and-click competitors became stronger contenders than the pure-click firms, since they had a larger pool of resources to work with and well-established brand names.

::: Company Orientations Toward the Marketplace

What philosophy should guide a company's marketing efforts? What relative weights should be given to the interests of the organization, the customers, and society? Very often these interests conflict. The competing concepts under which organizations have conducted marketing activities include: the production concept, product concept, selling concept, marketing concept, and holistic marketing concept.

The Production Concept

The production concept is one of the oldest concepts in business. It holds that consumers will prefer products that are widely available and inexpensive. Managers of production-oriented businesses concentrate on achieving high production efficiency, low costs, and mass distribution. This orientation makes sense in developing countries such as China where the largest PC manufacturer, Legend, and domestic appliances giant Haier take advantage of the country's huge inexpensive labor pool to dominate the market. It is also used when a company wants to expand the market.[14]

The Product Concept

The product concept holds that consumers will favor those products that offer the most quality, performance, or innovative features. Managers in these organizations focus on making superior products and improving them over time. However, these managers are sometimes caught up in a love affair with their products. They might commit the "better-mousetrap" fallacy, believing that a better mousetrap will lead people to beat a path to their door. A new or improved product will not necessarily be successful unless the product is priced, distributed, advertised, and sold properly.

The Selling Concept

The selling concept holds that consumers and businesses, if left alone, will ordinarily not buy enough of the organization's products. The organization must, therefore, undertake an aggressive selling and promotion effort. The selling concept is epitomized in the thinking of Sergio Zyman, Coca-Cola's former vice president of marketing: The purpose of marketing is to sell more stuff to more people more often for more money in order to make more profit.[15]

The selling concept is practiced most aggressively with unsought goods, goods that buyers normally do not think of buying, such as insurance, encyclopedias, and funeral plots. Most firms practice the selling concept when they have overcapacity. Their aim is to sell what they make rather than make what the market wants. However, marketing based on hard selling carries high risks. It assumes that customers who are coaxed into buying a product will like it; and that if they do not, they will not return it or bad-mouth it or complain to consumer organizations, or might even buy it again.

The Marketing Concept

The marketing concept emerged in the mid-1950s.[16] Instead of a product-centered, "make-and-sell" philosophy, business shifted to a customer-centered, "sense-and-respond" philosophy. Instead of "hunting," marketing is "gardening." The job is not to find the right customers for your products, but the right products for your customers. The marketing concept holds that the key to achieving organizational goals consists of the company being more effective than competitors in creating, delivering, and communicating superior customer value to its chosen target markets.

> Theodore Levitt of Harvard drew a perceptive contrast between the selling and marketing concepts: Selling focuses on the needs of the seller; marketing on the needs of the buyer. Selling is preoccupied with the seller's need to convert his product into cash; marketing with the idea of satisfying the needs of the customer by means of the product and the whole cluster of things associated with creating, delivering and finally consuming it.[17]

Several scholars have found that companies who embrace the marketing concept achieve superior performance.[18] This was first demonstrated by companies practicing a *reactive market orientation*—understanding and meeting customers' expressed needs. Some critics say this means companies develop only low-level innovations. Narver and his colleagues argue that high-level innovation is possible if the focus is on customers' latent needs. He calls this a *proactive marketing orientation*.[19] Companies such as 3M, HP, and Motorola have made a practice of researching or imagining latent needs through a "probe-and-learn" process. Companies that practice both a reactive and proactive marketing orientation are implementing a *total market orientation* and are likely to be the most successful.

DIEBOLD

The $1.9 billion automated teller machine (ATM) maker Diebold is not only focused on what its customers want, but looks ahead to what its customers' customers want. For instance, the North Canton, Ohio, company not only develops ATMs that have brighter screens or are easy to install, but embeds advanced end-user capabilities into the ATMs. These include on-demand banking statements, automatic bill payment and instant crediting of deposits—with or without a deposit envelope. With advances like these, Diebold's customers, mainly financial institutions and retailers, can offer more services to their customers after banking hours.[20]

In the course of converting to a marketing orientation, a company faces three hurdles: organized resistance, slow learning, and fast forgetting. Some company departments (often manufacturing, finance, and R&D) believe a stronger marketing function threatens their power in the organization. Initially, the marketing function is seen as one of several equally important functions in a check-and-balance relationship. Marketers argue that their function is more important. A few enthusiasts go further and say marketing is the major function of the enterprise, for without customers there is no company. Enlightened marketers clarify the issue by putting the customer at the center of the company. They argue for a customer orientation in which all functions work together to respond to, serve, and satisfy the customer.[21]

The Holistic Marketing Concept

A whole set of forces that appeared in the last decade call for new marketing and business practices. Companies have new capabilities that can transform the way they have been doing marketing (see "Marketing Insight: The Internet Advantage"). Companies need fresh thinking about how to operate and compete in a new marketing environment. Marketers in the twenty-first century are increasingly recognizing the need to have a more complete, cohesive approach that goes beyond traditional applications of the marketing concept. Look at Puma.

PUMA

German athletic footwear company Puma has used holistic marketing to bring its product back from being a sentimental mainstay of the 1970s to one of the trendiest athletic shoes around. Puma uses multiple marketing approaches that work synergistically to set Puma apart as an edgy, trend-setting brand. Puma designs products with distinct customer groups in mind—such as snowboarders, car racing fans, and yoga enthusiasts—using market research generated by its retailer partners. Puma also targets the armchair athlete—its two most popular models are the Mostro, a walking shoe with a nubbed wraparound sole, and the Speed Cat, a flat $65 sneaker modeled on shoes worn by Formula One race car drivers. It generates word of mouth or "viral marketing" by clever promotions—from partnering with BMW/Mini, Terence Conran Design Shop, and the Jamaican Olympic team—or holding promotional events at sushi restaurants during the 2002 World Cup to outfitting Serena Williams and showcasing products in well-chosen TV shows and movies. The approach is working: Puma's sales have increased for 10 straight years from 1994 to 2004, tripling in total.[22]

The **holistic marketing** concept is based on the development, design, and implementation of marketing programs, processes, and activities that recognizes their breadth and interdependencies. Holistic marketing recognizes that "everything matters" with marketing—and that a broad, integrated perspective is often necessary. Four components of holistic marketing are relationship marketing, integrated marketing, internal marketing, and social responsibility marketing.

Holistic marketing is thus an approach to marketing that attempts to recognize and reconcile the scope and complexities of marketing activities. Figure 1.3 provides a schematic overview of four broad themes characterizing holistic marketing.

RELATIONSHIP MARKETING Increasingly, a key goal of marketing is to develop deep, enduring relationships with all people or organizations that could directly or indirectly affect the success of the firm's marketing activities. **Relationship marketing** has the aim of building mutually satisfying long-term relationships with key parties—customers, suppliers, distributors, and

MARKETING INSIGHT — THE INTERNET ADVANTAGE

The Internet gives today's companies a new set of capabilities:

- Companies can operate a powerful new information and sales channel, the Internet, with augmented geographical reach to inform and promote their businesses and products worldwide. By establishing one or more Web sites, a company can list its products and services, its history, its business philosophy, its job opportunities, and other information of interest to visitors. Unlike the ads and brochures of the past, the Internet permits a company to transmit an almost unlimited amount of information.
- Companies can collect fuller and richer information about markets, customers, prospects, and competitors. They can also conduct fresh marketing research using the Internet to arrange for focus groups, send out questionnaires, and gather primary data in several other ways.
- Companies can facilitate and speed up internal communication among their employees by using the Internet as a private intranet. Employees can query one another, seek advice, and download or upload needed information from and to the company's main computer.
- Companies can have two-way communications with customers and prospects, and more efficient transactions. The Internet makes it easy for individuals to e-mail companies and receive replies, and more companies today are developing extranets with suppliers and distributors for sending and receiving information, placing orders, and making payments more efficiently.
- Companies are now able to send ads, coupons, samples, and information to customers who have requested these items or have given the company permission to send them.
- Companies can customize offerings and services by using database information on the number of visitors to their Web sites and visit frequency.
- Companies can improve purchasing, recruiting, training, and internal and external communications.
- Companies can achieve substantial savings by using the Internet to compare sellers' prices, and to purchase materials at auction or by posting their own terms. Companies can recruit new employees. Many are also preparing Internet training products that can be downloaded to employees, dealers, and agents.
- Companies can improve logistics and operations for substantial cost savings while improving accuracy and service quality. The Internet provides a more accurate and faster way to send and receive information, orders, transactions, and payments between companies, their business partners, and their customers.

FIG. 1.3

Holistic Marketing Dimensions

other marketing partners—in order to earn and retain their business.[23] Relationship marketing builds strong economic, technical, and social ties among the parties.

Relationship marketing involves cultivating the right kind of relationships with the right constituent groups. Marketing must not only do customer relationship management (CRM), but also partner relationship management (PRM) as well. Four key constituents for marketing are customers, employees, marketing partners (channels, suppliers, distributors, dealers, agencies), and members of the financial community (shareholders, investors, analysts).

The ultimate outcome of relationship marketing is the building of a unique company asset called a marketing network. A **marketing network** consists of the company and its supporting stakeholders (customers, employees, suppliers, distributors, retailers, ad agencies, university scientists, and others) with whom it has built mutually profitable business relationships. Increasingly, competition is not between companies but between marketing networks, with the prize going to the company that has built the better network. The operating principle is simple: Build an effective network of relationships with key stakeholders, and profits will follow.[24]

The development of strong relationships requires an understanding of the capabilities and resources of different groups, as well as their needs, goals, and desires. A growing number of today's companies are now shaping separate offers, services, and messages to individual customers. These companies collect information on each customer's past transactions, demographics, psychographics, and media and distribution preferences. They hope to achieve profitable growth through capturing a larger share of each customer's expenditures by building high customer loyalty and focusing on customer lifetime value.

The ability of a company to deal with customers one at a time has become practical as a result of advances in factory customization, computers, the Internet, and database marketing software. BMW's technology now allows buyers to design their own models from 350 variations, 500 options, 90 exterior colors, and 170 trims. The company claims that 80 percent of the cars bought by individuals in Europe and up to 30 percent of those in the United States are built to order. British supermarket giant Tesco is outpacing its rival store, Sainsbury, by using its Clubcard data to personalize offers according to individual customer attributes.[25]

Yet the practice of one-to-one marketing is not for every company: The required investment in information collection, hardware, and software may exceed the payout. It works best for companies that normally collect a great deal of individual customer information, carry a lot of products that can be cross-sold, carry products that need periodic replacement or upgrading, and sell products of high value.

Rich, multifaceted relationships with key constituents create the foundation for a mutually beneficial arrangement for both parties. For example, tired of having its big rigs return empty after making a delivery as often as 15 percent of the time, General Mills entered a program with Fort James and a dozen other companies to combine one-way shipping routes into a cross-country loop via a tag-team of contracted trucks. As a result, General Mills reduced its empty truck time to 6 percent, saving 7 percent on shipping costs in the process.[26]

FIG. 1.4

The Four P Components of the Marketing Mix

INTEGRATED MARKETING The marketer's task is to devise marketing activities and assemble fully integrated marketing programs to create, communicate, and deliver value for consumers. The marketing program consists of numerous decisions on value-enhancing marketing activities to use. Marketing activities come in all forms. One traditional depiction of marketing activities is in terms of the marketing mix, which has been defined as the set of marketing tools the firm uses to pursue its marketing objectives.[27] McCarthy classified these tools into four broad groups, which he called *the four Ps* of marketing: product, price, place, and promotion.[28]

The particular marketing variables under each P are shown in Figure 1.4. Marketing-mix decisions must be made for influencing the trade channels as well as the final consumers. Figure 1.5 shows the company preparing an offering mix of products, services, and prices, and utilizing a communications mix of advertising, sales promotion, events and experiences, public relations, direct marketing, and personal selling to reach the trade channels and the target customers.

The firm can change its price, sales force size, and advertising expenditures in the short run. It can develop new products and modify its distribution channels only in the long run. Thus the firm typically makes fewer period-to-period marketing-mix changes in the short run than the number of marketing-mix decision variables might suggest.

The four Ps represent the sellers' view of the marketing tools available for influencing buyers. From a buyer's point of view, each marketing tool is designed to deliver a customer

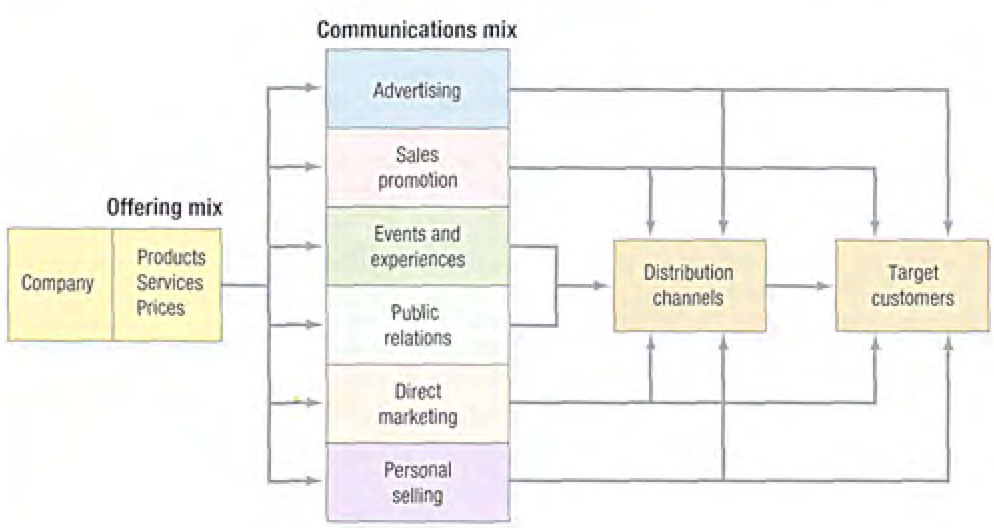


FIG. 1.5

Marketing-Mix Strategy

benefit. Robert Lauterborn suggested that the sellers' four Ps correspond to the customers' four Cs.[29]

Four Ps	Four Cs
Product	Customer solution
Price	Customer cost
Place	Convenience
Promotion	Communication

Winning companies will be those that can meet customer needs economically and conveniently and with effective communication.

Two key themes of integrated marketing are that (1) many different marketing activities are employed to communicate and deliver value and (2) all marketing activities are coordinated to maximize their joint effects. In other words, the design and implementation of any one marketing activity is done with all other activities in mind. Businesses must integrate their systems for demand management, resource management, and network management.

For example, an integrated communication strategy involves choosing communication options that reinforce and complement each other. A marketer might selectively employ television, radio, and print advertising, public relations and events, and PR and Web site communications so that each contributes on its own as well as improves the effectiveness of others. Because there was already a buzz for its remake of the cult 1974 film *The Texas Chainsaw Massacre*, New Line Cinema relied on a combination of both traditional TV ads and trailers, as well as interactive marketing via AOL's Instant Messenger and "bots"—robot agents—to help spread the word and get teens talking about the film. Their goal was to create a peer-to-peer communication, that is, getting teens to do the marketing for them![30] Integrated channel strategy involves ensuring that direct (e.g., online sales) and indirect channels (e.g., retail sales) work together to maximize sales and brand equity.

INTERNAL MARKETING Holistic marketing incorporates *internal marketing*, ensuring that everyone in the organization embraces appropriate marketing principles, especially senior management. Internal marketing is the task of hiring, training, and motivating able employees who want to serve customers well. Smart marketers recognize that marketing activities within the company can be as important as, or even more so than, marketing activities directed outside the company. It makes no sense to promise excellent service before the company's staff is ready to provide it.

Internal marketing must take place on two levels. At one level, the various marketing functions—sales force, advertising, customer service, product management, marketing research—must work together. Too often, the sales force thinks product managers set prices or sale quotas "too high"; or the advertising director and a brand manager cannot agree on an advertising campaign. All these marketing functions must be coordinated from the customer's point of view. The following example highlights the coordination problem:

> The marketing vice president of a major European airline wants to increase the airline's traffic share. His strategy is to build up customer satisfaction through providing better food, cleaner cabins, better-trained cabin crews, and lower fares; yet he has no authority in these matters. The catering department chooses food that keeps food costs down; the maintenance department uses cleaning services that keep down cleaning costs; the human resources department hires people without regard to whether they are naturally friendly; the finance department sets the fares. Because these departments generally take a cost or production point of view, the vice president of marketing is stymied in creating an integrated marketing mix.

At another level, marketing must be embraced by the other departments; they must also "think customer." Marketing is not a department so much as a company orientation. Marketing thinking must be pervasive throughout the company (see Table 1.1). Xerox goes so far as to include in every job description an explanation of how that job affects the customer. Xerox factory managers know that visits to the factory can help sell a potential customer if the factory is clean and efficient. Xerox accountants know that customer attitudes are affected by Xerox's billing accuracy and promptness in returning calls.

SOCIAL RESPONSIBILITY MARKETING Holistic marketing incorporates *social responsibility marketing* and understanding broader concerns and the ethical, environmental, legal, and social context of marketing activities and programs. The cause and effects of marketing

TABLE 1.1

Assessing Which Company Departments Are Customer-Minded

R&D

- They spend time meeting customers and listening to their problems.
- They welcome the involvement of marketing, manufacturing, and other departments to each new project.
- They benchmark competitors' products and seek "best of class" solutions.
- They solicit customer reactions and suggestions as the project progresses.
- They continuously improve and refine the product on the basis of market feedback.

Purchasing

- They proactively search for the best suppliers.
- They build long-term relationships with fewer but more reliable, high-quality suppliers.
- They don't compromise quality for price savings.

Manufacturing

- They invite customers to visit and tour their plants.
- They visit customer plants.
- They willingly work overtime to meet promised delivery schedules.
- They continuously search for ways to produce goods faster and/or at lower cost.
- They continuously improve product quality, aiming for zero defects.
- They meet customer requirements for "customization" where possible.

Marketing

- They study customer needs and wants in well-defined market segments.
- They allocate marketing effort in relation to the long-run profit potential of the targeted segments.
- They develop winning offers for each target segment.
- They measure company image and customer satisfaction on a continuous basis.
- They continuously gather and evaluate ideas for new products, product improvements, and services.
- They urge all company departments and employees to be customer-centered.

Sales

- They have specialized knowledge of the customer's industry.
- They strive to give the customer "the best solution."
- They only make promises that they can keep.
- They feed back customers' needs and ideas to those in charge of product development.
- They serve the same customers for a long period of time.

Logistics

- They set a high standard for service delivery time and meet this standard consistently.
- They operate a knowledgeable and friendly customer service department that can answer questions, handle complaints, and resolve problems in a satisfactory and timely manner.

Accounting

- They prepare periodic "profitability" reports by product, market segment, geographic areas (regions, sales territories), order sizes, channels, and individual customers.
- They prepare invoices tailored to customer needs and answer customer queries courteously and quickly.

Finance

- They understand and support marketing expenditures (e.g., image advertising) that produce long-term customer preference and loyalty.
- They tailor the financial package to the customer's financial requirements.
- They make quick decisions on customer creditworthiness.

Public Relations

- They send out favorable news about the company and "damage control" unfavorable news.
- They act as an internal customer and public advocate for better company policies and practices.

Source: Philip Kotler, *Kotler on Marketing*, 1999, New York: The Free Press, pp. 21–22.

clearly extend beyond the company and the consumer to society as a whole. Social responsibility also requires that marketers carefully consider the role that they are playing and could play in terms of social welfare.

Are companies that do an excellent job of satisfying consumer wants necessarily acting in the best long-run interests of consumers and society? Consider the following criticism:

> The fast-food hamburger industry offers tasty but unhealthy food. The hamburgers have a high fat content, and the restaurants promote fries and pies, two products high in starch and fat. The products are wrapped in convenient packaging, which leads to much waste. In satisfying consumer wants, these restaurants may be hurting consumer health and causing environmental problems.

Recognizing these criticisms, companies like McDonald's have added healthier items to their menus (e.g., salads) and introduced environmental initiatives (e.g., replacing polystyrene foam sandwich clamshells with paper wraps and lightweight recycled boxes). Recently, McDonald's announced its largest environmental initiative to date. McDonald's Corp., which buys 2.5 billion pounds of poultry, beef, and pork a year for its 30,000 restaurants worldwide, ordered its suppliers to eliminate the use of antibiotics that are also given to humans, specifically when those drugs are used to make chickens, pigs and, less often, cattle, grow faster. "We saw lots of evidence that showed the declining rate of effectiveness of antibiotics in human medicine," said Bob Langert, McDonald's senior director of social responsibility. "We started to look at what we could do."[31]

Situations like this one call for a new term that enlarges the marketing concept. Among those suggested are "humanistic marketing" and "ecological marketing." We propose calling it the "societal marketing concept." The *societal marketing concept* holds that the organization's task is to determine the needs, wants, and interests of target markets and to deliver the desired satisfactions more effectively and efficiently than competitors in a way that preserves or enhances the consumer's and the society's well-being.

The societal marketing concept calls upon marketers to build social and ethical considerations into their marketing practices. They must balance and juggle the often conflicting criteria of company profits, consumer want satisfaction, and public interest. Table 1.2 displays some different types of corporate social initiatives, as illustrated with McDonald's.

Yet a number of companies—including the Body Shop, Ben & Jerry's, and Patagonia—have achieved notable sales and profit gains by adopting and practicing a form of the societal marketing concept called *cause-related marketing*. Pringle and Thompson define this as

TABLE 1.2 Corporate Social Initiatives

Type	Description	Example
Corporate social marketing	Supporting behavior change campaigns	McDonald's promotion of a statewide childhood immunization campaign in Oklahoma
Cause marketing	Promoting social issues through efforts such as sponsorships, licensing agreements, and advertising	McDonald's sponsorship of Forest (a gorilla) at Sydney's Zoo—a 10-year sponsorship commitment, aimed at preserving this endangered species
Cause-related marketing	Donating a percentage of revenues to a specific cause based on the revenue occurring during the announced period of support	McDonald's earmarking of $1 for Ronald McDonald Children's Charities from the sale of every Big Mac and pizza sold on McHappy Day
Corporate philanthropy	Making gifts of money, goods, or time to help nonprofit organizations, groups, or individuals	McDonald's contributions to Ronald McDonald House Charities
Corporate community involvement	Providing in-kind or volunteer services in the community	McDonald's catering meals for firefighters in the December 1997 bushfires in Australia
Socially responsible business practices	Adapting and conducting business practices that protect the environment, and human and animal rights	McDonald's requirement that suppliers increase the amount of living space for laying hens on factory farms

Source: Philip Kotler and Nancy Lee, *Corporate Social Responsibility: Doing the Most Good for Your Company and Your Cause* (Wiley, December 2004).

activity by which a company with an image, product, or service to market builds a relationship or partnership with a "cause," or a number of "causes," for mutual benefit."[32]

Companies see cause-related marketing as an opportunity to enhance their corporate reputation, raise brand awareness, increase customer loyalty, build sales, and increase press coverage. They believe that customers will increasingly look for signs of good corporate citizenship that go beyond supplying rational and emotional benefits. Avon has been one of the most successful cause marketers.

Ben & Jerry's co-founders Ben Cohen (left) and Jerry Greenfield (right) feed Unilever US CEO Richard Goldstein in May 2000, when Ben & Jerry's was bought by Unilever. Cohen and Greenfield agreed to the deal after months of negotiations to ensure that the company's high standards and corporate social consciousness would be maintained.

THE AVON WALK FOR BREAST CANCER

The Avon Walk for Breast Cancer is one of many projects of the Avon Foundation Breast Cancer Crusade, a global initiative of Avon Products, Inc., that was launched in the United States in 1993. Its mission has been to support access to care and finding a cure for breast cancer, with a focus on those who are medically underserved, by funding education, screening and diagnosis, treatment, support services, and scientific research. Worldwide, Avon is the largest corporate supporter of the breast cancer cause, with more than $250 million generated since the first program in 1992. The Avon Breast Cancer Crusade raises funds to accomplish this mission through many programs: sales of special Crusade "pink ribbon" products by Avon's nearly 600,000 U.S. independent sales representatives; concerts, walks, races, and other special events around the world; direct online fund-raising; and the Avon Walk for Breast Cancer series of weekend events in the United States (avonfoundation.org, avonwalk.org).

Print ad for an Avon Walk for Breast Cancer series of weekend events.

::: Fundamental Marketing Concepts, Trends, and Tasks

To understand the marketing function, we need to understand certain fundamental concepts and tasks, along with current trends.

Core Concepts

A core set of concepts creates a foundation for marketing management and a holistic marketing orientation.

NEEDS, WANTS, AND DEMANDS The marketer must try to understand the target market's needs, wants, and demands. *Needs* are the basic human requirements. People need food, air, water, clothing, and shelter to survive. People also have strong needs for recreation, education, and entertainment. These needs become *wants* when they are directed to specific objects that might satisfy the need. An American needs food but may want a hamburger, French fries, and a soft drink. A person in Mauritius needs food but may want a mango, rice, lentils, and beans. Wants are shaped by one's society. *Demands* are wants for specific products backed by an ability to pay. Many people want a Mercedes; only a few are willing and able to buy one. Companies must measure not only how many people want their product but also how many would actually be willing and able to buy it.

These distinctions shed light on the frequent criticism that "marketers create needs" or "marketers get people to buy things they don't want." Marketers do not create needs: Needs preexist marketers. Marketers, along with other societal factors, influence wants. Marketers might promote the idea that a Mercedes would satisfy a person's need for social status. They do not, however, create the need for social status.

Understanding customer needs and wants is not always simple. Some customers have needs of which they are not fully conscious, or they cannot articulate these needs, or they use words that require some interpretation. What does it mean when the customer asks for a "powerful" lawnmower, a "fast" lathe, an "attractive" bathing suit, or a "restful" hotel? Consider the customer who says he wants an "inexpensive car." The marketer must probe further. We can distinguish among five types of needs:

1. Stated needs (the customer wants an inexpensive car).
2. Real needs (the customer wants a car whose operating cost, not its initial price, is low).
3. Unstated needs (the customer expects good service from the dealer).
4. Delight needs (the customer would like the dealer to include an onboard navigation system).
5. Secret needs (the customer wants to be seen by friends as a savvy consumer).

Responding only to the stated need may shortchange the customer. Many consumers do not know what they want in a product. Consumers did not know much about cellular phones when they were first introduced. Nokia and Ericsson fought to shape consumer perceptions of cellular phones. Consumers were in a learning mode and companies forged strategies to shape their wants. As stated by Carpenter, "Simply giving customers what they want isn't enough any more—to gain an edge companies must help customers learn what they want."[33]

In the past, "responding to customer needs" meant studying customer needs and making a product that fit these needs on the average, but some of today's companies instead respond to each customer's individual needs. Dell Computer does not prepare a perfect computer for its target market. Rather, it provides product platforms on which each person customizes the features he or she desires in the computer. This is a change from a "make-and-sell" philosophy to a philosophy of "sense and respond."

TARGET MARKETS, POSITIONING, AND SEGMENTATION A marketer can rarely satisfy everyone in a market. Not everyone likes the same cereal, hotel room, restaurant, automobile, college, or movie. Therefore, marketers start by dividing up the market into segments. They identify and profile distinct groups of buyers who might prefer or require varying product and services mixes by examining demographic, psychographic, and behavioral differences among buyers. The marketer then decides which segments present the greatest opportunity—which are its *target markets.* For each chosen target market, the firm develops a *market offering.* The offering is *positioned* in the minds of the target buyers as delivering some central benefit(s). For example, Volvo develops its cars for buyers to whom automobile

Positioning: "The First SUV with Anti-Rollover Technology." A Volvo ad focuses on the company's central benefit, safety.

safety is a major concern. Volvo, therefore, positions its car as the safest a customer can buy. Companies do best when they choose their target market(s) carefully and prepare tailored marketing programs.

OFFERINGS AND BRANDS Companies address needs by putting forth a value proposition, a set of benefits they offer to customers to satisfy their needs. The intangible value proposition is made physical by an *offering*, which can be a combination of products, services, information, and experiences.

A *brand* is an offering from a known source. A brand name such as McDonald's carries many associations in the minds of people: hamburgers, fun, children, fast food, convenience, and golden arches. These associations make up the brand image. All companies strive to build brand strength—that is, a strong, favorable, and unique brand image.

VALUE AND SATISFACTION The offering will be successful if it delivers value and satisfaction to the target buyer. The buyer chooses between different offerings on the basis of which is perceived to deliver the most value. *Value* reflects the perceived tangible and intangible benefits and costs to customers. Value can be seen as primarily a combination of quality, service, and price (qsp), called the "customer value triad." Value increases with quality and service and decreases with price, although other factors can also play an important role.

Value is a central marketing concept. Marketing can be seen as the identification, creation, communication, delivery, and monitoring of customer value. *Satisfaction* reflects a person's comparative judgments resulting from a product's perceived performance (or outcome) in relation to his or her expectations. If the performance falls short of expectations, the customer is dissatisfied and disappointed. If the performance matches the expectations, the customer is satisfied. If the performance exceeds expectations, the customer is highly satisfied or delighted.

MARKETING CHANNELS To reach a target market, the marketer uses three kinds of marketing channels. *Communication channels* deliver and receive messages from target buyers, and include newspapers, magazines, radio, television, mail, telephone, billboards, posters, fliers, CDs, audiotapes, and the Internet. Beyond these, communications are conveyed by facial expressions and clothing, the look of retail stores, and many other media. Marketers are increasingly adding dialogue channels (e-mail and toll-free numbers) to counterbalance the more normal monologue channels (such as ads).

The marketer uses *distribution channels* to display, sell, or deliver the physical product or service(s) to the buyer or user. They include distributors, wholesalers, retailers, and agents.

The marketer also uses *service channels* to carry out transactions with potential buyers. Service channels include warehouses, transportation companies, banks, and insurance companies that facilitate transactions. Marketers clearly face a design problem in *choosing the best mix of communication, distribution, and service channels for their* offerings.

SUPPLY CHAIN Whereas marketing channels connect the marketer to the target buyers, the supply chain describes a longer channel stretching from raw materials to components to final products that are carried to final buyers. The supply chain for women's purses starts with hides, and moves through tanning operations, cutting operations, manufacturing, and the marketing channels bringing products to customers. The supply chain represents a value delivery system. Each company captures only a certain percentage of the total value generated by the supply chain. When a company acquires competitors or moves upstream or downstream, its aim is to capture a higher percentage of supply chain value.

COMPETITION Competition includes all the actual and potential rival offerings and substitutes that a buyer might consider. Suppose an automobile company is planning to buy steel for its cars. There are several possible levels of competitors. The car manufacturer can buy steel from U.S. Steel or other integrated steel mills in the United States (e.g., from Bethlehem) or abroad (e.g., from Japan or Korea); or buy steel from a mini-mill such as Nucor at a cost savings; or buy aluminum for certain parts of the car to lighten the car's weight (e.g., from Alcoa); or buy engineered plastics for bumpers instead of steel (e.g., from GE Plastics). Clearly, U.S. Steel would be thinking too narrowly of competition if it thought only of other integrated steel companies. In fact, U.S. Steel is more likely to be hurt in the long run by substitute products than by its immediate steel company rivals. It must also consider whether to make substitute materials or stick only to those applications where steel offers superior performance.

MARKETING ENVIRONMENT Competition represents only one force in the environment in which the marketer operates. The marketing environment consists of the task environment and the broad environment.

The *task environment* includes the immediate actors involved in producing, distributing, and promoting the offering. The main actors are the company, suppliers, distributors, dealers, and the target customers. Included in the supplier group are material suppliers and service suppliers such as marketing research agencies, advertising agencies, banking and insurance companies, transportation companies, and telecommunications companies. Included with distributors and dealers are agents, brokers, manufacturer representatives, and others who facilitate finding and selling to customers.

The *broad environment* consists of six components: demographic environment, economic environment, physical environment, technological environment, political-legal environment, and social-cultural environment. These environments contain forces that can have a major impact on the actors in the task environment. Market actors must pay close attention to the trends and developments in these environments and make timely adjustments to their marketing strategies.

FIG. 1.6

Factors Influencing Company Marketing Strategy

MARKETING PLANNING In practice, there is a logical process that marketing follows. The marketing planning process consists of analyzing marketing opportunities; selecting target markets; designing marketing strategies; developing marketing programs; and managing the marketing effort. Figure 1.6 presents a grand summary of the marketing process and the forces shaping the company's marketing strategy.

Shifts in Marketing Management

A number of important trends and forces are eliciting a new set of beliefs and practices on the part of business firms. Marketers are fundamentally rethinking their philosophies, concepts, and tools. Here are 14 major shifts in marketing management that smart companies have been making in the twenty-first century. These major themes will be examined throughout this book to help marketers and companies sail safely through the rough but promising waters ahead. Successful companies will be those who can keep their marketing changing with the changes in their marketplace—and marketspace.

FROM MARKETING DOES THE MARKETING TO EVERYONE DOES THE MARKETING Companies generally establish a marketing department to be responsible for creating and delivering customer value. But as the late David Packard of Hewlett-Packard observed, "Marketing is far too important to leave to the marketing department." Companies now know that marketing is not done only by marketing, sales, and customer support personnel; every employee has an impact on the customer and must see the customer as the source of the company's prosperity. Consequently, companies are beginning to emphasize interdepartmental teamwork to manage key processes. More emphasis is also being placed on the smooth management of core business processes, such as new-product realization, customer acquisition and retention, and order fulfillment.

FROM ORGANIZING BY PRODUCT UNITS TO ORGANIZING BY CUSTOMER SEGMENTS Some companies are now switching from being solely product-centered with product managers and product divisions to manage them to being more customer-segment-centered. In late 1999, Royal Bank of Canada reorganized itself around customer segments, not products or territories. By studying these segments carefully, Royal Bank developed a number of new profit-generating products and services such as first mortgages and estate settlements. As a result, revenues increased by $1 billion over the next three years and the stock price rose 100 percent in the midst of a stagnant bear market.[34]

FROM MAKING EVERYTHING TO BUYING MORE GOODS AND SERVICES FROM OUTSIDE More companies are choosing to own brands rather than physical assets. Companies are also increasingly subcontracting activities to outsourcing firms. Their maxim: Outsource those activities that others can do more cheaply and better, but retain core activities.

FROM USING MANY SUPPLIERS TO WORKING WITH FEWER SUPPLIERS IN A "PARTNERSHIP" Companies are deepening partnering arrangements with key suppliers and distributors. Such companies have shifted from thinking of intermediaries as customers to treating them as partners in delivering value to final customers.

FROM RELYING ON OLD MARKET POSITIONS TO UNCOVERING NEW ONES In highly competitive marketplaces, companies must always be moving forward with marketing programs, innovating products and services, and staying in touch with customer needs. Companies must always be seeking new advantages rather than just relying on their past strengths.

FROM EMPHASIZING TANGIBLE ASSETS TO EMPHASIZING INTANGIBLE ASSETS Companies are recognizing that much of their market value comes from intangible assets, particularly their brands, customer base, employees, distributor and supplier relations, and intellectual capital.

FROM BUILDING BRANDS THROUGH ADVERTISING TO BUILDING BRANDS *THROUGH PERFORMANCE AND INTEGRATED COMMUNICATIONS* Marketers are moving from an overreliance on one communication tool such as advertising or sales force to blending several tools to deliver a consistent brand image to customers at every brand contact.

FROM ATTRACTING CUSTOMERS THROUGH STORES AND SALESPEOPLE TO MAKING PRODUCTS AVAILABLE ONLINE Consumers can access pictures of products, read the specs, shop among online vendors for the best prices and terms, and click to order and pay. Business-to-business purchasing is growing fast on the Internet. Personal selling can increasingly be conducted electronically, with buyer and seller seeing each other on their computer screens in real time.

FROM SELLING TO EVERYONE TO TRYING TO BE THE BEST FIRM SERVING WELL-DEFINED TARGET MARKETS Target marketing is being facilitated by the proliferation of special-interest magazines, TV channels, and Internet newsgroups. Companies are also making substantial investments in information systems as the key to lowering costs and gaining a competitive edge. They are assembling information about individual customers' purchases, preferences, demographics, and profitability.

FROM FOCUSING ON PROFITABLE TRANSACTIONS TO FOCUSING ON CUSTOMER LIFETIME VALUE Companies normally would aim to make a profit on each transaction. Now companies are focusing on their most profitable customers, products, and channels. They estimate individual customer lifetime value and design market offerings and prices to make a profit over the customer's lifetime. Companies now are placing much more emphasis on customer retention. Attracting a new customer may cost five times as much as doing a good job to retain existing customers.

FROM A FOCUS ON GAINING MARKET SHARE TO A FOCUS ON BUILDING CUSTOMER SHARE A bank aims to increase its share of the customer's wallet; the supermarket aims to capture a larger share of the customer's "stomach." Companies build customer share by offering a larger variety of goods to existing customers. They train their employees in cross-selling and up-selling.

FROM BEING LOCAL TO BEING "GLOCAL"—BOTH GLOBAL AND LOCAL Firms are adopting a combination of centralization and decentralization to better balance local adaptation and global standardization. The goal is to encourage more initiative and "intrepreneurship" at the local level, while preserving the necessary global guidelines and standards.[35]

FROM FOCUSING ON THE FINANCIAL SCORECARD TO FOCUSING ON THE MARKETING SCORECARD Top management is going beyond sales revenue alone to examine the marketing scorecard to interpret what is happening to market share, customer loss rate, customer satisfaction, product quality, and other measures. They know that changes in marketing indicators predict changes in financial results.

FROM FOCUSING ON SHAREHOLDERS TO FOCUSING ON STAKEHOLDERS Top management respects the importance of creating co-prosperity among all business partners and customers. These managers develop policies and strategies to balance the returns to all the key stakeholders.

Marketing Management Tasks

These core concepts and others provide the input for a set of tasks that make up successful marketing management. We'll use the following situation to illustrate these tasks in the context of the plan of the book.

> Zeus, Inc. (name disguised), operates in several industries, including chemicals, cameras, and film. The company is organized into SBUs. Corporate management is considering what to do with its Atlas camera division. At present, Atlas produces a range of 35 mm and digital cameras. The market for cameras is intensely competitive. Although Zeus has a sizable market share and is producing much revenue for the company, the 35 mm market itself is growing very slowly and its market share is slipping. In the faster-growing digital camera segment, Zeus is facing strong competition and has been slow to gain sales. Zeus's corporate management wants Atlas's marketing group to produce a strong turnaround plan for the division. Marketing management has to come up with a convincing marketing plan, sell corporate management on the plan, and then implement and control it.

DEVELOPING MARKETING STRATEGIES AND PLANS The first task facing Atlas is to identify its potential long-run opportunities given its market experience and core competencies (see Chapter 2). Atlas can design its cameras with better features. It can also consider making a line of video cameras, or it can use its core competency in optics to design a line of binoculars and telescopes. Whichever direction it chooses, it must develop concrete marketing plans that specify the marketing strategy and tactics going forward.

CAPTURING MARKETING INSIGHTS To understand what is happening inside and outside the company, Atlas needs a reliable marketing information system; it will want to closely monitor its marketing environment. Atlas's microenvironment consists of all the players who affect the company's ability to produce and sell cameras—suppliers, marketing intermediaries, customers, and competitors. Its macroenvironment consists of demographic, economic, physical, technological, political-legal, and social-cultural forces that affect sales and profits (see Chapter 3).

Atlas also needs a dependable marketing research system. Marketing research is an indispensable tool for assessing buyer wants and behavior and actual and potential market size. An important part of gathering environmental information includes measuring market potential and forecasting future demand. To transform marketing strategy into marketing programs, marketing managers must make basic decisions on marketing expenditures, marketing activities, and marketing allocation.[36] How many dollars should support Atlas's two or three camera lines? Direct versus distributor sales? Direct-mail advertising versus trade-magazine advertising? East Coast markets versus West Coast markets? To make these allocations, marketing managers may use sales-response functions that show how sales and profits would be affected by the amount of money spent in each application (see Chapter 4).

CONNECTING WITH CUSTOMERS Atlas must consider how to best create value for its chosen target markets and develop strong, profitable, long-term relationships with customers (see Chapter 5). To do so, Atlas needs to understand consumer markets (see Chapter 6). How many households plan to buy cameras? Who buys and why do they buy? What are they looking for in the way of features and prices? Where do they shop? What are their images of different brands? How does the digital segment differ from the 35 mm segment? Atlas also sells cameras to business markets, including large corporations, professional firms, retailers, and government agencies (see Chapter 7). Purchasing agents or buying committees make the decisions. Atlas needs to gain a full understanding of how organizational buyers buy. It needs a sales force that is well trained in presenting product benefits.

Atlas will not want to market to all possible customers. Modern marketing practice calls for dividing the market into major market segments, evaluating each segment, and targeting those market segments that the company can best serve (see Chapter 8).

BUILDING STRONG BRANDS Atlas must understand the strengths and weaknesses of the Zeus brand with customers (see Chapter 9). Is it so strongly associated with certain technologies that it could not be used to brand new products in related categories? Is its 35 mm film heritage a detriment in the digital camera market? Suppose Atlas decides to focus on the consumer market and develop a positioning strategy (see Chapter 10). Should Atlas position its cameras as the "Cadillac" brand, offering superior cameras at a premium price with excellent service and strong advertising? Should it build a simple, low-priced camera aimed at more price-conscious consumers? Should it develop a medium-quality, medium-priced camera? After launch the product's strategy will need modification at the different stages in the product life cycle: introduction, growth, maturity, and decline. Furthermore, strategy choice will depend on whether the firm is a market leader, challenger, follower, or nicher. Atlas must also pay close attention to competitors (see Chapter 11), anticipating its competitors' moves and knowing how to react quickly and decisively. It may want to initiate some surprise moves, in which case it needs to anticipate how its competitors will respond.

SHAPING THE MARKET OFFERINGS At the heart of the marketing program is the product—the firm's tangible offering to the market, which includes the product quality, design, features, and packaging (see Chapter 12). As part of its product offering, Atlas may provide various services, such as leasing, delivery, repair, and training (see Chapter 13). Such support services can provide a competitive advantage in the global marketplace.

A critical marketing decision relates to price (see Chapter 14). Atlas has to decide on wholesale and retail prices, discounts, allowances, and credit terms. Its price should be commensurate with the offer's perceived value; otherwise, buyers will turn to competitors' products.

DELIVERING VALUE Atlas must also determine how to properly deliver the value embodied by these products and services to the target market. Channel activities include the various activities the company undertakes to make the product accessible and available to target customers (see Chapter 15). Atlas must identify, recruit, and link various marketing facilitators to supply its products and services efficiently to the target market. It must understand the various types of retailers, wholesalers, and physical-distribution firms and how they make their decisions (see Chapter 16).

COMMUNICATING VALUE Atlas must also adequately communicate the value embodied by its products and services to the target market. Marketing communications activities are the means by which firms attempt to inform, persuade, and remind consumers—directly or indirectly—about the brands they sell. Atlas has to develop an integrated marketing communication program that maximizes the individual and collective contribution of all communication activities (see Chapter 17). Atlas has to set up mass communication programs consisting of advertising, sales promotion, events, and public relations (see Chapter 18). It also has to set up more personal communications in the form of direct and interactive marketing and must also hire, train, and motivate salespeople (see Chapter 19).

CREATING LONG-TERM GROWTH Atlas must also take a long-term view of its products and brands and how its profits should be grown. Based on its product positioning, it must initiate new-product development, testing, and launching (see Chapter 20). The strategy also will have to take into account changing global opportunities and challenges (see Chapter 21).

Finally, Atlas must organize its marketing resources and implement and control the marketing plan. The company must build a marketing organization that is capable of implementing the marketing plan (see Chapter 22). Because of surprises and disappointments that can occur as marketing plans are implemented, Atlas will need feedback and control.[37] Marketing evaluation and control processes are necessary to understand the efficiency and effectiveness of marketing activities and how both could be improved.

SUMMARY :::

1. From a managerial point of view, marketing is the process of planning and executing the conception, pricing, promotion, and distribution of ideas, goods, and services to create exchanges that satisfy individual and organizational goals. Marketing management is the art and science of choosing target markets and getting, keeping, and growing customers through creating, delivering, and communicating superior customer value.
2. Marketers are skilled at managing demand: They seek to influence the level, timing, and composition of demand. Marketers are involved in marketing many types of entities: goods, services, events, experiences, persons, places, properties, organizations, information, and ideas. They also operate in four different marketplaces: consumer, business, global, and nonprofit.
3. Businesses today face a number of challenges and opportunities, including globalization, the effects of advances in technology, and deregulation. They have responded by changing the way they conduct marketing in very fundamental ways.
4. There are five competing concepts under which organizations can choose to conduct their business: the production concept, the product concept, the selling concept, the marketing concept, and the holistic marketing concept. The first three are of limited use today.
5. The holistic marketing concept is based on the development, design, and implementation of marketing programs, processes, and activities that recognize their breadth and interdependencies. Holistic marketing recognizes that "everything matters" with marketing and that a broad, integrated perspective is often necessary. Four components of holistic marketing are relationship marketing, integrated marketing, internal marketing, and socially responsible marketing.
6. Marketing management has experienced a number of shifts in recent years as companies seek marketing excellence.
7. The set of tasks necessary for successful marketing management includes developing marketing strategies and plans, connecting with customers, building strong brands, shaping the market offerings, delivering and communicating value, capturing marketing insights and performance, and creating successful long-term growth.

APPLICATIONS :::

Marketing Debate Does Marketing Create or Satisfy Needs?

Marketing has often been defined in terms of satisfying customers' needs and wants. Critics, however, maintain that marketing goes beyond that and creates needs and wants that did not exist before. According to these critics, marketers encourage consumers to spend more money than they should on goods and services they really do not need.

Take a position: Marketing shapes consumer needs and wants versus Marketing merely reflects the needs and wants of consumers.

Marketing Discussion

Consider the broad shifts in marketing. Are there any themes that emerge in these shifts? Can they be related to the major societal forces? Which force has contributed to which shift?

MARKETING **SPOTLIGHT** COCA-COLA

Coca-Cola is the most ubiquitous brand in history. Each day, people in 200 countries around the world drink some 1.2 billion 8-ounce servings of the cola.

Marketing for the twenty-first century means leveraging the longtime marketing principles that work, while inventing new ways to stay relevant. Coca-Cola, which got its start in 1883, has successfully kept its brand relevant for over 100 years. Revenues in 2003 topped $21 billion.

Coke's first president, Asa Candler, instituted many of the marketing tactics that are entrenched principles now. To gain new customers, he printed coupons offering free first tastes of the Coca-Cola drink. To build brand recognition, he gave clocks, calendars, and weighing scales with the Coca-Cola logo to pharmacists who sold the drink. He hired the company's first celebrity, music hall performer Hilda Clark, in the 1890s.

During the heyday of mass-market TV advertising, Coke was the master of the 30-second TV spot. Its legendary "I'd like to buy the world a Coke" and "Mean Joe Greene" ads were rated as two of the best ads ever by *Advertising Age*.

Coca-Cola also expanded overseas. During World War II, when the army shipped Cokes to soldiers in Europe and Asia, Coke cemented its image as the "All-American beverage." But over time, Coke realized it would need a more local feel in each country. So, although it uses its signature red-and-white wave and lettering worldwide, the company uses different ad agencies in different countries in order to make the brand feel local. For example, the local versions of the "Mean Joe Greene" ad used sports figures famous in those regions, such as soccer stars. Similarly, ads for Coca-Cola in Spain show it as a mixer with wine, reflecting how consumers use the product in that country.

Coke also sells a wide range of different-flavored sodas in different countries. Visitors to the company's museum in Atlanta can try these beverages—everything from cool watermelon (China), to an intensely bitter herbal soda (Italy), to a zingy ginger soda (South Africa). In 2004, Coke launched a beer-flavored carbonated beverage in Japan.

Coca-Cola now gets two-thirds of its revenues from outside the United States. It's easier to name the countries where Coke is not: Myanmar, Cuba, and Syria. Everywhere else—including such tricky markets as Pakistan, Cambodia, Liberia, Zimbabwe, and Colombia—Coke is a beloved consumer staple. In fact, the brand is so strong and so entrenched that even the anti-American sentiments of 9/11 and after have not hurt sales. Coca-Cola's brand valuation actually increased from $68.95 billion in August 2001 to $70.45 billion in August 2003. (By comparison, rival Pepsi-Cola's brand value is a mere $11.78 billion.) Coca-Cola remains the top global brand, achieving the top ranking in *BusinessWeek*'s Global Brand Scorecard once again in 2003.

Despite its powerhouse status, Coke must continue to evolve its marketing. For example, the effectiveness of TV ads is declining due to media fragmentation and use of devices like TiVO that let viewers zap commercials. Ads that reached 70 percent of Americans during prime time in the 1960s only reached 15 percent in 2004. So Coke is diverting money previously spent on TV toward more experiential activities. For example, it's testing Coke Red Lounge gathering areas for teens in malls. The lounges offer exclusive music videos and video games and sell Coke drinks from a see-through Coke machine. In Britain, Coke's mycokemusic.com Web site lets surfers legally download over 250,000 songs.

Chris Lowe, a Coke marketing executive, explained how the company stays on top: "You can never betray the core values of the brand, but you can work to make those values fresh and relevant. If you can't speak to people in these times, then you become an old icon." Lowe described the iterative steps of generating a fresh ad campaign: "There's the communication strategy that you want to put across. You test it with consumers for validity and resonance. Then you take that core meaning and make it come alive with advertising. Then you take it back to consumers to test it again."

The results of Coke's latest marketing shift aren't known yet, but in 2003 its then Chairman, Douglas Daft, told investors that Coca-Cola Company has "arguably the strongest and most pervasive marketing and distribution system in the world." And with Coke being the first soda drunk in outer space, even the sky may not be the limit.

Discussion Questions

1. What have been the key success factors for Coca-Cola?
2. Where is Coca-Cola vulnerable? What should they watch out for?
3. What recommendations would you make to their senior marketing executives going forward? What should they be sure to do with their marketing?

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IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. How does marketing affect customer value?
2. How is strategic planning carried out at different levels of the organization?
3. What does a marketing plan include?

CHAPTER 2 ::: DEVELOPING MARKETING STRATEGIES AND PLANS

A key ingredient of the marketing management process is insightful, creative marketing strategies and plans that can guide marketing activities. Developing the right marketing strategy over time requires a blend of discipline and flexibility. Firms must stick to a strategy but must also find new ways to constantly improve it.[1] Marketing strategy also requires a clear understanding of how marketing works.[2]

Walk into a trendy Soho boutique in New York City and you might see high-fashion T-shirts selling for $250. Go into an H&M clothing store and you can see a version of the same style for $25. Founded 55 years ago as a provincial Swedish clothing company, H&M (Hennes and Mauritz) has morphed into a clothing colossus with 950 stores in 19 countries and an ambitious plan to expand by 100 stores a year. The reason H&M has reached this point while so many other stores—such as once-hot Italian retailer Benetton—have floundered is that the company has a clear mission and the creative marketing strategies and concrete plans with which to carry it out. "Our business concept is to give the customer unbeatable value by offering fashion and quality at the best price," is the H&M mission as expressed on the company's Web site. Nothing could sound simpler. Yet, fulfilling that mission requires a well-coordinated set of marketing activities. For instance, it takes H&M an average of three months to go from a designer's idea to a product on a store shelf, and that "time to market" falls >>>

An H&M store in Brussels, Belgium.

to three weeks for "high-fashion" products. H&M is able to put products out quickly and inexpensively by:

- *having few middlemen and owning no factories*
- *buying large volumes*
- *having extensive experience in the clothing industry*
- *having a great knowledge of which goods should be bought from which markets*
- *having efficient distribution systems*
- *being cost-conscious at every stage*

This chapter begins by examining some of the strategic marketing implications involved in creating customer value. It then provides several perspectives on planning and describes how to draw up a formal marketing plan.

::: Marketing and Customer Value

Marketing involves satisfying consumers' needs and wants. The task of any business is to deliver customer value at a profit. In a hypercompetitive economy with increasingly rational buyers faced with abundant choices, a company can win only by fine-tuning the value delivery process and choosing, providing, and communicating superior value.

The Value Delivery Process

The traditional view of marketing is that the firm makes something and then sells it (Figure 2.1[a]). In this view, marketing takes place in the second half of the process. The company knows what to make and the market will buy enough units to produce profits. Companies that subscribe to this view have the best chance of succeeding in economies marked by

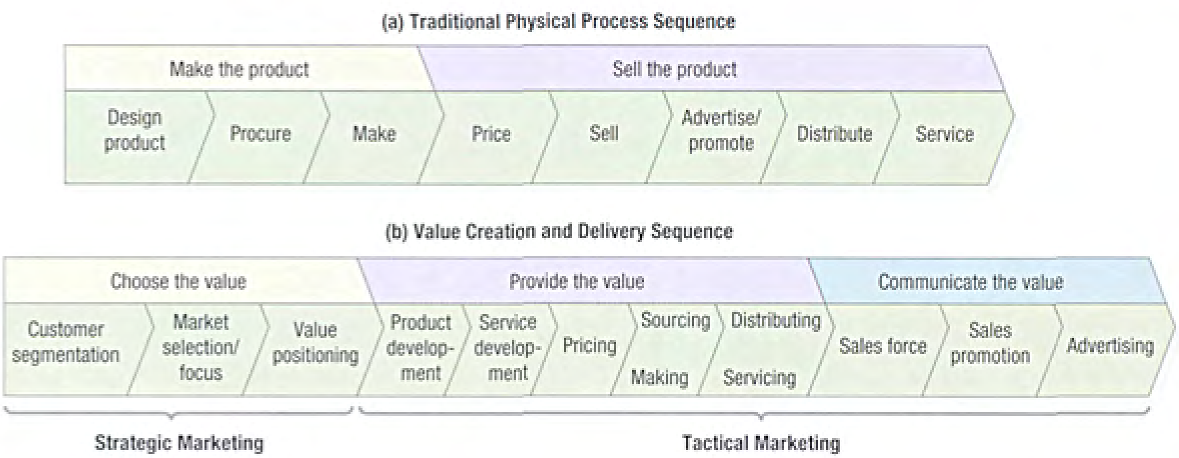


FIG. 2.1 Two Views of the Value Delivery Process

Source: Michael J. Lanning and Edward G. Michaels, "A Business Is a Value Delivery System," McKinsey Staff Paper no. 41, June 1988. Copyright © McKinsey & Co., Inc.

goods shortages where consumers are not fussy about quality, features, or style—for example, with basic staple goods in developing markets.

The traditional view of the business process, however, will not work in economies where people face abundant choices. There, the "mass market" is actually splintering into numerous micromarkets, each with its own wants, perceptions, preferences, and buying criteria. The smart competitor must design and deliver offerings for well-defined target markets. This belief is at the core of the new view of business processes, which places marketing at the beginning of planning. You can see this in action at your local mall. In the struggle to grow, retail chains are creating spinoffs that appeal to ever-smaller micromarkets:

SPINOFFS

Gymboree, a 530-store chain, sells children's clothing to upscale parents. Since there are not enough parents making more than $65,000 per year to support even more stores, Gymboree has created Janie and Jack, a chain selling upscale baby gifts. Hot Topic, a chain that sells rock-band-inspired clothes for teens, recently launched Torrid to give plus-size teens the same fashion options. Women's clothing store Ann Taylor spawned Ann Taylor Loft, with lower-priced fashions, and Chico's, a chain aimed at women in their forties and fifties, begat Pazo, for slightly younger working women.[3]

Instead of emphasizing making and selling, these companies see themselves as part of a value delivery process.

Figure 2.1(b) illustrates the value creation and delivery sequence. The process consists of three parts. The first phase, *choosing the value*, represents the "homework" marketing must do before any product exists. The marketing staff must segment the market, select the appropriate market target, and develop the offering's value positioning. The formula "segmentation, targeting, positioning (STP)" is the essence of strategic marketing. Once the business unit has chosen the value, the second phase is *providing the value*. Marketing must determine specific product features, prices, and distribution. The task in the third phase is *communicating the value* by utilizing the sales force, sales promotion, advertising, and other communication tools to announce and promote the product. Each of these value phases has cost implications.

NIKE

Critics of Nike often complain that its shoes cost almost nothing to make yet cost the consumer so much. True, the raw materials and manufacturing costs involved in the making of a sneaker are relatively cheap, but marketing the product to the consumer is expensive. Materials, labor, shipping, equipment, import duties, and suppliers' costs generally total less than $25 a pair. Compensating its sales team, its distributors, its administration, and its endorsers, as well as paying for advertising and R&D, adds $15 or so to the total. Nike sells its product to retailers to make a profit of $7. The retailer therefore pays roughly $47 to put a pair of Nikes on the shelf. When the retailer's overhead (typically $30 covering personnel, lease, and equipment) is factored in along with a $10 profit, the shoe costs the consumer over $80.

A pair of Nike shoes.

As Figure 2.1(b) shows, the value delivery process begins before there is a product and continues while it is being developed and after it becomes available. The Japanese have further refined this view with the following concepts:

- ***Zero customer feedback time.*** Customer feedback should be collected continuously after purchase to learn how to improve the product and its marketing.
- ***Zero product improvement time.*** The company should evaluate all improvement ideas and introduce the most valued and feasible improvements as soon as possible.
- ***Zero purchasing time.*** The company should receive the required parts and supplies continuously through just-in-time arrangements with suppliers. By lowering its inventories, the company can reduce its costs.
- ***Zero setup time.*** The company should be able to manufacture any of its products as soon as they are ordered, without facing high setup time or costs.
- ***Zero defects.*** The products should be of high quality and free of flaws.

Nirmalya Kumar has put forth a "3 Vs" approach to marketing: (1) define the *value segment* or customers (and his/her needs); (2) define the *value proposition;* and (3) define the *value network* that will deliver the promised service.[4] Dartmouth's Frederick Webster views marketing in terms of: (1) *value defining processes* (e.g., market research and company self-analysis), (2) *value developing processes* (e.g., new-product development, sourcing strategy, and vendor selection), and (3) *value delivering processes* (e.g., advertising and managing distribution).[5]

The Value Chain

Michael Porter of Harvard has proposed the **value chain** as a tool for identifying ways to create more customer value (see Figure 2.2).[6] According to this model, every firm is a synthesis of activities performed to design, produce, market, deliver, and support its product. The value chain identifies nine strategically relevant activities that create value and cost in a specific business. These nine value-creating activities consist of five primary activities and four support activities.

The *primary activities* cover the sequence of bringing materials into the business inbound logistics), converting them into final products (operations), shipping out final products (outbound logistics), marketing them (marketing and sales), and servicing them (service). The *support activities*—procurement, technology development, human resource management, and firm infrastructure—are handled in certain specialized departments, as well as elsewhere. Several departments, for example, may do procurement and hiring. The firm's infrastructure covers the costs of general management, planning, finance, accounting, legal, and government affairs.

The firm's task is to examine its costs and performance in each value-creating activity and to look for ways to improve it. The firm should estimate its competitors' costs and performances as *benchmarks* against which to compare its own costs and performance. It should go further and study the "best of class" practices of the world's best companies.[7]

The firm's success depends not only on how well each department performs its work, but also on how well the various departmental activities are coordinated to conduct *core business processes.*[8] These core business processes include:

- ***The market sensing process.*** All the activities involved in gathering market intelligence, disseminating it within the organization, and acting on the information.
- ***The new offering realization process.*** All the activities involved in researching, developing, and launching new high-quality offerings quickly and within budget.
- ***The customer acquisition process.*** All the activities involved in defining target markets and prospecting for new customers.
- ***The customer relationship management process.*** All the activities involved in building deeper understanding, relationships, and offerings to individual customers.
- ***The fulfillment management process.*** All the activities involved in receiving and approving orders, shipping the goods on time, and collecting payment.

Strong companies develop superior capabilities in managing and linking their core business processes. For example, Wal-Mart has superior strength in its stock replenishment process. As Wal-Mart stores sell their goods, sales information flows via computer not only to Wal-Mart's headquarters, but also to Wal-Mart's suppliers, who ship replacement mer-

FIG. 2.2

The Generic Value Chain

Source: Reprinted with the permission of The Free Press, an imprint of Simon & Schuster, from Michael E. Porter, *Competitive Advantage: Creating and Sustaining Superior Performance.* Copyright 1985 by Michael E. Porter.

chandise to the stores almost at the rate it moves off the shelf.[9] The idea is to manage flows of goods, not stocks of goods. Wal-Mart has turned over this responsibility to its leading vendors in a system known as vendor-managed inventories VMI).

Strong companies are also reengineering the work flows and building cross-functional teams responsible for each process.[10] At Xerox, a Customer Operations Group links sales, shipping, installation, service, and billing so that these activities flow smoothly into one another. Winning companies are those that excel at managing core business processes through cross-functional teams. AT&T, Polaroid, and Motorola have reorganized their employees into cross-functional teams; cross-functional teams are also found in nonprofit and government organizations as well. Drug store chain Rite Aid is using cross-functional teams to try to push its store from third to first place in the drug store hierarchy. The company has created teams to focus on sales and margin growth, operational excellence, market optimization, continued supply chain improvements, and continued cost control.[11]

To be successful, a firm also needs to look for competitive advantages beyond its own operations, into the value chains of suppliers, distributors, and customers. Many companies today have partnered with specific suppliers and distributors to create a superior **value delivery network** also called a **supply chain.**[12]

BAILEY CONTROLS

An Ohio-headquartered, $300-million-a-year manufacturer of control systems for big factories, Bailey Controls treats some of its suppliers as if they were departments within Bailey. The company recently plugged two of its suppliers directly into its inventory management system. Every week Bailey electronically sends Montreal-based Future Electronics its latest forecasts of the materials it will need for the next six months. Whenever a bin of parts falls below a designated level, a Bailey employee passes a laser scanner over the bin's bar code, alerting Future to send the parts at once. Although arrangements like this shift inventory costs to the suppliers, the suppliers expect those costs to be more than offset by the gain in volume. It is a win–win partnership.

Core Competencies

To carry out its core business processes, a company needs resources—labor power, materials, machines, information, and energy. Traditionally, companies owned and controlled most of the resources that entered their businesses, but this situation is changing. Many companies today outsource less critical resources if they can be obtained at better quality or lower cost. Frequently, outsourced resources include cleaning services, landscaping, and auto fleet management. Kodak even turned over the management of its data processing department to IBM.

The key, then, is to own and nurture the resources and competencies that make up the essence of the business. Nike, for example, does not manufacture its own shoes, because certain Asian manufacturers are more competent in this task; Nike nurtures its superiority in shoe design and shoe merchandising, its two core competencies. We can say that a **core competency** has three characteristics: (1) It is a source of competitive advantage in that it makes a significant contribution to perceived customer benefits, (2) it has applications in a wide variety of markets, and (3) it is difficult for competitors to imitate.[13]

Competitive advantage also accrues to companies that possess distinctive capabilities. Whereas core competencies tend to refer to areas of special technical and production expertise, *distinctive capabilities* tend to describe excellence in broader business processes. Consider Netflix, the pioneer online DVD rental service, based in Silicon Valley.[14]

NETFLIX

Back in 1997, while most people were still fumbling with programming their VCRs, Netflix founder Reed Hastings became convinced that DVDs were the home video medium of the future. He raised $120 million, attracted hundreds of thousands of customers, and took the company public in 2002, gaining another $90 million. Netflix has distinctive capabilities that promise to keep the company on top even as competitors like Blockbuster and Wal-Mart try to muscle in on its turf. One of the company's investors says that Netflix is really a sophisticated software company masquerading as a DVD rental service. The company has fine-tuned its file recommendation software, merchandising, and inventory control system to such a degree that new orders are automatically generated even as the old orders are returned. In addition, all 12 of the company's DVD distribution centers can be polled before a customer is told that the movie he or she wants next is out of stock.

George Day sees market-driven organizations as excelling in three distinctive capabilities: market sensing, customer linking, and channel bonding.[15]

Competitive advantage ultimately derives from how well the company has fitted its core competencies and distinctive capabilities into tightly interlocking "activity systems." Competitors find it hard to imitate companies such as Southwest Airlines, Dell, or IKEA because they are unable to copy their activity systems.

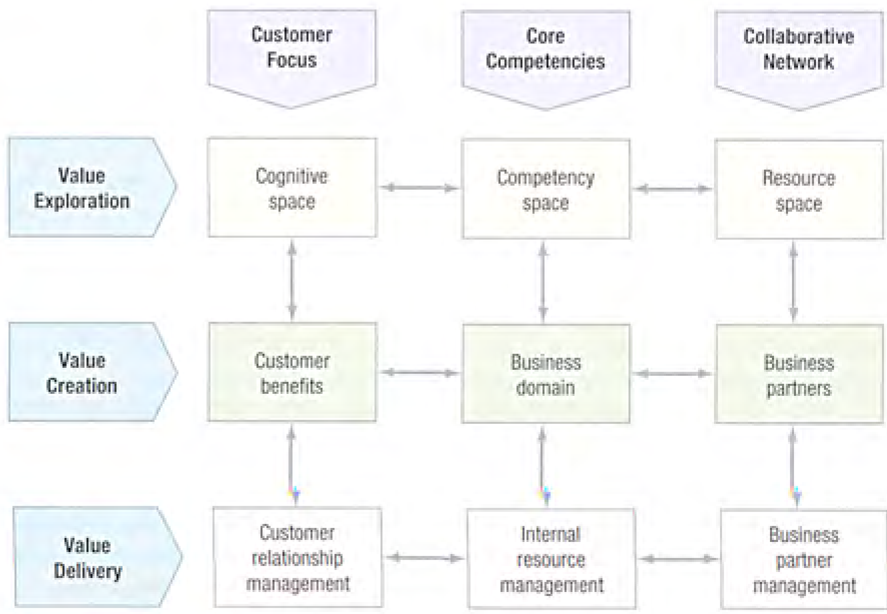
A Holistic Marketing Orientation and Customer Value

A holistic marketing orientation can also provide insight into the process of capturing customer value. One conception of holistic marketing views it as "integrating the value exploration, value creation, and value delivery activities with the purpose of building long-term, mutually satisfying relationships and co-prosperity among key stakeholders."[16] According to this view, holistic marketers succeed by managing a superior value chain that delivers a high level of product quality, service, and speed. Holistic marketers achieve profitable growth by expanding customer share, building customer loyalty, and capturing customer lifetime value. Figure 2.3, a holistic marketing framework, shows how the interaction between relevant actors (customers, company, and collaborators) and value-based activities (value exploration, value creation, and value delivery) helps to create, maintain, and renew customer value.

FIG. 2.3

A Holistic Marketing Framework

Source: P. Kotler, D. C. Jain, and S. Maesincee, "Formulating a Market Renewal Strategy," in *Marketing Moves* (Part 1), Fig. 1-1 (Boston: Harvard Business School Press, 2002), p. 29.



The holistic marketing framework is designed to address three key management questions:

1. ***Value exploration*** – How can a company identify new value opportunities?
2. ***Value creation*** – How can a company efficiently create more promising new value offerings?
3. ***Value delivery*** – How can a company use its capabilities and infrastructure to deliver the new value offerings more efficiently?

VALUE EXPLORATION Because value flows within and across markets that are themselves dynamic and competitive, companies need a well-defined strategy for value exploration. Developing such a strategy requires an understanding of the relationships and interactions among three spaces: (1) the customer's cognitive space; (2) the company's competence space; and (3) the collaborator's resource space. The customer's *cognitive space* reflects existing and latent needs and includes dimensions such as the need for participation, stability, freedom, and change.[17] The company's *competency space* can be described in terms of breadth—broad versus focused scope of business; and depth—physical versus knowledge-based capabilities. The collaborator's *resource space* involves horizontal partnerships, where companies choose partners based on their ability to exploit related market opportunities, and vertical partnerships, where companies choose partners based on their ability to serve their value creation.

VALUE CREATION To exploit a value opportunity, the company needs value-creation skills. Marketers need to: identify new customer benefits from the customer's view; utilize core competencies from its business domain; and select and manage business partners from its collaborative networks. To craft new customer benefits, marketers must understand what the customer thinks about, wants, does, and worries about. Marketers must also observe who customers admire, who they interact with, and who influences them.

Business realignment may be necessary to maximize core competencies. It involves three steps: (1) (re)defining the business concept (the "big idea"); (2) (re)shaping the business scope (the lines of business); and (3) (re)positioning the company's brand identity (how customers should see the company). This is what Kodak is doing as sales from its traditional core businesses of film, camera, paper, and photo development have sagged, and consumers have abandoned film cameras for increasingly cheaper digital equipment, products, and services. On September 25, 2003, Chairman and Chief Executive Daniel A. Carp stood in front of shareholders and unveiled the company's new strategy. He announced that Kodak was "determined to win in these new digital markets." In order to do that the company plans to expand its line of digital cameras, printers, and other equipment for consumers, who are now using the Internet to transmit and display their digital images. Kodak also is stepping up efforts to deliver on-demand, color printing products for business and wants to increase its market share of the lucrative medical images and information services businesses.[18]

VALUE DELIVERY Delivering value often means substantial investment in infrastructure and capabilities. The company must become proficient at customer relationship management, internal resource management, and business partnership management. *Customer relationship management* allows the company to discover who its customers are, how they behave, and what they need or want. It also enables the company to respond appropriately, coherently, and quickly to different customer opportunities. To respond effectively, the company requires *internal resource management* to integrate major business processes (e.g., order processing, general ledger, payroll, and production) within a single family of software modules. Finally, *business partnership management* allows the company to handle complex relationships with its trading partners to source, process, and deliver products.

The Central Role of Strategic Planning

Successful marketing thus requires companies to have capabilities such as understanding customer value, creating customer value, delivering customer value, capturing customer value, and sustaining customer value. "Marketing Insight: Views on Marketing from Chief Executive Officers" addresses some important senior management priorities in improving marketing. Only a handful of companies stand out as master marketers: Procter & Gamble, Southwest Airlines, Nike, Disney, Nordstrom, Wal-Mart, McDonald's, Marriott Hotels, and several Japanese (Sony, Toyota, Canon) and European (IKEA, Club Med, Bang & Olufsen,

MARKETING INSIGHT | VIEWS ON MARKETING FROM CHIEF EXECUTIVE OFFICERS

Marketing faces a number of challenges in the twenty-first century. Based on an extensive 2002 research study, McKinsey identified three main challenges as reflected by differences in opinion between chief executive officers (CEOs) and their most senior marketing executives or chief marketing officers (CMOs).

- ***Doing more with less.*** CEOs need and expect all areas of their organizations to be more efficient; CMOs indicate that they anticipate that their budgets will grow.
- ***Driving new business development.*** CEOs want marketing to play a more active role in driving new business development—not just new products but also new markets, channels, lines of business; CMOs cited new-product development as their primary concern.
- ***Becoming a full business partner.*** CEOs look for marketing to become a more central business partner that helps to drive profits; CMOs are unsure that their groups have the skills to do so.

McKinsey suggests that bridging these gaps will require changes in spending, organization skills, and culture for many marketers. To accommodate the pressure to simultaneously grow revenues while also reducing marketing costs as a percentage of sales, they offer three recommendations:

1. Link spending priorities to profit potential, for example, as measured by size and anticipated growth rate of current customers—not historical performance;
2. Focus spending on brand drivers (features and benefits truly important to customers), not antes (features and benefits that a brand needs to stay in the game); and
3. Deepen insights on how customers get product information and make buying decisions.

Based on research on companies that successfully develop big ideas, McKinsey identifies three characteristics that help to position marketers as business development leaders:

1. Force the widest view when defining their business, assets, and competencies;
2. Combine multiple perspectives, for example, using attitudinal and need profiles as well as behavior-based segments—to identify market opportunities or sweet spots; and
3. Focus idea generation through a combination of marketing insight and business analysis—but identify profitable unmet needs before they brainstorm creative solutions.

Finally, McKinsey offers two recommendations to overcome CEOs' concerns about the role and performance of marketing.

1. Marketers must test and develop programs more quickly as they enhance planning processes and research approaches; and
2. Marketers must more effectively evaluate the performance and profit impact of investments in the expanding marketing arena (e.g., CRM technology, sponsorships, Internet marketing, and word of mouth).

Source: David Court, Tom French, and Gary Singer, "How the CEO Sees Marketing," *Advertising Age*, March 3, 2003, p. 28.

Electrolux, Nokia, Lego, Tesco) companies. These companies focus on the customer and are organized to respond effectively to changing customer needs. They all have well-staffed marketing departments, and all their other departments—manufacturing, finance, research and development, personnel, purchasing—also accept the concept that the customer is king. (See "Marketing Insight: Keys to Long-Term Market Leadership.")

Creating, providing, and communicating value requires many different marketing activities. To ensure that the proper activities are selected and executed, strategic planning is paramount. Strategic planning calls for action in three key areas: The first is managing a company's businesses as an investment portfolio. The second involves assessing each business's strength by considering the market's growth rate and the company's position and fit in that market. The third is establishing a strategy. For each business, the company must develop a game plan for achieving its long-run objectives.

Marketing plays a critical role in this process. At Samsung Electronics America, strategic marketing could be considered a religion. When Samsung executives, engineers, marketers, and designers consider new products, they must answer one central question: "Is it wow?" If "wow" is the company mantra, then the high priest of "wow" is Peter Weedfald, the company's vice president of strategic marketing. His realm includes marketing, advertising, customer and partner relations, research, the consumer information center, and B2B and B2C commerce. He is responsible for crafting marketing strategies that reach across five different divisions: consumer electronics, information technology, telecom, semiconductors, and home appliances. Unlike many other companies, such as Sony, in which each division has its own marketing strategy, Samsung unifies strategy for all five divisions. "In most companies," says Weedfald, "there is a vice president of CRM [customer relationship management]

MARKETING INSIGHT | KEYS TO LONG-TERM MARKET LEADERSHIP

The question of what accounts for the success of long-lasting, successful companies was addressed in a six-year study by Collins and Porras called *Built to Last*. The Stanford researchers identified two companies in each of 18 industries, one that they called a "visionary company" and one that they called a "comparison company." The visionary companies were acknowledged as the industry leaders and widely admired; they set ambitious goals, communicated them to their employees, and embraced a high purpose beyond making money. They also outperformed the comparison companies by a wide margin. The visionary companies included General Electric, Hewlett-Packard, and Boeing; the corresponding comparison companies were Westinghouse, Texas Instruments, and McDonnell Douglas.

The authors found three commonalities among the 18 market leaders. First, the visionary companies each held a distinctive set of values from which they did not deviate. Thus, IBM has held to the principles of respect for the individual, customer satisfaction, and continuous quality improvement throughout its history; and Johnson & Johnson holds to the principle that its first responsibility is to its customers, its second to its employees, its third to its community, and its fourth to its stockholders. The second commonality is that visionary companies express their purpose in enlightened terms. Xerox wants to improve "office productivity" and Monsanto wants to "help end hunger in the world." According to Collins and Porras, a company's core purpose should not be confused with specific business goals or strategies and should not be simply a description of a company's product line. The third commonality is that visionary companies have developed a vision of their future and act to implement it. IBM worked at establishing leadership as a "network-centric" company and not simply as a computer manufacturer.

In his next book, *Good to Great*, Collins provided additional insight into enduring leadership. He defined a "good-to-great" transition as a 10-year fallow period followed by 15 years of increased profits. Examining every company that ever made the *Fortune* 500—approximately 1,400—he found 11 that met the criteria: Abbott, Circuit City, Fannie Mae, Gillette, Kimberly-Clark, Kroger, Nucor, Philip Morris, Pitney Bowes, Walgreen's, and Wells Fargo. Contrasting these 11 to the appropriate comparison companies again led to some clear conclusions. While the companies that achieved greatness were all in different industries, he found that making the transition from good to great didn't require a high-profile outside CEO, cutting-edge technology, or even a fine-tuned business strategy per se. Rather, what was found to be the key was a corporate culture that identified and promoted disciplined people to think and act in a disciplined manner. Leaders with a blend of personal humility and professional integrity were the most effective, and good-to-great companies were driven by core values and purpose that went beyond simply making money.

Sources: James C. Collins and Jerry I. Porras, *Built to Last: Successful Habits of Visionary Companies* (New York: HarperBusiness, 1994); F. G. Rodgers and Robert L. Shook, *The IBM Way: Insights into the World's Most Successful Marketing Organization* (New York: Harper and Row, 1986); James C. Collins, *Good to Great: Why Some Companies Make the Leap . . . and Others Don't* (New York: HarperCollins, 2001).

that doesn't even talk to the person in charge of TV advertising. . . . We're threaded holistically from global marketing in Korea to the last three feet of the sale." That last three feet is where the "wow" needs to kick in—when the consumer is still an arm's length away from the product, either literally, in the store, or online.[19]

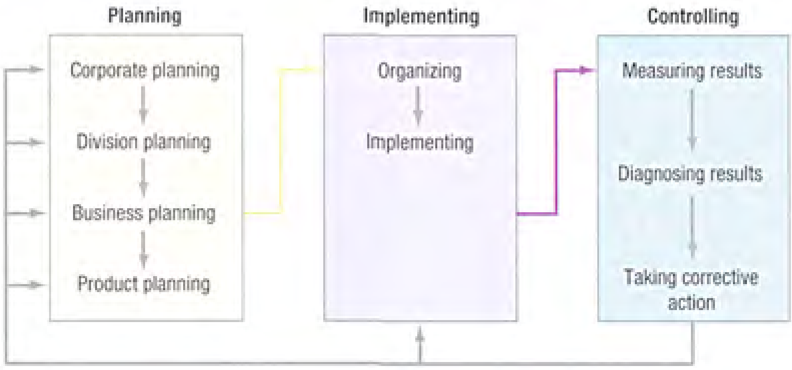
To understand marketing management, we must understand strategic planning. Most large companies consist of four organizational levels: the corporate level, the division level, the business unit level, and the product level. Corporate headquarters is responsible for designing a corporate strategic plan to guide the whole enterprise; it makes decisions on the amount of resources to allocate to each division, as well as on which businesses to start or eliminate. Each division establishes a plan covering the allocation of funds to each business unit within the division. Each business unit develops a strategic plan to carry that business unit into a profitable future. Finally, each product level (product line, brand) within a business unit develops a marketing plan for achieving its objectives in its product market.

The **marketing plan** is the central instrument for directing and coordinating the marketing effort. The marketing plan operates at two levels: strategic and tactical. The **strategic marketing plan** lays out the target markets and the value proposition that will be offered, based on an analysis of the best market opportunities. The **tactical marketing plan** specifies the marketing tactics, including product features, promotion, merchandising, pricing, sales channels, and service.

Today, teams develop the marketing plan with inputs and sign-offs from every important function. These plans are then implemented at the appropriate levels of the organization. Results are monitored, and necessary corrective action taken. The complete planning, implementation, and control cycle is shown in Figure 2.4. We next consider planning at each of these four levels of the organization.

FIG. 2.4

The Strategic Planning, Implementation, and Control Processes



::: Corporate and Division Strategic Planning

By preparing statements of mission, policy, strategy, and goals, headquarters establishes the framework within which the divisions and business units prepare their plans. Some corporations give their business units a lot of freedom to set their own sales and profit goals and strategies. Others set goals for their business units but let them develop their own strategies. Still others set the goals and participate in developing individual business unit strategies.[20]

All corporate headquarters undertake four planning activities:

1. Defining the corporate mission
2. Establishing strategic business units
3. Assigning resources to each SBU
4. Assessing growth opportunities

Defining the Corporate Mission

An organization exists to accomplish something: to make cars, lend money, provide a night's lodging, and so on. Its specific mission or purpose is usually clear when the business starts. Over time the mission may change, to take advantage of new opportunities or respond to new market conditions. Amazon.com changed its mission from being the world's largest online bookstore to aspiring to become the world's largest online store. eBay changed its mission from running online auctions for collectors to running online auctions covering all kinds of goods.

To define its mission, a company should address Peter Drucker's classic questions:[21] What is our business? Who is the customer? What is of value to the customer? What will our business be? What should our business be? These simple-sounding questions are among the most difficult a company will ever have to answer. Successful companies continuously raise these questions and answer them thoughtfully and thoroughly. A company must redefine its mission if that mission has lost credibility or no longer defines an optimal course for growth.[22]

Organizations develop **mission statements** to share with managers, employees, and (in many cases) customers. A clear, thoughtful mission statement provides employees with a shared sense of purpose, direction, and opportunity. The statement guides geographically dispersed employees to work independently and yet collectively toward realizing the organization's goals.

Mission statements are at their best when they reflect a vision, an almost "impossible dream" that provides a direction for the company for the next 10 to 20 years. Sony's former president, Akio Morita, wanted everyone to have access to "personal portable sound," so his company created the Walkman and portable CD player. Fred Smith wanted to deliver mail anywhere in the United States before 10:30 A.M. the next day, so he created FedEx. Table 2.1 gives examples of three mission statements.

Good mission statements have three major characteristics. First, they focus on a limited number of goals. The statement, "We want to produce the highest-quality products, offer the most service, achieve the widest distribution, and sell at the lowest prices" claims too much. Second, mission statements stress the company's major policies and values. They narrow the range of individual discretion so that employees act consistently on

TABLE 2.1

Sample Mission Statements

Rubbermaid Commercial Products, Inc.

"Our Vision is to be the Global Market Share Leader in each of the markets we serve. We will earn this leadership position by providing to our distributor and end-user customers innovative, high-quality, cost-effective and environmentally responsible products. We will add value to these products by providing legendary customer service through our Uncompromising Commitment to Customer Satisfaction."

Motorola

"The purpose of Motorola is to honorably serve the needs of the community by providing products and services of superior quality at a fair price to our customers; to do this so as to earn an adequate profit which is required for the total enterprise to grow; and by so doing provide the opportunity for our employees and shareholders to achieve their reasonable personal objectives."

eBay

"We help people trade practically anything on earth. We will continue to enhance the online trading experiences of all—collectors, dealers, small businesses, unique item seekers, bargain hunters, opportunity sellers, and browsers."

important issues. Third, they define the major competitive spheres within which the company will operate:

- ***Industry.*** The range of industries in which a company will operate. Some companies will operate in only one industry; some only in a set of related industries; some only in industrial goods, consumer goods, or services; and some in any industry. For example, DuPont prefers to operate in the industrial market, whereas Dow is willing to operate in the industrial and consumer markets. 3M will get into almost any industry where it can make money.
- ***Products and applications.*** The range of products and applications a company will supply. St. Jude Medical aims to "serve physicians worldwide with high-quality products for cardiovascular care."
- ***Competence.*** The range of technological and other core competencies that a company will master and leverage. Japan's NEC has built its core competencies in computing, communications, and components to support production of laptop computers, television receivers, and handheld telephones.
- ***Market segment.*** The type of market or customers a company will serve. For example, Porsche makes only expensive cars. Gerber serves primarily the baby market.
- ***Vertical.*** The number of channel levels from raw material to final product and distribution in which a company will participate. At one extreme are companies with a large vertical scope; at one time Ford owned its own rubber plantations, sheep farms, glass manufacturing plants, and steel foundries. At the other extreme are "hollow corporations" or "pure marketing companies" consisting of a person with a phone, fax, computer, and desk who contracts out for every service, including design, manufacture, marketing, and physical distribution.[23]
- ***Geographical.*** The range of regions, countries, or country groups in which a company will operate. At one extreme are companies that operate in a specific city or state. At the other are multinationals such as Unilever and Caterpillar, which operate in almost every country in the world.

Defining the Business

Companies often define their businesses in terms of products: They are in the "auto business" or the "clothing business." But Levitt argues that market definitions of a business are superior to product definitions.[24] A business must be viewed as a customer-satisfying process, not a goods-producing process. Products are transient; basic needs and customer groups endure forever. Transportation is a need: the horse and carriage, the automobile, the railroad, the airline, and the truck are products that meet that need.

Levitt encouraged companies to redefine their businesses in terms of needs, not products. Pitney-Bowes Inc., an old-line manufacturer of postage meters, is in the process of doing just that. With old-fashioned paper mail under siege, Pitney-Bowes can no longer

A Caterpillar ad in French, with the focus on users' confidence in CAT products: "Pascal knows very well that his clients won't accept any excuses. He Has been in the business long enough to know that what's important is to do the work well, without delays and within budget. People say he's a perfectionist. He answers that he is simply a good professional and that's why clients depend on him. . . . Pascal uses CAT." Multinationals such as Caterpillar operate in almost every country in the world.

afford to be defined by its main product, even though it currently holds 80 percent of the domestic market and 62 percent of the global market. The company is redefining itself as a *leading service provider in the much larger mail and document management industry.* With its wealth of engineers, cryptographers, and even workplace anthropologists, as well as 2,300 patents and several labs, Pitney-Bowes is well positioned to help companies organize their communications. In a new series of ads in business publications such as *Fortune*, Pitney-Bowes is spreading the word about its new mission. For instance, one ad boasts that "we can generate remarkable changes across your entire business, including a sizeable increase in profits. A good example: BP. Our document solution helped them shorten billing cycles and enabled rapid receipt of payments, freeing millions in working capital." The tagline: "Pitney-Bowes: Engineering the flow of communication."[25]

IBM redefined itself from a hardware and software manufacturer to a "builder of networks." Table 2.2 gives several examples of companies that have moved from a product to a market definition of their business. It highlights the difference between a target market definition and a strategic market definition. A *target market definition* tends to focus on selling a product or service. Pepsi could define its target market as everyone who drinks a cola beverage and competitors would therefore be other cola companies. A *strategic market definition* could be everyone who might drink something to quench his or her thirst. Suddenly, Pepsi's competition would then include non-cola soft drinks, bottled water, fruit juices, tea,

TABLE 2.2

Product-Oriented Versus Market-Oriented Definitions of a Business

Company	Product Definition	Market Definition
Missouri-Pacific Railroad	We run a railroad.	We are a people-and-goods mover.
Xerox	We make copying equipment.	We help improve office productivity.
Standard Oil	We sell gasoline.	We supply energy.
Columbia Pictures	We make movies.	We market entertainment.
Encyclopaedia Britannica	We sell encyclopedias.	We distribute information.
Carrier	We make air conditioners and furnaces.	We provide climate control in the home.

and coffee. To better compete, Pepsi might decide to sell additional beverages whose growth rate appears to be promising.

A business can be defined in terms of three dimensions: customer groups, customer needs, and technology.[26] Consider a small company that defines its business as designing incandescent lighting systems for television studios. Its customer group is television studios; the customer need is lighting; and the technology is incandescent lighting. The company might want to expand. It could make lighting for other customer groups, such as homes, factories, and offices; or it could supply other services needed by television studios, such as heating, ventilation, or air conditioning. It could design other lighting technologies for television studios, such as infrared or ultraviolet lighting.

Large companies normally manage quite different businesses, each requiring its own strategy. General Electric classified its businesses into 49 **strategic business units (SBUs)**. An SBU has three characteristics:

1. It is a single business or collection of related businesses that can be planned separately from the rest of the company.
2. It has its own set of competitors.
3. It has a manager who is responsible for strategic planning and profit performance and who controls most of the factors affecting profit.

The purpose of identifying the company's strategic business units is to develop separate strategies and assign appropriate funding. Senior management knows that its portfolio of businesses usually includes a number of "yesterday's has-beens" as well as "tomorrow's breadwinners." Yet it cannot rely on impressions; it needs analytical tools to classify its businesses by profit potential.[27]

Assessing Growth Opportunities

Assessing growth opportunities involves planning new businesses, downsizing, or terminating older businesses. The company's plans for existing businesses allow it to project total sales and profits. If there is a gap between future desired sales and projected sales, corporate management will have to develop or acquire new businesses to fill it.

Figure 2.5 illustrates this strategic-planning gap for a major manufacturer of blank compact disks called Musicale (name disguised). The lowest curve projects the expected sales over the next five years from the current business portfolio. The highest curve describes desired sales over the same period. Evidently, the company wants to grow much faster than its current businesses will permit. How can it fill the strategic-planning gap?

The first option is to identify opportunities to achieve further growth within current businesses (intensive opportunities). The second is to identify opportunities to build or acquire businesses that are related to current businesses integrative opportunities). The third is to identify opportunities to add attractive businesses that are unrelated to current businesses (diversification opportunities).

INTENSIVE GROWTH Corporate management's first course of action should be a review of opportunities for improving existing businesses. Ansoff proposed a useful framework for detecting new intensive growth opportunities called a "product–market expansion grid" (Figure 2.6).[28]

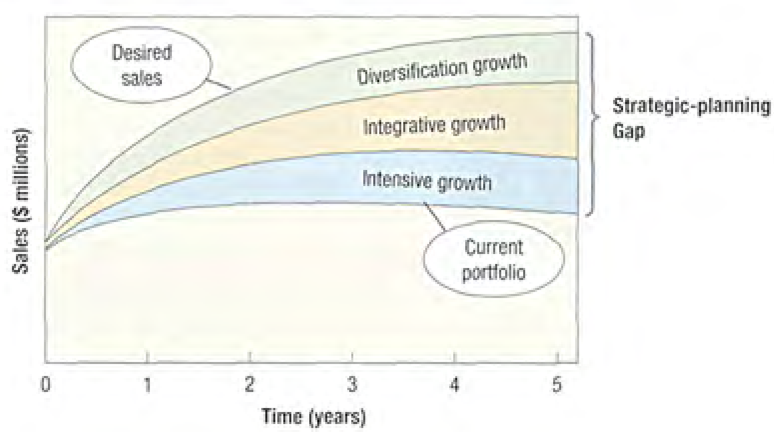


FIG. 2.5

The Strategic Planning Gap

FIG. 2.6

Three Intensive Growth Strategies:
Ansoff's Product–Market Expansion Grid

Source: Adapted and reprinted by permission, *Harvard Business Review.* From "Strategies for Diversification," by Igor Ansoff, September–October 1957. Copyright © 1957 by the President and Fellows of Harvard College. *All rights reserved.*

	Current Products	New Products
Current Markets	1. Market-penetration strategy	3. Product-development strategy
New Markets	2. Market-development strategy	(Diversification strategy)

The company first considers whether it could gain more market share with its current products in their current markets (market-penetration strategy). Next it considers whether it can find or develop new markets for its current products (market-development strategy). Then it considers whether it can develop new products of potential interest to its current markets (product-development strategy). Later it will also review opportunities to develop new products for new markets (diversification strategy).

STARBUCKS

Starbucks is a company that has achieved growth in many different ways. When Howard Schultz, Starbucks' CEO until 2000, came to the company in 1982, he recognized an unfilled niche for cafés serving gourmet coffee directly to customers. This became Starbucks' market-penetration strategy, and helped the company attain a loyal customer base in Seattle. The market-development strategy marked the next phase in Starbucks' growth: It applied the same successful formula that had worked wonders in Seattle, first to other cities in the Pacific Northwest, then throughout North America, and finally, across the globe. Once the company established itself as a presence in thousands of cities internationally, Starbucks sought to increase the number of purchases by existing customers with a product-development strategy that led to new in-store merchandise, including compilation CDs, a Starbucks Duetto Visa card that allows customers to receive points toward Starbucks purchases whenever they use it, and high-speed wireless Internet access at thousands of Starbucks "HotSpots" through a deal with T-Mobile. Finally, Starbucks pursued diversification into grocery store aisles with Frappuccino® bottled drinks, Starbucks brand ice cream, and the purchase of tea retailer Tazo® Tea.[29]

Howard Schultz of Starbucks waves after cutting the ribbon to inaugurate Starbucks' first store outside North America, in the Ginza in Tokyo, August 1996. Today Starbucks has stores across the globe.

How might Musicale use these three major intensive growth strategies to increase its sales? Musicale could try to encourage its current customers to buy more. This could work if its customers could be shown the benefits of using more compact disks for recording music or for data storage. Musicale could try to attract competitors' customers. This could work if Musicale noticed major weaknesses in competitors' products or marketing programs. Finally, Musicale could try to convince nonusers of compact disks to start using them. This could work if there are still enough people who are not able to or do not know how to burn a compact disk.

How can Musicale use a market-development strategy? First, it might try to identify potential user groups in the current sales areas. If Musicale has been selling compact disks only to consumer markets, it might go after office and factory markets. Second, it might seek additional distribution channels in its present locations. If it has been selling its disks only through stereo equipment dealers, it might add mass-merchandising channels.

Third, the company might consider selling in new locations in its home country or abroad. If Musicale sold only in the United States, it could consider entering the European market.

Management should also consider new-product possibilities. Musicale could develop new features, such as additional data storage capabilities or greater durability. It could offer the CD at two or more quality levels, or it could research an alternative technology such as digital audiotape.

By examining these intensive growth strategies, management may discover several ways to grow. Still, that growth may not be enough. In that case, management must also look for integrative growth opportunities.

INTEGRATIVE GROWTH A business's sales and profits may be increased through backward, forward, or horizontal integration within its industry. For example, drug company giant Merck has gone beyond just developing and selling ethical pharmaceuticals. It purchased Medco, a mail-order pharmaceutical distributor in 1993, formed a joint venture with DuPont to establish more basic research, and another joint venture with Johnson & Johnson to bring some of its ethical products into the over-the-counter market.

Media companies have long reaped the benefits of integrative growth. Here is how one business writer explains the potential that NBC could reap from its merger with Vivendi Universal Entertainment to become NBC Universal. Admittedly a far-fetched example, it gets across the possibilities inherent in this growth strategy:[30]

> [When] the hit movie *Seabiscuit* (produced by Universal Pictures) comes to television, it would air on Bravo (owned by NBC) or USA Network (owned by Universal), followed by the inevitable bid to make the movie into a TV series (by Universal Television Group), with the pilot being picked up by NBC, which passes on the show, but it's then revived in the "Brilliant But Canceled" series on cable channel Trio (owned by Universal) where its cult status leads to a Spanish version shown on Telemundo (owned by NBC) and the creation of a popular amusement-park attraction at Universal Studios.

How might Musicale achieve integrative growth? The company might acquire one or more of its suppliers (such as plastic material producers) to gain more control or generate more profit (backward integration). It might acquire some wholesalers or retailers, especially if they are highly profitable (forward integration). Finally, Musicale might acquire one or more competitors, provided that the government does not bar this move (horizontal integration). However, these new sources may still not deliver the desired sales volume. In that case, the company must consider diversification.

DIVERSIFICATION GROWTH Diversification growth makes sense when good opportunities can be found outside the present businesses. A good opportunity is one in which the industry is highly attractive and the company has the right mix of business strengths to be successful. For example, from its origins as an animated film producer, Walt Disney Company has moved into licensing characters for merchandised goods, entering the broadcast industry with its own Disney Channel as well as ABC and ESPN acquisitions, and developed theme parks and vacation and resort properties.

Several types of diversification are possible. First, the company could seek new products that have technological or marketing synergies with existing product lines, even though the new products themselves may appeal to a different group of customers (concentric strategy). It might start a laser disk manufacturing operation because it knows how to manufacture compact disks. Second, the company might search for new products that could appeal to current customers even though the new products are technologically unrelated to its current product line (horizontal strategy). Musicale might produce compact disk cases, even though producing them requires a different manufacturing process. Finally, the company might seek new businesses that have no relationship to its current technology, products, or markets (conglomerate strategy). Musicale might want to consider such new businesses as making application software or personal organizers.

DOWNSIZING AND DIVESTING OLDER BUSINESSES Companies must not only develop new businesses; they must also carefully prune, harvest, or divest tired old businesses in order to release needed resources and reduce costs. Weak businesses require a disproportionate amount of managerial attention. Managers should focus on growth opportunities, and not fritter away energy and resources trying to salvage hemorrhaging businesses. Heinz sold its 9-Lives and Kibbles 'n Bits pet food, StarKist tuna, College Inn broth, and All-in-One baby formulas to Del Monte in 2002 after years of stagnant sales, to allow it to focus on its core brands in ketchup, sauces, and frozen foods.

BLUE CROSS/BLUE SHIELD

William Van Faasen, CEO of Blue Cross/Blue Shield of Massachusetts, offers this advice: "If it's not core to your business, if it's not adding value to your customer's experience, if it's not bolstering the bottom line, get out of it." Van Faasen learned this lesson in 1996, when Blue Cross/Blue Shield was engaged in a number of peripheral activities that were draining its balance sheet—from owning and operating health centers to funding biotechnology ventures. At the same time, managed care came along and caused havoc with prices. At first the company priced services too low and then became aggressive and lost market share. The result was a $100 million loss in 1995 that served as a "two-by-four over the head" for Blue Cross/Blue Shield to create a clear, focused agenda. The company quickly got out of activities that were a drain on resources or not aligned with its core business.[31]

Organization and Organizational Culture

Strategic planning is done within the context of the organization. A company's **organization** consists of its structures, policies, and corporate culture, all of which can become dysfunctional in a rapidly changing business environment. Whereas structures and policies can be changed (with difficulty), the company's culture is very hard to change. Yet changing a corporate culture is often the key to successfully implementing a new strategy.

What exactly is a **corporate culture**? Most businesspeople would be hard-pressed to find words to describe this elusive concept, which some define as "the shared experiences, stories, beliefs, and norms that characterize an organization." Yet, walk into any company and the first thing that strikes you is the corporate culture—the way people are dressed, how they talk to one another, the way they greet customers.

Sometimes corporate culture develops organically and is transmitted directly from the CEO's personality and habits to the company employees. Such is the case with computer giant Microsoft, which began as an entrepreneurial upstart. Even as it grew to a $32 billion company in 2003, Microsoft did not lose the hard-driving culture established by founder Bill Gates. In fact, most feel that Microsoft's ultracompetitive culture is the biggest key to its success and to its much-criticized dominance in the computing industry.[32]

What happens when entrepreneurial companies grow and need to create a tighter structure? This was the case with Yahoo! Inc. When the Internet icon was floundering in 2001, new CEO Terry Semel imposed a more conservative, buttoned-down culture on the freewheeling Internet start-up. At the new Yahoo!, spontaneity is out and order is in. Whereas new initiatives used to roll ahead following free-form brainstorming sessions and a gut check, now they wind their way through tests and formal analysis. Ideas either rise or fall at near-weekly meetings of a group called the Product Council. The group sizes up business plans to make sure all new projects bring benefits to Yahoo!'s existing businesses.[33]

What happens when companies with clashing cultures enter a joint venture or merger? In a study by Coopers & Lybrand of 100 companies with failed or troubled mergers, 855 of executives polled said that differences in management style and practices were the major problem.[34] Conflict was certainly the case when Germany's Daimler merged with Chrysler in 1998.

DAIMLERCHRYSLER

Daimler-Benz AG and Chrysler Corp. merged in 1998 to form DaimlerChrysler. Executives from both companies thought a host of synergies would enable DaimlerChrysler to swiftly build a global automotive empire. Fundamental differences in the way the two corporations did business, however, contributed to early departures by executives, a stock price slide, management restructuring, and even considerable losses by the American manufacturer. The two companies had contrasting management styles, Daimler preferring to operate a classic bureaucracy and Chrysler traditionally giving decision-making ability to managers lower in the ranks.[35]

Successful companies may need to adopt a new view of how to craft their strategies. The traditional view is that senior management hammers out the strategy and hands it down. Gary Hamel offers the contrasting view that imaginative ideas on strategy exist in many places within a company.[36] Senior management should identify and encourage fresh ideas from three groups who tend to be underrepresented in strategy making: employees with youthful perspectives; employees who are far removed from company headquarters; and employees who are new to the industry. Each group is capable of challenging company orthodoxy and stimulating new ideas.

NOKIA

Finnish mobile-phone giant Nokia has managed to remain the frontrunner in the mobile-phone industry, with annual sales of $30.8 billion across 130 countries and a global market share of 38 percent, by installing a culture of innovation at all levels, using small, nimble, creative units to let new ideas bubble up through the ranks. Innovations are as likely to come from a junior application designer as from a seasoned engineer. One example of how the company creates its culture can be seen in the company cafeteria where employees view a slide show as they eat. It's not just any slide show, but one of pictures taken with camera phones by some of Nokia's 1,500 employees—part of an internal corporate competition that rewards staff creativity. Nokia even has a watchword for its culture of continuous innovation: "renewal."[37]

Strategy must be developed by identifying and selecting among different views of the future. The Royal Dutch/Shell Group has pioneered scenario analysis. A **scenario analysis** consists of developing plausible representations of a firm's possible future that make different assumptions about forces driving the market and include different uncertainties. Managers need to think through each scenario with the question: "What will we do if it happens?" They need to adopt one scenario as the most probable and watch for signposts that might confirm or disconfirm that scenario.[38]

::: Business Unit Strategic Planning

The business unit strategic-planning process consists of the steps shown in Figure 2.7. We examine each step in the sections that follow.

The Business Mission

Each business unit needs to define its specific mission within the broader company mission. Thus, a television studio-lighting-equipment company might define its mission as, "The company aims to target major television studios and become their vendor of choice for lighting technologies that represent the most advanced and reliable studio lighting arrangements." Notice that this mission does not attempt to win business from smaller television studios, win business by being lowest in price, or venture into nonlighting products.

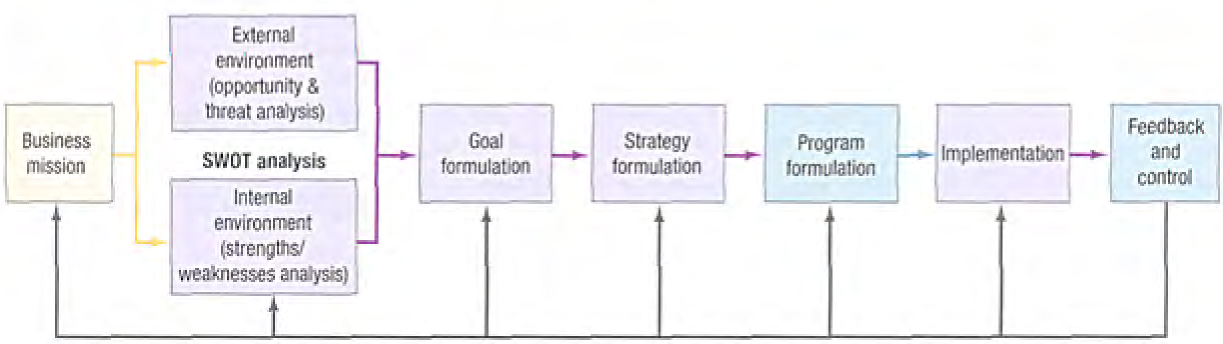


FIG. 2.7 | The Business Unit Strategic-Planning Process

SWOT Analysis

The overall evaluation of a company's strengths, weaknesses, opportunities, and threats is called SWOT analysis. It involves monitoring the external and internal marketing environment.

EXTERNAL ENVIRONMENT (OPPORTUNITY AND THREAT) ANALYSIS A business unit has to monitor key *macroenvironment forces* (demographic-economic, natural, technological, political-legal, and social-cultural) and significant *microenvironment actors* (customers, competitors, suppliers, distributors, dealers) that affect its ability to earn profits. The business unit should set up a marketing intelligence system to track trends and important developments. For each trend or development, management needs to identify the associated opportunities and threats.

A major purpose of environmental scanning is to discern new opportunities. In many ways, good marketing is the art of finding, developing, and profiting from opportunities.[39] A **marketing opportunity** is an area of buyer need and interest in which there is a high probability that a company can profitably satisfy that need. There are three main sources of market opportunities.[40] The first is to supply something that is in short supply. This requires little marketing talent, as the need is fairly obvious. The second is to supply an existing product or service in a new or superior way. There are several ways to uncover possible product or service improvements: by asking consumers for their suggestions (*problem detection method*); by asking consumers to imagine an ideal version of the product or service (*ideal method*); and by asking consumers to chart their steps in acquiring, using, and disposing of a product (*consumption chain method*). The third source often leads to a totally new product or service.

SEGWAY

Meeting a need with a new product or service is perhaps the most rewarding way—when you get it right—but it is the riskiest as well, as Segway LLC found out. When Dean Kamen created the Segway Human Transporter, a $5,000 electric scooter, he had high hopes that it would be a popular, nonpolluting alternative to walking. Yet, so far the high-priced scooter has not found its market, in part because it flies in the face of a powerful *macroenvironment force* —the current concern with obesity and interest in the health benefits of walking. The company may have more success in looking at how *microenvironment actors*—such as local government agencies and the military—can benefit from the product. Early reports indicate that Segway is well received in some government agencies; Seattle water meter readers have been testing Segways, and in Los Angeles, the police of the Metropolitan Transportation Authority have found the Segway useful.[41]

Opportunities can take many forms, and marketers have to be good at spotting them. Consider the following:

- A company may benefit from converging industry trends and introduce hybrid products or services that are new to the market. Example: At least five major cell phone manufacturers released phones with digital photo capabilities.
- A company may make a buying process more convenient or efficient. Example: Consumers can now use the Internet to find more books than ever and search for the lowest price with a few clicks.
- A company can meet the need for more information and advice. Example: Guru.com facilitates finding professional experts in a wide range of fields.
- A company can customize a product or service that was formerly offered only in a standard form. Example: P&G's Reflect.com Web site is capable of producing a customized skin care or hair care product to meet a customer's need.
- A company can introduce a new capability. Example: Consumers can now create and edit digital "iMovies" with the new iMac and upload them to an Apple Web server to share with friends around the world.
- A company may be able to deliver a product or a service faster. Example: FedEx discovered a way to deliver mail and packages much more quickly than the U.S. Post Office.

- A company may be able to offer a product at a much lower price. Example: Pharmaceutical firms have created generic versions of brand-name drugs.

To evaluate opportunities, companies can use **Market Opportunity Analysis (MOA)** to determine the attractiveness and probability of success:

1. Can the benefits involved in the opportunity be articulated convincingly to a defined target market(s)?
2. Can the target market(s) be located and reached with cost-effective media and trade channels?
3. Does the company possess or have access to the critical capabilities and resources needed to deliver the customer benefits?
4. Can the company deliver the benefits better than any actual or potential competitors?
5. Will the financial rate of return meet or exceed the company's required threshold for investment?

In the opportunity matrix in Figure 2.8(a), the best marketing opportunities facing the TV-lighting-equipment company are listed in the upper-left cell (#1). The opportunities in the lower-right cell (#4) are too minor to consider. The opportunities in the upper-right cell (#2) and lower-left cell (#3) should be monitored in the event that any improve in attractiveness and success probability.

Some developments in the external environment represent threats. An **environmental threat** is a challenge posed by an unfavorable trend or development that would lead, in the absence of defensive marketing action, to lower sales or profit. Threats should be classified according to seriousness and probability of occurrence. Figure 2.8(b) illustrates the threat matrix facing the TV-lighting-equipment company. The threats in the upper-left cell are major, because they can seriously hurt the company and they have a high probability of occurrence. To deal with them, the company needs contingency plans that spell out changes it can make before or during the threat. The threats in the lower-right cell are very minor and can be ignored. The threats in the upper-right and lower-left cells need to be monitored carefully in the event that they grow more serious.

FedEx employees walk to their trucks on the first Sunday delivery at the company's suburban Washington center. The new service was introduced based on customer request and market demand.

Once management has identified the major threats and opportunities facing a specific business unit; it can characterize that business's overall attractiveness.

INTERNAL ENVIRONMENT (STRENGTHS/WEAKNESSES) ANALYSIS It is one thing to find attractive opportunities and another to be able to take advantage of them. Each business needs to evaluate its internal strengths and weaknesses. It can do so by using a form like the one shown in "Marketing Memo: Checklist for Performing Strengths/Weaknesses Analysis."

Clearly, the business does not have to correct all its weaknesses, nor should it gloat about all its strengths. The big question is whether the business should limit itself to those opportunities where it possesses the required strengths or whether it should consider opportunities that mean it might have to acquire or develop certain strengths. For example, managers at Texas Instruments (TI) were split between those who wanted TI to stick to industrial electronics (where it has clear strength) and those who wanted the company to continue introducing consumer products (where it lacks some required marketing strengths).

Sometimes a business does poorly not because its people lack the required strengths, but because they do not work together as a team. In one major electronics company, the engineers look down on the salespeople as "engineers who couldn't make it," and the salespeople look down on the service people as "salespeople who couldn't make it." It is therefore critical to assess interdepartmental working relationships as part of the internal environmental audit. Honeywell does exactly this.

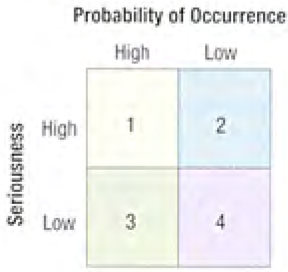
FIG. 2.8

Opportunity and Threat Matrices

(a) Opportunity Matrix

1. Company develops more powerful lighting system
2. Company develops device to measure energy efficiency of any lighting system
3. Company develops device to measure illumination level
4. Company develops software program to teach lighting fundamentals to TV studio personnel

(b) Threat Matrix



1. Competitor develops superior lighting system
2. Major prolonged economic depression
3. Higher costs
4. Legislation to reduce number of TV studio licenses

HONEYWELL

Each year, Honeywell asks each department to rate its own strengths and weaknesses and those of the other departments with which it interacts. The notion is that each department is a supplier to some departments and a customer of other departments. If Honeywell engineers frequently underestimate the cost and completion time of new products, for example, their "internal customers" (manufacturing, finance, and sales) will be hurt.

George Stalk, a leading management consultant, suggests that winning companies are those that have achieved superior in-company capabilities, not just core competencies.[42] Every company must manage some basic processes, such as new-product development, sales generation, and order fulfillment. Each process creates value and requires interdepartmental teamwork. Although each department may possess specific core competencies, the challenge is to develop superior competitive capability in managing the company's key processes. Stalk calls this *capabilities-based competition.*

Goal Formulation

Once the company has performed a SWOT analysis, it can proceed to develop specific goals for the planning period. This stage of the process is called **goal formulation**. Managers use the term *goals* to describe objectives that are specific with respect to magnitude and time.

Most business units pursue a mix of objectives including profitability, sales growth, market share improvement, risk containment, innovation, and reputation. The business unit sets these objectives and then manages by objectives (MBO). For an MBO system to work, the unit's objectives must meet four criteria:

1. ***They must be arranged hierarchically, from the most to the least important*** – For example, the business unit's key objective for the period may be to increase the rate of return on investment. This can be accomplished by increasing the profit level and reducing the amount of invested capital. Profit itself can be increased by increasing revenue and reducing expenses. Revenue can be increased by increasing market share and prices. By

MARKETING MEMO | CHECKLIST FOR PERFORMING STRENGTHS/WEAKNESSES ANALYSIS

	Performance					Importance		
	Major Strength	Minor Strength	Neutral	Minor Weakness	Major Weakness	Hi	Med	Low
Marketing								
1. Company reputation	___	___	___	___	___	___	___	___
2. Market share	___	___	___	___	___	___	___	___
3. Customer satisfaction	___	___	___	___	___	___	___	___
4. Customer retention	___	___	___	___	___	___	___	___
5. Product quality	___	___	___	___	___	___	___	___
6. Service quality	___	___	___	___	___	___	___	___
7. Pricing effectiveness	___	___	___	___	___	___	___	___
8. Distribution effectiveness	___	___	___	___	___	___	___	___
9. Promotion effectiveness	___	___	___	___	___	___	___	___
10. Sales force effectiveness	___	___	___	___	___	___	___	___
11. Innovation effectiveness	___	___	___	___	___	___	___	___
12. Geographical coverage	___	___	___	___	___	___	___	___
Finance								
13. Cost or availability of capital	___	___	___	___	___	___	___	___
14. Cash flow	___	___	___	___	___	___	___	___
15. Financial stability	___	___	___	___	___	___	___	___
Manufacturing								
16. Facilities	___	___	___	___	___	___	___	___
17. Economies of scale	___	___	___	___	___	___	___	___
18. Capacity	___	___	___	___	___	___	___	___
19. Able, dedicated workforce	___	___	___	___	___	___	___	___
20. Ability to produce on time	___	___	___	___	___	___	___	___
21. Technical manufacturing skill	___	___	___	___	___	___	___	___
Organization								
22. Visionary, capable leadership	___	___	___	___	___	___	___	___
23. Dedicated employees	___	___	___	___	___	___	___	___
24. Entrepreneurial orientation	___	___	___	___	___	___	___	___
25. Flexible or responsive	___	___	___	___	___	___	___	___

proceeding this way, the business can move from broad to specific objectives for specific departments and individuals.

2. ***Objectives should be stated quantitatively whenever possible*** – The objective "increase the return on investment (ROI)" is better stated as the goal "increase ROI to 15 percent within two years."
3. ***Goals should be realistic*** – They should arise from an analysis of the business unit's opportunities and strengths, not from wishful thinking.
4. ***Objectives must be consistent*** – It is not possible to maximize sales and profits simultaneously.

Other important trade-offs include short-term profit versus long-term growth, deep penetration of existing markets versus developing new markets, profit goals versus nonprofit goals, and high growth versus low risk. Each choice in this set of trade-offs calls for a different marketing strategy.

Many believe that adopting the goal of strong market share growth may mean having to forego strong short-term profits. For years, Compaq priced aggressively in order to build its market share in the computer market. Subsequently, Compaq decided to pursue profitability at the expense of growth. Yet Charan and Tichy believe that most businesses can be a growth business and can grow profitably.[43] They cite success stories such as GE Medical, Allied Signal, Citibank, and GE Capital, all enjoying profitable growth. Some so-called trade-offs may not be trade-offs at all.

Strategic Formulation

Goals indicate what a business unit wants to achieve; **strategy** is a game plan for getting there. Every business must design a strategy for achieving its goals, consisting of a *marketing strategy*, and a compatible *technology strategy* and *sourcing strategy*.

PORTER'S GENERIC STRATEGIES Michael Porter has proposed three generic strategies that provide a good starting point for strategic thinking: overall cost leadership, differentiation, and focus.[44]

- ***Overall cost leadership.*** The business works hard to achieve the lowest production and distribution costs so that it can price lower than its competitors and win a large market share. Firms pursuing this strategy must be good at engineering, purchasing, manufacturing, and physical distribution. They need less skill in marketing. The problem with this strategy is that other firms will usually compete with still lower costs and hurt the firm that rested its whole future on cost.
- ***Differentiation.*** The business concentrates on achieving superior performance in an important customer benefit area valued by a large part of the market. The firm cultivates those strengths that will contribute to the intended differentiation. Thus the firm seeking quality leadership, for example, must make products with the best components, put them together expertly, inspect them carefully, and effectively communicate their quality.
- ***Focus.*** The business focuses on one or more narrow market segments. The firm gets to know these segments intimately and pursues either cost leadership or differentiation within the target segment.

The online air travel industry provides a good example of these three strategies: Travelocity is pursuing a differentiation strategy by offering the most comprehensive range of services to the traveler. Lowestfare is pursuing a lowest-cost strategy; and Last Minute is pursuing a niche strategy in focusing on travelers who have the flexibility to travel on very short notice.

According to Porter, firms pursuing the same strategy directed to the same target market constitute a **strategic group**. The firm that carries out that strategy best will make the most profits. Firms that do not pursue a clear strategy and try to be good on all strategic dimensions do the worst. International Harvester went out of the farm equipment business because it did not stand out in its industry as lowest in cost, highest in perceived value, or best in serving some market segment. Porter drew a distinction between operational effectiveness and strategy.[45]

Many companies believe they can win by performing the same activities more effectively than their competitors; but competitors can quickly copy the operationally effective company using benchmarking and other tools, thus diminishing the advantage of operational effectiveness. Porter defines strategy as "the creation of a unique and valuable position involving a different set of activities." A company can claim that it has a strategy when it "performs different activities from rivals or performs similar activities in different ways." Companies such as IKEA, Southwest Airlines, Dell Computer, Saturn, and Home Depot run their businesses much differently from their competitors; and these competitors would find it hard to copy and synchronize all the different activities that a strategically differentiated company carries out.

STRATEGIC ALLIANCES Companies are also discovering that they need strategic partners if they hope to be effective. Even giant companies—AT&T, IBM, Philips, Siemens—

A celebration at a Star Alliance inaugural. The Star Alliance brings together 16 airlines that cover most of the globe.

often cannot achieve leadership, either nationally or globally, without forming alliances with domestic or multinational companies that complement or leverage their capabilities and resources.

Just doing business in another country may require the firm to license its product, form a joint venture with a local firm, or buy from local suppliers to meet "domestic content" requirements. As a result, many firms are rapidly developing global strategic networks, and victory is going to those who build the better global network. The Star Alliance, for example, brings together 16 airlines—Lufthansa, United Airlines, Mexicana, Air Canada, ANA, Austrian Airlines, British Midland, Singapore Airlines, Tyrolean, Lauda, SAS, Thai Airways, Varig, Air New Zealand, Asiana Airlines, and Spanair—into a huge global partnership that allows travelers to make nearly seamless connections to about 700 destinations.

Many strategic alliances take the form of marketing alliances. These fall into four major categories.

1. ***Product or service alliances*** – One company licenses another to produce its product, or two companies jointly market their complementary products or a new product. For instance, H&R Block and Hyatt Legal Services—two service businesses—have also joined together in a marketing alliance.
2. ***Promotional alliances*** – One company agrees to carry a promotion for another company's product or service. McDonald's, for example, has often teamed up with Disney to offer products related to current Disney films as part of its meals for children.
3. ***Logistics alliances*** – One company offers logistical services for another company's product. For example, Abbott Laboratories warehouses and delivers all of 3M's medical and surgical products to hospitals across the United States.
4. ***Pricing collaborations*** – One or more companies join in a special pricing collaboration. Hotel and rental car companies often offer mutual price discounts.

Companies need to give creative thought to finding partners that might complement their strengths and offset their weaknesses. Well-managed alliances allow companies to obtain a greater sales impact at less cost. To keep their strategic alliances thriving, corporations have begun to develop organizational structures to support them and have come to view the ability to form and manage partnerships as core skills (called **Partner Relationship Management, PRM**).[46]

Both pharmaceutical and biotech companies are starting to make partnership a core competency. In the 1980s and 1990s pharmaceutical and biotech firms were vertically integrated, doing all the research, development, and marketing and sales themselves. Now they are joining forces and leveraging their respective strengths. For example, Erbitux, a new drug to aid treatment of colorectal cancer, is the result of just such a partnership. The drug was originally discovered in biotech company ImClone Systems' clinical labs, but will be marketed via ImClone's partnership with pharmaceutical giant Bristol-Meyers Squibb.[47]

Program Formulation and Implementation

Once the business unit has developed its principal strategies, it must work out detailed support programs. A great marketing strategy can be sabotaged by poor implementation. If the unit has decided to attain technological leadership, it must plan programs to strengthen its R&D department, gather technological intelligence, develop leading-edge products, train the technical sales force, and develop ads to communicate its technological leadership.

Once the marketing programs are formulated, the marketing people must estimate their costs. Questions arise: Is participating in a particular trade show worth it? Will a specific sales contest pay for itself? Will hiring another salesperson contribute to the bottom line? Activity-based cost (ABC) accounting should be applied to each marketing program to determine whether it is likely to produce sufficient results to justify the cost.[48]

In implementing strategy, companies also must not lose sight of their multiple stakeholders and their needs. Traditionally, most businesses focused on stockholders. Today's businesses are increasingly recognizing that unless they nurture other stakeholders—customers, employees, suppliers, distributors—the business may never earn sufficient profits for the stockholders. A company can aim to deliver satisfaction levels above the minimum for different stakeholders. For example, it might aim to delight its customers, perform well for its employees, and deliver a threshold level of satisfaction to its suppliers. In setting these levels, a company must be careful not to violate the various stakeholder groups' sense of fairness about the relative treatment they are receiving.[49]

There is a dynamic relationship connecting the stakeholder groups. A smart company creates a high level of employee satisfaction, which leads to higher effort, which leads to higher-quality products and services, which creates higher customer satisfaction, which leads to more repeat business, which leads to higher growth and profits, which leads to high stockholder satisfaction, which leads to more investment, and so on. This is the virtuous circle that spells profits and growth. "Marketing Insight: Marketing's Contribution to Shareholder Value" highlights the increasing importance of the proper bottom-line view to marketing expenditures.

According to McKinsey & Company, strategy is only one of seven elements in successful business practice.[50] The first three elements—strategy, structure, and systems—are considered the "hardware" of success. The next four—style, skills, staff, and shared values—are the "software."

MARKETING INSIGHT | MARKETING'S CONTRIBUTION TO SHAREHOLDER VALUE

Companies normally focus on profit maximization rather than on shareholder value maximization. Doyle, in his *Value-Based Marketing*, charges that profit maximization leads to short-term planning and underinvestment in marketing. It leads to a focus on building sales, market share, and current profits. It leads to cost cutting and shedding assets to produce quick improvements in earnings, and erodes a company's long-term competitiveness by neglecting to invest in new market opportunities.

Companies normally measure their profit performance using ROI (return on investment, calculated by dividing profits by investment). This has two problems:

1. Profits are arbitrarily measured and subject to manipulation. Cash flow is more important. As someone observed: "Profits are a matter of opinion; cash is a fact."
2. Investment ignores the real value of the firm. More of a company's value resides in its intangible marketing assets—brands, market knowledge, customer relationships, and partner relationships—than in its balance sheet. These assets are the drivers of long-term profits.

Doyle argues that marketing will not mature as a profession until it can demonstrate the impact of marketing on shareholder value, the market value of a company minus its debt. The market value is the share price times the number of shares outstanding. The share price reflects what investors estimate is the present value of the future lifetime earnings of a company. When management is choosing a marketing strategy, Doyle wants it to apply shareholder value analysis (SVA) to see which alternative course of action will maximize shareholder value.

If Doyle's arguments are accepted, marketing will finally get the attention it deserves in the boardroom. Instead of seeing marketing as a specific function concerned only with increasing sales or market share, senior management will see it as an integral part of the whole management process. It will judge marketing by how much it contributes to shareholder value.

Source: Peter Doyle, *Value-Based Marketing: Marketing Strategies for Corporate Growth and Shareholder Value* (Chichester, England: John Wiley & Sons, 2000).

The first "soft" element, *style,* means that company employees share a common way of thinking and behaving. McDonald's employees smile at the customer, and IBM employees are very professional in their customer dealings. The second, *skills,* means that the employees have the skills needed to carry out the company's strategy. The third, *staffing,* means that the company has hired able people, trained them well, and assigned them to the right jobs. The fourth, *shared values,* means that the employees share the same guiding values. When these elements are present, companies are usually more successful at strategy implementation.[51]

Another study of management practices found that superior performance over time depended on flawless execution, a company culture based on aiming high, a structure that is flexible and responsive, and a strategy that is clear and focused.[52]

Feedback and Control

As it implements its strategy, a firm needs to track the results and monitor new developments. Some environments are fairly stable from year to year. Other environments evolve slowly in a fairly predictable way. Still other environments change rapidly in major and unpredictable ways. Nonetheless, a company can count on one thing: The marketplace will change; and when it does, the company will need to review and revise its implementation, programs, strategies, or even objectives.

A company's strategic fit with the environment will inevitably erode because the market environment changes faster than the company's 7 Ss. Thus, a company might remain efficient while it loses effectiveness. Peter Drucker pointed out that it is more important to "do the right thing" (effectiveness) than "to do things right" (efficiency). The most successful companies excel at both.

Once an organization fails to respond to a changed environment, it becomes increasingly hard to recapture its lost position. Consider what happened to Lotus Development Corporation. Its Lotus 1-2-3 software was once the world's leading software program, and now its market share in desktop software has slipped so low that analysts do not even bother to track it.

LOTUS

Sales of the original IBM-PC were driven by Lotus 1-2-3, which combined an accounting spreadsheet with a program that could turn rows of numbers into charts and graphs. Yet Lotus ultimately did not keep pace as the PC evolved, and missed opportunities with Apple Macintosh, Microsoft Windows, and suite applications. Following IBM's acquisition of the company in 1995, Lotus capitalized on the growing popularity of corporate e-mail systems with its Notes software, but Microsoft's ability to tie applications to operating systems gave it an unbeatable advantage. The company now works in concert with Microsoft to make sure its latest Smart Suite software takes full advantage of Windows software.[53]

Organizations, especially large ones, are subject to inertia. Inertia has been affecting giant Kraft Foods, Inc., a company renowned for its expertise in creating brand extensions.

KRAFT

While the company was busy rolling out products like Jell-O gel cups, Mini Oreos, and Ooey Gooey Warm N' Chewy Chips Ahoy!, it missed some important trends in supermarket food. As supermarkets' own private labels put out deeply discounted cheeses and cookies and other processed foods, Kraft has become increasingly perceived as too high-priced. More important, Kraft neglected the trend toward healthier products with organic ingredients and less fat. Alongside brands like Stonyfield Farm, Starbucks, or SilkSoy products, Kraft has begun looking more like a producer of expensive processed food.[54]

Organizations are set up as efficient machines, and it is difficult to change one part without adjusting everything else. Yet organizations can be changed through strong leadership, preferably in advance of a crisis. The key to organizational health is willingness to examine the changing environment and to adopt new goals and behaviors.

Product Planning: The Nature and Contents of a Marketing Plan

To carry out their responsibilities, marketing managers follow a marketing process. Working within the plans set by the levels above them, product managers come up with a marketing plan for individual products, lines, brands, channels, or customer groups. Each product level (product line, brand) must develop a marketing plan for achieving its goals. A **marketing plan** is a written document that summarizes what the marketer has learned about the marketplace and indicates how the firm plans to reach its marketing objectives.[55] *It contains tactical guidelines for the marketing programs and financial allocations* over the planning period.[56] It is one of the most important outputs of the marketing process.

Marketing plans are becoming more customer- and competitor-oriented and better reasoned and more realistic than in the past. The plans draw more inputs from all the functions and are team-developed. Marketing executives increasingly see themselves as professional managers first, and specialists second. Planning is becoming a continuous process to respond to rapidly changing market conditions.

SONY

Sony originally planned to sell 10 million PlayStation 2 units worldwide within the first year of introduction. The marketing plan called for an aggressive presale promotional campaign to build demand and overshadow competitive game units from Nintendo and other rivals. Sony initially launched the new product in Japan, where the planned hype caused a buying frenzy in which almost 1 million units were sold within the first three days. However, unexpected components shortages kept the company from building enough units to stay on schedule. As a result, Sony was forced to revise its marketing plan by delaying the European launch and reducing the number of PlayStation 2 units shipped to stores in Europe and the United States; this delay, in turn, prevented Sony from reaching its corporate sales and profit objectives for the year.[57]

At the same time, marketing planning procedures and content vary considerably among companies. The plan is variously called a "business plan," a "marketing plan," and sometimes a "battle plan." Most marketing plans cover one year. The plans vary in length from under 5 to over 50 pages. Some companies take their plans very seriously, whereas others see them only as a rough guide to action. Eisenhower once observed: "In preparing for battle I have always found that plans are useless but planning is indispensable." The most frequently cited shortcomings of current marketing plans, according to marketing executives, are lack of realism, insufficient competitive analysis, and a short-run focus. (See "Marketing Memo: Marketing Plan Criteria" for some guideline questions to ask in developing marketing plans.)

What, then, does a marketing plan look like? What does it contain?

Contents of the Marketing Plan

- ***Executive summary and table of contents.*** The marketing plan should open with a brief summary of the main goals and recommendations. The executive summary permits senior management to grasp the plan's major thrust. A table of contents that outlines the rest of the plan and all the supporting rationale and operational detail should follow the executive summary.

- ***Situation analysis.*** This section presents relevant background data on sales, costs, the market, competitors, and the various forces in the macroenvironment. How is the market defined, how big is it, and how fast is it growing? What are the relevant trends affecting the market? What is the product offering and what are the critical issues facing the company? Pertinent historical information can be included to provide context. All this information is used to carry out a SWOT (strengths, weaknesses, opportunities, threats) analysis.

- ***Marketing strategy.*** Here the product manager defines the mission and marketing and financial objectives. The manager also defines those groups and needs that the market offerings are intended to satisfy. The manager then establishes the product line's competitive positioning, which will inform the "game plan" to accomplish the plan's objectives. All this is done with inputs from other organizational areas, such as purchasing, manufacturing, sales,

MARKETING MEMO | MARKETING PLAN CRITERIA

Here are some questions to ask in evaluating a marketing plan.

1. ***Is the plan simple?*** Is it easy to understand and act on? Does it communicate its content easily and practically?
2. ***Is the plan specific?*** Are its objectives concrete and measurable? Does it include specific actions and activities, each with specific dates of completion, specific persons responsible, and specific budgets?
3. ***Is the plan realistic?*** Are the sales goals, expense budgets, and milestone dates realistic? Has a frank and honest self-critique been conducted to raise possible concerns and objections?
4. ***Is the plan complete?*** Does it include all the necessary elements?

Source: Tim Berry and Doug Wilson, *On Target: The Book on Marketing Plans* (Eugene, OR: Palo Alto Software, 2000).

finance, and human resources, to ensure that the company can provide proper support for effective implementation. The marketing strategy should be specific about the branding strategy and customer strategy that will be employed.

- ***Financial projections.*** Financial projections include a sales forecast, an expense forecast, and a break-even analysis. On the revenue side, the projections show the forecasted sales volume by month and product category. On the expense side, the projections show the expected costs of marketing, broken down into finer categories. The break-even analysis shows how many units must be sold monthly to offset the monthly fixed costs and average per-unit variable costs.
- ***Implementation controls.*** The last section of the marketing plan outlines the controls for monitoring and adjusting implementation of the plan. Typically, the goals and budget are spelled out for each month or quarter so management can review each period's results and take corrective action as needed. A number of different internal and external measures must be taken to assess progress and suggest possible modifications. Some organizations include contingency plans outlining the steps management would take in response to specific environmental developments, such as price wars or strikes.

Sample Marketing Plan: Pegasus Sports International*

1.0 Executive Summary

Pegasus Sports International is a start-up aftermarket inline skating accessory manufacturer. In addition to the aftermarket products, Pegasus is developing SkateTours, a service that takes clients out, in conjunction with a local skate shop, and provides them with an afternoon of skating using inline skates and some of Pegasus' other accessories such as SkateSails. The aftermarket skate accessory market has been largely ignored. Although there are several major manufacturers of the skates themselves, the accessory market has not been addressed. This provides Pegasus with an extraordinary opportunity for market growth. Skating is a booming sport. Currently, most of the skating is recreational. There are, however, a growing number of skating competitions, including team-oriented competitions such as skate hockey as well as individual competitions such as speed skate racing. Pegasus will work to grow these markets and develop the skate transportation market, a more utilitarian use of skating. Several of Pegasus' currently developed products have patents pending, and local market research indicates that there is great demand for these products. Pegasus will achieve fast, significant market penetration through a solid business model, long-range planning, and a strong management team that is able to execute this exciting opportunity. The three principals on the management team have over 30 years of combined personal and industry experience. This extensive experience provides Pegasus with the empirical information as well as the passion to provide the skating market with much-needed aftermarket products. Pegasus will sell its products initially through

*Sample plan provided by and copyrighted by Palo Alto Software, Inc. Find more complete sample marketing plans at www.mplans.com.

its Web site. This "Dell" direct-to-the-consumer approach will allow Pegasus to achieve higher margins and maintain a close relationship with the customers, which is essential for producing products that have a true market demand. By the end of the year, Pegasus will have also developed relationships with different skate shops and will begin to sell some of its products through retailers.

TABLE 1.0 | Sales Forecast

	Sales Forecast		
Sales	**2003**	**2004**	**2005**
Recreational	$455,740	$598,877	$687,765
Competitive	$72,918	$95,820	$110,042
Total Sales	$528,658	$694,697	$797,807
Direct Cost of Sales	**2003**	**2004**	**2005**
Recreational	$82,033	$107,798	$123,798
Competitive	$13,125	$17,248	$19,808
Subtotal Cost of Sales	$95,159	$125,046	$143,605

2.0 Situation Analysis

Pegasus is entering its first year of operation. Its products have been well received, and marketing will be key to the development of brand and product awareness as well as the growth of the customer base. Pegasus International offers several different aftermarket skating accessories, serving the growing inline skating industry.

2.1 Market Summary

Pegasus possesses good information about the market and knows a great deal about the common attributes of the most prized customer. This information will be leveraged to better understand who is served, what their specific needs are, and how Pegasus can better communicate with them.

Target Markets

Recreational
Fitness
Speed
Hockey
Extreme

2.1.1 Market Demographics

The profile for the typical Pegasus customer consists of the following geographic, demographic, and behavior factors:

Geographics

- Pegasus has no set geographic target area. By leveraging the expansive reach of the Internet and multiple delivery services, Pegasus can serve both domestic and international customers.
- The total targeted population is 31 million users.

Demographics

- There is an almost equal ratio between male and female users.
- Ages 13–46, with 48 percent clustering around ages 23–34. The recreational users tend to cover the widest age range, including young users through active adults. The fitness users tend to be ages 20–40. The speed users tend to be in their late twenties and early thirties. The hockey players are

TABLE 2.1 | Target Market Forecast

				Target Market Forecast			
Potential Customers	**Growth**	**2003**	**2004**	**2005**	**2006**	**2007**	**CAGR**
Recreational	10%	19,142,500	21,056,750	23,162,425	25,478,668	28,026,535	10.00%
Fitness	15%	6,820,000	7,843,000	9,019,450	10,372,368	11,928,223	15.00%
Speed	10%	387,500	426,250	468,875	515,763	567,339	10.00%
Hockey	6%	2,480,000	2,628,800	2,786,528	2,953,720	3,130,943	6.00%
Extreme	4%	2,170,000	2,256,800	2,347,072	2,440,955	2,538,593	4.00%
Total	10.48%	31,000,000	34,211,600	37,784,350	41,761,474	46,191,633	10.48%

generally in their teens through their early twenties. The extreme segment is of similar age to the hockey players.

- Of the users who are over 20, 65 percent have an undergraduate degree or substantial undergraduate coursework.
- The adult users have a median personal income of $47,000.

Behavior Factors

- Users enjoy fitness activities not as a means for a healthy life, but as an intrinsically enjoyable activity in itself.
- Users spend money on gear, typically sports equipment.
- Users have active lifestyles that include some sort of recreation at least 2–3 times a week.

2.1.2 Market Needs

Pegasus is providing the skating community with a wide range of accessories for all variations of skating. The company seeks to fulfill the following benefits that are important to its customers:

- ***Quality craftsmanship.*** The customers work hard for their money and do not enjoy spending it on disposable products that only work for a year or two.
- ***Well-thought-out designs.*** The skating market has not been addressed by well-thought-out products that serve skaters' needs. Pegasus' industry experience and personal dedication to the sport will provide it with the needed information to produce insightfully designed products.
- ***Customer Service.*** Exemplary service is required to build a sustainable business that has a loyal customer base.

2.1.3 Market Trends

Pegasus will distinguish itself by marketing products not previously available to skaters. The emphasis in the past has been to sell skates and very few replacement parts. The number of skaters is not restricted to any one single country, continent, or age group, so there is a world market. Pegasus has products for virtually every group of skaters. The fastest-growing segment of this sport is the fitness skater. Therefore, the marketing is being directed toward this group. BladeBoots will enable users to enter establishments without having to remove their skates. BladeBoots will be aimed at the recreational skater, the largest segment. SkateAids, on the other hand, are great for everyone.

The sport of skating will also grow through SkateSailing. This sport is primarily for the medium-to-advanced skater, and its growth potential is tremendous. The sails that Pegasus has manufactured have been sold in Europe, following a pattern similar to windsurfing. Windsailing originated in Santa Monica but did not take off until it had already grown big in Europe.

Another trend is group skating. More and more groups are getting together on skating excursions in cities all over the world. For example, San Francisco has night group skating that attracts hundreds of people. The market trends are showing continued growth in all directions of skating.

2.1.4 Market Growth

With the price of skates going down due to competition by so many skate companies, the market has had steady growth throughout the world, with 22.5 million units sold in 1999 to over 31 million in 2002. The growth statistics for 2003 were estimated to be over 35 million units. More and more people are discovering—and in many cases rediscovering—the health benefits and fun of skating.

2.2 SWOT Analysis

The following SWOT analysis captures the key strengths and weaknesses within the company, and describes the opportunities and threats facing Pegasus.

2.2.1 Strengths

- In-depth industry experience and insight.
- Creative, yet practical product designers.
- The use of a highly efficient, flexible business model utilizing direct customer sales and distribution.

2.2.2 Weaknesses

- The reliance on outside capital necessary to grow the business.
- A lack of retailers who can work face-to-face with the customer to generate brand and product awareness.
- The difficulty of developing brand awareness as a start-up company.

2.2.3 Opportunities

- Participation within a growing industry.
- Decreased product costs through economy of scale.
- The ability to leverage other industry participants' marketing efforts to help grow the general market.

2.2.4 Threats

- Future/potential competition from an already established market participant.
- A slump in the economy that could have a negative effect on people's spending of discretionary income on fitness/recreational products.
- The release of a study that calls into question the safety of skating or the inability to prevent major skating-induced traumas.

2.3 Competition

Pegasus Sports International is forming its own market. Although there are a few companies that do make sails and foils that a few skaters are using, Pegasus is the only brand that is truly designed for and by skaters. The few competitors' sails on the market are not designed for skating, but for windsurfing or for skateboards. In the case of foils, storage and carrying are not practical. There are different indirect competitors who are manufacturers of the actual skates. After many years in the market, these companies have yet to become direct competitors by manufacturing accessories for the skates that they make.

2.4 Product Offering

Pegasus Sports International now offers several products:

- The first product that has been developed is BladeBoots, a cover for the wheels and frame of inline skates, which allows skaters to enter places that normally would not allow them in with skates on. BladeBoots come with a small pouch and belt which converts to a well-designed skate carrier.
- The second product is SkateSails. These sails are specifically designed for use while skating. Feedback that Pegasus has received from skaters indicates skatesailing could become a very popular sport. Trademarking this product is currently in progress.
- The third product, SkateAid, will be in production by the end of the year. Other ideas for products are under development, but will not be disclosed until Pegasus can protect them through pending patent applications.

2.5 Keys to Success

The keys to success are designing and producing products that meet market demand. In addition, Pegasus must ensure total customer satisfaction. If these keys to success are achieved, it will become a profitable, sustainable company.

2.6 Critical Issues

As a start-up business, Pegasus is still in the early stages. The critical issues are for Pegasus to:

- Establish itself as the premier skating accessory company.
- Pursue controlled growth that dictates that payroll expenses will never exceed the revenue base. This will help protect against recessions.
- Constantly monitor customer satisfaction, ensuring that the growth strategy will never compromise service and satisfaction levels.

3.0 Marketing Strategy

The key to the marketing strategy is focusing on the speed, health and fitness, and recreational skaters. Pegasus can cover about 80 percent of the skating market because it produce products geared toward each segment. Pegasus is able to address all of the different segments within the market because, although each segment is distinct in terms of its users and equipment, its products are useful to all of the different segments.

3.1 Mission

Pegasus Sports International's mission is to provide the customer with the finest skating accessories available. "We exist to attract and maintain customers. With a strict adherence to this maxim, success will be ensured. Our services and products will exceed the expectations of the customers."

3.2 Marketing Objectives

- Maintain positive, strong growth each quarter (notwithstanding seasonal sales patterns).
- Achieve a steady increase in market penetration.
- Decrease customer acquisition costs by 1.5 percent per quarter.

3.3 Financial Objectives

- Increase the profit margin by 1 percent per quarter through efficiency and economy-of-scale gains.
- Maintain a significant research and development budget (as a percentage relative to sales) to spur future product developments.
- A double- to triple-digit growth rate for the first three years.

3.4 Target Markets

With a world skating market of over 31 million that is steadily growing (statistics released by the Sporting Goods Manufacturers Association), the niche has been created. Pegasus' aim is to expand this market by promoting SkateSailing, a new sport which is popular in both Santa Monica and Venice Beach in California. The Sporting Goods Manufacturers Association survey indicates that skating now has more participation than football, softball, skiing, and snowboarding combined. The breakdown of participation in skating is as follows: 1+% speed (growing), 8% hockey (declining), 7% extreme/aggressive (declining), 22% fitness (nearly 7 million—the fastest growing), and 61% recreational (first-timers). Pegasus' products are targeting the fitness and recreational groups, because they are the fastest growing. These groups are gearing themselves toward health and fitness, and combined, they can easily grow to 85 percent (or 26 million) of the market in the next five years.

3.5 Positioning

Pegasus will position itself as the premier aftermarket skating accessory company. This positioning will be achieved by leveraging Pegasus' competitive edge: industry experience and passion. Pegasus is a skating company formed by skaters for skaters. Its management is able to use its vast experience and personal passion for the sport to develop innovative, useful accessories for a broad range of skaters.

3.6 Strategies

The single objective is to position Pegasus as the premier skating accessory manufacturer, serving the domestic market as well as the international market. The marketing strategy will seek to first create customer awareness concerning the offered products and services and then develop the customer base. The message that Pegasus will seek to communicate is that it offers the best-designed, most useful skating accessories. This message will be communicated through a variety of methods. The first will be the Pegasus Web site, which will provide a rich source of product information and offer consumers the opportunity to purchase. A lot of time and money will be invested in the site to provide the customer with the perception of total professionalism and utility for Pegasus' products and services.

The second marketing method will be advertisements placed in numerous industry magazines. The skating industry is supported by several different glossy magazines designed to promote the industry as a whole. In addition, a number of smaller periodicals serve the smaller market segments within the skating industry. The last method of communication is the use of printed sales literature. The two previously mentioned marketing methods will create demand for the sales literature, which will be sent out to customers. The cost of the sales literature will be fairly minimal, because it will use the already compiled information from the Web site.

3.7 Marketing Mix

Pegasus' marketing mix is comprised of the following approaches to pricing, distribution, advertising and promotion, and customer service.

- ***Pricing.*** This will be based on a per-product retail price.
- ***Distribution.*** Initially, Pegasus will use a direct-to-consumer distribution model. Over time, it will use retailers as well.
- ***Advertising and Promotion.*** Several different methods will be used for the advertising effort.
- ***Customer Service.*** Pegasus will strive to achieve benchmarked levels of customer care.

3.8 Marketing Research

Pegasus is blessed with the good fortune of being located in the center of the skating world: Venice, California. It will be able to leverage this opportune location by working with many of the different skaters that live in the area. Pegasus was able to test all of its products not only with its principals, who are accomplished skaters, but also with the many other dedicated and "newbie" users located in Venice. The extensive product testing by a wide variety of users provided Pegasus with valuable product feedback and has led to several design improvements.

4.0 Financials

This section will offer the financial overview of Pegasus related to marketing activities. Pegasus will address break-even analysis, sales forecasts, expense forecast, and indicate how these activities link to the marketing strategy.

4.1 Break-even Analysis

The break-even analysis indicates that $7,760 will be required in monthly sales revenue to reach the break-even point.

Break-even Analysis

Break-even point = where line intersects with 0

TABLE 4.1 | Break-even Analysis

Break-even Analysis:	
Monthly Units Break-even	62
Monthly Sales Break-even	$ 7,760
Assumptions:	
Average Per-Unit Revenue	$125.62
Average Per-Unit Variable Cost	$ 22.61
Estimated Monthly Fixed Cost	$ 6,363

4.2 Sales Forecast

Pegasus feels that the sales forecast figures are conservative. It will steadily increase sales as the advertising budget allows. Although the target market forecast (Table 2.1) listed all of the potential customers divided into separate groups, the sales forecast groups customers into two categories: Recreational and Competitive. Reducing the number of categories allows the reader to quickly discern information, making the chart more functional.

Monthly Sales Forecast

TABLE 4.2 Sales Forecast

Sales Forecast			
Sales	**2003**	**2004**	**2005**
Recreational	$455,740	$598,877	$687,765
Competitive	$ 72,918	$ 95,820	$110,042
Total Sales	$528,658	$694,697	$797,807
Direct Cost of Sales	**2003**	**2004**	**2005**
Recreational	$ 82,033	$107,798	$123,798
Competitive	$ 13,125	$ 17,248	$ 19,808
Subtotal Cost of Sales	$ 95,159	$125,046	$143,605

4.3 Expense Forecast

The expense forecast will be used as a tool to keep the department on target and provide indicators when corrections/modifications are needed for the proper implementation of the marketing plan.

Monthly Expense Budget

TABLE 4.3 Marketing Expense Budget

Marketing Expense Budget	2003	2004	2005
Web site	$25,000	$8,000	$10,000
Advertisements	$8,050	$15,000	$20,000
Printed Material	$1,725	$2,000	$3,000
Total Sales and Marketing Expenses	$34,775	$25,000	$33,000
Percent of Sales	6.58%	3.60%	4.14%
Contribution Margin	$398,725	$544,652	$621,202
Contribution Margin/Sales	75.42%	78.40%	77.86%

5.0 Controls

The purpose of Pegasus' marketing plan is to serve as a guide for the organization. The following areas will be monitored to gauge performance:

- Revenue: monthly and annual
- Expenses: monthly and annual
- Customer satisfaction
- New product development

5.1 Implementation

The following milestones identify the key marketing programs. It is important to accomplish each one on time and on budget.

Milestones

TABLE 5.1 Milestones

Milestones	Plan				
Milestone	**Start Date**	**End Date**	**Budget**	**Manager**	**Department**
Marketing plan completion	1/1/03	2/1/03	$0	Stan	Marketing
Web site completion	1/1/03	3/15/03	$20,400	outside firm	Marketing
Advertising campaign #1	1/1/03	6/30/03	$3,500	Stan	Marketing
Advertising campaign #2	3/1/99	12/30/03	$4,550	Stan	Marketing
Development of the retail channel	1/1/03	11/30/03	$0	Stan	Marketing
Totals			$28,450		

5.2 Marketing Organization

Stan Blade will be responsible for the marketing activities.

5.3 Contingency Planning

Difficulties and Risks

- Problems generating visibility, a function of being an Internet-based start-up organization.
- An entry into the market by an already established market competitor.

Worst Case Risks Include

- Determining that the business cannot support itself on an ongoing basis.
- Having to liquidate equipment or intellectual capital to cover liabilities.

SUMMARY :::

1. The value delivery process involves choosing (or identifying), providing (or delivering), and communicating superior value. The value chain is a tool for identifying key activities that create value and costs in a specific business.
2. Strong companies develop superior capabilities in managing core business processes such as new-product realization, inventory management, and customer acquisition and retention. Managing these core processes effectively means creating a marketing network in which the company works closely with all parties in the production and distribution chain, from suppliers of raw materials to retail distributors. Companies no longer compete—marketing networks do.
3. According to one view, holistic marketing maximizes value exploration by understanding the relationships between the customer's cognitive space, the company's competence space, and the collaborator's resource space; maximizes value creation by identifying new customer benefits from the customer's cognitive space, utilizing core competencies from its business domain, and selecting and managing business partners from its collaborative networks; and maximizes value delivery by becoming proficient at customer relationship management, internal resource management, and business partnership management.
4. Market-oriented strategic planning is the managerial process of developing and maintaining a viable fit between the organization's objectives, skills, and resources and its changing market opportunities. The aim of strategic planning is to shape the company's businesses and products so that they yield target profits and growth. Strategic planning takes place at four levels: corporate, division, business unit, and product.
5. The corporate strategy establishes the framework within which the divisions and business units prepare their strategic plans. Setting a corporate strategy entails four activities: defining the corporate mission, establishing strategic business units (SBUs), assigning resources to each SBU based on its market attractiveness and business strength, and planning new businesses and downsizing older businesses.
6. Strategic planning for individual businesses entails the following activities: defining the business mission, analyzing external opportunities and threats, analyzing internal strengths and weaknesses, formulating goals, formulating strategy, formulating supporting programs, implementing the programs, and gathering feedback and exercising control.
7. Each product level within a business unit must develop a marketing plan for achieving its goals. The marketing plan is one of the most important outputs of the marketing process.

APPLICATIONS :::

Marketing Debate What Good is a Mission Statement?

Virtually all firms have mission statements to help guide and inspire employees as well as signal what is important to the firm to those outside the firm. Mission statements are often the product of much deliberation and discussion. At the same time, some critics claim that mission statements sometimes lack "teeth" and specificity. Moreover, critics also maintain that in many cases, mission statements do not vary much from firm to firm, and make the same empty promises.

Take a position: Mission statements are critical to a successful marketing organization, *or* Mission statements rarely provide useful marketing value.

Marketing Discussion

Consider Porter's value chain and the holistic marketing orientation model. What implications do they have for marketing planning? How would you structure a marketing plan to incorporate some of their concepts?

MARKETING SPOTLIGHT | NIKE

Nike hit the ground running in 1962. Originally known as Blue Ribbon Sports, the company focused on providing high-quality running shoes designed especially for athletes by athletes. Founder Philip Knight believed that high-tech shoes for runners could be manufactured at competitive prices if imported from abroad. The company's commitment to designing innovative footwear for serious athletes helped it build a cult following among American consumers. By 1980, Nike had become the number-one athletic shoe company in the United States.

From the start, Nike's marketing campaigns featured winning athletes as spokespeople. The company signed on its first spokesperson, runner Steve Prefontaine, in 1973. Prefontaine's irreverent attitude matched Nike's spirit. Marketing campaigns featuring winning athletes made sense. Nike saw a "pyramid of influence"—it saw that product and brand choices are influenced by the preferences and behavior of a small percentage of top athletes. Using professional athletes in its advertising campaigns was both efficient and effective for Nike.

In 1985, Nike signed up then-rookie guard Michael Jordan as a spokesperson. Jordan was still an up-and-comer, but he personified superior performance. Nike's bet paid off: The Air Jordan line of basketball shoes flew off the shelves, with revenues of over $100 million in the first year alone. Jordan also helped build the psychological image of the Nike brand. Phil Knight said: "Sports are at the heart of American culture, so a lot of emotion already exists around it. Emotions are always hard to explain, but there's something inspirational about watching athletes push the limits of performance. You can't explain much in 60 seconds, but when you show Michael Jordan, you don't have to."

In 1988, Nike aired its first ads in the "Just Do It" ad campaign. The $20 million month-long blitz—subtly encouraging Americans to participate more actively in sports—featured 12 TV spots in all. The campaign challenged a generation of athletic enthusiasts to chase their goals; it was a natural manifestation of Nike's attitude of self-empowerment through sports. The campaign featured celebrities and noncelebrities. One noncelebrity ad featured Walt Stack, an 80-year-old long-distance runner, running across the Golden Gate bridge as part of his morning routine. The "Just Do It" trailer appeared on the screen as the shirtless Stack ran on a chilly morning. Talking to the camera as it zoomed in, and while still running, Stack remarked, "People ask me how I keep my teeth from chattering when it's cold." Pausing, Stack matter-of-factly replied, "I leave them in my locker."

As Nike began expanding overseas to Europe, it found that its American-style ads were seen as too aggressive. The brand image was perceived as too fashion-oriented. Nike realized that it had to "authenticate" its brand in Europe the way it had in America. That meant building credibility and relevance in European sports, especially soccer. Nike became actively involved as a sponsor of soccer youth leagues, local clubs, and national teams. Authenticity required that consumers see the product being used by athletes, especially by athletes who win. The big break came in 1994, when the Brazilian team (the only national team for which Nike had any real sponsorships) won the World Cup. The victory led Nike to sign other winning teams, and by 2003 overseas revenues surpassed U.S. revenues for the first time. Nike also topped $10 billion in sales for the first time in that year as well.

Today, Nike dominates the athletic footwear market. Nine of the 10 top-selling basketball shoes, for example, are Nikes. Nike introduces hundreds of shoes each year for 30 sports—averaging one new shoe style every day of the year. Swooshes abound on everything from wristwatches to golf clubs to swimming caps.

Discussion Questions

1. What have been the key success factors for Nike?
2. Where is Nike vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should they be sure to do with its marketing?

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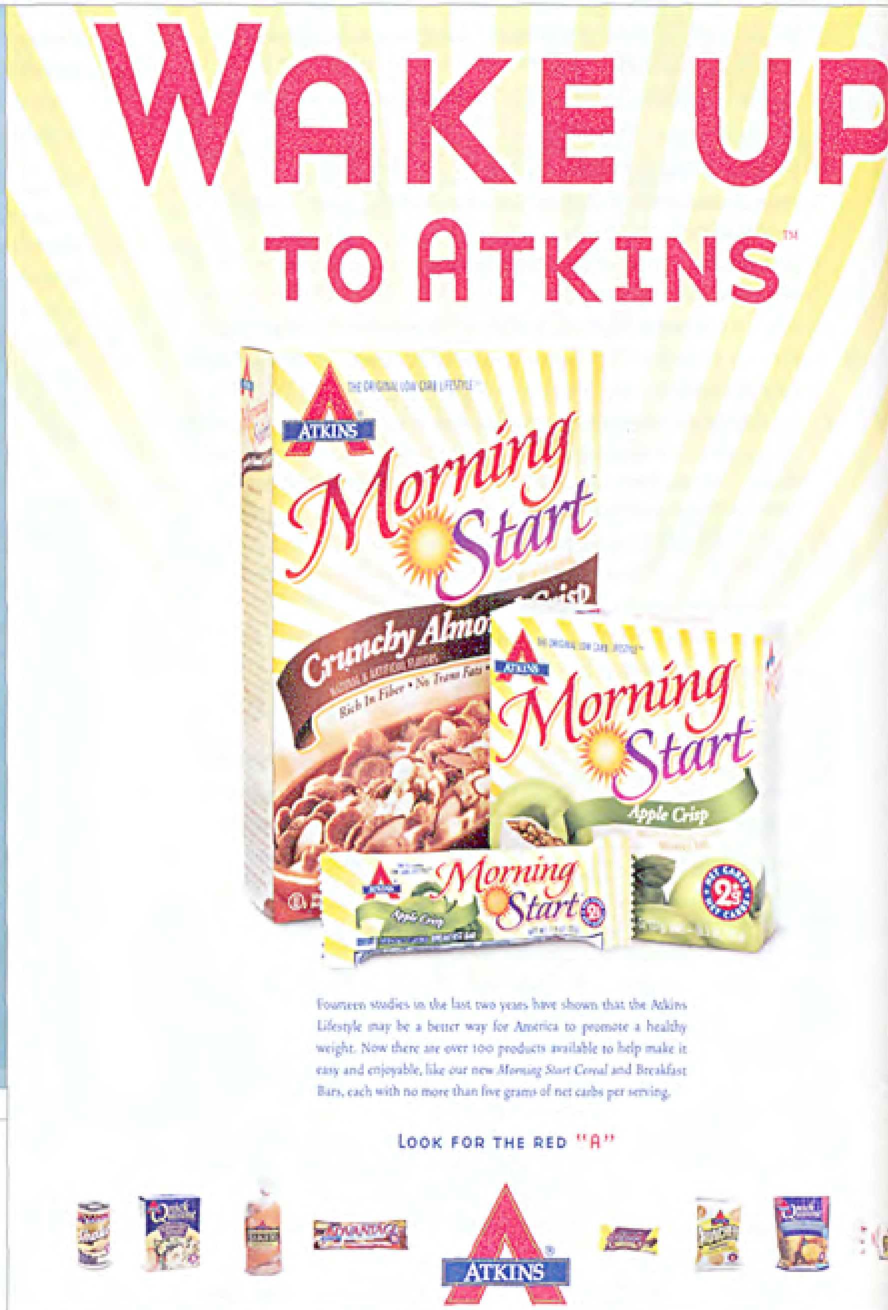
PART 2

CAPTURING MARKETING INSIGHTS

IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What are the components of a modern marketing information system?
2. What are useful internal records?
3. What is involved in a marketing intelligence system?
4. What are the key methods for tracking and identifying opportunities in the macroenvironment?
5. What are some important macroenvironment developments?



CHAPTER 3 ::: GATHERING INFORMATION AND SCANNING THE ENVIRONMENT

Developing and implementing marketing plans involves a number of decisions. Making those decisions is both an art and a science. To provide insight into and inspiration for marketing decision making, companies must possess comprehensive, up-to-date information on macro trends as well as more micro effects particular to their business. Holistic marketers recognize that the marketing environment is constantly presenting new opportunities and threats, and they understand the importance of continuously monitoring and adapting to that environment.

Obesity has officially been called an epidemic by the Centers for Disease Control (CDC): 30 percent of U.S adults are considered obese and its prevalence among kids age 6 to 11 has quadrupled since the 1970s. Obesity is caused by several factors—poor eating habits, a lack of exercise, and sedentary lifestyles—but there has been increased scrutiny of the $200 billion packaged-foods industry. Company responses have taken all forms. Frito-Lay reformulated its entire line of chips and pretzels so that they had zero grams of trans fat. Nestlé has been looking for growth with nutritionally enhanced products that cross food and pharmaceuticals, dubbed "phood." The company sells a breakfast bar called Nesvital containing carbohydrates that are absorbed quickly and make people feel full more quickly. The low-carbohydrate craze drove the sales of products like >>>

An ad for Atkins Nutritionals breakfast products.

Michelob Ultra and Miller Lite beer (which happily proclaimed it contained half the carbs of category leader Bud Light) and a whole line of products from Atkins Nutritionals.[1]

The food industry isn't alone in having to make adjustments. The sales slump in the apparel sector has been attributed in part to a failure to properly design and size clothing to reflect a wider variety of American shapes, sizes, and cultures.[2] In this chapter, we consider how firms can develop processes to track trends. We also identify a number of important macroenvironment trends. Chapter 4 reviews how marketers can conduct more customized research that addresses specific marketing problems or issues.

::: Components of a Modern Marketing Information System

The major responsibility for identifying significant marketplace changes falls to the company's marketers. More than any other group in the company, they must be the trend trackers and opportunity seekers. Although every manager in an organization needs to observe the outside environment, marketers have two advantages: They have disciplined methods for collecting information and they also spend more time interacting with customers and observing competition.

Some firms have developed marketing information systems that provide management with rich detail about buyer wants, preferences, and behavior.

DUPONT

DuPont commissioned marketing studies to uncover personal pillow behavior for its Dacron Polyester unit, which supplies filling to pillow makers and sells its own Comforel brand. One challenge is that people don't give up their old pillows: 37 percent of one sample described their relationship with their pillow as being like "an old married couple," and an additional 13 percent characterized it as being like a "childhood friend." They found that people fell into distinct groups in terms of pillow behavior: stackers (23%), plumpers (20%), rollers or folders (16%), cuddlers (16%), and smashers, who pound their pillows into a more comfy shape (10%). Women were more likely to plump, whereas men were more likely to fold. The prevalence of stackers led the company to sell more pillows packaged as pairs, as well as to market different levels of softness or firmness.[3]

Marketers also have extensive information about how consumption patterns vary across countries. On a per capita basis within Western Europe, for example, the Swiss consume the most chocolate, the Greeks eat the most cheese, the Irish drink the most tea, and the Austrians smoke the most cigarettes.

Nevertheless, many business firms are not sophisticated about gathering information. Many do not have a marketing research department. Others have a department that limits its work to routine forecasting, sales analysis, and occasional surveys. Many managers complain about not knowing where critical information is located in the company; getting too much information that they cannot use and too little that they really need; getting important information too late; and doubting the information's accuracy. Companies with superior information enjoy a competitive advantage. The company can choose its markets better, develop better offerings, and execute better marketing planning.

TABLE 3.1

Information Needs Probes

1. What decisions do you regularly make?
2. What information do you need to make these decisions?
3. What information do you regularly get?
4. What special studies do you periodically request?
5. What information would you want that you are not getting now?
6. What information would you want daily? Weekly? Monthly? Yearly?
7. What magazines and trade reports would you like to see on a regular basis?
8. What topics would you like to be kept informed of?
9. What data analysis programs would you want?
10. What are the four most helpful improvements that could be made in the present marketing information system?

Every firm must organize and distribute a continuous flow of information to its marketing managers. Companies study their managers' information needs and design marketing information systems (MIS) to meet these needs. A **marketing information system (MIS)** consists of people, equipment, and procedures to gather, sort, analyze, evaluate, and distribute needed, timely, and accurate information to marketing decision makers. A marketing information system is developed from internal company records, marketing intelligence activities, and marketing research. The first two topics are discussed here; the latter topic is reviewed in the next chapter.

The company's marketing information system should be a cross between what managers think they need, what managers really need, and what is economically feasible. An internal MIS committee can interview a cross section of marketing managers to discover their information needs. Table 3.1 displays some useful questions.

::: Internal Records and Marketing Intelligence

Marketing managers rely on internal reports on orders, sales, prices, costs, inventory levels, receivables, payables, and so on. By analyzing this information, they can spot important opportunities and problems.

The Order-to-Payment Cycle

The heart of the internal records system is the order-to-payment cycle. Sales representatives, dealers, and customers send orders to the firm. The sales department prepares invoices and transmits copies to various departments. Out-of-stock items are back ordered. Shipped items are accompanied by shipping and billing documents that are sent to various departments.

Today's companies need to perform these steps quickly and accurately. Customers favor firms that can promise timely delivery. Customers and sales representatives fax or e-mail their orders. Computerized warehouses quickly fill these orders. The billing department sends out invoices as quickly as possible. An increasing number of companies are using the Internet and extranets to improve the speed, accuracy, and efficiency of the order-to-payment cycle.

Sales Information Systems

Marketing managers need timely and accurate reports on current sales. Wal-Mart, for example, knows the sales of each product by store and total each evening. This enables it to transmit nightly orders to suppliers for new shipments of replacement stock. Wal-Mart shares its sales data with its larger suppliers such as P&G and expects P&G to re-supply Wal-Mart stores in a timely manner. Wal-Mart has entrusted P&G with the management of its inventory.[4]

Companies must carefully interpret the sales data so as not to get the wrong signals. Michael Dell gave this illustration: "If you have three yellow Mustangs sitting on a dealer's lot and a customer wants a red one, the salesman may be really good at figuring out how to sell the yellow Mustang. So the yellow Mustang gets sold, and a signal gets sent back to the factory that, hey, people want yellow Mustangs."

Technological gadgets are revolutionizing sales information systems and allowing representatives to have up-to-the-second information. In visiting one of the 10,000 golf shops around the country, sales reps for TaylorMade used to spend up to two hours counting golf clubs in stock before filling new orders by hand. Since the company gave its reps handheld devices with bar-code readers and Internet connections, the reps now simply point their handhelds at the bar codes and automatically tally inventory. By using the two hours they save to focus on boosting sales to retail customers, sales reps improved productivity by 20 percent.[5]

Databases, Data Warehousing, and Data Mining

Today companies organize their information in databases—customer databases, product databases, salesperson databases—and then combine data from the different databases. For example, the customer database will contain every customer's name, address, past transactions, and even demographics and psychographics (activities, interests, and opinions) in some instances. Instead of a company sending a mass "carpet bombing" mailing of a new offer to every customer in its database, it will score the different customers according to purchase recency, frequency, and monetary value. It will send the offer only to the highest scoring customers. Besides saving on mailing expenses, this will often achieve a double-digit response rate.

PIZZA HUT

Pizza Hut claims to have the largest fast-food customer data warehouse in the world, with 40 million U.S. households—or between 40 and 50 percent of the U.S. market. The millions of customer records are gleaned from point-of-sale transactions at its restaurants. Pizza Hut can slice and dice data by favorite toppings, date of last order, or by whether you order a salad with your pepperoni pizza. Using its Teradata Warehouse Miner, Pizza Hut has not only been able to purge expensive duplicates from its direct-mail campaigns, but can also target its marketing to find the best coupon offers for each household and predict the success of campaigns.[6]

Companies warehouse these data and make them easily accessible to decision makers. Furthermore, by hiring analysts skilled in sophisticated statistical methods, they can "mine" the data and garner fresh insights into neglected customer segments, recent customer trends, and other useful information. The customer information can be cross-tabbed with product and salesperson information to yield still deeper insights. To manage all the different databases efficiently and effectively, more firms are using business integration software (see "Marketing Insight: Putting Data to Work with Business Integration Software").

Using its own in-house technology, for example, Wells Fargo has developed the ability to track and analyze every bank transaction made by its 10 million retail customers—whether at ATMs, bank branches, or online. When transaction data are combined with personal information provided by customers, Wells Fargo can come up with targeted offerings to coincide with a customer's life-changing event. As a result, compared with the industry average of 2.2 products per customer, Wells Fargo sells 4.[7]

The Marketing Intelligence System

The internal records system supplies *results* data, but the marketing intelligence system supplies *happenings* data. A **marketing intelligence system** is a set of procedures and sources managers use to obtain everyday information about developments in the marketing environment. Marketing managers collect marketing intelligence by reading books, newspapers, and trade publications; talking to customers, suppliers, and distributors; and meeting with other company managers.

A company can take several steps to improve the quality of its marketing intelligence.

- ***A company can train and motivate the sales force to spot and report new developments.*** Sales representatives are positioned to pick up information missed by other means, yet they often fail to pass on that information. The company must "sell" its sales force on their impor-

MARKETING INSIGHT | PUTTING DATA TO WORK WITH BUSINESS INTEGRATION SOFTWARE

In the 1990s, companies spent billions installing giant databases and data warehouses and then enormous sums on consultants trying to make sense of it all. A typical large retailer now has 80 terabytes worth of stored information—equivalent to 16 million digital photos or 320 miles of bookshelves. Wal-Mart has a staggering 285 terabytes in its data warehouse.

But data have value only if they can be used. As one analyst put it, "It's like having a bank account with millions of dollars in it but no ATM card. If you can't get it out and can't make it work for you, then it is not really useful." Business integration (BI) software is designed to analyze and interpret massive quantities of data. Typical BI applications cull information out of giant databases and put them into "data marts"—smaller clusters of similar information. Breaking data down in this way helps to more easily and thoroughly diffuse information through the organization.

Consider how business integration software allows Ben & Jerry's to monitor a pint of ice cream from inception to consumption. At Ben & Jerry's headquarters in Burlington, Vermont, each pint of ice cream is stamped after manufacture and its tracking number put in an Oracle database. Using Business Objects software, the sales team can then see which flavors are generating the most sales (Cherry Garcia is a perennial favorite). The marketing department can check to see whether orders online require additional philanthropic donations. The finance people are able to record sales and close their books more quickly. Consumer affairs can match up the pints with the roughly 225 calls and e-mails the company receives each week to make sure there are not systematic problems with any particular ingredients.

BI software is seen as relatively inexpensive and convenient to install, and the results can show up quickly. The Sesame Workshop installed the software for the 2003 holiday season to track its Elmo dolls and was able to cut its back orders by a third. Red Robin Gourmet Burgers, a 196-location chain, used BI software to fine-tune its marketing and operations. It found it was wasting thousands on unused sauces. Staples long devoted space to high-margin furniture. With BI, it found that small items were more profitable. Successes like these are why the market for business integration software is expected to reach $7.5 billion in 2006.

Source: Adapted from Julie Schlosser, "Looking for Intelligence in Ice Cream," *Fortune*, March 17, 2003, pp. 114–120.

tance as intelligence gatherers. Sales reps should know which types of information to send to which managers. Grace Performance Chemicals, a division of W. R. Grace, supplies materials and chemicals to the construction and packaging industries. Grace sales reps were instructed to observe the innovative ways customers used its products to suggest possible new products. For example, some customers were using Grace waterproofing materials to soundproof their cars and patch boots and tents. Seven new-product ideas emerged in total, worth millions in sales to the company.[8]

- ***A company can motivate distributors, retailers, and other intermediaries to pass along important intelligence.*** Many companies hire specialists to gather marketing intelligence. Service providers often send mystery shoppers to their stores to assess how employees treat customers. Mystery shoppers for McDonald's discovered that only 46 percent of its restaurants nationwide met internal speed-of-service standards, forcing the company to rethink processes and training.[9] Retailers also use mystery shoppers. Neiman Marcus employs a professional shopper agency to shop at its stores nationwide. It finds stores that consistently score high on the service have the best sales. Typical questions their mystery shoppers report on are: How long before a sales associate greeted you? Did the sales associate act as if he or she wanted your business? Was the sales associate knowledgeable about products in stock?[10]

- ***A company can network externally.*** It can purchase competitors' products; attend open houses and trade shows; read competitors' published reports; attend stockholders' meetings; talk to employees, dealers, distributors, suppliers, and freight agents; collect competitors' ads; and look up news stories about competitors. Software developer Cognos created an internal Web site called Street Fighter where any of the firm's 3,000 workers can submit scoops about competitors and win prizes.[11] Competitive intelligence must be done legally and ethically, though. Procter & Gamble reportedly paid a multimillion-dollar settlement to Unilever when some external operatives hired as part of a P&G corporate intelligence program to learn about Unilever's hair care products were found to have engaged in such unethical behavior as "dumpster diving."[12]

- ***A company can set up a customer advisory panel.*** Members might include representative customers or the company's largest customers or its most outspoken or sophisticated customers. Many business schools have advisory panels made up of alumni and recruiters who provide valuable feedback on the curriculum.

TABLE 3.2

Secondary Commercial Data Sources

- Nielsen Company: Data on products and brands sold through retail outlets (Retail Index Services), supermarket scanner data (Scantrack), data on television audiences (Media Research Services), magazine circulation data (Neodata Services, Inc.), and others.
- MRCA Information Services: Data on weekly family purchases of consumer products (National Consumer Panel) and data on home food consumption (National Menu Census).
- Information Resources, Inc.: Supermarket scanner data (InfoScan) and data on the impact of supermarket promotions (PromotioScan).
- SAMI/Burke: Reports on warehouse withdrawals to food stores in selected market areas (SAMI reports) and supermarket scanner data (Samscam).
- Simmons Market Research Bureau (MRB Group): Annual reports covering television markets, sporting goods, and proprietary drugs, with demographic data by sex, income, age, and brand preferences (selective markets and media reaching them).
- Other commercial research houses selling data to subscribers include the Audit Bureau of Circulation; Arbitron, Audits and Surveys; Dun & Bradstreet's; National Family Opinion; Standard Rate & Data Service; and Starch.

- ***A company can take advantage of government data resources.*** The 2000 U.S. census provides an in-depth look at the population swings, demographic groups, regional migrations, and changing family structure of 281,421,906 people. Census marketer Claritas cross-references census figures with consumer surveys and its own grassroots research for clients such as Procter & Gamble, Dow Jones, and Ford Motor. Partnering with "list houses" that provide customer phone and address information, Claritas can help firms select and purchase mailing lists with specific clusters.[13]
- ***A company can purchase information from outside suppliers.*** Well-known data suppliers include the A.C. Nielsen Company and Information Resources, Inc. (see Table 3.2). These research firms gather consumer-panel data at a much lower cost than the company could manage on its own. Biz360 has specialized databases to provide reports from 7,000 sources on the extent and nature of media coverage a company is receiving.[14]
- ***A company can use online customer feedback systems to collect competitive intelligence.*** Online customer feedback facilitates collection and dissemination of information on a global scale, usually at low cost. Through online customer review boards or forums, one customer's evaluation of a product or a supplier can be distributed to a large number of other potential buyers and, of course, to marketers seeking information on the competition. Currently existing channels for feedback include message boards, threaded discussion forums that allow users to post new and follow up existing posts; discussion forums, which are more like bulletin boards; opinion forums, which feature more in-depth, lengthy reviews; and chat rooms. While chat rooms have the advantage of allowing users to share experiences and impressions, their unstructured nature makes it difficult for marketers to find relevant messages. To address this issue, various companies have adopted structured systems, such as customer discussion boards or customer reviews. See "Marketing Memo: Clicking on the Competition" for a summary of the major categories of structured online feedback systems.[15]

Some companies circulate marketing intelligence. The staff scans the Internet and major publications, abstracts relevant news, and disseminates a news bulletin to marketing managers. It collects and files relevant information and assists managers in evaluating new information.

::: Analyzing the Macroenvironment

Successful companies recognize and respond profitably to unmet needs and trends. Companies could make a fortune if they could solve any of these problems: a cure for cancer; chemical cures for mental diseases; desalinization of seawater; nonfattening, tasty nutritious food; practical electric cars; and affordable housing.

MARKETING MEMO | CLICKING ON THE COMPETITION

There are four main ways marketers can find relevant online information on competitors' product strengths and weaknesses, and summary comments and overall performance rating of a product, service, or supplier.

- ***Independent customer goods and service review forums.*** These forums include well-known Web sites such as Epinions.com, Rateital.com, Consumerreview.com, and Bizrate.com. Bizrate.com combines consumer feedback from two sources: its 1.2 million members who have volunteered to provide ratings and feedback to assist other shoppers, and survey results on service quality collected from customers of stores listed in Bizrate. These sites have the advantage of being independent from the goods and service providers, which may reduce bias.
- ***Distributor or sales agent feedback sites.*** These sites offer both positive and negative product or service reviews, but the stores or distributors have built the sites themselves. Amazon.com, for instance, offers an interactive feedback opportunity through which buyers, readers, editors, and others may review all products listed in the site, especially books. Elance.com is an online professional services provider that allows contractors to describe their level of satisfaction with subcontractors and provide details of their experiences.
- ***Combo-sites offering customer reviews and expert opinions.*** This type of site is concentrated in financial services and high-tech products that require professional knowledge. Zdnet.com, an online advisor on technology products, offers customer comments and evaluations based on ease of use, features, and stability, along with expert reviews. Zdnet summarizes the number of positive and negative evaluations and total download numbers within a certain period (commonly a week or a month) for each software program. The advantage of this type of review site lies in the fact that a product supplier can compare opinions from the experts with those from consumers.
- ***Customer complaint sites.*** These forums are designed mainly for dissatisfied customers. Reviewers at most opinion sites tend to offer positive comments due to financial incentives and potential lawsuits for slanderous or libelous negative comments. In contrast, some Web sites offer a complaining forum with a moderator. For instance, Planetfeedback.com allows customers to voice unfavorable experiences with specific companies. Another site, Complaints.com, is devoted to customers who want to vent their frustrations with particular firms or their offerings.

Source: Adapted from Robin T. Peterson and Zhilin Yang, "Web Product Reviews Help Strategy," *Marketing News*, April 7, 2004, p. 18.

Needs and Trends

Enterprising individuals and companies manage to create new solutions to unmet needs. FedEx was created to meet the need for next-day mail delivery. Dockers was created to meet the needs of baby boomers who could no longer really wear—or fit into!—their jeans and wanted a physically and psychologically comfortable pair of pants. Amazon was created to offer more choice and information for books and other products.

We can draw distinctions among fads, trends, and megatrends. A **fad** is "unpredictable, short-lived, and without social, economic, and political significance." A company can cash in on a fad such as Beanie Babies, Furbies, and Tickle Me Elmo dolls, but this is more a matter of luck and good timing than anything else.[16]

A **trend** is a direction or sequence of events that has some momentum and durability. Trends are more predictable and durable than fads. A trend reveals the shape of the future and provides many opportunities. For example, the percentage of people who value physical fitness and well-being has risen steadily over the years, especially in the under-30 group, the young women and upscale group, and people living in the West. Marketers of health foods and exercise equipment cater to this trend with appropriate products and communications.

Megatrends have been described as "large social, economic, political and technological changes [that] are slow to form, and once in place, they influence us for some time—between seven and ten years, or longer."[17] See "Marketing Insight: Ten Megatrends Shaping the Consumer Landscape" for a look into the forces in play during the next decade or so.

Trends and megatrends merit close attention. A new product or marketing program is likely to be more successful if it is in line with strong trends rather than opposed to them, but detecting a new market opportunity does not guarantee success, even if it is technically feasible. For example, today some companies sell portable "electronic books"; but there may not be a sufficient number of people interested in reading a book on a computer screen or willing to pay the required price. This is why market research is necessary to determine an opportunity's profit potential.

To help marketers spot cultural shifts that might bring new opportunities or threats, several firms offer social-cultural forecasts. The Yankelovich Monitor interviews 2,500 people nationally

MARKETING INSIGHT | TEN MEGATRENDS SHAPING THE CONSUMER LANDSCAPE

- ***Aging Boomers.*** As baby boomers grow older, their impact on consumer spending can hardly be overstated. That's because unlike previous generations, boomers are deciding to delay the aging process and will continue to earn and spend as they age.
- ***Delayed Retirement.*** Baby boomers have delayed every life stage transition, such as getting married and having children. So it's highly likely that they will also delay their retirement. Between 2000 and 2010, the Bureau of Labor Statistics forecasts a 33 percent increase in the number of people ages 65 to 74 in the workforce.
- ***The Changing Nature of Work.*** More than half of all U.S. workers are employed in management, in professional or related occupations, or in a sales or other office-based position.
- ***Greater Educational Attainment—Especially Among Women.*** With so many jobs requiring intellectual skills, the number of high school graduates attending college is rising. While men and women are equally likely to graduate from high school, women are more likely to attend college. The long-term implications of this trend are that people with a college education will have higher lifetime incomes, and there should be an increase in women's earning power.
- ***Labor Shortages.*** Although more service workers are needed in suburban areas, fewer people can afford to live there. Suburban locales will turn to service automation or a greater reliance on immigrant labor.
- ***Increased Immigration.*** Based on Census 2000, the Census Bureau estimated that 40 percent of the nation's population growth was due to immigration. As our citizens age, the population growth for newborns will be outpaced by the growth due to immigration.
- ***Rising Hispanic Influence.*** Already the largest minority group in the United States, with 35 million people, the Hispanic population is projected by the Census Bureau to increase 35 percent in this decade. Though Hispanic households represented only 9 percent of U.S. households in 2000, they accounted for 20 percent of the 4 million children born in this country that year.
- ***Shifting Birth Trends.*** These are represented by three mini-trends: (1) the increasing incidence of births by older women—35 and older—who have higher spending power, (2) the declining number of births by teenagers, and (3) the rising diversity among young children. About two-thirds of women of childbearing age are non-Hispanic whites, but they accounted for less than half (43.5%) of births in 2000.
- ***Widening Geographic Differences.*** This trend has two elements. There is an increasing demographic difference between cities, suburbs, and rural areas, along with a rise in distinctive regional consumer markets. For example, the very low population growth in New England has led to a median age of 37.1 in that region compared to a median age of 32.3 in Texas or 33.3 in California. Non-Hispanic whites make up 84 percent of total population in New England but only 53 percent of population in the West.
- ***Changing Age Structure.*** In the future the differences in size between one age cohort and the next will be much smaller. Over the next decade there is likely to be only a slight change, 1 percent or less annually, in the number of consumers in each age cohort younger than 35.

Source: Adapted from Peter Francese, "Top Trends for 2003," *American Demographics* (December 2002/January 2003): 48–51.

each year and has tracked 35 social trends since 1971, such as "anti-bigness," "mysticism," "living for today," "away from possessions," and "sensuousness." It describes the percentage of the population who share the attitude as well as the percentage who do not.

Identifying the Major Forces

Companies and their suppliers, marketing intermediaries, customers, competitors, and publics all operate in a macroenvironment of forces and trends that shape opportunities and pose threats. These forces represent "noncontrollables," which the company must monitor and to which it must respond. In the economic arena, companies and consumers are increasingly affected by global forces (see Table 3.3).

The beginning of the new century brought a series of new challenges: the steep decline of the stock market, which affected savings, investment, and retirement funds; increasing unemployment; corporate scandals; and of course, the rise of terrorism. These dramatic events were accompanied by the continuation of other, already-existing longer-term trends that have profoundly influenced the global landscape.

Within the rapidly changing global picture, the firm must monitor six major forces: demographic, economic, social-cultural, natural, technological, and political-legal. Although these forces will be described separately, marketers must pay attention to their interactions, because these will lead to new opportunities and threats. For example, explosive population growth (demographic) leads to more resource depletion and pollution (natural), which leads consumers to call for more laws (political-legal), which stimulate new technological solutions and products (technological), which, if they are affordable (economic), may actually change attitudes and behavior (social-cultural).

TABLE 3.3

Global Forces Affecting Marketing

1. The substantial speedup of international transportation, communication, and financial transactions, leading to the rapid growth of world trade and investment, especially tripolar trade (North America, Western Europe, Far East).
2. The movement of manufacturing capacity and skills to lower-cost countries.
3. The rise of trade blocs such as the European Union and the NAFTA signatories.
4. The severe debt problems of a number of countries, along with the increasing fragility of the international financial system.
5. The increasing use of barter and countertrade to support international transactions.
6. The move toward market economies in formerly socialist countries along with rapid privatization of publicly owned companies.
7. The rapid dissemination of global lifestyles.
8. The development of emerging markets, namely, China, India, Eastern Europe, the Arab countries, and Latin America.
9. The increasing tendency of multinationals to transcend locational and national characteristics and become transnational firms.
10. The increasing number of cross-border corporate strategic alliances—for example, airlines.
11. The increasing ethnic and religious conflicts in certain countries and regions.
12. The growth of global brands across a wide variety of industries such as autos, food, clothing, and electronics.

::: The Demographic Environment

Demographic trends are highly reliable for the short and intermediate run. There is little excuse for a company's being suddenly surprised by demographic developments. The Singer Company should have known for years that its sewing machine business would be hurt by smaller families and more working wives, yet it was slow in responding.

The main demographic force that marketers monitor is *population*, because people make up markets. Marketers are keenly interested in the size and growth rate of population in cities, regions, and nations; age distribution and ethnic mix; educational levels; household patterns; and regional characteristics and movements.

Worldwide Population Growth

The world population is showing explosive growth: It totaled 6.1 billion in 2000 and will exceed 7.9 billion by the year 2025.[18] Here is an interesting picture:

> If the world were a village of 1,000 people, it would consist of 520 women and 480 men, 330 children, and 60 people over age 65, 10 college graduates and 335 illiterate adults. The village would contain 52 North Americans, 55 Russians, 84 Latin Americans, 95 East and West Europeans, 124 Africans, and 584 Asians. Communication would be difficult because 165 people would speak Mandarin, 86 English, 83 Hindi/Urdu, 64 Spanish, 58 Russian, and 37 Arabic, and the rest would speak one of over 200 other languages. There would be 329 Christians, 178 Moslems, 132 Hindus, 62 Buddhists, 3 Jews, 167 nonreligious, 45 atheists, and 86 others.[19]

The population explosion has been a source of major concern. Unchecked population growth and consumption could eventually result in insufficient food supply, depletion of key minerals, overcrowding, pollution, and an overall deterioration in the quality of life. Moreover, population growth is highest in countries and communities that can least afford it. The less developed regions of the world currently account for 76 percent of the world population and are growing at 2 percent per year, whereas the population in the more developed countries is growing at only 0.6 percent per year. In developing countries, the death rate has been falling as a result of modern medicine, but the birthrate has remained fairly stable. Feeding, clothing, and educating children, while also providing a rising standard of living, is nearly impossible in these countries.

A Mattel ad in Chinese for its Hot Wheels toy. The headline reads: "Hot Wheels Performance Tracks—Great Varieties, Great Challenges!"

Explosive population growth has major implications for business. A growing population does not mean growing markets unless these markets have sufficient purchasing power. Nonetheless, companies that carefully analyze their markets can find major opportunities. For example, to curb its skyrocketing population, the Chinese government has passed regulations limiting families to one child. One consequence of these regulations: These children are spoiled and fussed over as never before. Known in China as "little emperors," Chinese children are being showered with everything from candy to computers as a result of the "six pocket syndrome." As many as six adults—parents, grandparents, great-grandparents, and aunts and uncles—may be indulging the whims of each child. This trend has encouraged toy companies, such as Japan's Bandai Company, Denmark's Lego Group, and the U.S.'s Hasbro and Mattel to aggressively enter the Chinese market.[20]

Population Age Mix

National populations vary in their age mix. At one extreme is Mexico, a country with a very young population and rapid population growth. At the other extreme is Japan, a country with one of the world's oldest populations. Milk, diapers, school supplies, and toys would be important products in Mexico. Japan's population would consume many more adult products.

However, there is a global trend toward an aging population. According to a survey in *The Economist,* more people will grow old in this century than ever before. In 2004 or 2005, the population of people aged 60 or over will surpass the proportion of under fives, and there are unlikely to ever again be more toddlers than seniors. It is the start of what the Japanese are calling The Silver Century. The graying of the population is affected by another trend, the widespread fall in fertility rates. In most countries, women are not having enough babies to replace the people who die. The result will be fewer working people to replace those who retire. In a decade's time, many countries—Japan, the United States, and the European countries, for instance—will face the huge problem of having to support a vastly larger population of elderly people.[21]

A population can be subdivided into six age groups: preschool, school-age children, teens, young adults age 25 to 40, middle-aged adults age 40 to 65, and older adults age 65 and up. For marketers, the most populous age groups shape the marketing environment. In the United States, the "baby boomers," the 78 million people born between 1946 and 1964, are one of the most powerful forces shaping the marketplace. Baby boomers are fixated on their youth, not their age.

With many baby boomers well into their fifties and even the last wave turning 40, demand for products to turn back the hands of time has exploded. According to one survey, half of all boomers were depressed that they were no longer young and nearly one in five were actively resisting the aging process. The 40-plus age group will be 60 percent bigger than the 18 to 39 group by 2010, and it now controls three-quarters of the country's wealth. As they search for the fountain of youth, sales of hair replacement and coloring aids, health club memberships, home gym equipment, skin-tightening creams, nutritional supplements, and organic foods have all soared.[22]

Boomers grew up with TV advertising, so they are an easier market to reach than the 45 million born between 1965 and 1976, dubbed Generation X (and also the shadow generation, twenty-somethings, and baby busters).[23] Generation-Xers are typically cynical about hard-sell marketing pitches that promise more than they can deliver, but some marketers have been able to break through.

VW

Volkswagen sales in the United States rose from under 50,000 cars in 1993 to over 300,000 a decade later partly as a result of a "Drivers Wanted" ad campaign that targeted fun-loving or youthful drivers. Rather than appealing to the mass market, VW went after a younger demographic willing to spend a little extra on a Volkswagen because of the car's German engineering, sportier image, and versatility. The voiceover on the introductory TV spot identifies the target audience by saying, "On the road of life, there are passengers and there are drivers."[24]

Both baby boomers and Generation-Xers will be passing the torch to the latest demographic group, Generation Y or the echo boomers, born between 1977 and 1994. Now numbering 72 million, this group is almost equal in size to baby boomers. One distinguishing characteristic of this age group is their utter fluency and comfort with computer and Internet technology. Don Tapscott has christened them "Net-Gens" for this reason. He says: "To them, digital technology is no more intimidating than a VCR or a toaster."[25]

Ethnic and Other Markets

Countries also vary in ethnic and racial makeup. At one extreme is Japan, where almost everyone is Japanese; at the other is the United States, where people come from virtually all nations. The United States was originally called a "melting pot," but there are increasing signs that the melting didn't occur. Now people call the United States a "salad bowl" society, with ethnic groups maintaining their ethnic differences, neighborhoods, and cultures.

According to the 2000 census, the U.S. population of 276.2 million was 72 percent white. African Americans constituted 13 percent, and Latinos 11 percent. The Latino population had been growing fast, with the largest subgroups of Mexican (5.4 percent), Puerto Rican (1.1 percent), and Cuban (0.4 percent) descent. Asian Americans constituted 3.8 percent of the U.S. population, with the Chinese as the largest group, followed by the Filipinos, Japanese, Asian Indians, and Koreans, in that order. Latino and Asian American consumers are concentrated in the far western and southern parts of the country, although some dispersal is taking place. Moreover, there were nearly 25 million people living in the United States—more than 9 percent of the population—who were born in another country.

A frequently noted megatrend, the increase in the percentage of Hispanics in the total population, represents a major shift in the nation's center of gravity. Hispanics made up half of all new workers in the past decade and will bump up to 25 percent of workers in two generations. Despite their lagging family incomes, Hispanic buying power is soaring. Disposable income has jumped 29 percent since 2001, to $652 billion in 2003—double the pace of the rest of the population. From the food Americans eat, to the clothing they wear, the music they listen to, and the cars they buy, Hispanics are having a huge impact. Companies are scrambling to refine their products and their marketing to reach this fastest-growing and most influential consumer group:[26]

- ***Procter & Gamble.*** In 2000 the company set up a 65-person bilingual team to better target Latino consumers. Now the company tailors its products to appeal to Latino tastes. For example, it added a third scent to its Gain detergent called "White Water Fresh" after finding that 57 percent of Latinos like to smell their purchases.
- ***Kroger.*** The nation's number-one grocery chain spent $1.8 million to convert its 59,000 square-foot Houston store into a *Supermercado* with Spanish-language signage and products such as plantain leaves and Mexican cocoa. The company has also expanded its private-label Buena Comida line to 105 different items.
- ***PacifiCare Health Systems.*** When this Cypress, California–based insurance company found that 20 percent of its 3 million policyholders are Hispanic, it set up a new unit, Latino Health Solutions. The unit markets PacifiCare health insurance products in Spanish, directs Hispanics to Spanish-speaking doctors, and translates documents into Spanish for Hispanic workers.

Ethnic groups have certain specific wants and buying habits. Several food, clothing, and furniture companies have directed their products and promotions to one or more of these groups.[27] Charles Schwab is one of the leading financial services firms serving Asian Americans with a carefully targeted marketing program.[28]

CHARLES SCHWAB

San Francisco–based Charles Schwab recognized the growing power of the Asian consumer after the 1990 census. It now employs over 200 people who speak Chinese, Korean, and Vietnamese at call centers dedicated to Asian American customers who either want to communicate in their own languages or to whom cultural affinity is important. There is a Chinese-language Web site for trading, research, and online news service. Fourteen Schwab branches are found in predominantly Asian neighborhoods across the country. The company also advertises on Asian TV channels, in newspapers, on radio, and at online community Web sites.

Yet marketers must be careful not to overgeneralize about ethnic groups. Within each ethnic group are consumers who are quite different from each other. "There is really no such thing as an Asian market," says Greg Macabenta, whose ethnic advertising agency specializes in the Filipino market. Macabenta emphasizes that the five major Asian American groups have their own very specific market characteristics, speak different languages, consume different cuisines, practice different religions, and represent very distinct national cultures.[29]

The home page of Schwab's Chinese-language Web site. Customers who prefer to use Chinese can trade, do research, and get the latest news.

Diversity goes beyond ethnic and racial markets. More than 50 million Americans have disabilities, and they constitute a market for home delivery companies such as Peapod, and for various medical services.

Educational Groups

The population in any society falls into five educational groups: illiterates, high school dropouts, high school diplomas, college degrees, and professional degrees. In Japan, 99 percent of the population is literate, whereas in the United States 10 to 15 percent of the population may be functionally illiterate. However, the United States has one of the world's highest percentages of college-educated citizens, around 36 percent. The high number of educated people in the United States spells a high demand for quality books, magazines, and travel, and a high supply of skills.

BRAND NAME UNIVERSITIES

The higher levels of educational attainment in the United States have led to both an increased emphasis on marketing to college students and the increased marketing of colleges and universities as definable "brands." Heightened competition for the top students and concerns about institutions' reputations and rankings are prompting these institutions to create a brand image. No one disputes the strength of the "Harvard" name as a symbol of educational excellence and preeminence. Bottom-line pressures due to tuition discounting and comparative shopping by prospective students and their parents are encouraging lesser-known colleges to take a market-oriented approach. Georgia Tech defines itself as the "twenty-first-century technology university" by focusing on its quality programs, cutting-edge research, and aggressive technology transfer. Clark University in Worcester, Massachusetts, emphasizes its size (Clark is among the smallest of the major research universities), its history as an innovator, and a student body comprised of individuals who are obsessed with their own areas of interest.[30]

Household Patterns

The "traditional household" consists of a husband, wife, and children (and sometimes grandparents). Yet, in the United States today, one out of eight households is "diverse" or "nontraditional," and includes single live-alones, adult live-togethers of one or both sexes, single-parent families, childless married couples, and empty-nesters. More people are divorcing or separating, choosing not to marry, marrying later, or marrying without the intention to have children. Each group has a distinctive set of needs and buying habits. For example, people in the SSWD group (single, separated, widowed, divorced) need smaller apartments; inexpensive and smaller appliances, furniture, and furnishings; and smaller-size food packages. Marketers must increasingly consider the special needs of nontraditional households, because they are now growing more rapidly than traditional households.

Married couple households—the dominant cohort since the formation of the United States—have slipped from nearly 80 percent in the 1950s to around 50 percent today. Americans are delaying marriage longer than ever, cohabiting in greater numbers, forming more same-sex partnerships, living far longer, and remarrying less after splitting up. By 2010, nearly 30 percent of homes will be inhabited by someone who lives alone. A record number of children—33 percent—are now born to single parents, many of them underemployed mothers. But singles can also have much buying power and spend more on themselves than those who live in larger households. Products such as the George Foreman grill that target people who live alone and value convenience can be successful.[31]

A study by Cava Research Group at the University of Leeds in the United Kingdom emphasizes that single doesn't necessarily mean "alone." Researchers interviewed hundreds of people between the ages of 25 and 60 and concluded that "friends are the new family." They observed a growing trend for "neo-tribes" of 20-somethings to live communally. At the other end of the spectrum, older divorced people were seen centering their lives on their children and friends and keeping their romantic lives separate. This emphasis on friendship can influence marketers in everything from whom they target to how they craft their marketing messages. Travel with friends or with a group, for instance, now appeals to a wider swath of singles than college students on spring break or seniors going off to an elderhostel.[32] Online services are recognizing this trend.

FRIENDSTER.COM

Founded in Sunnyvale, California, in 2003, Friendster connects people for dating, making friends, business propositions, and plain old online voyeurism. The founder of Friendster created it after trying an online dating service and finding that he was not "keen on messaging random weirdoes." The premise of Friendster is that it's better to connect to new people through people you already know. It's the old friend of a friend of a friend strategy for meeting and dating. Users can browse through the profiles of their friends, friends' friends, and so on in their network. With just 20 friends, a user can be linked to 50,000 or more people. The profiles include photos, favorite books, and other interests, along with pictures of their friends on the network. When users find someone interesting, they can see how they are connected and write a note. It's like being the star of your own game of "Six Degrees of Separation"—the notion that anyone can be linked to anyone else in the world via six connections. The site, which is free to members, has about 7 million users and has spawned a number of knock-off social networking sites such as Tribe, Rise, and Google's Orkut.[33]

The gay market is a particularly lucrative segment. Academics and marketing experts estimate that the gay and lesbian population ranges between 4 and 8 percent of the total U.S. population, with an even higher percentage in urban areas.[34] Compared to the average American, respondents who classify themselves as gay are over 10 times more likely to be in professional jobs, almost twice as likely to own a vacation home, eight times more likely to own a computer notebook, and twice as likely to own individual stocks.[35] Companies such as Absolut, American Express, IKEA, Procter & Gamble, and Subaru have recognized the potential of this market and the nontraditional household market as a whole.

GAY.COM

Gays and lesbians are also the perfect online consumer group since they spend up to 10 times longer online than the average Internet user, according to a recent Forrester Research study. It shouldn't be surprising, then, that the number-one American Web site to reach single men with household incomes over $75,000 is *not* CNN sports, but Gay.com. The site pulls in big-name mainstream advertisers such as American Airlines, Viacom, Procter & Gamble, General Motors, and IBM. These smart marketers know that gays and lesbians are among the most brand-loyal of consumers, with 87 percent more likely to give their business to companies that target them specifically. That's why Gay.com's parent company, PlanetOutPartners, has taken an aggressive approach toward advertisers with this pitch: "The average middle-class family spends over $1 million to raise a child through age 22. Some gay people have kids. Most don't. Where are they spending their money? On your products."[36]

Geographical Shifts in Population

This is a period of great migratory movements between and within countries. Forward-looking companies and entrepreneurs are taking advantage of the growth in immigrant populations and marketing their wares specifically to these new members of the population.

Within countries, population movement also occurs as people migrate from rural to urban areas, and then to suburban areas. Although the United States experienced a rural rebound in the 1990s as nonmetropolitan counties attracted large numbers of urban refugees, the twenty-first century saw urban markets grow more rapidly again due to a higher birth rate, a lower death rate, and rapid growth from foreign immigration.[37]

Location makes a difference in goods and service preferences. The movement to the Sunbelt states has lessened the demand for warm clothing and home heating equipment and increased the demand for air conditioning. Those who live in large cities such as New York, Chicago, and San Francisco account for most of the sales of expensive furs, perfumes, luggage, and works of art. These cities also support the opera, ballet, and other forms of culture. Americans living in the suburbs lead more casual lives, do more outdoor living, and have greater neighbor interaction, higher incomes, and younger families. Suburbanites buy vans, home workshop equipment, outdoor furniture, lawn and gardening tools, and outdoor cooking equipment. There are also regional differences: People in Seattle buy more toothbrushes per capita than people in any other U.S. city; people in Salt Lake City eat more candy bars; people from New Orleans use more ketchup; and people in Miami drink more prune juice.

Suburban growth and a disdain for commuting has helped those businesses that cater to the growing SOHO (small office—home office) segment. Nearly 40 million Americans are working out of their homes with the help of electronic conveniences like computers, cell phones, fax machines, and personal organizers. Makers of RTA (ready to assemble) furniture might find a strong consumer base among all the cashed-out former city residents setting up offices in small towns or telecommuting from there to larger companies. One company that is shifting gears to appeal to the SOHO segment is Kinko's Copy Centers.

KINKO'S COPY CENTERS

Founded in the 1970s as a campus photocopying business, Kinko's is now reinventing itself as the well-appointed office outside the home. Where once there were copy machines, the 1,200 Kinko's stores in this country and abroad now feature a mix of fax machines, ultra-fast color printers, and networks of computers equipped with popular software programs and high-speed Internet connections. Kinko's is now a $2 billion company that offers an unprecedented array of office services. People can come to a Kinko's store to do all their office jobs: copy, send and receive faxes, use various programs on the computer, go on the Internet, order stationery and other printed supplies, and even teleconference. And as more people work at home, Kinko's offers an escape from the isolation of the home office. Kinko's acquisition by FedEx in early 2004 resulted in further integration with the overnight delivery pioneer.[38]

Marketers also look at where consumers are gathering. Almost one in two people over the age of five (120 million) moved at least one time between 1995 and 2000, according to a Census 2000 brief. The brief's state-by-state analysis clearly shows that the shift has been toward the Sunbelt states, away from the Midwest and Northeast.[39] From Virginia on down to Florida, and western Sunbelt states such as Texas, Nevada, or Arizona, these "hot" states are luring more roamers. An interesting facet of this trend is that these Sunbelt states are no longer seen solely as retiree meccas, but are luring young people to settle there, too. Naples, Florida, is a case in point.

NAPLES, FLORIDA

The most recent U.S. census found that Naples, Florida, a city of 21,000, and surrounding Collier County have been acquiring young, single, college-educated residents at a faster clip than any other part of the United States. Once young people might have just visited their retired parents in Naples or helped them move there. Now, they may move in. Aside from being drawn by the balmy weather—Naples has 333 days of sunshine a year and an average temperature of 75 degrees—they are tempted by employment. There are jobs in companies catering to the needs of well-to-do seasonal residents and retirees as well as new technology ventures based in and around Naples that have won national, even international, clients and reputations. Entrepreneurs, many relatively young themselves, have been moving to Naples and its environs to launch companies in telecommunications, computer software, marketing, and other fields. Young people are asking themselves "why wait to retire here. I want this quality of life now."[40]

::: Other Major Macroenvironments

Other macroenvironment forces profoundly affect the fortunes of marketers. Here we review developments in the economic, social-cultural, natural, technological, and political-legal environments.

Economic Environment

Markets require purchasing power as well as people. The available purchasing power in an economy depends on current income, prices, savings, debt, and credit availability. Marketers must pay careful attention to trends affecting purchasing power because they can have a strong impact on business, especially for companies whose products are geared to high-income and price-sensitive consumers.

INCOME DISTRIBUTION Nations vary greatly in level and distribution of income and industrial structure. There are four types of industrial structures: *subsistence economies* (few opportunities for marketers); *raw-material-exporting economies* like Zaire (copper) and Saudi Arabia (oil), with good markets for equipment, tools, supplies, and luxury goods for the rich; *industrializing economies*, like India, Egypt, and the Philippines, where a new rich class and a growing middle class demand new types of goods; and *industrial economies*, which are rich markets for all sorts of goods.

In a global economy, marketers need to pay attention to the shifting income distribution in countries around the world, particularly countries where affluence levels are rising.

INDIA

With its surfeit of low-cost, high-IQ, English-speaking employees, India is snapping up programming and call-center jobs once held by Americans in a wave of outsourcing that shows no signs of stopping. By 2008, IT services and back-office work in India will swell fivefold, to a $57 billion annual export industry employing 4 million people and accounting for 7 percent of India's gross domestic product. While India's ascendance inevitably means lost jobs and anguish for American white-collar workers, it also means a larger market for American and Western goods—and anguish for traditional Indian families. Along with training in American accents and geography, India's legions of call-center employees are absorbing new ideas about family, material possessions, and romance. "I call these kids 'liberalization children,' " says Rama Bijapurkar, a Bombay-based marketing consultant. "This generation has a hunger in the belly for achievement." Liberalization children are questioning conservative traditions such as arranged marriages and no public kissing. They want to watch Hollywood movies, listen to Western music, chat on cell phones, buy on credit—rather than saving—and eat out in restaurants or cafés. And they are being targeted relentlessly by companies that have waited to see India develop a Western-style consumer class.[41]

Marketers often distinguish countries with five different income-distribution patterns: (1) very low incomes; (2) mostly low incomes; (3) very low, very high incomes; (4) low, medium, high incomes; and (5) mostly medium incomes. Consider the market for Lamborghinis, an automobile costing more than $150,000. The market would be very small in countries with type (1) or (2) income patterns. One of the largest single markets for Lamborghinis turns out to be Portugal [income pattern (3)]—one of the poorer countries in Western Europe, but one with enough wealthy families to afford expensive cars.

Over the past three decades in the United States, the rich have grown richer, the middle class has shrunk, and the poor have remained poor. From 1973 to 1999, earnings for U.S. households in the top 5 percent of the income distribution grew 65 percent, compared with growth of 11 percent for the middle fifth households during the same period. This is leading to a two-tier U.S. market, with affluent people able to buy expensive goods and working-class people having to spend more carefully, shopping at discount stores and factory outlet malls, and selecting less expensive store brands. Conventional retailers who offer medium-priced goods are the most vulnerable to these changes. Companies that respond to the trend by tailoring their products and pitches to these two very different Americas stand to gain.[42]

GAP

GAP pursues a segmented market strategy with three tiers of retail clothing stores: the upscale Banana Republic, the mid-market GAP, and the budget-priced Old Navy. Jeans sell for $70 at Banana Republic stores and for as much as $50 at GAP stores. Old Navy jeans sell for under $25. Each store has its own look, its own clothing lines, and its own in-house advertising. This segmented strategy helped GAP grow from a $7 billion to a $14 billion business between 1996 and 2003.[43]

SAVINGS, DEBT, AND CREDIT AVAILABILITY Consumer expenditures are affected by savings, debt, and credit availability. U.S. consumers have a high debt-to-income ratio, which slows down further expenditures on housing and large-ticket items. Credit is very available in the United States but at fairly high interest rates, especially to lower-income borrowers. Here the Internet can offer a helping hand: Consumers seeking a mortgage can go to lendingtree.com, fill out a single loan application, and receive several loan package proposals from competing banks within 48 hours.

OUTSOURCING AND FREE TRADE An economic issue of increasing importance is the migration of manufacturers and service jobs off shore. Outsourcing is seen as a competitive necessity by many firms, but as a cause of unemployment by many domestic workers. For example, in December 2003, IBM decided to move the jobs of nearly 5,000 programmers to India and China. GE has moved much of its research and development overseas. Microsoft, Dell, American Express, and virtually every major multinational from Accenture to Yahoo! have already offshored work or are considering doing so.

The savings are dramatic, with companies cutting 20 to 70 percent of their labor costs, assuming the work is of comparable quality. However, beyond the short-term gain for employers and pain for displaced domestic white-collar employees is the scarier long-term prospect. The exodus of programming work, in particular, throws the future of America's tech dominance into doubt. Many wonder whether the United States can continue to lead the industry as software programming spreads around the globe from India to Bulgaria. In Bombay, for example, there is high-speed Internet access, a world-class university, and a venture capital industry—all the ingredients you need to spawn the next earthshaking technology innovation.[44]

Outside the labor market, advocates for and against free trade debate the merits of protective tariffs.

A GAP storefront displays the familiar, recognizable GAP "look."

FAIR TRADE COFFEE

Activist group Global Exchange, a human rights organization dedicated to promoting environmental, political, and social justice around the world, has pressured the coffee industry to support Fair Trade Certified coffee. More than 500,000 farmers around the world produce and sell more than 170 million pounds of coffee each year through the Fair Trade network. Over 100 Fair Trade coffee brands are sold worldwide in approximately 35,000 retail outlets (7,000 in the United States). To become Fair Trade certified, an importer must meet stringent international criteria, such as paying a minimum price per pound of $1.26. Global Exchange chose to target Starbucks to participate in the network, given its high profile. A grassroots campaign led to the introduction of whole bean Fair Trade Certified coffee at over 2,300 Starbucks stores as part of a broader corporate social responsibility initiative on the part of the company.[45]

Social-Cultural Environment

Purchasing power is directed toward certain goods and services and away from others according to people's tastes and preferences. Society shapes the beliefs, values, and norms that largely define these tastes and preferences. People absorb, almost unconsciously, a worldview that defines their relationships to themselves, to others, to organizations, to society, to nature, and to the universe.

- ***Views of themselves.*** People vary in the relative emphasis they place on self-gratification. In the United States during the 1960s and 1970s, "pleasure seekers" sought fun, change, and escape. Others sought "self-realization." People bought dream cars and dream vacations and spent more time in health activities (jogging, tennis), in introspection, and in arts and crafts (see Table 3.4 for a current profile). Today, some people are adopting more conservative behaviors and ambitions. Marketers must recognize that there are many different groups with different views of themselves.

- ***Views of others.*** People are concerned about the homeless, crime and victims, and other social problems. They would like to live in a more humane society. At the same time, people are seeking out their "own kind" and avoiding strangers. They hunger for serious and long-lasting relationships with a few others. These trends portend a growing market for social-support products and services that promote direct relations between human beings, such as health clubs, cruises, and religious activity. They also suggest a growing market for "social surrogates," things that allow people who are alone to feel that they are not, such as television, home video games, and chat rooms on the Internet.

- ***Views of organizations.*** People vary in their attitudes toward corporations, government agencies, trade unions, and other organizations. Most people are willing to work for these organizations, but there has been an overall decline in organizational loyalty. The massive wave of company downsizings and corporate accounting scandals such as those at Enron, WorldCom, and Tyco has bred cynicism and distrust.[46] Many people today see work not as a source of satisfaction, but as a required chore to earn money to enjoy their nonwork hours. This outlook has several marketing implications. Companies need to find new ways to win back consumer and employee confidence. They need to make sure that they are good corporate citizens and that their consumer messages are honest.

- ***Views of society.*** People vary in their attitudes toward their society. Some defend it (preservers), some run it (makers), some take what they can from it (takers), some want to change it (changers), some are looking for something deeper (seekers), and some want to leave it (escapers).[47] Consumption patterns often reflect social attitude. Makers tend to be high achievers who eat, dress, and live well. Changers usually live more frugally, drive smaller cars, and wear simpler clothes. Escapers and seekers are a major market for movies, music, surfing, and camping.

- ***Views of nature.*** People vary in their attitudes toward nature. Some feel subjugated by it, others feel in harmony with it, and still others seek mastery over it. A long-term trend has been humankind's growing mastery of nature through technology. More recently, however, people have awakened to nature's fragility and finite resources. They recognize that nature can be destroyed by human activities. Business has responded to increased interest in camping, hiking, boating, and fishing with hiking boots, tenting equipment, and other gear. Tour operators are packaging tours to wilderness areas and to places like Antarctica.

- ***Views of the universe.*** People vary in their beliefs about the origin of the universe and their place in it. Most Americans are monotheistic, although religious conviction and practice have been waning through the years. Certain evangelical movements are reaching out to bring people back into organized religion. Some of the religious impulse has been redirected into an interest in Eastern religions, mysticism, the occult, and the human potential movement.

As people lose their religious orientation, they seek self-fulfillment and immediate gratification. At the same time, every trend seems to breed a countertrend, as indicated by a worldwide rise in religious fundamentalism. Here are some other cultural characteristics of interest to marketers: the persistence of core cultural values, the existence of subcultures, and shifts of values through time.

HIGH PERSISTENCE OF CORE CULTURAL VALUES The people living in a particular society hold many *core beliefs* and values that tend to persist. Most Americans still believe in work, in getting married, in giving to charity, and in being honest. Core beliefs and values are passed on from parents to children and are reinforced by major social institutions—schools, churches, businesses, and governments. *Secondary beliefs* and values are more open to change. Believing in the institution of marriage is a core belief; believing that people ought to get married early is a secondary belief. Thus family-planning marketers could make some

TABLE 3.4

Most Popular American Leisure Activities (percent of adults who participate)

Walking for exercise	59%
Gardening	45%
Swimming	35%
Photography	26%
Bicycling	25%
Fishing	23%
Bowling	21%
Camping	21%
Jogging or running	18%
Free weights or circuit training	17%
Golf	16%
Adult continuing education	16%
Hiking/backpacking	14%
Power boating	9%

Source: Scarborough Research, 2001, as summarized in "Where Does the Time Go?" *American Demographics* (April 2002) 56.

headway arguing that people should get married later, rather than that they should not get married at all.

Marketers have some chance of changing secondary values but little chance of changing core values. For instance, the nonprofit organization Mothers Against Drunk Drivers (MADD) does not try to stop the sale of alcohol, but it does promote the idea of appointing a designated driver who will not drink that evening. The group also lobbies to raise the legal drinking age.

EXISTENCE OF SUBCULTURES Each society contains **subcultures**, groups with shared values emerging from their special life experiences or circumstances. Members of subcultures share common beliefs, preferences, and behaviors. To the extent that subcultural groups exhibit different wants and consumption behavior, marketers can choose particular subcultures as target markets.

Marketers sometimes reap unexpected rewards in targeting subcultures. Marketers have always loved teenagers because they are society's trendsetters in fashion, music, entertainment, ideas, and attitudes. Marketers also know that if they attract someone as a teen, there is a good chance they will keep the person as a customer later in life. Frito-Lay, which draws 15 percent of its sales from teens, said it saw a rise in chip-snacking by grown-ups. "We think it's because we brought them in as teenagers," said Frito-Lay's marketing director.[48]

SHIFTS OF SECONDARY CULTURAL VALUES THROUGH TIME Although core values are fairly persistent, cultural swings do take place. In the 1960s, hippies, the Beatles, Elvis Presley, and other cultural phenomena had a major impact on young people's hairstyles, clothing, sexual norms, and life goals. Today's young people are influenced by new heroes and new activities: U2's Bono, the NBA's LeBron James, golf's Tiger Woods, and skateboarder Tony Hawk.

Natural Environment

The deterioration of the natural environment is a major global concern. In many world cities, air and water pollution have reached dangerous levels. There is great concern about "greenhouse gases" in the atmosphere due to the burning of fossil fuels; about the depletion of the ozone layer due to certain chemicals; and about growing shortages of water. In Western Europe, "green" parties have vigorously pressed for public action to reduce industrial pollution. In the United States, experts have documented ecological deterioration, and watchdog groups such as the Sierra Club and Friends of the Earth carry these concerns into political and social action.

New regulations hit certain industries very hard. Steel companies and public utilities have had to invest billions of dollars in pollution-control equipment and more environmentally friendly fuels. The auto industry has had to introduce expensive emission controls in cars. The soap industry has had to increase its products' biodegradability. The major hope is that companies will adopt practices that will protect the natural environment. Great opportunities await companies and marketers who can create new solutions that promise to reconcile prosperity with environmental protection.

Consumers often appear conflicted about the natural environment. One research study showed that although 80 percent of U.S. consumers stated that whether or not a product is safe for the environment influenced their decision to buy that product, only a little over half asserted that they bought recycled or environmentally safe products.[49] Young people especially were more likely to feel that nothing that they did personally made a difference. Increasing the number of green products that are bought requires breaking consumers' loyalty habits, overcoming consumer skepticism about the motives behind the introduction of green products and their quality level, and changing consumer attitudes about the role they play in environmental protection. (See "Marketing Insight: Green Marketing".)

Marketers need to be aware of the threats and opportunities associated with four trends in the natural environment: the shortage of raw materials, especially water; the increased cost of energy; increased pollution levels; and the changing role of governments.

SHORTAGE OF RAW MATERIALS The earth's raw materials consist of the infinite, the finite renewable, and the finite nonrenewable. *Infinite resources,* such as air and water, are becoming a problem. Water shortages are already a political issue, and the danger is no longer long term. *Finite renewable resources,* such as forests and food, must be used wisely. Forestry companies are required to reforest timberlands in order to protect the soil and to ensure sufficient wood to meet future demand. Because the amount of arable land is fixed and urban areas are constantly encroaching on farmland, food supply can also be a major problem. *Finite nonrenewable resources*—oil, coal, platinum, zinc, silver—will pose a serious problem as the point of depletion approaches. Firms making products that require these increasingly scarce minerals face substantial cost increases. Firms engaged in research and development have an excellent opportunity to develop substitute materials.

INCREASED ENERGY COSTS One finite nonrenewable resource, oil, has created serious problems for the world economy. In October 2004, oil prices shot up to over $55 a barrel, reinforcing the need for alternative energy forms. Companies are searching for practical means to harness solar, nuclear, wind, and other forms of energy. In the solar energy field alone, hundreds of firms introduced first-generation products to harness solar energy for heating homes and other uses. Other firms are engaged in building practical electric automobiles, with a potential prize of billions for the winner. Practical combination vehicles, like the Toyota Prius, *Motor Trend* magazine's 2004 Car of the Year, are already available.

ANTI-POLLUTION PRESSURES Some industrial activity will inevitably damage the natural environment. Consider the dangerous mercury levels in the ocean, the quantity of DDT and other chemical pollutants in the soil and food supply, and the littering of the environment with bottles, plastics, and other packaging materials. A large market has been created for pollution-control solutions, such as scrubbers, recycling centers, and landfill systems. Its existence leads to a search for alternative ways to produce and package goods. 3M runs a Pollution Prevention Pays program that has led to a substantial reduction in pollution and costs. Dow Chemical built a new ethylene plant in Alberta that uses 40 percent less energy and releases 97 percent less wastewater. AT&T uses a special

MARKETING INSIGHT | GREEN MARKETING

Although environmental issues have long affected marketing practices, especially in Europe, their relevance has increased in the last decade or so. With the well-publicized Earth Day activities in the United States in April 1990, the "green marketing" movement was born. An explosion of "environmentally friendly" products and marketing programs appeared as firm after firm tried to capitalize on consumers' perceived increased sensitivity to environmental issues.

From a branding perspective, however, "green marketing" programs have not been entirely successful. For example, in 1994, Philips Electronics NV branded its eco-friendly, energy-saving fluorescent bulbs as "Earthlight." Due to a lack of sales success, the product was repackaged in 2000 as convenient, seven-year life "Marathon" bulbs, and sales grew steadily at 7 percent annually. Faced with slumping sales, Ben & Jerry's dropped its "Rainforest Crunch" flavor of ice cream, introduced on Earth Day in 1990 to tout conservation and nuts from rainforest trees. Despite a concerted marketing effort, Green Mountain Energy has found it difficult to sell electricity from eco-friendly power plants.

Many other marketers tried and failed with green sales pitches over the last decade. What obstacles did this movement encounter?

- ***Overexposure and lack of credibility.*** So many companies made environmental claims that the public became skeptical of their validity. Government investigations into some "green" claims (e.g., the degradability of trash bags) and media reports of the spotty environmental track records behind others only increased consumers' doubts. This backlash resulted in many consumers thinking environmental claims were just marketing gimmicks.
- ***Consumer behavior.*** Research studies have shown that consumers as a whole may not be willing to pay a premium for environmental benefits, although certain market segments will be. Most consumers appear unwilling to give up the benefits of other alternatives to choose green products. For example, some consumers dislike the performance, appearance, or texture of recycled paper and household products. And some consumers are unwilling to give up the convenience of disposable products such as diapers.
- ***Poor implementation.*** In jumping on the green marketing bandwagon, many firms did a poor job implementing their marketing program. Products were poorly designed in terms of environmental worthiness, overpriced, and inappropriately promoted. Some ads failed to make the connection between what the company was doing for the environment and how it affected individual consumers.

To get around these obstacles and make sure environmental initiatives are implemented, some companies recommend relying on the efforts of a "Green Champion"—an environmentalist who works internally to make companies greener. Jean Palmateer, an environmental engineer, is a "green champion" for DePuy Orthopaedics, a division of Johnson & Johnson. She recommends getting broad goals accomplished by personalizing the issue. For instance, when Palmeteer wanted to keep the medical device makers' wastewater tanks clean, she told workers that better maintained tanks would not just help the earth, but save them from 3:00 A.M. phone calls when the tanks failed to discharge. Now the tanks are cleaner and workers are sleeping better at night.

There have been some notable green marketing successes through the years. Chevron' s highly visible "People Do" ad campaign attempted to transform consumers' negative perceptions of oil companies and their effect on the environment by describing specific Chevron programs designed to save wildlife, preserve seashores, and so on.

McDonald's has introduced a number of well-publicized environmental initiatives through the years, such as unbleached paper carryout bags and replacing polystyrene foam sandwich clamshells with paper wraps and lightweight recycled boxes. McDonald's received the EPA WasteWise Partner of the Year award for waste reduction efforts that: (1) conserved 3,200 tons of paper and cardboard by replacing sandwich containers with single-layer flexible sandwich wraps; (2) eliminated 1,100 tons of cardboard materials that would have been used for shipping by switching to light drink cups; and (3) resulted in spending $355 million on recycled content products.

Sources: Jacquelyn Ottman, *Green Marketing: Opportunity for Innovation*, 2nd ed. (Chicago: NTC/Contemporary Publishing Company, 1998); Geoffrey Fowler, "'Green' Sales Pitch Isn't Moving Many Products," *Wall Street Journal*, March 6, 2002, p. B4; Lynn J. Cook, "Our Electrons Are Greener," *Forbes*, June 23, 2003, p. 101; Kevin Lane Keller, *Strategic Brand Management*, 2nd ed. (Upper Saddle River, NJ: Prentice Hall, 2003); Maggie Jackson, "Earth-Friendly Company Changes Come from One 'Green Champion' at a Time," *Boston Globe*, May 9, 2004, p. G1.

software package to choose the least harmful materials, cut hazardous waste, reduce energy use, and improve product recycling in its operations.[50]

CHANGING ROLE OF GOVERNMENTS Governments vary in their concern and efforts to promote a clean environment. For example, the German government is vigorous in its pursuit of environmental quality, partly because of the strong green movement in Germany and partly because of the ecological devastation in the former East Germany. Many poor nations are doing little about pollution, largely because they lack the funds or the political will. It is in the richer nations' interest to help the poorer nations control their pollution, but even the richer nations today lack the necessary funds.

Technological Environment

One of the most dramatic forces shaping people's lives is technology. Technology has released such wonders as penicillin, open-heart surgery, and the birth control pill. It has released such horrors as the hydrogen bomb, nerve gas, and the submachine gun. It has also released such mixed blessings as the automobile and video games.

Every new technology is a force for "creative destruction." Transistors hurt the vacuum-tube industry, xerography hurt the carbon paper business, autos hurt the railroads, and television hurt the newspapers. Instead of moving into the new technologies, many old industries fought or ignored them, and their businesses declined. Yet it is the essence of market capitalism to be dynamic and tolerate the creative destructiveness of technology as the price of progress.

Look out Dell, HP, Apple, and Microsoft: According to some seers, "smart" mobile phones will eventually eclipse the PC.

SMART PHONES

"One day, 2 or 3 billion people will have cell phones, and they are all not going to have PCs," says Jeff Hawkins, inventor of the Palm Pilot and chief technology officer for PalmOne. "The mobile phone will become their digital life," Hawkins predicts. After a slow start, mobile phones have become more ubiquitous—there are 1.5 billion in the world today—and smarter. Today's most sophisticated phones already have the processing power of a mid-1990s PC while consuming 100 times less electricity. The phones are used to send e-mail, browse the Web, take pictures, and play video games. Hawkins predicts that within the next few decades all phones will be mobile phones, capable of receiving voice and Internet signals at broadband speeds, and that mobile-phone bills will shrink to a few dollars a month as phone companies pay off their investment in new networks. New smart phones in the works include Palm's pocket-size Treo600, with a tiny keyboard, a built-in digital camera, and slots for added memory; and Motorola's MPx, which features a "dual-hinge" design. The handset opens in one direction and appears to be a regular phone, but it also flips open on another axis to look like an e-mail device, with the expanded phone keypad serving as a small, conventional qwerty keypad.[51]

The economy's growth rate is affected by how many major new technologies are discovered. Unfortunately, technological discoveries do not arise evenly through time—the railroad industry created a lot of investment, and then investment petered out until the auto industry emerged. Later, radio created a lot of investment, which then petered out until television appeared. In the time between major innovations, an economy can stagnate. In the meantime, minor innovations fill the gap: freeze-dried coffee, combination shampoo and conditioner, antiperspirants and deodorants, and the like. They involve less risk, but they also divert research effort away from major breakthroughs.

New technology also creates major long-run consequences that are not always foreseeable. The contraceptive pill, for example, led to smaller families, more working wives, and larger discretionary incomes—resulting in higher expenditures on vacation travel, durable goods, and luxury items.

The marketer should monitor the following trends in technology: the pace of change, the opportunities for innovation, varying R&D budgets, and increased regulation.

ACCELERATING PACE OF CHANGE Many of today's common products were not available 40 years ago. John F. Kennedy did not know personal computers, digital wristwatches, video recorders, fax machines, personal digital assistants, or the Internet; nor has the pace of technological change slowed down. The Human Genome project promises to usher in the Biological Century as biotech workers create new medical cures, new foods, and new materials. Electronic researchers are building smarter chips to make our cars, homes, and offices more responsive to changing conditions. The blending of personal computers, scanners, fax and copy machines, wireless phones, the Internet, and e-mail has made it possible for people to *telecommute*—that is, work at home or on the road instead of traveling to an office. This trend may reduce auto pollution, bring the family closer together, and create more home-centered shopping and entertainment.

An increasing number of ideas are being worked on, and the time between the appearance of new ideas and their successful implementation is all but disappearing. So is the time between introduction and peak production. Ninety percent of all the scientists who ever lived are alive today, and technology feeds upon itself.

UNLIMITED OPPORTUNITIES FOR INNOVATION Scientists today are working on a startling range of new technologies that will revolutionize products and production processes. Some of the most exciting work is being done in biotechnology, computers, microelectronics, telecommunications, robotics, and designer materials. Researchers are working on AIDS cures, happiness pills, painkillers, totally safe contraceptives, and nonfattening foods. They are designing robots for firefighting, underwater exploration, and home nursing. In addition, scientists also work on fantasy products, such as small flying cars, three-dimensional television, and space colonies. The challenge in each case is to develop affordable versions of these products.

SAMSUNG

In an ambitious endeavor, Samsung has launched a digital home business. In Korea, Samsung has 6,000 networked homes that are outfitted with Internet-enabled ovens, refrigerators, security cameras, and wall-mounted flat-panel displays. Samsung is looking to take the idea abroad. Wiring homes in the United States will cost from $2,000 to $10,000, making adoption relatively affordable. Besides overcoming a few technical challenges, however, Samsung must also contend with consumers who worry about the complexity or even need for such products. But experts look to the further penetration of broadband access to propel the adoption of the digital home as consumers learn to access digital media and commerce from more devices.[52]

Companies are already harnessing the power of *virtual reality (VR)*, the combination of technologies that allows users to experience three-dimensional, computer-generated environments through sound, sight, and touch. Virtual reality has already been applied to gathering consumer reactions to new automobile designs, kitchen layouts, exterior home designs, and other potential offerings.

VARYING R&D BUDGETS Although the United States leads the world in annual R&D expenditures, a growing portion of U.S. R&D expenditures is going into the development side of R&D, raising concerns about whether the United States can maintain its lead in basic science. Many companies are content to put their money into copying competitors' products and making minor feature and style improvements. Even basic research companies such as DuPont, Bell Laboratories, and Pfizer are proceeding cautiously, and more research directed toward major breakthroughs is being conducted by consortiums of companies rather than by single companies.

INCREASED REGULATION OF TECHNOLOGICAL CHANGE As products become more complex, the public needs to be assured of its safety. Consequently, government agencies' powers to investigate and ban potentially unsafe products have been expanded. In the United States, the Federal Food and Drug Administration must approve all drugs before they can be sold. Safety and health regulations have also increased in the areas of food, automobiles, clothing, electrical appliances, and construction. Marketers must be aware of these regulations when proposing, developing, and launching new products.

Political-Legal Environment

Marketing decisions are strongly affected by developments in the political and legal environment. This environment is composed of laws, government agencies, and pressure groups that influence and limit various organizations and individuals. Sometimes these laws also create new opportunities for business. For example, mandatory recycling laws have given the recycling industry a major boost and spurred the creation of dozens of new companies making new products from recycled materials. Two major trends deal with the increase in business legislation and the growth of special interest groups.

GreenDisk, a company that produces high-quality recycled disks.

INCREASE IN BUSINESS LEGISLATION Business legislation has three main purposes: to protect companies from unfair competition, to protect consumers from unfair business practices, and to protect the interests of society from unbridled business behavior. A major purpose of business legislation and enforcement is to charge businesses with the social costs created by their products or production processes. A central concern is this: At what point do the costs of regulation exceed the benefits? The laws are not always administered fairly; regulators and enforcers may be lax or overzealous. Although each new law may have a legitimate rationale, it may have the unintended effect of sapping initiative and retarding economic growth.

Legislation affecting business has increased steadily over the years. The European Commission has been active in establishing a new framework of laws covering competitive behavior, product standards, product liability, and commercial transactions for the 25 member nations of the European Union. The United States has many laws on its books covering such issues as competition, product safety and liability, fair trade and credit practices, and packaging and labeling.[53]

Several countries have gone further than the United States in passing strong consumer protection legislation. Norway bans several forms of sales promotion—trading stamps, contests, premiums—as inappropriate or "unfair" instruments for promoting products. Thailand requires food processors selling national brands to market low-price brands also, so that low-income consumers can find economy brands. In India, food companies need

Checking the nutrition labels in the supermarket; the nutrition label on a box of Kellogg's Kenmei Rice Bran.

special approval to launch brands that duplicate what already exists on the market, such as another cola drink or brand of rice.

Marketers must have a good working knowledge of the major laws protecting competition, consumers, and society. Companies generally establish legal review procedures and promulgate ethical standards to guide their marketing managers, and as more business takes place in cyberspace, marketers must establish new parameters for doing electronic business ethically.

Unit pricing labels for cereals on a supermarket shelf.

GROWTH OF SPECIAL-INTEREST GROUPS

The number and power of special-interest groups have increased over the past three decades. Political action committees (PACs) lobby government officials and pressure business executives to pay more attention to consumers' rights, women's rights, senior citizens' rights, minority rights, and gay rights.

Many companies have established public affairs departments to deal with these groups and issues. An important force affecting business is the **consumerist movement**—an organized movement of citizens and government to strengthen the rights and powers of buyers in relation to sellers. Consumerists have advocated and won the right to know the true interest cost of a loan, the true cost per standard unit of competing brands (unit pricing), the basic ingredients in a product, the nutritional quality of food, the freshness of products, and the true benefits of a product.

With consumers increasingly willing to swap personal information for customized products from firms—as long as they can be trusted—privacy issues will continue to be a public policy hot button.[54] Consumer concerns are that they will be robbed or cheated; that private information will be used against them; that someone will steal their identity; that they will be bombarded with solicitations; and that children will be targeted.[55] Several companies have established consumer affairs departments to help formulate policies and respond to consumer complaints. Companies are careful to answer their e-mail and to resolve and learn from any customer complaints.

Clearly, new laws and growing numbers of pressure groups have put more restraints on marketers. Marketers have to clear their plans with the company's legal, public relations, public affairs, and consumer affairs departments. Insurance companies directly or indirectly affect the design of smoke detectors; scientific groups affect the design of spray products by condemning aerosols. In essence, many private marketing transactions have moved into the public domain.

SUMMARY :::

1. To carry out their analysis, planning, implementation, and control responsibilities, marketing managers need a marketing information system (MIS). The role of the MIS is to assess the managers' information needs, develop the needed information, and distribute that information in a timely manner.
2. An MIS has three components: (a) an internal records system, which includes information on the order-to-payment cycle and sales reporting systems; (b) a marketing intelligence system, a set of procedures and sources used by managers to obtain everyday information about pertinent developments in the marketing

environment; and (c) a marketing research system that allows for the systematic design, collection, analysis, and reporting of data and findings relevant to a specific marketing situation.

3. Many opportunities are found by identifying trends (directions or sequences of events that have some momentum and durability) and megatrends (major social, economic, political, and technological changes that have long-lasting influence).
4. Within the rapidly changing global picture, marketers must monitor six major environmental forces: demographic, economic, social-cultural, natural, technological, and political-legal.
5. In the demographic environment, marketers must be aware of worldwide population growth; changing mixes of age, ethnic composition, and educational levels; the rise of nontraditional families; large geographic shifts in population; and the move to micromarketing and away from mass marketing.
6. In the economic arena, marketers need to focus on income distribution and levels of savings, debt, and credit availability.
7. In the social-cultural arena, marketers must understand people's views of themselves, others, organizations, society, nature, and the universe. They must market products that correspond to society's core and secondary values, and address the needs of different subcultures within a society.
8. In the natural environment, marketers need to be aware of raw materials shortages, increased energy costs and pollution levels, and the changing role of governments in environmental protection.
9. In the technological arena, marketers should take account of the accelerating pace of technological change, opportunities for innovation, varying R&D budgets, and the increased governmental regulation brought about by technological change.
10. In the political-legal environment, marketers must work within the many laws regulating business practices and with various special-interest groups.

APPLICATIONS

Marketing Debate Is Consumer Behavior More a Function of a Person's Age or Generation?

One of the widely debated issues in developing marketing programs that target certain age groups is how much consumers change over time. Some marketers maintain that age differences are critical and that the needs and wants of a 25-year-old in 2002 are not that different from those of a 25-year-old in 1972. Others dispute that contention and argue that cohort and generation effects are critical and that marketing programs must therefore suit the times.

Take a position: Age differences are fundamentally more important than cohort effects versus Cohort effects can dominate age differences.

Marketing Discussion

What brands and products do you feel successfully "speak to you" and effectively target your age group? Why? Which ones do not? What could they do better?

MARKETING SPOTLIGHT BUDWEISER

Budweiser Lager was first brewed in 1876 by E. Anheuser & Co., St. Louis. Today, Anheuser-Busch is the largest brewer in the world in terms of volume, and it competes across a diverse range of markets. The company oversees more than 30 different beer brands, including the domestic market leader Budweiser, a number of other alcoholic and nonalcoholic beverages, a group of theme parks, and a real estate enterprise.

While retaining its brewing traditions, the company has adopted new technological traditions that improve its business and marketing effectiveness. In 1997, chairman August Busch III vowed to make his company a leader in mining its customers' buying patterns. The key to Anheuser-Busch's real-time analysis of marketing effectiveness is timely data: getting information back from wholesalers and retailers on what is selling where and when.

"Wholesaler and store-level data has become the lifeblood of our organization," said Joe Patti, Anheuser's vice president for retail planning and category management. Therefore, Anheuser-Busch created BudNET to connect to wholesalers, retailers, and other Anheuser-Busch business partners. The system handles sales reporting, customer development, retail promotion notices, and weekly sales forecasting, as well as a wide array of logistics-related functions. BudNET is the information channel for an Anheuser-Busch system called WEARS (Wholesaler Equity Agreement Reporting System). Through BudNET, the delivery people of the 700 U.S. distributors of Budweiser can become the eyes and ears of the brewer.

WEARS and BudNET do much more than just keep tabs on the flow of icy-cold Bud off retailers' refrigerated shelves. Using portable transaction computers, the delivery people also log data on competing products, identifying what else is on the retailers' shelves. At the end of the day, Anheuser-Busch gets the data and looks for trends. "If Anheuser-Busch loses shelf space in a store in Clarksville, Tennessee, they know it right away," said Joe Thompson, president of Independent Beverage Group, a research and consulting firm. "They're better at this game than anyone, even Coca-Cola."

Understanding consumers means more than just gathering data on your own product or on your competitor's product. Anheuser-Busch also analyzes syndicated bar-code scan data gathered by Information Resources Inc. (IRI), to track consumer purchasing behavior across a full range of products. Anheuser-Busch successfully launched low-carb Michelob Ultra after seeing data on consumer shifts in dietary habits in other food groups.

Timely, fine-grain data also help sharpen Anheuser-Busch's marketing and product assortment. With store-level data, the company can create targeted marketing materials. For example, gay models appear on posters in San Francisco's Castro district, but not on those in the Mission district. Better data also help predict local sales during holidays, such as knowing that Atlantans celebrate Fourth of July more than St. Patrick's Day. Demographic data help Anheuser-Busch know where cans sell better than bottles (blue-collar neighborhoods), and helped the company launch a range of Latin-inspired beverages such as Tequiza and Sauza Diablo for the growing Hispanic market.

Anheuser-Busch uses a variety of internal and external data sources—including consumer demographics, POS, and market data—to guide product assortment decisions. Anheuser-Busch uses the six-step, industry-standard, best practice called Efficient Item Assortment (EIA) that is published by the Food Marketing Institute. Software, co-developed with an outside software vendor, creates a top-line master assortment product list for individual stores and store clusters. This tool won a Technology Leadership Award from *Consumer Goods Technology (CGT)* magazine.

Anheuser-Busch's use of IT is international. Budexchange.co.uk, hosted on BudNET, tracks key data and sales of 5,000 British outlets. The system rewards the loyalty of trade customers with Budweiser-branded support materials. Anheuser-Busch uses the data provided by the outlets in its proactive segmented marketing communications program. In a market in which overall sales are down 5.7 percent, Budweiser sales are up 7 percent.

Anheuser-Busch continues to expand its use of datalinks, using its market clout to improve data gathering and data sharing. August Busch IV, president for domestic operations, promised that "brewers and wholesalers with a clear, data-driven focus will have a distinct competitive advantage." Market share data confirm the success of the company's strategy—Anheuser-Busch now commands 50.1 percent of the market in 2003, up from 48.9 percent in 2002.

Discussion Questions

1. What have been the key success factors for Anheuser-Busch?
2. Where is Anheuser-Busch vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should the company be sure to do with its marketing?

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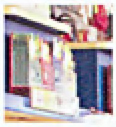


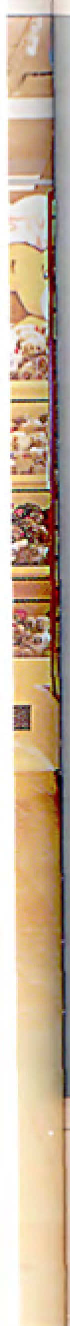
IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What constitutes good marketing research?
2. What are good metrics for measuring marketing productivity?
3. How can marketers assess their return on investment of marketing expenditures?
4. How can companies more accurately measure and forecast demand?

CHAPTER 4 ::: CONDUCTING MARKETING RESEARCH AND FORECASTING DEMAND

In addition to monitoring a changing marketing environment, marketers also need to develop specific knowledge about their particular markets. Good marketers want information to help them interpret past performance as well as plan future activities. Marketers need timely, accurate, and actionable information on consumers, competition, and their brands. They need to make the best possible tactical decisions in the short run and strategic decisions in the long run. Discovering a consumer insight and understanding its marketing implications can often lead to a successful product launch or spur the growth of a brand.

St. Louis-based Build-A-Bear Workshop has cleverly capitalized on the "kiddie-craft" trend in children's toys as well as the trend for interactive entertainment retailing. Instead of making pottery or play jewelry, the chain, with more than 160 stores in the United States, Canada, the United Kingdom, Japan, Denmark, and Korea, allows kids (and adults too) to design their own teddy bears and other stuffed animals, complete with clothing, shoes, and accessories. The chain boasts an average of over $500 per square foot in annual revenue, double the U.S. mall average. Ten percent of sales in 2003 came from hosting nearly 100,000 parties at a cost to customers of approximately $250 for two hours, which includes a stuffed animal for each child. Build-A-Bear has created a database on 9 million kids and their households by inviting customers to register their bears: >>>



A Build-A-Bear Workshop customer leaving the store.

By including a barcode inside the bear, the company can reunite the owner with the bear if it gets lost. The database allows Build-A-Bear to contact customers by surface and e-mail with gift certificates, promotions, and party reminders.[1]

In this chapter, we review the steps involved in the marketing research process. We also consider how marketers can develop effective metrics for measuring marketing productivity. Finally, we outline how marketers can develop good sales forecasts.

::: The Marketing Research System

Marketing managers often commission formal marketing studies of specific problems and opportunities. They may request a market survey, a product-preference test, a sales forecast by region, or an advertising evaluation. It is the job of the marketing researcher to produce insight into the customer's attitudes and buying behavior. We define **marketing research** as the systematic design, collection, analysis, and reporting of data and findings relevant to a specific marketing situation facing the company. Marketing research is now about a $16.5 billion industry globally, according to ESOMAR, the World Association of Opinion and Market Research Professionals.

A company can obtain marketing research in a number of ways. Most large companies have their own marketing research departments, which often play crucial roles within the organization.[2]

PROCTER & GAMBLE

P&G's large market research function is called Consumer & Market Knowledge (CMK). Its goal is to bring consumer insight to decision making at all levels. Dedicated CMK groups work for P&G businesses around the world, including Global Business Units (GBUs), which focus on long-term brand equity and initiative development, and Market Development Organizations (MDOs), which focus on local market expertise and retail partnerships. There is also a relatively smaller, centralized corporate CMK group which, in partnership with the line businesses, focuses on three kinds of work: (1) proprietary research methods development, (2) expert application of, and cross-business learning from, core research competencies, and (3) shared services and infrastructure. CMK leverages traditional research basics such as brand tracking. CMK also finds, invents, or co-develops leading-edge research approaches such as experiential consumer contacts, proprietary modeling methods, and scenario-planning or knowledge synthesis events. CMK professionals connect market insights from all these sources to shape company strategies and decisions. They influence day-to-day operational choices, such as which product formulations are launched, as well as long-term plans, such as which corporate acquisitions best round out the product portfolio.

Yet, marketing research is not limited to large companies with big budgets and marketing research departments. At much smaller companies, marketing research is often carried out by everyone in the company—and by customers, too.

KARMALOOP.COM

Karmaloop bills itself as an online urban boutique, and it has built its reputation as a top shop for Fashionistas because of its relentless tracking of trendsetters. The five-year-old Boston company has made streetwear fashion a science by keeping tabs on young tastemakers' buying habits. In addition to its crew of 15 moonlighting artists, DJs, and designers, Karmaloop recruits street team members to ferret out new trends and to spread the word about Karmaloop brands. The street teams, which now boast 3,000 reps, pass out fliers and stickers at nightclubs, concerts, and on the street, but also report on what they see at events, in the way of trends.[3]

Companies normally budget marketing research at 1 to 2 percent of company sales. A large percentage of that is spent on the services of outside firms. Marketing research firms fall into three categories:

1. ***Syndicated-service research firms*** – These firms gather consumer and trade information, which they sell for a fee. Examples: Nielsen Media Research, SAMI/Burke.
2. ***Custom marketing research firms*** – These firms are hired to carry out specific projects. They design the study and report the findings.
3. ***Specialty-line marketing research firms*** – These firms provide specialized research services. The best example is the field-service firm, which sells field interviewing services to other firms.

Small companies can hire the services of a marketing research firm or conduct research in creative and affordable ways, such as:

1. ***Engaging students or professors to design and carry out projects*** – One Boston University MBA project helped American Express develop a successful advertising campaign geared toward young professionals. The cost: $15,000.
2. ***Using the Internet*** – A company can collect considerable information at very little cost by examining competitors' Web sites, monitoring chat rooms, and accessing published data.
3. ***Checking out rivals*** – Many small companies routinely visit their competitors. Tom Coohill, a chef who owns two Atlanta restaurants, gives managers a food allowance to dine out and bring back ideas. Atlanta jeweler Frank Maier Jr., who often visits out-of-town rivals, spotted and copied a dramatic way of lighting displays.[4]

Most companies, such as Fuji Photo Film, use a combination of marketing research resources to study their industries, competitors, audiences, and channel strategies:

FUJI PHOTO FILM

At the highest level, Fuji relies on data from market research syndicate NDP Group to study the market for products ranging from digital cameras to ink jet photo paper. Fuji also does custom research with a variety of research partners, and it conducts internal research for projects requiring quick information, such as changes to package design. Regardless of how the marketing research data are collected, it is a top priority for Fuji, which has had to adapt its film and digital imaging products to a rapidly changing marketplace. "If you don't have market research to help you figure out what is changing and what the future will be, you will be left behind," says Fuji's director of category management and trade marketing.[5]

::: The Marketing Research Process

Effective marketing research involves the six steps shown in Figure 4.1. We will illustrate these steps with the following situation:

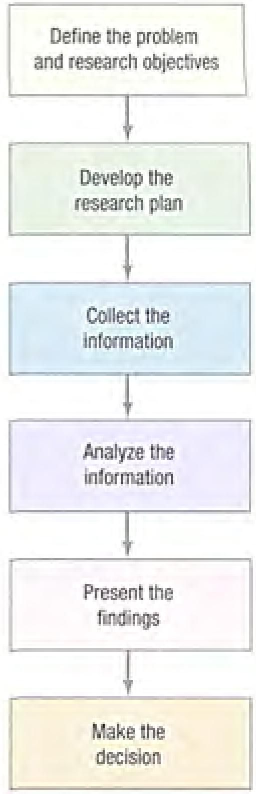


FIG. 4.1

The Marketing Research Process

> American Airlines (AA) is constantly looking for new ways to serve its passengers; it was one of the first companies to install phone handsets. Now it is reviewing many new ideas, especially to cater to its first-class passengers on very long flights, many of whom are businesspeople whose high-priced tickets pay most of the freight. Among these ideas are: (1) to supply an Internet connection with limited access to Web pages and e-mail messaging; (2) to offer 24 channels of satellite cable TV; and (3) to offer a 50-CD audio system that lets each passenger create a customized play list of music and movies to enjoy during the flight. The marketing research manager was assigned to investigate how first-class passengers would rate these services and how much extra they would be willing to pay if a charge was made. He was asked to focus specifically on the Internet connection. One estimate says that airlines might realize revenues of $70 billion over the next decade from in-flight Internet access, if enough first-class passengers would be willing to pay $25 for it. AA could thus recover its costs in a reasonable time. Making the connection available would cost the airline $90,000 per plane.[6]

Step 1: Define the Problem, the Decision Alternatives, and the Research Objectives

Marketing management must be careful not to define the problem too broadly or too narrowly for the marketing researcher. A marketing manager who instructs the marketing researcher to "Find out everything you can about first-class air travelers' needs," will collect a lot of unnecessary information. One who says, "Find out if enough passengers aboard a B747 flying direct between Chicago and Tokyo would be willing to pay $25 for an Internet connection so that American Airlines would break even in one year on the cost of offering this service," is taking too narrow a view of the problem. The marketing researcher might even raise this question: "Why does the Internet connection have to be priced at $25 as opposed to $10, $50, or some other price? Why does American have to break even on the cost of the service, especially if it attracts new users to AA?"

In discussing the problem, American's managers discover another issue. If the new service were successful, how fast could other airlines copy it? Airline marketing research is replete with examples of new services that have been so quickly copied by competitors that no airline has gained a sustainable competitive advantage. How important is it to be first, and how long could the lead be sustained?

The marketing manager and marketing researcher agreed to define the problem as follows: "Will offering an in-flight Internet service create enough incremental preference and profit for American Airlines to justify its cost against other possible investments American might make?" To help in designing the research, management should first spell out the decisions it might face and then work backward. Suppose management spells out these decisions: (1) Should American offer an Internet connection? (2) If so, should the service be offered to first-class only, or include business class, and possibly economy class? (3) What price(s) should be charged? (4) On what types of planes and lengths of trips should it be offered?

Now management and marketing researchers are ready to set specific research objectives: (1) What types of first-class passengers would respond most to using an in-flight Internet service? (2) How many first-class passengers are likely to use the Internet service at different price levels? (3) How many extra first-class passengers might choose American because of this new service? (4) How much long-term goodwill will this service add to American Airlines' image? (5) How important is Internet service to first-class passengers relative to providing other services such as a power plug, or enhanced entertainment?

Not all research projects can be this specific. Some research is exploratory—its goal is to shed light on the real nature of the problem and to suggest possible solutions or new ideas. Some research is descriptive—it seeks to ascertain certain magnitudes, such as how many first-class passengers would purchase in-flight Internet service at $25. Some research is causal—its purpose is to test a cause-and-effect relationship.

Step 2: Develop the Research Plan

The second stage of marketing research calls for developing the most efficient plan for gathering the needed information. The marketing manager needs to know the cost of the research plan before approving it. Suppose the company made a prior estimate that launching the in-flight Internet service would yield a long-term profit of $50,000. The manager believes that doing the research would lead to an improved pricing and promotional plan and a long-term profit of $90,000. In this case, the manager should be willing to spend up to $40,000 on this research. If the research would cost more than $40,000, it is not worth doing.[7] Designing a research plan calls for decisions on the data sources, research approaches, research instruments, sampling plan, and contact methods.

DATA SOURCES The researcher can gather secondary data, primary data, or both. *Secondary data* are data that were collected for another purpose and already exist somewhere. *Primary data* are data freshly gathered for a specific purpose or for a specific research project.

Researchers usually start their investigation by examining some of the rich variety of secondary data to see whether the problem can be partly or wholly solved without collecting costly primary data. Secondary data provide a starting point and offer the advantages of low cost and ready availability. When the needed data do not exist or are dated, inaccurate, incomplete, or unreliable, the researcher will have to collect primary data. Most marketing research projects involve some primary-data collection. The normal procedure is to interview some people individually or in groups, to get a sense of how people feel about the topic in question, and then develop a formal research instrument, debug it, and carry it into the field.

A focus group in session, with marketing people observing through a two-way mirror.

RESEARCH APPROACHES Primary data can be collected in five main ways: through observation, focus groups, surveys, behavioral data, and experiments.

Observational Research Fresh data can be gathered by observing the relevant actors and settings.[8] Consumers can be unobtrusively observed as they shop or as they consume products. Ogilvy & Mather's Discovery Group creates documentary-style videos by sending researchers into consumers' homes with handheld video cameras. Hours of footage are edited to a 30-minute "highlight reel" which the group uses to analyze consumer behavior. Other researchers equip consumers with pagers and instruct them to write down what they are doing whenever prompted, or hold more informal interview sessions at a café or bar. The American Airlines researchers might meander around first-class lounges to hear how travelers talk about the different carriers and their features. They can fly on competitors' planes to observe in-flight service.

Focus Group Research A **focus group** is a gathering of six to ten people who are carefully selected based on certain demographic, psychographic, or other considerations and brought together to discuss at length various topics of interest. Participants are normally paid a small sum for attending. A professional research moderator provides questions and probes based on a discussion guide or agenda prepared by the responsible marketing managers to ensure that the right material gets covered.

Moderators attempt to track down potentially useful insights as they try to discern the real motivations of consumers and why they are saying and doing certain things. The sessions are typically recorded in some fashion, and marketing managers often remain behind two-way mirrors in the next room. In the American Airlines research, the moderator might start with a broad question, such as, "How do you feel about first-class air travel?" Questions then move to how people view the different airlines, different existing services, different proposed services, and specifically, Internet service. Although focus-group research has been shown to be a useful exploratory step, researchers must avoid generalizing the reported feelings of the focus-group participants to the whole market, because the sample size is too small and the sample is not drawn randomly. "Marketing Insight: Conducting Informative Focus Groups" has some practical tips to improve the quality of focus groups.

Survey Research Companies undertake surveys to learn about people's knowledge, beliefs, preferences, and satisfaction, and to measure these magnitudes in the general population. A company such as American Airlines might prepare its own survey instrument to gather the information it needs, or it might add questions to an omnibus survey that carries the questions of several companies, at a much lower cost. It can also put the questions to an ongoing consumer panel run by itself or another company. It may do a mall intercept study by having researchers approach people in a shopping mall and ask them questions.

Behavioral Data Customers leave traces of their purchasing behavior in store scanning data, catalog purchases, and customer databases. Much can be learned by analyzing these data. Customers' actual purchases reflect preferences and often are more reliable than statements they offer to market researchers. People may report preferences for popular brands, and yet the data show them actually buying other brands. For example, grocery

MARKETING INSIGHT | CONDUCTING INFORMATIVE FOCUS GROUPS

Focus groups allow marketers to observe how and why consumers accept or reject concepts, ideas, or any specific notion. The key to using focus groups successfully is to *listen.* It is critical to eliminate biases as much as possible. Although many useful insights can emerge from thoughtfully run focus groups, there can be questions as to their validity, especially in today's marketing environment.

Some researchers believe that consumers have been so bombarded with ads, they unconsciously (or perhaps cynically) parrot back what they have already heard as compared to what they think. There is also always a concern that participants are just trying to maintain their self-image and public persona or have a need to identify with the other members of the group. Participants may not be willing to admit in public—or may not even recognize—their behavior patterns and motivations. There is also always the "loudmouth" problem—when one highly opinionated person drowns out the rest of the group. It may be expensive to recruit qualified subjects ($3,000 to $5,000 per group), but getting the right participants is crucial.

Even when multiple groups are involved, it may be difficult to generalize the results to a broader population. For example, within the United States, focus-group findings often vary from region to region. One firm specializing in focus-group research claimed that the best city to conduct focus groups was Minneapolis because it could get a fairly well-educated sample of people who were honest and forthcoming about their opinions. Many marketers interpret focus groups carefully in New York and other northeastern cities because the people in these areas tend to be highly critical and generally do not report that they like much. Too often, managers become comfortable with a particular focus-group format and apply it generally and automatically to every circumstance. Europeans typically need more time than American marketers are usually willing to give—a focus group there rarely takes less than two hours and often more than four.

Participants must feel as relaxed as possible and feel a strong obligation to "speak the truth." Physical surroundings can be crucial. Researchers at one agency knew they had a problem when a fight broke out between participants at one of their sessions. As one executive noted, "we wondered why people always seemed grumpy and negative—people were resistant to any idea we showed them." The problem was the room itself: cramped, stifling, forbidding: "It was a cross between a hospital room and a police interrogation room." To fix the problem, the agency gave the room a makeover. Other firms are adapting the look of the room to fit the theme of the topic—like designing the room to look like a playroom when speaking to children.

Although many firms are substituting observational research for focus groups, ethnographic research can be expensive and tricky: Researchers have to be highly skilled, participants have to be on the level, and mounds of data have to be analyzed. The beauty of focus groups, as one marketing executive noted, is that "it's still the most cost-effective, quickest, dirtiest way to get information in rapid time on an idea." In analyzing the pros and cons, Wharton's Americus Reed might have said it best: "A focus group is like a chain saw. If you know what you're doing, it's very useful and effective. If you don't, you could lose a limb."

Sources: Sarah Stiansen, "How Focus Groups Can Go Astray," *Adweek*, December 5, 1988, pp. FK 4–6; Jeffrey Kasner, "Fistfights and Feng Shui," *Boston Globe*, July 21, 2001, pp. C1–C2; Leslie Kaufman, "Enough Talk," *Newsweek*, August 18, 1997, pp. 48–49; Linda Tischler, "Every Move You Make," *Fast Company*, April 2004, pp. 73–75; Alison Stein Wellner, "The New Science of Focus Groups," *American Demographics* (March 2003): 29–33; Dennis Rook, "Out-of-Focus Groups," *Marketing Research* 15; no. 2 (Summer 2003): 11; Dennis W. Rook, "Loss of Vision: Focus Groups Fail to Connect Theory, Current Practice," *Marketing News*, September 15, 2003, p. 40.

shopping data show that high-income people do not necessarily buy the more expensive brands, contrary to what they might state in interviews; and many low-income people buy some expensive brands. Clearly, American Airlines can learn many useful things about its passengers by analyzing ticket purchase records.

Experimental Research The most scientifically valid research is experimental research. The purpose of experimental research is to capture cause-and-effect relationships by eliminating competing explanations of the observed findings. To the extent that the design and execution of the experiment eliminate alternative hypotheses that might explain the results, research and marketing managers can have confidence in the conclusions.

Experiments call for selecting matched groups of subjects, subjecting them to different treatments, controlling extraneous variables, and checking whether observed response differences are statistically significant. To the extent that extraneous factors are eliminated or controlled, the observed effects can be related to the variations in the treatments. American Airlines might introduce in-flight Internet service on one of its regular flights from Chicago to Tokyo. It might charge $25 one week and charge only $15 the next week. If the plane carried approximately the same number of first-class passengers each week and the particular weeks made no difference, any significant difference in the number of calls made could be related to the different prices charged. The experimental design could be elaborated by trying other prices and including other air routes.

MARKETING MEMO — QUESTIONNAIRE DOS AND DON'TS

1. ***Ensure that questions are without bias.*** Do not lead the respondent into an answer.
2. ***Make the questions as simple as possible.*** Questions that include multiple ideas or two questions in one will confuse respondents.
3. ***Make the questions specific.*** Sometimes it is advisable to add memory cues. For example, it is good practice to be specific with time periods.
4. ***Avoid jargon or shorthand.*** Avoid trade jargon, acronyms, and initials not in everyday use.
5. ***Steer clear of sophisticated or uncommon words.*** Only use words in common speech.
6. ***Avoid ambiguous words.*** Words such as "usually" or "frequently" have no specific meaning.
7. ***Avoid questions with a negative in them.*** It is better to say "Do you ever . . . ?" than "Do you never . . . ?"
8. ***Avoid hypothetical questions.*** It is difficult to answer questions about imaginary situations. Answers cannot necessarily be trusted.
9. ***Do not use words that could be misheard.*** This is especially important when the interview is administered over the telephone. "What is your opinion of sects?" could yield interesting but not necessarily relevant answers.
10. ***Desensitize questions by using response bands.*** For questions that ask people their age or companies their employee turnover, it is best to offer a range of response bands.
11. ***Ensure that fixed responses do not overlap.*** Categories used in fixed response questions should be sequential and not overlap.
12. ***Allow for "other" in fixed response questions.*** Precoded answers should always allow for a response other than those listed.

Source: Adapted from Paul Hague and Peter Jackson, *Market Research: A Guide to Planning, Methodology, and Evaluation* (London: Kogan Page, 1999). See also, Hans Baumgartner and Jan-Benedict E. M. Steenkamp, "Response Styles in Marketing Research: A Cross-National Investigation," *Journal of Marketing Research* (May 2001): 143–156.

RESEARCH INSTRUMENTS Marketing researchers have a choice of three main research instruments in collecting primary data: questionnaires, qualitative measures, and mechanical devices.

Questionnaires A questionnaire consists of a set of questions presented to respondents. Because of its flexibility, the questionnaire is by far the most common instrument used to collect primary data. Questionnaires need to be carefully developed, tested, and debugged before they are administered on a large scale. In preparing a questionnaire, the researcher carefully chooses the questions and their form, wording, and sequence. The form of the question can influence the response. Marketing researchers distinguish between closed-end and open-end questions. Closed-end questions specify all the possible answers and provide answers that are easier to interpret and tabulate. Open-end questions allow respondents to answer in their own words and often reveal more about how people think. They are especially useful in exploratory research, where the researcher is looking for insight into how people think rather than measuring how many people think a certain way. Table 4.1 provides examples of both types of questions; and see "Marketing Memo: Questionnaire Dos and Don'ts."

Qualitative Measures Some marketers prefer more qualitative methods for gauging consumer opinion because consumer actions do not always match their answers to survey questions. *Qualitative research techniques* are relatively unstructured measurement approaches that permit a range of possible responses, and they are a creative means of ascertaining consumer perceptions that may otherwise be difficult to uncover. The range of possible qualitative research techniques is limited only by the creativity of the marketing researcher. Here are seven techniques employed by design firm IDEO for understanding the customer experience:[9]

- *Shadowing*—observing people using products, shopping, going to hospitals, taking the train, using their cell phones.
- *Behavior mapping*—photographing people within a space, such as a hospital waiting room, over two or three days.
- *Consumer journey*—keeping track of all the interactions a consumer has with a product, service, or space.

TABLE 4.1 Types of Questions

Name	Description	Example
A. Closed-end Questions		
Dichotomous	A question with two possible answers.	In arranging this trip, did you personally phone American? Yes No
Multiple choice	A question with three or more answers.	With whom are you traveling on this flight? ☐ No one ☐ Children only ☐ Spouse ☐ Business associates/friends/relatives ☐ Spouse and children ☐ An organized tour group
Likert scale	A statement with which the respondent shows the amount of agreement/disagreement.	Small airlines generally give better service than large ones. Strongly disagree 1___ Disagree 2___ Neither agree nor disagree 3___ Agree 4___ Strongly agree 5___
Semantic differential	A scale connecting two bipolar words. The respondent selects the point that represents his or her opinion.	American Airlines Large -- Small Experienced ------------------------------------ Inexperienced Modern --- Old-fashioned
Importance scale	A scale that rates the importance of some attribute.	Airline food service to me is Extremely important 1___ Very important 2___ Somewhat important 3___ Not very important 4___ Not at all important 5___
Rating scale	A scale that rates some attribute from "poor" to "excellent."	American food service is Excellent 1___ Very Good 2___ Good 3___ Fair 4___ Poor 5___
Intention-to-buy scale	A scale that describes the respondent's intention to buy.	If an in-flight telephone were available on a long flight, I would Definitely buy 1___ Probably buy 2___ Not sure 3___ Probably not buy 4___ Definitely not buy 5___
B. Open-end Questions		
Completely unstructured	A question that respondents can answer in an almost unlimited number of ways.	What is your opinion of American Airlines?
Word association	Words are presented, one at a time, and respondents mention the first word that comes to mind.	What is the first word that comes to your mind when you hear the following? Airline ______________ American ______________ Travel ______________
Sentence completion	An incomplete sentence is presented and respondents complete the sentence.	When I choose an airline, the most important consideration in my decision is ______________.
Story completion	An incomplete story is presented, and respondents are asked to complete it.	"I flew American a few days ago. I noticed that the exterior and interior of the plane had very bright colors. This aroused in me the following thoughts and feelings. . . ." Now complete the story.
Picture	A picture of two characters is presented, with one making a statement. Respondents are asked to identify with the other and fill in the empty balloon.	
Thematic Apperception Test (TAT)	A picture is presented and respondents are asked to make up a story about what they think is happening or may happen in the picture.	

- *Camera journals*—asking consumers to keep visual diaries of their activities and impressions relating to a product.
- *Extreme user interviews*—talking to people who really know—or know nothing—about a product or service and evaluating their experience using it.
- *Storytelling*—prompting people to tell personal stories about their consumer experiences.
- *Unfocus groups*—interviewing a diverse group of people: To explore ideas about sandals, IDEO gathered an artist, a bodybuilder, a podiatrist, and a shoe fetishist.

Because of the freedom afforded both researchers in their probes and consumers in their responses, qualitative research can often be a useful first step in exploring consumers' brand and product perceptions. There are also drawbacks to qualitative research. The in-depth insights that emerge have to be tempered by the fact that the samples involved are often very small and may not necessarily generalize to broader populations. Moreover, given the qualitative nature of the data, there may also be questions of interpretation. Different researchers examining the same results from a qualitative research study may draw very different conclusions. "Marketing Insight: Getting into Consumers' Heads with Qualitative Research" describes some popular approaches.

MARKETING INSIGHT | GETTING INTO CONSUMERS' HEADS WITH QUALITATIVE RESEARCH

Here are some commonly used qualitative research approaches to getting inside consumers' minds and finding out what they are thinking or feeling about brands and products:

1. ***Word associations.*** People can be asked what words come to mind when they hear the brand's name. "What does the Timex name mean to you? Tell me what comes to mind when you think of Timex watches." The primary purpose of free association tasks is to identify the range of possible brand associations in consumers' minds. But they may also provide some rough indication of the relative strength, favorability, and uniqueness of brand associations too.
2. ***Projective techniques.*** People are presented an incomplete stimulus and asked to complete it or given an ambiguous stimulus that may not make sense in and of itself and are asked to make sense of it. The argument is that people will reveal their true beliefs and feelings. One such approach is "bubble exercises" based on cartoons or photos. Different people are depicted buying or using certain products or services. Empty bubbles, like those found in cartoons, are placed in the scenes to represent the thoughts, words, or actions of one or more of the participants. People are then asked to "fill in the bubble" by indicating what they believed was happening or being said. Another technique is comparison tasks. People are asked to convey their impressions by comparing brands to people, countries, animals, activities, fabrics, occupations, cars, magazines, vegetables, nationalities, or even other brands.
3. ***Visualization.*** People can be asked to create a collage from magazine photos or drawings to depict their perceptions. ZMET is a research technique that starts with a group of participants, who are asked in advance to select a minimum of 12 images from their own sources (e.g., magazines, catalogs, and family photo albums) that represent their thoughts and feelings about the research topic. The participants bring these images to a personal one-on-one interview with a study administrator, who uses advanced interview techniques to explore the images with the participant and reveal hidden meanings. Finally, the participants use a computer program to create a collage with these images that communicates their subconscious thoughts and feelings about the topic. One ZMET study probed what women thought of panty hose. Twenty hose-wearing women were asked to collect pictures that captured their feelings about wearing panty hose. Some of the pictures showed fence posts encased in plastic wrap or steel bands strangling trees, suggesting that panty hose are tight and inconvenient. Another picture showed tall flowers in a vase, suggesting that the product made a woman feel thin, tall, and sexy.
4. ***Brand personification.*** People can be asked to describe what kind of person they think of when the brand is mentioned: "If the brand were to come alive as a person, what would it be like, what would it do, where would it live, what would it wear, who would it talk to if it went to a party (and what would it talk about)?" For example, they may say that the John Deere brand makes them think of a rugged Midwestern male who is hardworking and trustworthy. The brand personality delivers a picture of the more human qualities of the brand.
5. ***Laddering.*** A series of increasingly more specific "why" questions can be used to gain insight into consumer motivation and consumers' deeper, more abstract goals. Ask why someone wants to buy a Nokia cellular phone. "They look well built" (attribute). "Why is it important that the phone be well built?" "It suggests that the Nokia is reliable" (a functional benefit). "Why is reliability important?" "Because my colleagues or family can be sure to reach me" (an emotional benefit). "Why must you be available to them at all times?" "I can help them if they are in trouble" (brand essence). The brand makes this person feel like a Good Samaritan, ready to help others.

Sources: Allen Adamson, "Why Traditional Brand Positioning Can't Last," *Brandweek*, November 17, 2003, pp. 38–40; Todd Wasserman, "Sharpening the Focus," *Brandweek*, November 3, 2003, pp. 28–32; Linda Tischler, "Every Move You Make," *Fast Company*, April 2004, pp. 73–75; Gerald Zaltman, *How Customers Think: Essential Insights into the Mind of the Market* (Boston: Harvard Business School Press, 2003).

Mechanical Devices Mechanical devices are occasionally used in marketing research. For example, galvanometers can measure the interest or emotions aroused by exposure to a specific ad or picture. The tachistoscope flashes an ad to a subject with an exposure interval that may range from less than one hundredth of a second to several seconds. After each exposure, the respondent describes everything he or she recalls. Eye cameras study respondents' eye movements to see where their eyes land first, how long they linger on a given item, and so on. As one would expect, in recent years technology has advanced to such a degree that now devices like skin sensors, brain wave scanners, and full body scanners are being used to get consumer responses.[10]

Technology has replaced the diaries that participants in media surveys used to have to keep. Audiometers can be attached to television sets in participating homes to record when the set is on and to which channel it is tuned. Electronic devices can record the number of radio programs a person is exposed to during the day or, using Global Positioning System (GPS) technology, how many billboards a person may walk by or drive by during a day.

SAMPLING PLAN After deciding on the research approach and instruments, the marketing researcher must design a sampling plan. This calls for three decisions:

1. ***Sampling unit: Who is to be surveyed?*** The marketing researcher must define the target population that will be sampled. In the American Airlines survey, should the sampling unit be only first-class business travelers, first-class vacation travelers, or both? Should travelers under age 18 be interviewed? Should both husbands and wives be interviewed? Once the sampling unit is determined, a sampling frame must be developed so that everyone in the target population has an equal or known chance of being sampled.
2. ***Sample size: How many people should be surveyed?*** Large samples give more reliable results than small samples. However, it is not necessary to sample the entire target population or even a substantial portion to achieve reliable results. Samples of less than 1 percent of a population can often provide good reliability, with a credible sampling procedure.
3. ***Sampling procedure: How should the respondents be chosen?*** To obtain a representative sample, a probability sample of the population should be drawn. Probability sampling allows the calculation of confidence limits for sampling error. Thus, one could conclude after the sample is taken that "the interval 5 to 7 trips per year has 95 chances in 100 of containing the true number of trips taken annually by first-class passengers flying between Chicago and Tokyo." Three types of probability sampling are described in Table 4.2 part A. When the cost or time involved in probability sampling is too high, marketing researchers will take nonprobability samples. Table 4.2 part B describes three types. Some marketing researchers feel that nonprobability

TABLE 4.2

Probability and Nonprobability Samples

A. Probability Sample	
Simple random sample	Every member of the population has an equal chance of selection.
Stratified random sample	The population is divided into mutually exclusive groups (such as age groups), and random samples are drawn from each group.
Cluster (area) sample	The population is divided into mutually exclusive groups (such as city blocks), and the researcher draws a sample of the groups to interview.
B. Nonprobability Sample	
Convenience sample	The researcher selects the most accessible population members.
Judgment sample	The researcher selects population members who are good prospects for accurate information.
Quota sample	The researcher finds and interviews a prescribed number of people in each of several categories.

samples are very useful in many circumstances, even though they do not allow sampling error to be measured.

CONTACT METHODS Once the sampling plan has been determined, the marketing researcher must decide how the subject should be contacted: mail, telephone, personal, or online interview.

Mail Questionnaire The *mail questionnaire* is the best way to reach people who would not give personal interviews or whose responses might be biased or distorted by the interviewers. Mail questionnaires require simple and clearly worded questions. Unfortunately, the response rate is usually low or slow.

Telephone Interview *Telephone interviewing* is the best method for gathering information quickly; the interviewer is also able to clarify questions if respondents do not understand them. The response rate is typically higher than in the case of mailed questionnaires. The main drawback is that the interviews have to be short and not too personal. Telephone interviewing is getting more difficult because of consumers' growing antipathy toward telemarketers calling them in their homes and interrupting their lives. In late 2003, Congress passed legislation allowing the Federal Trade Commission to restrict telemarketing calls to consumers through its "Do Not Call" registry. Even though marketing research firms are exempt, many think that the legislation spells the beginning of the end of telephone surveys as a marketing research method.

Personal Interview *Personal interviewing* is the most versatile method. The interviewer can ask more questions and record additional observations about the respondent, such as dress and body language. At the same time, personal interviewing is the most expensive method and requires more administrative planning and supervision than the other three. It is also subject to interviewer bias or distortion. Personal interviewing takes two forms. In *arranged interviews*, respondents are contacted for an appointment, and often a small payment or incentive is offered. *Intercept interviews* involve stopping people at a shopping mall or busy street corner and requesting an interview. Intercept interviews can have the drawback of being nonprobability samples, and the interviews must not require too much time.

An intercept interview at a mall.

Online Interview There is increased use of online methods. Online research was up 20 to 30 percent in 2003 and was expected to continue along the same growth trajectory in 2004. Furthermore, online research is estimated to make up 25 percent of all survey-based research in 2004.[11]

There are so many ways to use the Net to do research. A company can include a questionnaire on its Web site and offer an incentive to answer the questionnaire; or it can place a banner on some frequently visited site such as Yahoo!, inviting people to answer some questions and possibly win a prize. The company can sponsor a chat room or bulletin board and introduce questions from time to time, or host a real-time panel or virtual focus group. A company can learn about individuals who visit its site by following how they *clickstream* through the Web site and move to other sites. A company can post different prices, use different headlines, offer different product features on different Web sites or at different times to learn the relative effectiveness of its offerings.

Online product testing, in which companies float trial balloons for new products, is also growing and providing information much faster than traditional marketing research techniques used to develop new products. For instance, marketers for Mattel's Hot Wheels toys rely heavily on the Web to interact with collectors to help develop new products, promotions, and licensed goods.

Following one fan survey, marketing executives learned that they could expand licensed offerings to boys ages 11 to 16 to keep them in the brand franchise, resulting in extended partnerships with Bell Motorcycles and BMX bikes.[12]

HERSHEY'S FOOD CORP.

Candymaker Hershey was an early innovator in the area of online product testing. In 1999 through 2000, the company moved its new product testing online along with its entire historical product testing. It combined more than 1,200 historical concept tests with about 300 to 400 online test results to create an online "turnkey" system that works both as a reporting tool and as an archival system. The move to online product testing has cut Hershey's new product development process by two-thirds—a strategic advantage in a mature market—and keeps a wealth of institutional data on hand even as research personnel change over the years.[13]

While marketers are right to be infatuated with the possibilities of online research, it's important to remember that the field is still in its infancy and is constantly evolving to meet the needs of companies, advertising agencies, and consumers. "Marketing Memo: Pros and Cons of Online Research" outlines some of the advantages and disadvantages of online research thus far.

Step 3: Collect the Information

The data collection phase of marketing research is generally the most expensive and the most prone to error. In the case of surveys, four major problems arise. Some respondents will not be at home and must be contacted again or replaced. Other respondents will refuse to cooperate. Still others will give biased or dishonest answers. Finally, some interviewers will be biased or dishonest. Getting the right respondents is critical.

MEDIAMARK RESEARCH

Mediamark Research interviews 26,000 Americans in their homes on the kinds of media they use, the brands and products they use, and their attitudes toward topics such as sports and politics. Up until 2002, however, the company had tended to exclude non-English-speaking Hispanics from the research. As the Hispanic population increased in numbers and buying power, the company recognized that it could no longer afford this limiting and potentially biased approach. Mediamark recruited a bilingual traveling task force so that when interviewers come to a Hispanic household, respondents can answer the survey in English or Spanish. They also are creating a more seamless interviewing database by asking the same questions to all people no matter what language they speak and what level of acculturation they have.[14]

Data collection methods are rapidly improving thanks to computers and telecommunications. Some research firms interview from a centralized location. Professional interviewers sit in booths and draw telephone numbers at random. When the phone is answered, the interviewer reads a set of questions from a monitor and types the respondents' answers into a computer. This procedure eliminates editing and coding, reduces errors, saves time, and produces all the required statistics. Other research firms have set up interactive terminals in shopping centers. Persons willing to be interviewed sit at a terminal, read the questions from the monitor, and type in their answers.

One savvy marketer gets primary data via online surveys from a highly coveted demographic as they play games.

NEOPETS.COM

With more than 22 million members and 27,000 new ones joining every day, Neopets is one of the most popular children's Web sites. The Web site is free, and it allows users to create, nurture, and care for cyberpets as they earn "neopoints." They raise their neopet in a virtual neighborhood that includes eating at

MARKETING MEMO | PROS AND CONS OF ONLINE RESEARCH

Advantages

- *Online research is inexpensive.* The cost of gathering survey information electronically is much less expensive than by traditional means. A typical e-mail survey costs about half what a conventional survey costs, and return rates can be as high as 50 percent. For instance, Virgin.net used online research to launch its broadband service in the United Kingdom in 2002. Now the company does all its research online. The brand has seen an increase in response rates from 17 percent with paper-based research to almost 72 percent and costs have dropped 90 percent.
- *Online research is faster.* Online surveys are faster to complete since the survey can automatically direct respondents to applicable questions and be sent electronically to the research supplier once finished. One estimate is that 75 to 80 percent of a survey's targeted response can be generated in 48 hours using online methods, as compared to a telephone survey that can take 70 days to obtain 150 interviews.
- *People tend to be more honest online than they are in personal or telephone interviews.* Britain's online polling company YouGov.com took 500 people and surveyed half via intercom in a booth and the other half online, asking them politically correct questions such as "Should there be more aid to Africa?" Online answers were deemed much more honest. People may be more open about their opinions when they can respond to a survey privately and not to another person whom they feel might be judging them, especially on sensitive topics.
- *Online research is more versatile.* The multimedia applications of online research are especially advantageous. For instance, virtual reality software lets visitors inspect 3-D models of products such as cameras, cars, and medical equipment, and product characteristics can be easily manipulated online. Even at the most basic level, online surveys make answering a questionnaire easier and more fun than paper-and-pencil versions.

Disadvantages

- *Samples can be small and skewed.* Perhaps the largest criticism leveled against online research is that not everyone is online. Research subjects who respond to online surveys are more likely to be tech-savvy middle-class males. Some 40 percent of households are without Internet access in the United States—and there is an even higher percentage without access when you reach out to international markets. These people are likely to differ in socioeconomic and education levels from those online. While marketers can be certain that more and more people will go online, it is important for online market researchers to find creative ways to reach certain population segments that are less likely to be online, such as older Americans or Hispanics. One option is to combine offline sources with online findings. Providing temporary Internet access at locations such as malls and recreation centers is another strategy. Some research firms use statistical models to fill in the gaps in market research left by offline consumer segments.
- *Online market research is prone to technological problems and inconsistencies.* Because online research is a relatively new method, many market researchers have not gotten survey designs right. A common error occurs in transferring a written survey to the screen. Others overuse technology, concentrating on the bells and whistles and graphics, while ignoring basic survey design guidelines. Problems also arise because browser software varies. The Web designer's final product may be seen very differently depending upon the research subject's screen and operating system.

Sources: Catherine Arnold, "Not Done Net; New Opportunities Still Exist in Online Research," *Marketing News*, April 1, 2004, p. 17; Nima M. Ray and Sharon W. Tabor, "Contributing Factors; Several Issues Affect e-Research Validity," *Marketing News*, September 15, 2003, p. 50; Louella Miles, "Online, On Tap," *Marketing*, June 16, 2004, pp. 39–40; Joe Dysart, "Cutting Market Research Costs with On-Site Surveys," *The Secured Lender* (March/April 2004): 64–67; Suzy Bashford, "The Opinion Formers," *Revolution*, May 2004, pp. 42–46; Bob Lamons, "Eureka! Future of B-to-B Research is Online," *Marketing News*, September 24, 2001, pp. 9–10.

McDonald's, watching Disney movie clips, feeding pets General Mills cereal, or playing Reese's Puffs Mini Golf with them. In this unique form of interactive product placement, advertisers pay to become part of the branded Neopet environment. In return, they get increased exposure to their products or services and data on their target market's consumer behavior. "We live and breathe market research," says Rik Kinney, executive vice president of the Glendale, California, company. The primary research mechanism at Neopets is a link to an online survey, prominently displayed on the homepage. Members are rewarded with Neopoints for answering questions about their shopping habits, and users complete 6,000 to 8,000 surveys a day. Interestingly, despite building a profitable business around selling information on its loyal users, Neopets has won kudos from privacy advocates because the company only releases data about its user base as a whole or about certain segments, but does not reveal any facts on individual users.[15]

MARKETING INSIGHT | GLOBAL ONLINE MARKET RESEARCH CHALLENGES

When chipmaker Intel Research wanted to know how people in countries around the world use technology, it sent an anthropologist to find out. Dr. Genevieve Bell visited 100 households in 19 cities in 7 countries in Asia and the Pacific. She came back to Intel with 20 gigabytes of digital photos, 19 field notebooks, and insights about technology, culture, and design that would challenge company assumptions about digital technology.

It stands to reason that Intel—a global tech powerhouse—would want to know how technology is used in its international markets. Yet all companies have a stake in knowing how the rest of the world sees and uses what most Westerners take for granted: Internet technology. With online research becoming the fastest-growing market research tool, marketers with global ambitions need to know which countries are online and why, or why not.

Internet penetration is low in most parts of Asia, Latin America, and Central and Eastern Europe. In Brazil, for example, only 7 percent of the population is online. While most people assume that the low penetration is due to economies that don't support an expensive technological infrastructure, there are other factors involved. There's climate, for one. In Malaysia, power surges caused by monsoons can fry computer motherboards. Government is also a powerful spur or barrier to Internet penetration. While the Chinese economy is zooming ahead, it's unlikely the authoritarian Chinese government will feel comfortable with market researchers gathering information from its citizens via the Internet. Contrast this with South Korea, where the government has made widespread broadband Internet access a priority, and has provided incentives to PC makers to bring cheaper models to market.

Other significant factors that can keep computers and Wi-Fi and data ports from crossing the threshold are religion and culture. Dr. Bell found that values of humility and simplicity are deemed incompatible with Internet technology and make it less welcome in some Hindu homes in India or Muslim homes in Malaysia and Indonesia. She also noted that while Americans have private space in the home for leisure activities, Japan's tighter quarters afford little privacy. This may explain the huge popularity of text messaging on mobile phones among Japan's young people.

Dr. Bell's findings on global responses to technology point up one of the biggest obstacles to conducting international research, whether online or not: a lack of consistency. Nan Martin, global accounts director for Synovate Inc., a market research firm with offices in 46 countries, says: "In global research, we have to adapt culturally to how, where and with whom we are doing the research . . . A simple research study conducted globally becomes much more complicated as a result of the cultural nuances, and it's necessary for us to be sensitive to those nuances in data collection and interpretation." For instance, suppose Internet penetration is equal. In Latin America, where consumers are uncomfortable with the impersonal nature of the Internet, researchers might need to incorporate interactive elements into a survey so participants feel they are talking to a real person. In Asia, focus groups are challenging because of the cultural tendency to conform. Online surveys may bring more honest responses and keep respondents from "losing face."

And what if a researcher collects data face-to-face in Mexico, but by Internet in the United States? Nan Martin says that, "not only are the subjects answering the question differently because of cultural difference, but the data are being collected by a different method. That can shake the underpinnings of how research scientists feel about collecting data: that every time you change a variable, you're making interpretation of the results more challenging. It is so challenging, in fact, that some say this is an area where global marketers are best served by hiring an expert—an outside research firm with an expertise in acquiring and analyzing international data."

Sources: Arundhati Parmar, "Stumbling Blocks; Net Research Is Not Quite Global," *Marketing News*, March 3, 2003, p. 51; Catherine Arnold, "Global Perspective; Synovate Exec Discusses Future of International Research," *Marketing News*, May 15, 2004, p. 43; Michael Erard, "For Technology, No Small World After All," *New York Times*, May 6, 2004, p. G5; Deborah L. Vence, "Global Consistency: Leave It to the Experts," *Marketing News*, April 28, 2003, p. 37.

It is important to recognize that not everyone in the sample population will be online. (See "Marketing Insight: Global Online Market Research Challenges.")

Step 4: Analyze the Information

The next-to-last step in the process is to extract findings from the collected data. The researcher tabulates the data and develops frequency distributions. Averages and measures of dispersion are computed for the major variables. The researcher will also apply some advanced statistical techniques and decision models in the hope of discovering additional findings.

Step 5: Present the Findings

As the last step, the researcher presents the findings. The researcher should present findings that are relevant to the major marketing decisions facing management. The main survey findings for the American Airlines case show that:

1. The chief reasons for using in-flight Internet service are to pass the time surfing, and to send and receive messages from colleagues and family. The charge would be put on passengers' charge accounts and paid by their companies.

2. About 5 first-class passengers out of every 10 would use the Internet service during a flight at \$25; about 6 would use it at \$15. Thus, a charge of \$15 would produce less revenue (\$90 = 6 × \$15) than \$25 (\$125 = 5 × \$25). By charging \$25, AA would collect \$125 per flight. Assuming that the same flight takes place 365 days a year, AA would annually collect \$45,625 (= \$125 × 365). Since the investment is \$90,000, it will take approximately two years before American Airlines breaks even.
3. Offering in-flight service would strengthen the public's image of American Airlines as an innovative and progressive airline. American would gain some new passengers and customer goodwill.

Step 6: Make the Decision

The managers who commissioned the research need to weigh the evidence. If their confidence in the findings is low, they may decide against introducing the in-flight Internet service. If they are predisposed to launching the service, the findings support their inclination. They may even decide to study the issues further and do more research. The decision is theirs, but hopefully the research provided them with insight into the problem. (See Table 4.3.)[16]

A growing number of organizations are using a marketing decision support system to help their marketing managers make better decisions. MIT's John Little defines a **marketing decision support system (MDSS)** as a coordinated collection of data, systems, tools, and techniques with supporting software and hardware by which an organization gathers and interprets relevant information from business and environment and turns it into a basis for marketing action.[17]

A classic MDSS example is the CALLPLAN model which helps salespeople determine the number of calls to make per period to each prospect and current client. The model takes into account travel time as well as selling time. When launched, the model was tested at United Airlines with an experimental group that managed to increase its sales over a matched control group by 8 percentage points.[18] Once a year, *Marketing News* lists hundreds of current marketing and sales software programs that assist in designing marketing research studies, segmenting markets, setting prices and advertising budgets, analyzing media, and planning sales force activity.

TABLE 4.3

The Seven Characteristics of Good Marketing Research

1. Scientific method.	Effective marketing research uses the principles of the scientific method: careful observation, formulation of hypotheses, prediction, and testing.
2. Research creativity.	At its best, marketing research develops innovative ways to solve a problem: a clothing company catering to teenagers gave several young men video cameras, then used the videos for focus groups held in restaurants and other places teens frequent.
3. Multiple methods.	Marketing researchers shy away from overreliance on any one method. They also recognize the value of using two or three methods to increase confidence in the results.
4. Interdependence of models and data.	Marketing researchers recognize that data are interpreted from underlying models that guide the type of information sought.
5. Value and cost of information.	Marketing researchers show concern for estimating the value of information against its cost. Costs are typically easy to determine, but the value of research is harder to quantify. It depends on the reliability and validity of the findings and management's willingness to accept and act on those findings.
6. Healthy skepticism.	Marketing researchers show a healthy skepticism toward glib assumptions made by managers about how a market works. They are alert to the problems caused by "marketing myths."
7. Ethical marketing.	Marketing research benefits both the sponsoring company and its customers. The misuse of marketing research can harm or annoy consumers, increasing resentment at what consumers regard as an invasion of their privacy or a disguised sales pitch.

Overcoming Barriers to the Use of Marketing Research

In spite of the rapid growth of marketing research, many companies still fail to use it sufficiently or correctly, for several reasons:[19]

- ***A narrow conception of the research.*** Many managers see marketing research as a fact-finding operation. They expect the researcher to design a questionnaire, choose a sample, conduct interviews, and report results, often without a careful definition of the problem or of the decisions facing management. When fact-finding fails to be useful, management's idea of the limited usefulness of marketing research is reinforced.
- ***Uneven caliber of researchers.*** Some managers view marketing research as little more than a clerical activity and treat it as such. Less competent marketing researchers are hired, and their weak training and deficient creativity lead to unimpressive results. The disappointing results reinforce management's prejudice against marketing research. Management continues to pay low salaries to its market researchers, thus perpetuating the basic problem.
- ***Poor framing of the problem.*** In the famous case where Coca-Cola introduced the New Coke after much research, the failure of the New Coke was largely due to not setting up the research problem correctly, from a marketing perspective. The issue was how consumers felt about Coca-Cola as a brand and not necessarily the taste in isolation.
- ***Late and occasionally erroneous findings.*** Managers want results that are accurate and conclusive. They may want the results tomorrow. Yet good marketing research takes time and money. Managers are disappointed when marketing research costs too much or takes too much time.
- ***Personality and presentational differences.*** Differences between the styles of line managers and marketing researchers often get in the way of productive relationships. To a manager who wants concreteness, simplicity, and certainty, a marketing researcher's report may seem abstract, complicated, and tentative. Yet in the more progressive companies, marketing researchers are being included as members of the product management team, and their influence on marketing strategy is growing.

Failure to use marketing research properly has led to numerous gaffes, including this historic one:

STAR WARS

In the 1970s, a successful research executive left General Foods for a daring gambit: Bring market research to Hollywood to give film studios access to the same research that had spurred General Foods' success. A major studio handed him a science fiction film proposal and asked him to research and predict its success or failure: His views would inform their decision about whether or not to back the film. He concluded the film would fail. For one, he argued, Watergate had made America less trusting of its institutions and, as a result, Americans in the 1970s prized realism and authenticity over science fiction. This particular film also had the word "war" in its title; he reasoned that America, suffering from its post-Vietnam hangover, would stay away in droves. The film was *Star Wars*. What this researcher delivered was information, not insight. He failed to study the script itself, to see that it was a fundamentally human story—of love, conflict, loss, and redemption—that merely played out against the backdrop of space.[20]

::: Measuring Marketing Productivity

An important task of marketing research is to assess the efficiency and effectiveness of marketing activities. Marketers increasingly are being held accountable for their investments and must be able to justify marketing expenditures to senior management.[21] In a recent Accenture survey, 70 percent of marketing executives stated that they did not have a handle on the return on their marketing investments.[22] Another study revealed that 63 percent of senior management said they were dissatisfied with their marketing performance measurement system and wanted marketing to supply prior and posterior estimates of the impact of marketing programs.[23] With marketing costs already high and continuing to rise, senior executives are tired of seeing what they consider to be wasteful marketing—failed new products and lavish ad campaigns, extensive sales calls, and expensive promotions that are unable to move the sales needle.

Marketing research can help address this increased need for accountability. Two complementary approaches to measure marketing productivity are: (1) marketing metrics to assess marketing effects and (2) marketing-mix modeling to estimate causal relationships and how marketing activity affects outcomes. Some developments in the financial tools that can be used to measure key marketing assets are described in "Marketing Insight: Seeing the Big Picture and Getting to the Bottom Line in Marketing."

Marketing Metrics

Marketers employ a wide variety of measures to assess marketing effects. **Marketing metrics** is the set of measures that helps firms to quantify, compare, and interpret their marketing performance. Marketing metrics can be used by brand managers to design marketing programs and by senior management to decide on financial allocations. When marketers can estimate the dollar contribution of marketing activities, they are better able to justify the value of marketing investments to senior management.[24]

MARKETING INSIGHT | SEEING THE BIG PICTURE AND GETTING TO THE BOTTOM LINE IN MARKETING

To provide a financial overview of marketing activity, several authors have developed new approaches to thinking about marketing. Here are three notable ones.

Peter Doyle maintains that:

> value-based marketing is not primarily about numbers. . . . [Rather,] it consists of three main elements. First is a set of beliefs about the objectives of marketing. The . . . primary task is to develop strategies that will maximize shareholder return. . . . Second is a set of principles for choosing marketing strategies and making marketing decisions that are consistent with these beliefs. These principles are based on estimating the future cash flow associated with a strategy to calculate the shareholder value added. Finally, it is a set of processes that ensure that marketing develops, selects, and implements a strategy that is consistent with these beliefs and principles. These processes concern management of the financial, marketing and organizational value drivers of the business. The financial value drivers are those key ratios that have the most significant impact on shareholder value. The marketing drivers are the customer-oriented plans necessary to drive improvement in the financial ratios. The organizational value drivers are the core capabilities, systems and leadership styles needed to create and implement the shareholder value orientation in the business.

According to Doyle, financial value drivers relate to sales growth, operating margin, and investment; marketing value drivers relate to strong brands, customer loyalty, strategic relationships, market selection, and differential advantage.

Roger Best maintains that:

> Market-based management is at the base of a business with a strong market orientation. A strong market orientation translates into a strong customer focus, competitor orientation, and a team approach that cuts across organizational functions. The result is a market-based business that is in a strong position to develop and deliver market-based strategies designed to attract, satisfy, and retain customers. Implemented successfully across a wide range of market situations, a market-based approach . . . will deliver higher levels of profitability, cash flow, and shareholder value than will a cost-based approach.

Best maintains that the only source of positive cash flow is the customer and therefore the customer must be the focus of market-based management.

Tim Ambler suggests that if firms think they are already measuring marketing performance adequately, they should ask themselves five questions:

1. Do you routinely research consumer behavior (retention, acquisition, usage, etc.) and why consumers behave that way (awareness, satisfaction, perceived quality, etc.)?
2. Are the results of this research routinely reported to the board in a format integrated with financial marketing metrics?
3. In those reports, are the results compared with the levels previously forecasted in the business plans?
4. Are they also compared with the levels achieved by your key competitor using the same indicators?
5. Is short-term performance adjusted according to the change in your marketing-based asset(s)?

Ambler believes firms must give priority to measuring and reporting marketing performance through marketing metrics. He believes evaluation can be split into two parts: (1) short-term results and (2) changes in brand equity. Short-term results often reflect profit-and-loss concerns as shown by sales turnover, shareholder value, or some combination of the two. Brand-equity measures include awareness, market share, relative price, number of complaints, distribution and availability, total number of customers, perceived quality, and loyalty/retention. Ambler also recommends developing employee measures and metrics, arguing that "End users are the ultimate customers, but your own staff are your first; you need to measure the health of the internal market."

Sources: Peter Doyle, *Value-Based Marketing: Marketing Strategies for Corporate Growth and Shareholder Value* (Chichester, England: John Wiley & Sons, 2000); Roger J. Best, *Market-Based Management: Strategies for Growing Customer Value and Profitability*, 2nd ed. (Upper Saddle River, NJ: Prentice Hall, 2000); Tim Ambler, *Marketing and the Bottom Line: The New Methods of Corporate Wealth* (London: Financial Times/Prentice Hall, 2000).

TABLE 4.4

Sample Marketing Metrics

I. External	II. Internal
Awareness	Awareness of goals
Market share (volume or value)	Commitment to goals
Relative price (market share value/volume)	Active innovation support
Number of complaints (level of dissatisfaction)	Resource adequacy
Consumer satisfaction	Staffing/skill levels
Distribution/availability	Desire to learn
Total number of customers	Willingness to change
Perceived quality/esteem	Freedom to fail
Loyalty/retention	Autonomy
Relative perceived quality	Relative employee satisfaction

Source: Tim Ambler, "What Does Marketing Success Look Like?" *Marketing Management* (Spring 2001), 13–18.

Many marketing metrics relate to customer-level concerns such as their attitudes and behavior; others relate to brand-level concerns such as market share, relative price premium, or profitability.[25] Companies can also monitor an extensive set of metrics internal to the company. One important set of measures relates to a firm's innovativeness. For example, 3M tracks the proportion of sales resulting from its recent innovations. Another key set relates to employees. Table 4.4 summarizes a list of popular internal and external marketing metrics from a survey in the United Kingdom.[26]

Amazon.com is a firm renowned for constantly monitoring its marketing activities. CEO Jeff Bezos wants to know average customer contacts per order, average time per contact, the breakdown of e-mail versus telephone contacts, and the total cost to the company of each. The man in charge of Amazon's customer service and its warehouse and distribution operations looks at about 300 charts a week for his division.[27]

Firms are also employing organizational processes and systems to make sure that the value of all of these different metrics is maximized by the firm. A summary set of relevant internal and external measures can be assembled in a *marketing dashboard* for synthesis and interpretation. Some companies are also appointing marketing controllers to review budget items and expenses. Increasingly, these controllers are using business intelligence software to create digital versions of marketing dashboards that aggregate data from disparate internal and external sources.

MILWAUKEE ELECTRIC TOOL CORP.

Milwaukee Electric Tool is a manufacturer of items ranging from screwdrivers to gaskets and drill bits to heavy industrial machinery. For years, the company had deployed a data platform that let it gather information on its distribution, financials, manufacturing, sales, marketing, payables, receivables, and manufacturing operation. The company needed a way to bring all the data together and match trends. After the company changed to a new software package, Essbase XTD Analytic Server and Customer Focus Suite, its marketing manager could understand the mix of products a specific customer group was ordering and develop programs to promote more sales.[28]

As input to the marketing dashboard, companies can prepare two market-based scorecards that reflect performance and provide possible early warning signals. A **customer-performance scorecard** records how well the company is doing year after year on such customer-based measures as shown in Table 4.5. Norms should be set for each measure, and management should take action when results get out of bounds.

The second measure is called a **stakeholder-performance scorecard**. Companies need to track the satisfaction of various constituencies who have a critical interest in and impact on the company's performance: employees, suppliers, banks, distributors, retailers, stockholders. Again, norms should be set for each group and management should take action when one or more groups register increased levels of dissatisfaction.[29] Consider Hewlett-Packard's program.

TABLE 4.5

Sample Customer-Performance Scorecard Measures

- Percentage of new customers to average number of customers.
- Percentage of lost customers to average number of customers.
- Percentage of win-back customers to average number of customers.
- Percentage of customers falling into very dissatisfied, dissatisfied, neutral, satisfied, and very satisfied categories.
- Percentage of customers who say they would repurchase the product.
- Percentage of customers who say they would recommend the product to others.
- Percentage of target market customers who have brand awareness or recall.
- Percentage of customers who say that the company's product is the most preferred in its category.
- Percentage of customers who correctly identify the brand's intended positioning and differentiation.
- Average perception of company's product quality relative to chief competitor.
- Average perception of company's service quality relative to chief competitor.

HEWLETT-PACKARD

Each division of Hewlett-Packard evaluates its performance on a customer-based scorecard that monitors 18 to 20 "business fundamentals." Some, such as customer satisfaction and on-time delivery, are rated for all divisions; other indicators are tracked according to the nature of the division's business. The company is thus able to gauge the effects of its marketing strategies on sales and profits and to identify areas where improvements in performance can lead to improved quantitative results.[30]

Measuring Marketing Plan Performance

Marketers today have better marketing metrics for measuring the performance of marketing plans.[31] They can use four tools to check on plan performance: sales analysis, market share analysis, marketing expense-to-sales analysis, and financial analysis.

SALES ANALYSIS **Sales analysis** consists of measuring and evaluating actual sales in relation to goals. Two specific tools are used in sales analysis.

Sales-variance analysis measures the relative contribution of different factors to a gap in sales performance. Suppose the annual plan called for selling $4,000 widgets in the first quarter at $1 per widget, for total revenue of $4,000. At quarter's end, only 3,000 widgets were sold at $.80 per widget, for total revenue of $2,400. How much of the sales performance is due to the price decline and how much to the volume decline? The following calculation answers this question:

Variance due to price decline	= ($1.00−$.80) (3,000)	= $ 600	37.5%
Variance due to volume decline	= ($1.00) (4,000−3,000)	= $1,000	62.5%
		$1,600	100.0%

Almost two-thirds of the variance is due to failure to achieve the volume target. The company should look closely at why it failed to achieve expected sales volume.

Microsales analysis looks at specific products, territories, and so forth that failed to produce expected sales. Suppose the company sells in three territories and expected sales were 1,500 units, 500 units, and 2,000 units, respectively. The actual sales volume was 1,400 units, 525 units, and 1,075 units, respectively. Thus territory 1 showed a 7 percent shortfall in terms of expected sales; territory 2, a 5 percent improvement over expectations; and territory 3, a 46 percent shortfall! Territory 3 is causing most of the trouble. The sales vice president needs to check into territory 3: Maybe territory 3's sales rep is underperforming; a major competitor has entered this territory; or business is in a recession in this territory.

MARKET SHARE ANALYSIS Company sales do not reveal how well the company is performing relative to competitors. For this purpose, management needs to track its market share.

Market share can be measured in three ways: **Overall market share** is the company's sales expressed as a percentage of total market sales. **Served market share** is its sales expressed as a percentage of the total sales to its served market. Its **served market** is all the buyers who are able and willing to buy its product. Served market share is always larger than overall market share. A company could capture 100 percent of its served market and yet have a relatively small share of the total market. **Relative market share** can be expressed as market share in relation to its largest competitor. A relative market share over 100 percent indicates a market leader. A relative market share of exactly 100 percent means that the company is tied for the lead. A rise in relative market share means a company is gaining on its leading competitor.

Conclusions from market share analysis, however, are subject to certain qualifications:

- ***The assumption that outside forces affect all companies in the same way is often not true.*** The U.S. Surgeon General's Report on the harmful consequences of cigarette smoking caused total cigarette sales to falter, but not equally for all companies.
- ***The assumption that a company's performance should be judged against the average performance of all companies is not always valid.*** A company's performance should be judged against the performance of its closest competitors.
- ***If a new firm enters the industry, then every existing firm's market share might fall.*** A decline in market share might not mean that the company is performing any worse than other companies. Share loss depends on the degree to which the new firm hits the company's specific markets.
- ***Sometimes a market share decline is deliberately engineered to improve profits.*** For example, management might drop unprofitable customers or products.
- ***Market share can fluctuate for many minor reasons.*** For example, it can be affected by whether a large sale occurs on the last day of the month or at the beginning of the next month. Not all shifts in market share have marketing significance.[32]

A useful way to analyze market share movements is in terms of four components:

Overall market share = *Customer penetration* × *Customer loyalty* × *Customer selectivity* × *Price selectivity*

where:

Customer penetration: percentage of all customers who buy from the company.

Customer loyalty: purchases from the company by its customers expressed as a percentage of their total purchases from all suppliers of the same products.

Customer selectivity: size of the average customer purchase from the company expressed as a percentage of the size of the average customer purchase from an average company.

Price selectivity: average price charged by the company expressed as a percentage of the average price charged by all companies.

Now suppose the company's dollar market share falls during the period. The overall market share equation provides four possible explanations: The company lost some of its customers (lower customer penetration); existing customers are buying less from the company (lower customer loyalty); the company's remaining customers are smaller in size (lower customer selectivity); or the company's price has slipped relative to competition (lower price selectivity).

MARKETING EXPENSE-TO-SALES ANALYSIS Annual-plan control requires making sure that the company is not overspending to achieve sales goals. The key ratio to watch is *marketing expense-to-sales.* In one company, this ratio was 30 percent and consisted of five component expense-to-sales ratios: sales force-to-sales (15 percent); advertising-to-sales (5 percent); sales promotion-to-sales (6 percent); marketing research-to-sales (1 percent); and sales administration-to-sales (3 percent).

Management needs to monitor these ratios. Fluctuations outside the normal range are cause for concern. The period-to-period fluctuations in each ratio can be tracked on a *control chart* (see Figure 4.2). This chart shows that the advertising expense-to-sales ratio normally fluctuates between 8 and 12 percent, say 99 out of 100 times. In the fifteenth period, however, the ratio exceeded the upper control limit. One of two hypotheses can

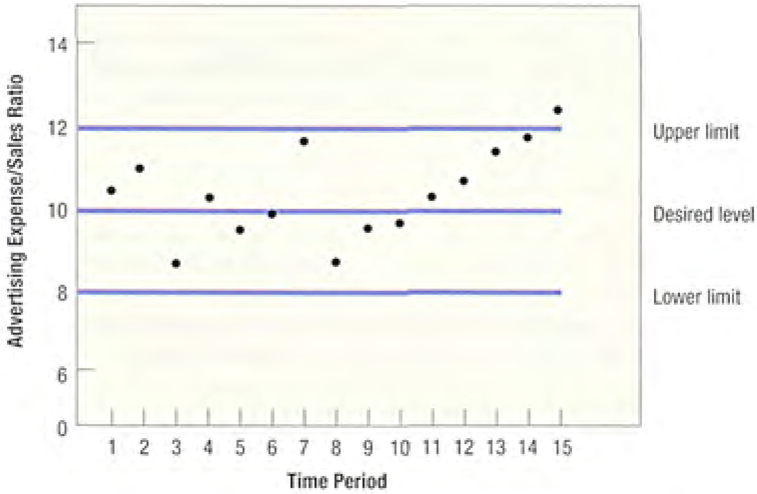


FIG. 4.2

The Control-Chart Model

explain this occurrence: (1) The company still has good expense control, and this situation represents a rare chance event. (2) The company has lost control over this expense and should find the cause. If no investigation is made, the risk is that some real change might have occurred, and the company will fall behind. If the environment is investigated, the risk is that the investigation will uncover nothing and be a waste of time and effort.

The behavior of successive observations even within the upper and lower control limits should be watched. Note in Figure 4.2 that the level of the expense-to-sales ratio rose steadily from the ninth period onward. The probability of encountering six successive increases in what should be independent events is only 1 in 64.[33] This unusual pattern should have led to an investigation sometime before the fifteenth observation.

FINANCIAL ANALYSIS The expense-to-sales ratios should be analyzed in an overall financial framework to determine how and where the company is making its money. Marketers are increasingly using financial analysis to find profitable strategies beyond sales building.

Management uses financial analysis to identify the factors that affect the company's *rate of return on net worth*.[34] The main factors are shown in Figure 4.3, along with illustrative numbers for a large chain-store retailer. The retailer is earning a 12.5 percent return on net worth. The return on net worth is the product of two ratios, the company's *return on assets* and its *financial leverage*. To improve its return on net worth, the company must increase its ratio of net profits to its assets or increase the ratio of its assets to its net worth. The company should analyze the composition of its assets (i.e., cash, accounts receivable, inventory, and plant and equipment) and see if it can improve its asset management.

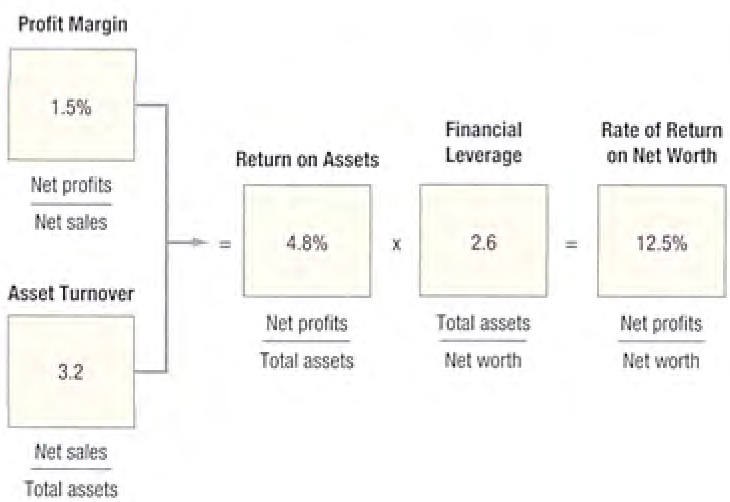


FIG. 4.3

Financial Model of Return on Net Worth

The return on assets is the product of two ratios, the *profit margin* and the *asset turnover*. The profit margin in Figure 4.3 seems low, whereas the asset turnover is more normal for retailing. The marketing executive can seek to improve performance in two ways: (1) Increase the profit margin by increasing sales or cutting costs; and (2) increase the asset turnover by increasing sales or reducing assets (e.g., inventory, receivables) that are held against a given level of sales.[35]

Profitability Analysis

Companies can benefit from deeper financial analysis, and should measure the profitability of their products, territories, customer groups, segments, trade channels, and order sizes. This information can help management determine whether any products or marketing activities should be expanded, reduced, or eliminated. The results can often be surprising. Here are some disconcerting findings from a bank profitability study:

> We have found that anywhere from 20 to 40 percent of an individual institution's products are unprofitable, and up to 60 percent of their accounts generate losses. Our research has shown that, in most firms, more than half of all customer relationships are not profitable, and 30 to 40 percent are only marginally so. It is frequently a mere 10 to 15 percent of a firm's relationships that generate the bulk of its profits. Our profitability research into the branch system of a regional bank produced some surprising results . . . 30 percent of the bank's branches were unprofitable.[36]

MARKETING-PROFITABILITY ANALYSIS We will illustrate the steps in marketing-profitability analysis with the following example:

The marketing vice president of a lawnmower company wants to determine the profitability of selling its lawnmower through three types of retail channels: hardware stores, garden supply shops, and department stores. The company's profit-and-loss statement is shown in Table 4.6.

Step 1: Identifying Functional Expenses Assume that the expenses listed in Table 4.6 are incurred to sell the product, advertise it, pack and deliver it, and bill and collect for it. The first task is to measure how much of each expense was incurred in each activity.

Suppose that most of the salary expense went to sales representatives and the rest went to an advertising manager, packing and delivery help, and an office accountant. Let the breakdown of the $9,300 be $5,100, $1,200, $1,400, and $1,600, respectively. Table 4.7 shows the allocation of the salary expense to these four activities.

Table 4.7 also shows the rent account of $3,000 allocated to the four activities. Because the sales reps work away from the office, none of the building's rent expense is assigned to selling. Most of the expenses for floor space and rented equipment are for packing and delivery. The supplies account covers promotional materials, packing materials, fuel purchases for delivery, and home office stationery. The $3,500 in this account is reassigned to the functional uses made of the supplies.

TABLE 4.6

A Simplified Profit-and-Loss Statement

Sales		$60,000
Cost of goods sold		39,000
Gross margin		$21,000
Expenses		
Salaries	$9,300	
Rent	3,000	
Supplies	3,500	
		15,800
Net profit		$5,200

TABLE 4.7

Mapping Natural Expenses into Functional Expenses

Natural Accounts	Total	Selling	Advertising	Packing and Delivery	Billing and Collecting
Salaries	$9,300	$5,100	$1,200	$1,400	$1,600
Rent	3,000	—	400	2,000	600
Supplies	3,500	400	1,500	1,400	200
	$15,800	$5,500	$3,100	$4,800	$2,400

Step 2: Assigning Functional Expenses to Marketing Entities The next task is to measure how much functional expense was associated with selling through each type of channel. Consider the selling effort. The selling effort is indicated by the number of sales made in each channel. This number is found in the selling column of Table 4.8. Altogether, 275 sales calls were made during the period. Because the total selling expense amounted to $5,500 (see Table 4.8), the selling expense averaged $20 per call.

Advertising expense can be allocated according to the number of ads addressed to different channels. Because there were 100 ads altogether, the average ad cost $31.

The packing and delivery expense is allocated according to the number of orders placed by each type of channel. This same basis was used for allocating billing and collection expense.

Step 3: Preparing a Profit-and-Loss Statement for Each Marketing Entity A profit-and-loss statement can now be prepared for each type of channel (see Table 4.9). Because hardware stores accounted for half of total sales ($30,000 out of $60,000), this channel is charged with half the cost of goods sold ($19,500 out of $39,000). This leaves a gross margin from hardware stores of $10,500. From

TABLE 4.8

Bases for Allocating Functional Expenses to Channels

Channel Type	Selling	Advertising	Packing and Delivery	Billing and Collecting
Hardware	200	50	50	50
Garden supply	65	20	21	21
Department stores	10	30	9	9
	275	**100**	**80**	**80**
Functional expense	$5,500	$3,100	$4,800	$2,400
÷ No. of Units	275	100	80	80
Equals	**$ 20**	**$ 31**	**$ 60**	**$ 30**

TABLE 4.9

Profit-and-Loss Statements for Channels

	Hardware	Garden Supply	Dept. Stores	Whole Company
Sales	$30,000	$10,000	$20,000	$60,000
Cost of goods sold	19,500	6,500	13,000	39,000
Gross margin	$10,500	$ 3,500	$ 7,000	$21,000
Expenses				
Selling ($20 per call)	$ 4,000	$ 1,300	$ 200	$ 5,500
Advertising ($31 per advertisement)	1,550	620	930	3,100
Packing and delivery ($60 per order)	3,000	1,260	540	4,800
Billing ($30 per order)	1,500	630	270	2,400
Total Expenses	$10,050	$ 3,810	$ 1,940	$ 15,800
Net profit or loss	$ 450	$ (310)	$ 5,060	$ 5,200

this must be deducted the proportions of the functional expenses hardware stores consumed. According to Table 4.8, hardware stores received 200 out of 275 total sales calls. At an imputed value of $20 a call, hardware stores have to be charged with a $4,000 selling expense. Table 4.8 also shows that hardware stores were the target of 50 ads. At $31 an ad, the hardware stores are charged with $1,550 of advertising. The same reasoning applies in computing the share of the other functional expenses to charge to hardware stores. The result is that hardware stores gave rise to $10,050 of the total expenses. Subtracting this from the gross margin, the profit of selling through hardware stores is only $450.

This analysis is repeated for the other channels. The company is losing money in selling through garden supply shops and makes virtually all of its profits through department stores. Notice that gross sales is not a reliable indicator of the net profits for each channel.

DETERMINING CORRECTIVE ACTION It would be naive to conclude that the company should drop garden supply shops and possibly hardware stores so that it can concentrate on department stores. The following questions need to be answered first:

- To what extent do buyers buy on the basis of type of retail outlet versus brand?
- What are the trends with respect to the importance of these three channels?
- How good are the company marketing strategies directed at the three channels?

On the basis of the answers, marketing management can evaluate five alternatives:

1. Establish a special charge for handling smaller orders.
2. Give more promotional aid to garden supply shops and hardware stores.
3. Reduce the number of sales calls and the amount of advertising going to garden supply shops and hardware stores.
4. Do not abandon any channel entirely, but only the weakest retail units in each channel.
5. Do nothing.

In general, marketing-profitability analysis indicates the relative profitability of different channels, products, territories, or other marketing entities. It does not prove that the best course of action is to drop the unprofitable marketing entities, nor does it capture the likely profit improvement if these marginal marketing entities are dropped.

DIRECT VERSUS FULL COSTING Like all information tools, marketing-profitability analysis can lead or mislead marketing executives, depending on how well they understand its methods and limitations. The lawnmower company showed some arbitrariness in its choice of bases for allocating the functional expenses to its marketing entities. "Number of sales calls" was used to allocate selling expenses, when in principle "number of sales working hours" is a more accurate indicator of cost. The former base was used because it involves less record keeping and computation.

Far more serious is another judgmental element affecting profitability analysis. The issue is whether to allocate full costs or only direct and traceable costs in evaluating a marketing entity's performance. The lawnmower company sidestepped this problem by assuming only simple costs that fit in with marketing activities, but the question cannot be avoided in real-world analyses of profitability. Three types of costs have to be distinguished:

1. ***Direct costs*** – These are costs that can be assigned directly to the proper marketing entities. Sales commissions are a direct cost in a profitability analysis of sales territories, sales representatives, or customers. Advertising expenditures are a direct cost in a profitability analysis of products to the extent that each advertisement promotes only one product. Other direct costs for specific purposes are sales force salaries and traveling expenses.
2. ***Traceable common costs*** – These are costs that can be assigned only indirectly, but on a plausible basis, to the marketing entities. In the example, rent was analyzed this way.
3. ***Nontraceable common costs*** – These are common costs whose allocation to the marketing entities is highly arbitrary. To allocate "corporate image" expenditures equally to all products would be arbitrary, because all products do not benefit equally. To allocate them proportionately to the sales of the various products would be arbitrary because relative product sales reflect many factors besides corporate image making. Other examples are top management salaries, taxes, interest, and other overhead.

No one disputes the inclusion of direct costs in marketing cost analysis. There is a small amount of controversy about including traceable common costs, which lump together costs that would change with the scale of marketing activity and costs that would not change. If the lawnmower company drops garden supply shops, it would probably continue to pay the same rent. In this event, its profits would not rise immediately by the amount of the present loss in selling to garden supply shops ($310).

The major controversy concerns whether the nontraceable common costs should be allocated to the marketing entities. Such allocation is called the *full-cost approach*, and its advocates argue that all costs must ultimately be imputed in order to determine true profitability. However, this argument confuses the use of accounting for financial reporting with its use for managerial decision making. Full costing has three major weaknesses:

1. The relative profitability of different marketing entities can shift radically when one arbitrary way to allocate nontraceable common costs is replaced by another.
2. The arbitrariness demoralizes managers, who feel that their performance is judged adversely.
3. The inclusion of nontraceable common costs could weaken efforts at real cost control.

Operating management is most effective in controlling direct costs and traceable common costs. Arbitrary assignments of nontraceable common costs can lead managers to spend their time fighting arbitrary cost allocations instead of managing controllable costs well.

Companies are showing a growing interest in using marketing-profitability analysis or its broader version, activity-based cost accounting (ABC), to quantify the true profitability of different activities.[37] To improve profitability, managers can then examine ways to reduce the resources required to perform various activities, or make the resources more productive or acquire them at lower cost. Alternatively, management may raise prices on products that consume heavy amounts of support resources. The contribution of ABC is to refocus management's attention away from using only labor or material standard costs to allocate full cost, and toward capturing the actual costs of supporting individual products, customers, and other entities.

Marketing-Mix Modeling

Marketing accountability also means that marketers can more precisely estimate the effects of different marketing investments. *Marketing-mix models* analyze data from a variety of sources, such as retailer scanner data, company shipment data, pricing, media, and promotion spending data, to understand more precisely the effects of specific marketing activities. To deepen understanding, multivariate analyses are conducted to sort through how each marketing element influences marketing outcomes of interest such as brand sales or market share.[38]

Especially popular with packaged-goods marketers such as Procter & Gamble, Clorox, and Colgate, the findings from marketing-mix modeling are used to allocate or reallocate expenditures. Analyses explore which part of ad budgets are wasted, what optimal spending levels are, and what minimum investment levels should be.[39] Although marketing-mix modeling helps to isolate effects, it is less effective at assessing how different marketing elements work in combination.

::: Forecasting and Demand Measurement

One major reason for undertaking marketing research is to identify market opportunities. Once the research is complete, the company must measure and forecast the size, growth, and profit potential of each market opportunity. Sales forecasts are used by finance to raise the needed cash for investment and operations; by the manufacturing department to establish capacity and output levels; by purchasing to acquire the right amount of supplies; and by human resources to hire the needed number of workers. Marketing is responsible for preparing the sales forecasts. If its forecast is far off the mark, the company will be saddled with excess inventory or have inadequate inventory. Sales forecasts are based on estimates of demand. Managers need to define what they mean by market demand. Here is a good example of the importance of defining the market correctly:

COCA-COLA

When Roberto Goizueta became CEO of Coca-Cola, many people thought that Coke's sales were maxed out. Goizueta, however, reframed the view of Coke's market share. He said Coca-Cola accounted for less than 2 ounces of the 64 ounces of fluid that each of the world's 4.4 billion people drank on average every day. "The enemy is coffee, milk, tea, water," he told his people at Coke, and he ushered in a huge period of growth.

An ad for a Clorox product, Gladware. Clorox is one of the companies that uses marketing-mix modeling to test the effectiveness of its advertising.

The Measures of Market Demand

Companies can prepare as many as 90 different types of demand estimates (see Figure 4.4). Demand can be measured for six different product levels, five different space levels, and three different time levels.

Each demand measure serves a specific purpose. A company might forecast short-run demand for a particular product for the purpose of ordering raw materials, planning production, and borrowing cash. It might forecast regional demand for its major product line to decide whether to set up regional distribution.

Forecasts also depend on which type of market is being considered. The size of a market hinges on the number of buyers who might exist for a particular market offer. But there are many productive ways to break down the market:

- The **potential market** is the set of consumers who profess a sufficient level of interest in a market offer. However, consumer interest is not enough to define a market. Potential consumers must have enough income and must have access to the product offer.
- The **available market** is the set of consumers who have interest, income, and access to a particular offer. For some market offers, the company or government may restrict sales to certain groups. For example, a particular state might ban motorcycle sales to anyone under 21 years of age. The eligible adults constitute the *qualified available market*—the set of consumers who have interest, income, access, and qualifications for the particular market offer.
- The **target market** is the part of the qualified available market the company decides to pursue. The company might decide to concentrate its marketing and distribution effort on the East Coast. The company will end up selling to a certain number of buyers in its target market.
- The **penetrated market** is the set of consumers who are buying the company's product.

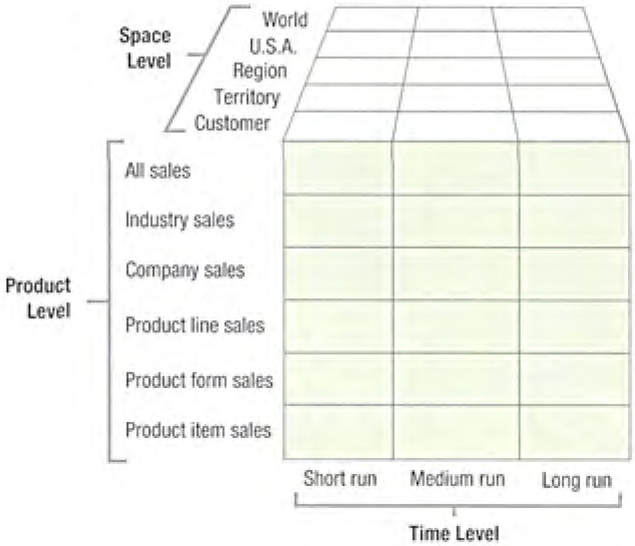


FIG. 4.4

Ninety Types of Demand Measurement (6 × 5 × 3)

These definitions are a useful tool for market planning. If the company is not satisfied with its current sales, it can take a number of actions. It can try to attract a larger percentage of buyers from its target market. It can lower the qualifications for potential buyers. It can expand its available market by opening distribution elsewhere or lowering its price; or it can reposition itself in the minds of its customers. Consider the case of Target Stores.

TARGET

Facing stiff competition from top retailers Wal-Mart and Kmart, Target Stores decided to reach more affluent shoppers and woo them away from department stores. The Midwestern discount retailer ran an unusual advertising campaign in some unusual spots: the Sunday magazines of the *New York Times*, the *Los Angeles Times*, and the *San Francisco Examiner*. One ad showed a woman riding a vacuum cleaner through the night sky. The ad simply said "Fashion and Housewares," with the Target logo in the lower right-hand corner. These hip spots gained Target Stores a reputation as the "upstairs" mass retailer, or "Kmart for Yuppies," as one shopper put it. In 2001, Target brought "fashion to food" by adding grocery sections to its retail concept and creating 175,000-square-foot SuperTargets. By 2004, there were 1,249 Target stores in 47 states (with 119 SuperTarget stores).[40]

A Vocabulary for Demand Measurement

The major concepts in demand measurement are market demand and company demand. Within each, we distinguish among a demand function, a sales forecast, and a potential.

MARKET DEMAND As we have seen, the marketer's first step in evaluating marketing opportunities is to estimate total market demand. **Market demand** for a product is the total volume that would be bought by a defined customer group in a defined geographical area in a defined time period in a defined marketing environment under a defined marketing program.

Market demand is not a fixed number, but rather a function of the stated conditions. For this reason, it can be called the *market demand function*. The dependence of total market demand on underlying conditions is illustrated in Figure 4.5(a). The horizontal axis shows different possible levels of industry marketing expenditure in a given time period. The vertical axis shows the resulting demand level. The curve represents the estimated market demand associated with varying levels of industry marketing expenditure.

Some base sales (called the *market minimum*, labeled *Q1* in the figure) would take place without any demand-stimulating expenditures. Higher levels of industry marketing expenditures would yield higher levels of demand, first at an increasing rate, then at a decreasing rate. Marketing expenditures beyond a certain level would not stimulate much further demand, thus suggesting an upper limit to market demand called the *market potential* (labeled *Q2* in the figure).

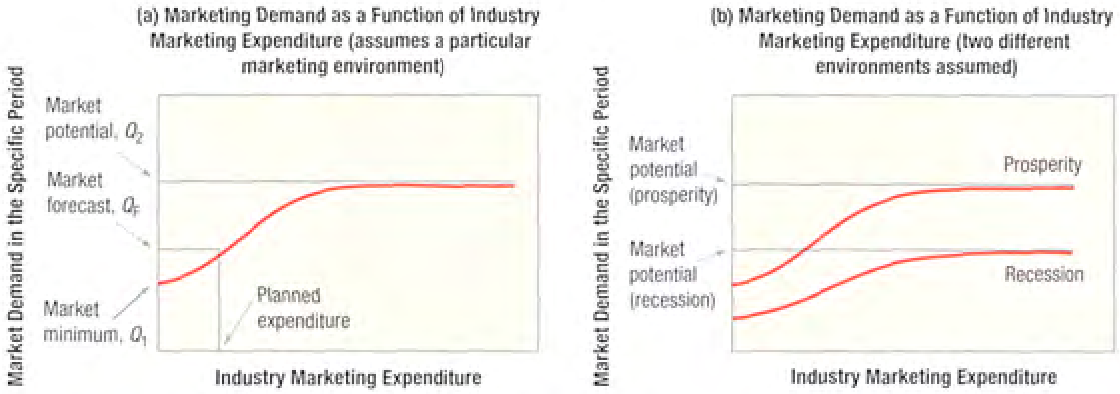


FIG. **4.5** Market Demand Functions

The distance between the market minimum and the market potential shows the overall *marketing sensitivity of demand.* We can think of two extreme types of markets, the expansible and the nonexpansible. An *expansible market,* such as the market for racquetball playing, is very much affected in its total size by the level of industry marketing expenditures. In terms of Figure 4.5(a), the distance between Q1 and Q2 is relatively large. A *nonexpansible market*—for example, the market for opera—is not much affected by the level of marketing expenditures; the distance between Q1 and Q2 is relatively small. Organizations selling in a nonexpansible market must accept the market's size (the level of *primary demand* for the product class) and direct their efforts to winning a larger **market share** for their product (the level of selective demand for the company's product).

It pays to compare the current level of market demand to the potential demand level. The result is called the **market penetration index**. A low market penetration index indicates substantial growth potential for all the firms. A high market penetration index suggests that there will be increased costs in attracting the few remaining prospects. Generally, price competition increases and margins fall when the market penetration index is already high.

A company should also compare its current market share to its potential market share. The result is called the company's **share penetration index**. A low share penetration index indicates that the company can greatly expand its share. The underlying factors holding it back could be many: low brand awareness, low brand availability, benefit deficiencies, too high a price. A firm should calculate the share penetration increases that would occur with investments to remove each deficiency, to see which investments would produce the greatest improvement in share penetration.[41]

It is important to remember that the market demand function is not a picture of market demand over time. Rather, the curve shows alternative current forecasts of market demand associated with alternative possible levels of industry marketing effort in the current period.

MARKET FORECAST Only one level of industry marketing expenditure will actually occur. The market demand corresponding to this level is called the **market forecast**.

MARKET POTENTIAL The market forecast shows expected market demand, not maximum market demand. For the latter, we have to visualize the level of market demand resulting from a "very high" level of industry marketing expenditure, where further increases in marketing effort would have little effect in stimulating further demand. **Market potential** is the limit approached by market demand as industry marketing expenditures approach infinity for a given marketing environment.

The phrase "for a given market environment" is crucial. Consider the market potential for automobiles in a period of recession versus a period of prosperity. The market potential is higher during prosperity. The dependence of market potential on the environment is illustrated in Figure 4.5(b). Market analysts distinguish between the position of the market demand function and movement along it. Companies cannot do anything about the posi-

One of the highest percentages of ownership/use of a product in the U.S. is that for television: 98% of Americans own a TV, and most families own more than one. (a) The big TV in the family/living room; (b) doing homework with the bedroom TV; (c) following a cooking show in the kitchen.

tion of the market demand function, which is determined by the marketing environment. However, companies influence their particular location on the function when they decide how much to spend on marketing.

Companies interested in market potential have a special interest in the **product penetration percentage**, which is the percentage of ownership or use of a product or service in a population. Here are some U.S. percentages: television (98%), health insurance (84%), car (81%), home ownership (67%), PC (54%), stock ownership (48%), gun ownership (41%), and fax (12%).[42] Companies assume that the lower the product penetration percentage, the higher the market potential, although this assumes that everyone will eventually be in the market for every product.

COMPANY DEMAND We are now ready to define company demand: **Company demand** is the company's estimated share of market demand at alternative levels of company marketing effort in a given time period. The company's share of market demand depends on how its products, services, prices, communications, and so on are perceived relative to the competitors'. If other things are equal, the company's market share would depend on the size and effectiveness of its market expenditures relative to competitors. Marketing model builders have developed sales response functions to measure how a company's sales are affected by its marketing expenditure level, marketing mix, and marketing effectiveness.[43]

COMPANY SALES FORECAST Once marketers have estimated company demand, their next task is to choose a level of marketing effort. The chosen level will produce an expected level of sales. The **company sales forecast** is the expected level of company sales based on a chosen marketing plan and an assumed marketing environment.

The company sales forecast is represented graphically with company sales on the vertical axis and company marketing effort on the horizontal axis, as in Figure 4.5. Too often the sequential relationship between the company forecast and the company marketing plan is confused. One frequently hears that the company should develop its marketing plan on the basis of its sales forecast. This forecast-to-plan sequence is valid if "forecast" means an estimate of national economic activity or if company demand is nonexpansible. The sequence is not valid, however, where market demand is expansible or where "forecast" means an estimate of company sales. The company sales forecast does not establish a basis for deciding what to spend on marketing. On the contrary, the sales forecast is the result of an assumed marketing expenditure plan.

Two other concepts are worth mentioning in relation to the company sales forecast. A **sales quota** is the sales goal set for a product line, company division, or sales representative. It is primarily a managerial device for defining and stimulating sales effort. Management sets sales quotas on the basis of the company sales forecast and the psychology of stimulating its achievement. Generally, sales quotas are set slightly higher than estimated sales to stretch the sales force's effort.

A **sales budget** is a conservative estimate of the expected volume of sales and is used primarily for making current purchasing, production, and cash flow decisions. The sales budget is based on the sales forecast and the need to avoid excessive risk. Sales budgets are generally set slightly lower than the sales forecast.

COMPANY SALES POTENTIAL Company sales potential is the sales limit approached by company demand as company marketing effort increases relative to that of competitors. The absolute limit of company demand is, of course, the market potential. The two would be equal if the company got 100 percent of the market. In most cases, company sales potential is less than the market potential, even when company marketing expenditures increase considerably, relative to competitors. The reason is that each competitor has a hard core of loyal buyers who are not very responsive to other companies' efforts to woo them.

Estimating Current Demand

We are now ready to examine practical methods for estimating current market demand. Marketing executives want to estimate total market potential, area market potential, and total industry sales and market shares.

TOTAL MARKET POTENTIAL Total market potential is the maximum amount of sales that might be available to all the firms in an industry during a given period, under a given level of industry marketing effort and environmental conditions. A common way to estimate total market potential is as follows: Estimate the potential number of buyers times the average quantity purchased by a buyer times the price.

If 100 million people buy books each year, and the average book buyer buys three books a year, and the average price of a book is $20, then the total market potential for books is $6 billion (100 million × 3 × $20). The most difficult component to estimate is the number of buyers for the specific product or market. One can always start with the total population in the nation, say, 261 million people. The next step is to eliminate groups that obviously would not buy the product. Let us assume that illiterate people and children under 12 do not buy books, and they constitute 20 percent of the population.

This means that only 80 percent of the population, or approximately 209 million people, would be in the suspect pool. We might do further research and find that people of low income and low education do not read books, and they constitute over 30 percent of the suspect pool. Eliminating them, we arrive at a prospect pool of approximately 146.3 million book buyers. We would use this number of potential buyers to calculate total market potential.

A variation on this method is the *chain-ratio method*. It involves multiplying a base number by several adjusting percentages. Suppose a brewery is interested in estimating the market potential for a new light beer. An estimate can be made by the following calculation:

> Demand for the new light beer = Population × personal discretionary income per capita average percentage of discretionary income spent on food × average percentage of amount spent on food that is spent on beverages × average percentage of amount spent on beverages that is spent on alcoholic beverages × average percentage of amount spent on alcoholic beverages that is spent on beer × expected percentage of amount spent on beer that will be spent on light beer.

AREA MARKET POTENTIAL Companies face the problem of selecting the best territories and allocating their marketing budget optimally among these territories. Therefore, they need to estimate the market potential of different cities, states, and nations. Two major methods of assessing area market potential are available: the market-buildup method, which is used primarily by business marketers, and the multiple-factor index method, which is used primarily by consumer marketers.

Market-Buildup Method The **market-buildup method** calls for identifying all the potential buyers in each market and estimating their potential purchases. This method produces accurate results if we have a list of all potential buyers and a good estimate of what each will buy. Unfortunately, this information is not always easy to gather.

Consider a machine-tool company that wants to estimate the area market potential for its wood lathe in the Boston area. Its first step is to identify all potential buyers of wood lathes in the area. The buyers consist primarily of manufacturing establishments that have to shape or ream wood as part of their operation, so the company could compile a list from a directory of all manufacturing establishments in the Boston area. Then it could estimate the number of lathes each industry might purchase based on the number of lathes per thousand employees or per $1 million of sales in that industry.

An efficient method of estimating area market potentials makes use of the *North American Industry Classification System (NAICS)*, developed by the U.S. Bureau of the Census in conjunction with the Canadian and Mexican governments.[44] The NAICS classifies all manufacturing into 20 major industry sectors. Each sector is further broken into a six-digit, hierarchical structure as follows (illustrated with paging).

51	Industry Sector (Information)
513	Industry Subsector (Broadcasting and telecommunications)
5133	Industry Group (Telecommunications)
51332	Industry (Wireless telecommunications carriers, except satellite)
513321	National Industry (U.S. Paging)

For each six-digit NAICS number, a company can purchase CD-ROMs of business directories that provide complete company profiles of millions of establishments, subclassified by location, number of employees, annual sales, and net worth.

To use the NAICS, the lathe manufacturer must first determine the six-digit NAICS codes that represent products whose manufacturers are likely to require lathe machines. To get a full picture of all six-digit NAICS industries that might use lathes, the company can (1) determine past customers' NAICS codes; (2) go through the NAICS manual and check off all the six-digit industries that might have an interest in lathes; (3) mail questionnaires to a wide range of companies inquiring about their interest in wood lathes.

The company's next task is to determine an appropriate base for estimating the number of lathes that will be used in each industry. Suppose customer industry sales are the most appropriate base. Once the company estimates the rate of lathe ownership relative to the customer industry's sales, it can compute the market potential.

Multiple-Factor Index Method Like business marketers, consumer companies also have to estimate area market potentials, but the customers of consumer companies are too numerous to be listed. The method most commonly used in consumer markets is a straightforward index method. A drug manufacturer, for example, might assume that the market potential for drugs is directly related to population size. If the state of Virginia has 2.28 percent of the U.S. population, the company might assume that Virginia will be a market for 2.28 percent of total drugs sold.

A single factor, however, is rarely a complete indicator of sales opportunity. Regional drug sales are also influenced by per capita income and the number of physicians per 10,000 people. Thus it makes sense to develop a multiple-factor index, with each factor assigned a specific weight. The numbers are the weights attached to each variable. For example, suppose Virginia has 2.00 percent of the U.S. disposable personal income, 1.96 percent of U.S. retail sales, and 2.28 percent of U.S. population, and the respective weights are 0.5, 0.3, and 0.2. The buying-power index for Virginia would be 2.04 $[0.5(2.00) + 0.3(1.96) + 0.2(2.28)]$. Thus 2.04 percent of the nation's drug sales might be expected to take place in Virginia.

The weights used in the buying-power index are somewhat arbitrary. Other weights can be assigned if appropriate. Furthermore, a manufacturer would want to adjust the market potential for additional factors, such as competitors' presence in that market, local promotional costs, seasonal factors, and local market idiosyncrasies.

Many companies compute other area indexes as a guide to allocating marketing resources. Suppose the drug company is reviewing the six cities listed in Table 4.10. The first two columns show its percentage of U.S. brand and category sales in these six cities. Column 3 shows the **brand development index (BDI)**, which is the index of brand sales to category sales. Seattle, for example, has a BDI of 114 because the brand is relatively more developed than the category in Seattle. Portland has a BDI of 65, which means that the brand in Portland is relatively underdeveloped. Normally, the lower the BDI, the higher the market opportunity, in that there is room to grow the brand. However, other marketers would argue the opposite, that marketing funds should go into the brand's strongest markets—where it might be important to reinforce loyalty or more easily capture additional brand share.[45]

TABLE 4.10

Calculating the Brand Development Index (BDI)

Territory	(a) Percent of U.S. Brand Sales	(b) Percent of U.S. Category Sales	BDI (a ÷ b) × 100
Seattle	3.09	2.71	114
Portland	6.74	10.41	65
Boston	3.49	3.85	91
Toledo	.97	.81	120
Chicago	1.13	.81	140
Baltimore	3.12	3.00	104

After the company decides on the city-by-city allocation of its budget, it can refine each city allocation down to census tracts or zip+4 code centers. *Census tracts* are small, locally defined statistical areas in metropolitan areas and some other counties. They generally have stable boundaries and a population of about 4,000. Zip+4 code centers (which were designed by the U.S. Post Office) are a little larger than neighborhoods. Data on population size, median family income, and other characteristics are available for these geographical units. Marketers have found these data extremely useful for identifying high-potential retail areas within large cities or for buying mailing lists to use in direct-mail campaigns (see Chapter 8).

INDUSTRY SALES AND MARKET SHARES Besides estimating total potential and area potential, a company needs to know the actual industry sales taking place in its market. This means identifying competitors and estimating their sales.

The industry trade association will often collect and publish total industry sales, although it usually does not list individual company sales separately. With this information, each company can evaluate its performance against the whole industry. Suppose a company's sales are increasing by 5 percent a year, and industry sales are increasing by 10 percent. This company is actually losing its relative standing in the industry.

Another way to estimate sales is to buy reports from a marketing research firm that audits total sales and brand sales. Nielsen Media Research audits retail sales in various product categories in supermarkets and drugstores and sells this information to interested companies. These audits can give a company valuable information about its total product-category sales as well as brand sales. It can compare its performance to the total industry or any particular competitor to see whether it is gaining or losing share.

Business-goods marketers typically have a harder time estimating industry sales and market shares. Business marketers have no Nielsens to rely on. Distributors typically will not supply information about how much of competitors' products they are selling. Business-goods marketers therefore operate with less knowledge of their market share results.

Estimating Future Demand

Very few products or services lend themselves to easy forecasting; those that do generally involve a product whose absolute level or trend is fairly constant and where competition is nonexistent (public utilities) or stable (pure oligopolies). In most markets, total demand and company demand are not stable. Good forecasting becomes a key factor in company success. The more unstable the demand, the more critical is forecast accuracy, and the more elaborate is forecasting procedure.

Companies commonly use a three-stage procedure to prepare a sales forecast. They prepare a macroeconomic forecast first, followed by an industry forecast, followed by a company sales forecast. The macroeconomic forecast calls for projecting inflation, unemployment, interest rates, consumer spending, business investment, government expenditures, net exports, and other variables. The end result is a forecast of gross national product, which is then used, along with other environmental indicators, to forecast industry sales. The company derives its sales forecast by assuming that it will win a certain market share.

How do firms develop their forecasts? Firms may do it internally or buy forecasts from outside sources such as marketing research firms, which develop a forecast by interviewing customers, distributors, and other knowledgeable parties. Specialized forecasting firms produce long-range forecasts of particular macroenvironmental components, such as population, natural resources, and technology. Some examples are Global Insight (a merger of Data Resources and Wharton Econometric Forecasting Associates), Forrester Research, and the Gartner Group. Futurist research firms produce speculative scenarios; three examples are the Institute for the Future, Hudson Institute, and the Futures Group.

All forecasts are built on one of three information bases: what people say, what people do, or what people have done. The first basis—what people say—involves surveying the opinions of buyers or those close to them, such as salespeople or outside experts. It includes three methods: surveys of buyer's intentions, composites of sales force opinions, and expert opinion. Building a forecast on what people do involves another method—putting the product into a test market to measure buyer response. The final basis—what people have done—involves analyzing records of past buying behavior or using time-series analysis or statistical demand analysis.

SURVEY OF BUYERS' INTENTIONS **Forecasting** is the art of anticipating what buyers are likely to do under a given set of conditions. Because buyer behavior is so important, buyers should be surveyed. For major consumer durables (for example, major appliances), several research organizations conduct periodic surveys of consumer buying intentions. These organizations ask questions like the following:

Do you intend to buy an automobile within the next six months?

0.00	0.20	0.40	0.60	0.80	1.00
No chance	Slight possibility	Fair possibility	Good possibility	High possibility	Certain

This is called a **purchase probability scale**. The various surveys also inquire into consumers' present and future personal finances and their expectations about the economy. The various bits of information are then combined into a consumer confidence (Conference Board) or consumer sentiment measure (Survey Research Center of the University of Michigan). Consumer durable-goods producers subscribe to these indexes in the hope of anticipating major shifts in buying intentions so they can adjust production and marketing plans accordingly.

For business buying, research firms can carry out buyer-intention surveys regarding plant, equipment, and materials. Their estimates tend to fall within a 10 percent error band of the actual outcomes. Buyer-intention surveys are particularly useful in estimating demand for industrial products, consumer durables, product purchases where advanced planning is required, and new products. The value of a buyer-intention survey increases to the extent that the cost of reaching buyers is small, the buyers are few, they have clear intentions, they implement their intentions, and they willingly disclose their intentions.

COMPOSITE OF SALES FORCE OPINIONS When buyer interviewing is impractical, the company may ask its sales representatives to estimate their future sales. Each sales representative estimates how much each current and prospective customer will buy of each of the company's products.

Few companies use sales force estimates without making some adjustments. Sales representatives might be pessimistic or optimistic, or they might go from one extreme to another because of a recent setback or success. Furthermore, they are often unaware of larger economic developments and do not know how their company's marketing plans will influence future sales in their territory. They might deliberately underestimate demand so that the company will set a low sales quota, or they might lack the time to prepare careful estimates or might not consider the effort worthwhile. To encourage better estimating, the company could offer certain aids or incentives. For example, sales reps might receive a record of their past forecasts compared with actual sales and also a description of company assumptions on the business outlook, competitor behavior, and marketing plans.

Involving the sales force in forecasting brings a number of benefits. Sales reps might have better insight into developing trends than any other single group. After participating in the forecasting process, reps might have greater confidence in their sales quotas and more incentive to achieve them. Also, a "grassroots" forecasting procedure provides detailed estimates broken down by product, territory, customer, and sales rep.

EXPERT OPINION Companies can also obtain forecasts from experts, including dealers, distributors, suppliers, marketing consultants, and trade associations. Large appliance companies periodically survey dealers for their forecasts of short-term demand, as do car companies. Dealer estimates are subject to the same strengths and weaknesses as sales force estimates. Many companies buy economic and industry forecasts from well-known economic-forecasting firms. These specialists are able to prepare better economic forecasts than the company because they have more data available and more forecasting expertise.

Occasionally, companies will invite a group of experts to prepare a forecast. The experts exchange views and produce a group estimate (*group-discussion method*); or the experts supply their estimates individually, and an analyst combines them into a single estimate (*pooling of individual estimates*). Alternatively, the experts supply individual estimates and assumptions that are reviewed by the company, then revised. Further rounds of estimating and refining follow (this is the Delphi method).[46]

PAST-SALES ANALYSIS Sales forecasts can be developed on the basis of past sales. *Time-series analysis* consists of breaking down past time series into four components (trend, cycle, seasonal, and erratic) and projecting these components into the future. *Exponential smoothing* consists of projecting the next period's sales by combining an average of past sales and the most recent sales, giving more weight to the latter. *Statistical demand analysis* consists of measuring the impact level of each of a set of causal factors (e.g., income, marketing expenditures, price) on the sales level. Finally, *econometric analysis* consists of building sets of equations that describe a system, and proceeding to fit the parameters statistically.

MARKET-TEST METHOD When buyers do not plan their purchases carefully or experts are not available or reliable, a direct-market test is desirable. A direct-market test is especially desirable in forecasting new-product sales or established product sales in a new distribution channel or territory. (We discuss market testing in detail in Chapter 20.)

SUMMARY :::

1. Companies can conduct their own marketing research or hire other companies to do it for them. Good marketing research is characterized by the scientific method, creativity, multiple research methods, accurate model building, cost-benefit analysis, healthy skepticism, and an ethical focus.
2. The marketing research process consists of defining the problem and research objective, developing the research plan, collecting the information, analyzing the information, presenting the findings to management, and making the decision.
3. In conducting research, firms must decide whether to collect their own data or use data that already exist. They must also decide which research approach (observational, focus-group, survey, behavioral data, or experimental) and which research instruments (questionnaire or mechanical instruments) to use. In addition, they must decide on a sampling plan and contact methods.
4. Analysis should ensure that the company achieves the sales, profits, and other goals established in its annual plan. The main tools are sales analysis, market share analysis, marketing expense-to-sales analysis, and financial analysis of the marketing plan.
5. Profitability analysis seeks to measure and control the profitability of various products, territories, customer groups, trade channels, and order sizes. An important part of controlling for profitability is assigning costs and generating profit-and-loss statements.
6. There are two types of demand: market demand and company demand. To estimate current demand, companies attempt to determine total market potential, area market potential, industry sales, and market share. To estimate future demand, companies survey buyers' intentions, solicit their sales force's input, gather expert opinions, or engage in market testing. Mathematical models, advanced statistical techniques, and computerized data collection procedures are essential to all types of demand and sales forecasting.

APPLICATIONS :::

Marketing Debate What is the Best Type of Marketing Research?

Many market researchers have their favorite research approaches or techniques, although different researchers often have different preferences. Some researchers maintain that the only way to really learn about consumers or brands is through in-depth, qualitative research. Others contend that the only legitimate and defensible form of marketing research involves quantitative measures.

Take a position: Marketing research should be quantitative versus Marketing research should be qualitative.

Marketing Discussion

When was the last time you participated in a survey? How helpful do you think was the information you provided? How could the research have been done differently to make it more effective?

MARKETING **SPOTLIGHT** SONY

Sony started as a radio repair shop, founded by Masuru Ikura and Akio Morita after World War II. The company began its long history of producing compact consumer electronics in 1957, when it introduced the world's first pocket-sized all-transistor radio. The company's name, Sony, was taken from *sonus*, the Latin word for "sound." Sony went on to invent a series of transistor-based TVs and increasingly smaller audiocassette recorders. In 1979, the Sony Walkman introduced the world to a new, portable way of listening to music. Sony became a world leader in consumer electronics and was the first Japanese company to have its shares traded on the New York Stock Exchange.

In the late 1980s, Sony began expanding into media, purchasing a U.S. record company (CBS Records for $22 billion in 1988) and a major Hollywood studio (Columbia Pictures for $4.9 billion in 1989). The purchases made Sony a major force in the entertainment industry.

The importance of marketing at Sony started with Akio Morita, who said that for a company to be successful, it must have three kinds of creativity: creativity to make inventions, creativity in product planning and production, and creativity in marketing.

Creativity in marketing at Sony means not just clever ads, but deep insight into its customers. For example, Sony knows its PlayStation customers like to find clues and to decode things. So Sony's ads for PlayStation 2, like "Signs," feature a young man walking the streets of a city where he encounters various signs foreshadowing the events. Mannequins appear in a store window, arms outstretched, and point enigmatically to something that's about to happen. "The lead character is almost in the midst of his own role-playing game. He needs to follow clues to save the heroine," said Andrew House, Sony's executive vice president of marketing. In the ads, "we were essentially trying to tap into a range of emotions that we think we deliver in the games—intrigue, foreboding, excitement, panic, relief and achievement at the end."

Sony's marketing also includes careful measurement of each campaign's effectiveness. For example, Sony runs 30-second commercials for its PlayStation as part of the previews in more than 1,800 theaters and on 8,000 movie screens. The ads appear before such films as "The Cat in the Hat." Sony Computer Entertainment America has been running movie ads for six years. "Cinema advertising has been very effective for us," said Ami Blaire, director of product marketing. "The reason why we have committed to cinema every year is the tremendous unaided recall shown by our own research and Communicus-commissioned ad tracking."

Another example of measurement is Sony's GenY youth marketing efforts. "The online program promoting the NetMD, ATRAC CD Walkman and Cybershot U30 ran July 1 through September 30 2003, and we found that more than 70 percent of the clickthroughs were spurred by rich media ads via Eyeblaster, versus static banners," said Serge Del Grosso, Director of Media and Internet Strategy, Sony Electronics.

In fact, Sony has even developed a direct-marketing solution which it sells to other companies who want to measure marketing effectiveness. The product, called eBridge[TM], allows marketers to use video, measure the effectiveness of the campaign, and gain insight into the target audience, all in one package.

Sony expects that the next big breakthrough will not come from a single new electronic device. Rather, Sony president Kunitake Ando says that the future lies in making a whole range of devices more useful by linking them in a networked home-entertainment system. The company believes that its clout in consumer electronics, combined with its media content, will allow it to steer that convergence in a way that suits it. Whether the future of convergence resides in TVs or PCs or devices, $62-billion Sony makes every one of them—with a strong brand name that gives them an extra push off retail shelves around the world.

Discussion Questions

1. What have been the key success factors for Sony?
2. Where is Sony vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should they be sure to do with its marketing?

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PART

3

CONNECTING WITH CUSTOMERS

IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What are customer value, satisfaction, and loyalty, and how can companies deliver them?
2. What is the lifetime value of customers?
3. How can companies both attract and retain customers?
4. How can companies cultivate strong customer relationships?
5. How can companies deliver total quality?
6. What is database marketing?

CHAPTER 5 ::: CREATING CUSTOMER VALUE, SATISFACTION, AND LOYALTY

Today, companies face their toughest competition ever. Moving from a product and sales philosophy to a marketing philosophy, however, gives a company a better chance of outperforming competition. And the cornerstone of a well-conceived marketing orientation is strong customer relationships. Marketers must connect with customers—informing, engaging, and maybe even energizing them in the process. John Chambers, CEO of Cisco Systems, put it well: "Make your customer the center of your culture." Customer-centered companies are adept at building customer relationships, not just products; they are skilled in market engineering, not just product engineering.

Walk into most banks, and you'll notice that human contact is kept to a minimum. The scenario at a branch of Washington Mutual, known affectionately as "WaMu" (Wa-moo) by its employees and loyal customers, is a sharp contrast. There are no teller windows. No ropes. If you need to open a checking account (with free checking), you step right up to the concierge station and a friendly person directs you to the right "nook." WaMu gets cozier with customers by training its sales associates to be approachable and to find out about customers' needs. If a customer's child just got into college, they can walk him or her over to a loan officer or they can steer a prospective homeowner to the mortgage desk. If your children are with you and get restless, you can send them to the WaMu Kids® corner

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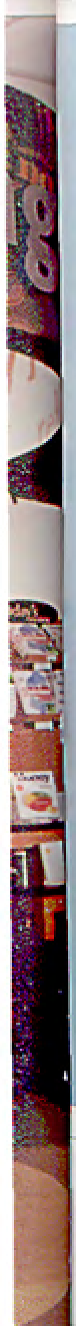


Employee welcomes customers to a Las Vegas WaMu bank: Washington Mutual prides itself on being customer-friendly.

to play. The bank's format, known as its Occasio™ style, which is Latin for "favorable opportunity," is carefully designed to facilitate cross-selling of products. This is important, because when customers buy multiple products, they are more likely to remain a customer of the bank and are far more profitable. After four years, the average customer who opens a free checking account and then purchases additional products has an exponentially more profitable relationship with the bank, and this is reflected in higher than average deposit, investment, consumer-loan, and mortgage-loan bank balances. This kind of growth has propelled the formerly unknown Seattle thrift bank into a $268 billion major player in under a decade. "WaMu" is now the nation's largest thrift bank and the sixth-largest bank overall.[1]

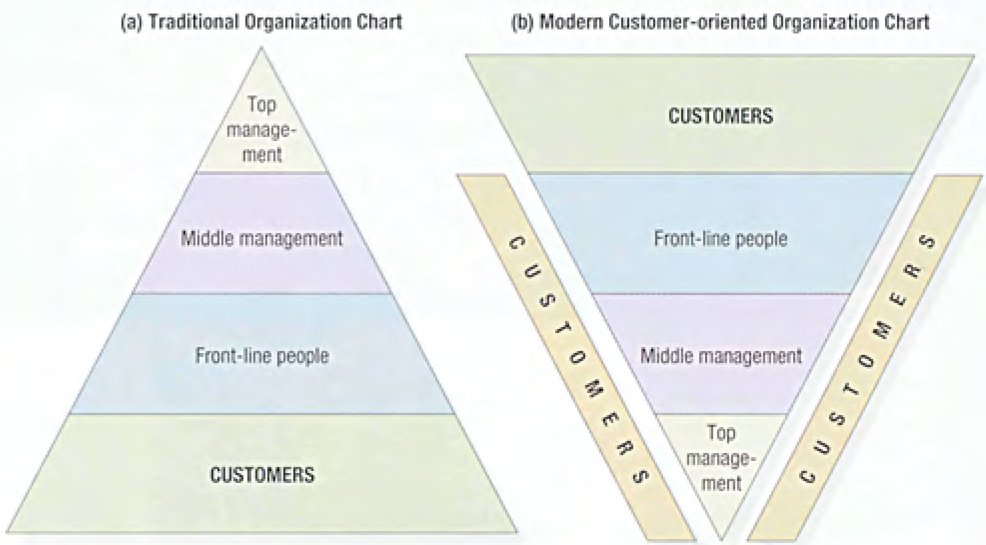
As Washington Mutual's experience shows, successful marketers are the ones that fully satisfy their customers. In this chapter, we spell out in detail the ways companies can go about winning customers and beating competitors. The answer lies largely in doing a better job of meeting or exceeding customer expectations.

::: Building Customer Value, Satisfaction, and Loyalty

Managers who believe the customer is the company's only true "profit center" consider the traditional organization chart in Figure 5.1a—a pyramid with the president at the top, management in the middle, and front-line people and customers at the bottom—obsolete. Successful marketing companies invert the chart (Figure 5.1b). At the top are customers; next in importance are front-line people who meet, serve, and satisfy customers; under them are the middle managers, whose job is to support the front-line people so they can serve customers well; and at the base is top management, whose job is to hire and support

FIG. 5.1

Traditional Organization Versus Modern Customer-Oriented Company Organization



good middle managers. We have added customers along the sides of Figure 5.1(b) to indicate that managers at every level must be personally involved in knowing, meeting, and serving customers.

Some companies have been founded with the customer-on-top business model and customer advocacy has been their strategy—and competitive advantage—all along. Online auction giant eBay Inc., epitomizes this New World Order:

EBAY

eBay helped facilitate the exchange of $20 billion of goods in 2003. Consumer trust is the key element of that success, which enabled the company to grow and support commerce between millions of anonymous buyers and sellers. To establish trust, eBay tracks and publishes the reputations of both buyers and sellers on the basis of feedback from each transaction, and eBay's millions of passionate users have come to demand a voice in all major decisions the company makes. eBay sees listening, adapting, and enabling as its main roles. This is clear in one of the company's most cherished institutions: the Voice of the Customer program. Every few months, eBay brings in as many as a dozen sellers and buyers and asks them questions about how they work and what else eBay needs to do. At least twice a week the company holds hour-long teleconferences to poll users on almost every new feature or policy. The result is that users (eBay's customers) feel like owners, and they have taken the initiative to expand the company into ever-new territory.[2]

With the rise of digital technologies like the Internet, today's increasingly informed consumers expect companies to do more than connect with them, more than satisfy them, and even more than delight them. For instance, customers now have a quick and easy means of doing comparison shopping through sites like Biz.rate, Shopping.com, and Pricegrabber.com. The Internet also facilitates communication between customers. Web sites like Epinions.com and Amazon.com enable customers to share information about their experiences in using various products and services.

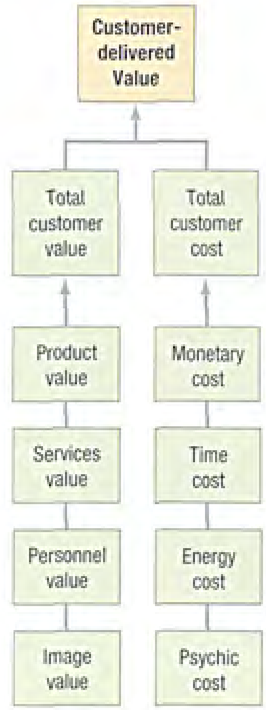


FIG. 5.2

Determinants of Customer-Delivered Value

Customer Perceived Value

Consumers are more educated and informed than ever, and they have the tools to verify companies' claims and seek out superior alternatives.[3] How then do they ultimately make choices? Customers tend to be value-maximizers, within the bounds of search costs and limited knowledge, mobility, and income. Customers estimate which offer will deliver the most perceived value and act on it (Figure 5.2). Whether or not the offer lives up to expectation affects customer satisfaction and the probability that he or she will purchase the product again.

Customer perceived value (CPV) is the difference between the prospective customer's evaluation of all the benefits and all the costs of an offering and the perceived alternatives. **Total customer value** is the perceived monetary value of the bundle of economic, functional, and psychological benefits customers expect from a given market offering. **Total customer cost** is the bundle of costs customers expect to incur in evaluating, obtaining, using, and disposing of the given market offering, including monetary, time, energy, and psychic costs.

Customer perceived value is thus based on the difference between what the customer gets and what he or she gives for different possible choices. The customer gets benefits and assumes costs. The marketer can increase the value of the customer offering by some combination of raising functional or emotional benefits and/or reducing one or more of the various types of costs. The customer who is choosing between two value offerings, V1 and V2, will examine the ratio V1:V2 and favor V1 if the ratio is larger than one, favor V2 if the ratio is smaller than one, and will be indifferent if the ratio equals one.

APPLYING VALUE CONCEPTS An example will help here. Suppose the buyer for a large construction company wants to buy a tractor from Caterpillar or Komatsu. The competing salespeople carefully describe their respective offers. The buyer wants to use the tractor in residential construction work. He would like the tractor to deliver certain levels of reliability, durability, performance, and resale value. He evaluates the tractors and decides that Caterpillar has a higher product value based on perceptions of those attributes. He also perceives differences in the accompanying services—delivery, training, and maintenance—and decides that Caterpillar provides better service and more knowledgeable and responsive personnel. Finally, he places higher value on Caterpillar's corporate image. He adds up all

Caterpillar sells tractors like this one not just on the product's attributes, but also on the value of the services, personnel, and image the company offers.

the values from these four sources—product, services, personnel, and image—and perceives Caterpillar as delivering greater customer value.

Does he buy the Caterpillar tractor? Not necessarily. He also examines his total cost of transacting with Caterpillar versus Komatsu, which consists of more than the money. As Adam Smith observed over two centuries ago, "The real price of anything is the toil and trouble of acquiring it." Total customer cost includes the buyer's time, energy, and psychic costs. The buyer evaluates these elements together with the monetary cost to form a total customer cost. Then the buyer considers whether Caterpillar's total customer cost is too high in relation to the total customer value Caterpillar delivers. If it is, the buyer might choose the Komatsu tractor. The buyer will choose whichever source he thinks delivers the highest customer perceived value.

Now let us use this decision-making theory to help Caterpillar succeed in selling to this buyer. Caterpillar can improve its offer in three ways. First, it can increase total customer value by improving product, services, personnel, and/or image benefits. Second, it can reduce the buyer's nonmonetary costs by reducing the time, energy, and psychic costs. Third, it can reduce its product's monetary cost to the buyer.

Suppose Caterpillar concludes that the buyer sees its offer as worth $20,000. Further, suppose Caterpillar's cost of producing the tractor is $14,000. This means that Caterpillar's offer potentially generates $6,000 over the company's cost, so Caterpillar needs to charge a price between $14,000 and $20,000. If it charges less than $14,000, it won't cover its costs; if it charges more than $20,000, it will price itself out of the market.

The price Caterpillar charges will determine how much value will be delivered to the buyer and how much will flow to Caterpillar. For example, if Caterpillar charges $19,000, it is creating $1,000 of customer perceived value and keeping $5,000 for itself. The lower Caterpillar sets its price, the higher the customer perceived value and, therefore, the higher the customer's incentive to purchase. To win the sale, Caterpillar must offer more customer perceived value than Komatsu does.[4]

CHOICES AND IMPLICATIONS Some marketers might argue that the process we have described is too rational. Suppose the customer chooses the Komatsu tractor. How can we explain this choice? Here are three possibilities.

1. ***The buyer might be under orders to buy at the lowest price.*** The Caterpillar salesperson's task is to convince the buyer's manager that buying on price alone will result in lower long-term profits.
2. ***The buyer will retire before the company realizes that the Komatsu tractor is more expensive to operate.*** The buyer will look good in the short run; he or she is maximizing personal benefit. The Caterpillar salesperson's task is to convince other people in the customer company that Caterpillar delivers greater customer value.
3. ***The buyer enjoys a long-term friendship with the Komatsu salesperson.*** In this case, Caterpillar's salesperson needs to show the buyer that the Komatsu tractor will draw complaints from the tractor operators when they discover its high fuel cost and need for frequent repairs.

The point of these examples is clear: Buyers operate under various constraints and occasionally make choices that give more weight to their personal benefit than to the company's benefit.

Customer perceived value is a useful framework that applies to many situations and yields rich insights. Here are its implications: First, the seller must assess the total customer value and total customer cost associated with each competitor's offer in order to know how his or her offer rates in the buyer's mind. Second, the seller who is at a customer perceived value disadvantage has two alternatives: to increase total customer value or to decrease total customer cost. The former calls for strengthening or augmenting the offer's product, services, personnel, and image benefits. The latter calls for reducing the buyer's costs by reducing the price, simplifying the ordering and delivery process, or absorbing some buyer risk by offering a warranty.[5]

DELIVERING HIGH CUSTOMER VALUE Consumers have varying degrees of loyalty to specific brands, stores, and companies. Oliver defines **loyalty** as "A deeply held commitment to re-buy or re-patronize a preferred product or service in the future despite situational influences and marketing efforts having the potential to cause switching behavior."[6] A 2002 survey of American consumers revealed that some of the brands that have great consumer loyalty include Avis rental cars, Sprint long-distance service, Nokia mobile phones, Ritz-Carlton hotels, and Miller Genuine Draft beer.[7]

The key to generating high customer loyalty is to deliver high customer value. Michael Lanning, in his *Delivering Profitable Value*, says that a company must design a competitively superior value proposition aimed at a specific market segment, backed by a superior value-delivery system.[8]

The **value proposition** consists of the whole cluster of benefits the company promises to deliver; it is more than the core positioning of the offering. For example, Volvo's core positioning has been "safety," but the buyer is promised more than just a safe car; other benefits include a long-lasting car, good service, and a long warranty period. Basically, the value proposition is a statement about the resulting experience customers will gain from the company's market offering and from their relationship with the supplier. The brand must represent a promise about the total experience customers can expect. Whether the promise is kept depends on the company's ability to manage its value-delivery system. The **value-delivery system** includes all the experiences the customer will have on the way to obtaining and using the offering.

BRITISH AIRWAYS

British Airways and American Airlines may use the same kind of aircraft to fly executives first class between New York and London, but British Airways (BA) beats American Airlines by meeting customers' needs for convenience and rest at every step of the journey. BA's value-delivery system includes a separate first-class express check-in and security clearance, plus a pre-flight express meal service in the first-class lounge so that time-pressed executives can maximize sleep time on the plane without the distraction of in-flight meals. BA was the first to put seats that recline into perfectly flat beds in its first-class section, and in the United Kingdom a fast-track customs area speeds busy executives on their way.[9]

A similar theme is emphasized by Simon Knox and Stan Maklan in their *Competing on Value*.[10] Too many companies create a value gap by failing to align brand value with customer value. Brand marketers try to distinguish their brand from others by a slogan ("washes whiter") or a unique selling proposition ("A Mars a day helps you work, rest, and play"), or by augmenting the basic offering with added services ("Our hotel will provide a computer upon request"). Yet, they are less successful in delivering distinctive customer value, primarily because their marketing people focus on the brand image and not enough on actual product or service performance. Whether customers will actually receive the promised value proposition will depend on the marketer's ability to influence various core business processes. Knox and Maklan want company marketers to spend as much time influencing the company's core processes as they do designing the brand profile. Here is an example of a company that is a master at delivering customer value.

SUPERQUINN

Superquinn is Ireland's largest supermarket chain and its founder, Feargal Quinn, is Ireland's master marketer. A greeter is posted at the store entrance to welcome and help customers and even offer coffee, and to provide umbrellas in case of rain and carryout service to customers' cars. Department managers post themselves in the aisles to interact with customers and answer questions. There is a high-quality salad bar, fresh bread baked every four hours, and indications of when produce arrived, including the farmers' pictures. Superquinn also operates a child-care center. It offers a loyalty program that gives points for the amount purchased and for discovering anything wrong with the store, such as dented cans or bad tomatoes. The loyalty card is recognized by a dozen other firms (a bank, gas station, etc.) who give points for purchasing at their establishments. Because everything is done to exceed normal customer expectations, Superquinn stores enjoy an almost-cult following.[11]

Total Customer Satisfaction

Whether the buyer is satisfied after purchase depends on the offer's performance in relation to the buyer's expectations. In general, **satisfaction** is a person's feelings of pleasure or disappointment resulting from comparing a product's perceived performance (or outcome) in relation to his or her expectations. If the performance falls short of expectations, the customer is dissatisfied. If the performance matches the expectations, the customer is satisfied. If the performance exceeds expectations, the customer is highly satisfied or delighted.[12]

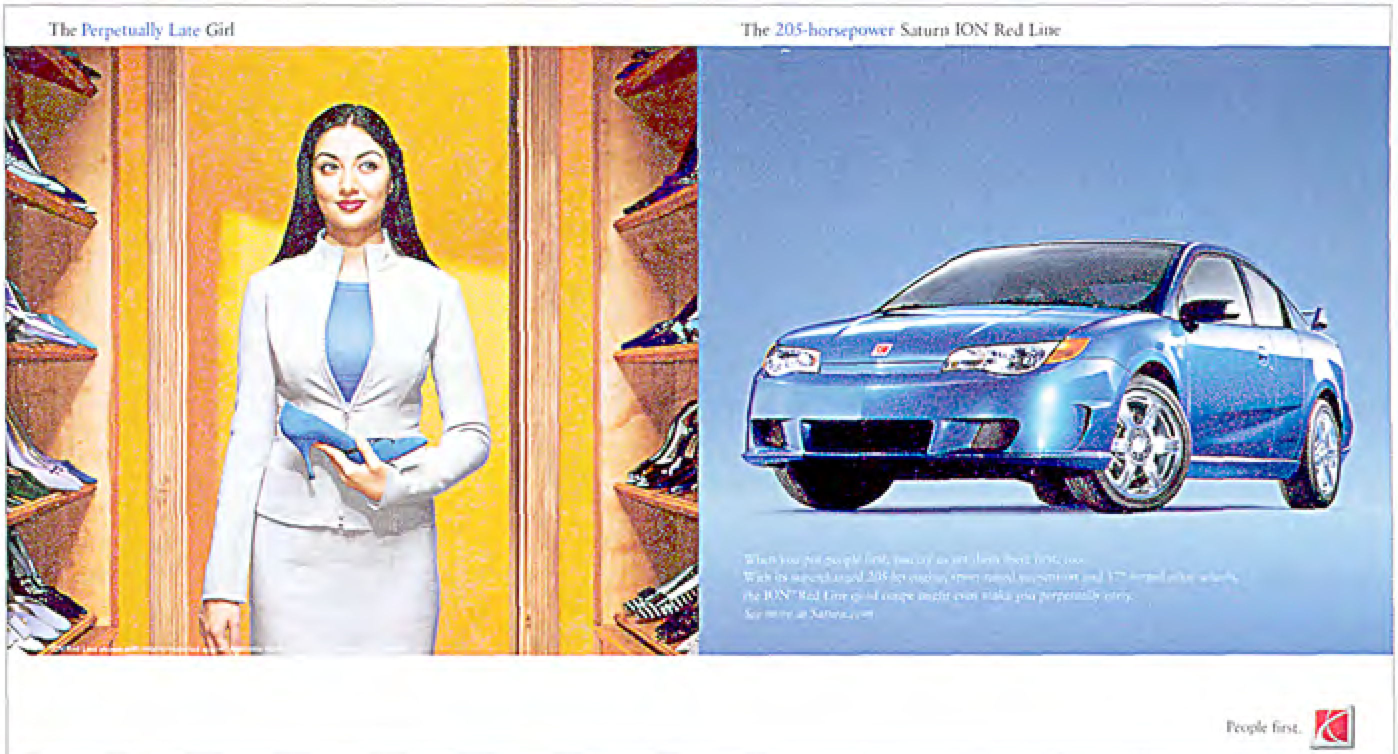
Although the customer-centered firm seeks to create high customer satisfaction, that is not its ultimate goal. If the company increases customer satisfaction by lowering its price or increasing its services, the result may be lower profits. The company might be able to increase its profitability by means other than increased satisfaction (for example, by improving manufacturing processes or investing more in R&D). Also, the company has many stakeholders, including employees, dealers, suppliers, and stockholders. Spending more to increase customer satisfaction might divert funds from increasing the satisfaction of other "partners." Ultimately, the company must operate on the philosophy that it is trying to deliver a high level of customer satisfaction subject to delivering acceptable levels of satisfaction to the other stakeholders, given its total resources.

CUSTOMER EXPECTATIONS How do buyers form their expectations? From past buying experience, friends' and associates' advice, and marketers' and competitors' information and promises. If marketers raise expectations too high, the buyer is likely to be disappointed. However, if the company sets expectations too low, it won't attract enough buyers (although it will satisfy those who do buy).[13] Some of today's most successful companies are raising expectations and delivering performances to match. When General Motors launched the Saturn car division, it changed the whole buyer–seller relationship with a New Deal for car buyers: There would be a fixed price (none of the traditional haggling); a 30-day guarantee or money back; and salespeople on salary, not on commission (none of the traditional hard sell).[14] Look at what high satisfaction can do.

JETBLUE

JetBlue Airways, founded in New York in 1999, significantly raised customer expectations of low-fare carriers. With its brand new Airbus jets, comfy leather seats, live satellite TV, free wireless Internet access, and a consumer-friendly policy of never bumping a passenger, it has inspired lots of low-fare/high-service copycats. Like pioneer Southwest, where JetBlue's CEO David Neeleman tried out his wings, JetBlue finds employees who know how to keep customers coming back. He asks each person he hires to follow a few corporate commandments known as the Values, including safety, caring, integrity, fun, and passion. Even CEO Neeleman and the pilots get on their hands and knees to pick trash out from between seats and scrub the restrooms to prep planes for the next trip. The pitch-in prepping keeps turnaround time down, another reason more and more customers come to JetBlue. The proof is in the numbers: While almost every other airline is drowning in red ink, JetBlue is in the black. In 2003 the airline pulled in a $104 million profit on revenues of $998 million. It now carries more people from New York to Fort Lauderdale than any other airline.[15]

A customer's decision to be loyal or to defect is the sum of many small encounters with the company. Consulting firm Forum Corporation says that in order for all these small encounters to add up to customer loyalty, companies need to create a "branded customer experience." Here is how San Francisco's Joie de Vivre chain does this.



This Saturn Ion ad looks like a lot of other car ads. But buying a Saturn has unique advantages: no haggling over price, a 30-day money-back guarantee, and salespeople on salary, not commission.

JOIE DE VIVRE

Joie de Vivre Hospitality Inc., operates a chain of boutique hotels, restaurants, and resorts in the San Francisco area. Each property's unique décor, quirky amenities, and thematic style are often loosely based on popular magazines. For example, the Hotel del Sol—a converted motel bearing a yellow exterior and surrounded by palm trees wrapped with festive lights—is described as "kind of *Martha Stewart Living* meets *Islands* magazine."[16] Two Silicon Valley hotels offer guests high-speed Internet connections in their rooms and by the pool.[17] The boutique concept enables the hotels to offer personal touches such as vitamins in place of chocolates on pillows. Joie de Vivre now owns the largest number of independent hotel properties in the Bay Area.

Measuring Satisfaction

Many companies are systematically measuring customer satisfaction and the factors shaping it. For example, IBM tracks how satisfied customers are with each IBM salesperson they encounter, and makes this a factor in each salesperson's compensation.

A company would be wise to measure customer satisfaction regularly because one key to customer retention is customer satisfaction. A highly satisfied customer generally stays loyal longer, buys more as the company introduces new products and upgrades existing products, talks favorably about the company and its products, pays less attention to competing brands and is less sensitive to price, offers product or service ideas to the company, and costs less to serve than new customers because transactions are routine.

The link between customer satisfaction and customer loyalty, however, is not proportional. Suppose customer satisfaction is rated on a scale from one to five. At a very low level of customer satisfaction (level one), customers are likely to abandon the company and even bad-mouth it. At levels two to four, customers are fairly satisfied but still find it easy to switch when a better offer comes along. At level five, the customer is very likely to repurchase and even spread good word of mouth about the company. High satisfaction or delight creates an emotional bond with the brand or company, not just a rational preference. Xerox's senior management found out that its "completely satisfied" customers were six times more likely to repurchase Xerox products over the following 18 months than its "very satisfied" customers.[18]

When customers rate their satisfaction with an element of the company's performance—say, delivery—the company needs to recognize that customers vary in how they define good delivery. It could mean early delivery, on-time delivery, order completeness, and so on. The company must also realize that two customers can report being "highly satisfied" for different reasons. One may be easily satisfied most of the time and the other might be hard to please but was pleased on this occasion.[19]

A number of methods exist to measure customer satisfaction. *Periodic surveys* can track customer satisfaction directly. Respondents can also be asked additional questions to measure repurchase intention and the likelihood or willingness to recommend the company and brand to others. Paramount attributes the success of its five theme parks to the thousands of Web-based guest surveys it sends to customers who have agreed to be contacted. During the past year, the company conducted more than 55 Web-based surveys and netted 100,000 individual responses that described guest satisfaction on topics including rides, dining, shopping, games, and shows.[20]

Companies can monitor the *customer loss rate* and contact customers who have stopped buying or who have switched to another supplier to learn why this happened. Finally, companies can hire *mystery shoppers* to pose as potential buyers and report on strong and weak points experienced in buying the company's and competitors' products. Managers themselves can enter company and competitor sales situations where they are unknown and experience firsthand the treatment they receive, or phone their own company with questions and complaints to see how the calls are handled.

For customer satisfaction surveys, it's important that companies ask the right questions. Frederick Reichheld suggests that perhaps only one question really matters: "Would you recommend this product or service to a friend?" He maintains that marketing departments typically focus surveys on the areas they can control, such as brand image, pricing, and product features. According to Reichheld, a customer's willingness to recommend to a friend results from how well the customer is treated by front-line employees, which in turn is determined by all the functional areas that contribute to a customer's experience.[21]

In addition to tracking customer value expectations and satisfaction, companies need to monitor their competitors' performance in these areas. One company was pleased to find that 80 percent of its customers said they were satisfied. Then the CEO found out that its leading competitor had a 90 percent customer satisfaction score. He was further dismayed when he learned that this competitor was aiming for a 95 percent satisfaction score.

For customer-centered companies, customer satisfaction is both a goal and a marketing tool. Companies need to be especially concerned today with their customer satisfaction level because the Internet provides a tool for consumers to spread bad word of mouth—as well as good word of mouth—to the rest of the world. On Web sites like troublebenz.com and lemonmb.com, angry Mercedes-Benz owners have been airing their complaints on everything from faulty key fobs and leaky sunroofs to balky electronics that leave drivers and their passengers stranded.[22]

Companies that do achieve high customer satisfaction ratings make sure their target market knows it. When J. D. Power began to rate national home mortgage leaders, Countrywide was quick to advertise its number-one ranking in customer satisfaction. Dell Computer's meteoric growth in the computer systems industry can be partly attributed to achieving and advertising its number-one rank in customer satisfaction.

The University of Michigan's Claes Fornell has developed the American Customer Satisfaction Index (ACSI) to measure the perceived satisfaction consumers feel with different firms, industries, economic sectors, and national economies.[23] Examples of firms that led their respective industries with high ACSI scores in 2003 are Dell (78), Cadillac (87), FedEx (82), Google (82), Heinz (88), Kenmore (84), Southwest Airlines (75), and Yahoo! (78).

Product and Service Quality

Satisfaction will also depend on product and service quality. What exactly is quality? Various experts have defined it as "fitness for use," "conformance to requirements," "freedom from variation," and so on.[24] We will use the American Society for Quality Control's definition: **Quality** is the totality of features and characteristics of a product or service that bear on its ability to satisfy stated or implied needs.[25] This is clearly a customer-centered definition. We

A Countrywide ad touts its #1 Customer Satisfaction rating from J. D. Power and Associates. Ratings like these are important to a customer-centered company, because word of mouth, good and bad, spreads so quickly on the Internet.

can say that the seller has delivered quality whenever the seller's product or service meets or exceeds the customers' expectations. A company that satisfies most of its customers' needs most of the time is called a quality company, but it is important to distinguish between *conformance* quality and *performance* quality (or grade). A Lexus provides higher performance quality than a Hyundai: The Lexus rides smoother, goes faster, and lasts longer. Yet both a Lexus and a Hyundai can be said to deliver the same conformance quality if all the units deliver their respective promised quality.

Total quality is the key to value creation and customer satisfaction. Total quality is everyone's job, just as marketing is everyone's job. This idea was expressed well by Daniel Beckham:

> Marketers who don't learn the language of quality improvement, manufacturing, and operations will become as obsolete as buggy whips. The days of functional marketing are gone. We can no longer afford to think of ourselves as market researchers, advertising people, direct marketers, strategists—we have to think of ourselves as customer satisfiers—customer advocates focused on whole processes.[26]

Marketing managers have two responsibilities in a quality-centered company. First, they must participate in formulating strategies and policies to help the company win through total quality excellence. Second, they must deliver marketing quality alongside production quality. Each marketing activity—marketing research, sales training, advertising, customer service, and so on—must be performed to high standards.

Total Quality Management

The quest to maximize customer satisfaction led some firms to adopt total quality management principles. **Total quality management (TQM)** is an organization-wide approach to continuously improving the quality of all the organization's processes, products, and services.

According to GE's former chairman, John F. Welch Jr., "Quality is our best assurance of customer allegiance, our strongest defense against foreign competition, and the only path to sustained growth and earnings."[27] The drive to produce goods that are superior in world markets has led some countries—and groups of countries—to recognize or award prizes to companies that exemplify the best quality practices (e.g., the Deming Prize in Japan, the Malcolm Baldridge National Quality Award in the United States, and the European Quality Award).

Product and service quality, customer satisfaction, and company profitability are intimately connected. Higher levels of quality result in higher levels of customer satisfaction, which support higher prices and (often) lower costs. Studies have shown a high correlation between relative product quality and company profitability.[28]

In practicing TQM, however, some firms ran into implementation problems as they became overly focused—perhaps even obsessed—with processes and *how* they were doing business. They lost sight of the needs and wants of customers and *why* they were doing business. In some cases, companies were able to achieve benchmarks against top quality standards, but only by incurring prohibitive increases in costs. For example, scientific equipment maker Varian embraced TQM principles but found itself rushing to meet production schedules and deadlines that managers now feel may not have been that important to their customers to begin with.

In a reaction to this somewhat myopic behavior, some companies now concentrate their efforts on "return on quality" or ROQ. ROQ adherents advocate improving quality only on those dimensions that produce tangible customer benefits, lower costs, or increased sales. This bottom-line orientation forces companies to make sure that the quality of the product offerings is in fact the quality consumers actually want.[29]

Rust, Moorman, and Dickson studied managers seeking to increase their financial returns from quality improvements.[30] They found that firms that adopted primarily a revenue expansion emphasis (externally focusing on growing demand through catering to and increasing consumers' preferences for quality) performed better as compared to firms that adopted primarily a cost-reduction emphasis (internally focusing on improving the efficiency of internal processes) or firms that attempted to adopt both emphases simultaneously.

Marketers play several roles in helping their companies define and deliver high-quality goods and services to target customers. First, they bear the major responsibility for correctly identifying the customers' needs and requirements. Second, they must communicate customer expectations properly to product designers. Third, they must make sure that customers' orders are filled correctly and on time. Fourth, they must check that customers have received proper instructions, training, and technical assistance in the use of the product. Fifth, they must stay in touch with customers after the sale to ensure that they are satisfied and remain satisfied. Sixth, they must gather customer ideas for product and service improvements and convey them to the appropriate departments. When marketers do all this, they are making substantial contributions to total quality management and customer satisfaction, as well as to customer and company profitability.

::: Maximizing Customer Lifetime Value

Ultimately, marketing is the art of attracting and keeping profitable customers. According to James V. Putten of American Express, the best customers outspend others by ratios of 16 to 1 in retailing, 13 to 1 in the restaurant business, 12 to 1 in the airline business, and 5 to 1 in the hotel and motel industry.[31] Yet every company loses money on some of its customers. The well-known 20–80 rule says that the top 20 percent of the customers may generate as much as 80 percent of the company's profits. Sherden suggested amending the rule to read 20–80–30, to reflect the idea that the top 20 percent of customers generate 80 percent of the company's profits, half of which are lost serving the bottom 30 percent of unprofitable customers.[32] The implication is that a company could improve its profits by "firing" its worst customers.

Furthermore, it is not necessarily the company's largest customers who yield the most profit. The largest customers demand considerable service and receive the deepest discounts. The smallest customers pay full price and receive minimal service, but the costs of transacting with small customers reduce their profitability. The midsize customers receive good service and pay nearly full price and are often the most profitable. This fact helps explain why many large firms are now invading the middle market. Major air express carriers, for instance, are finding that it does not pay to ignore small and midsize international shippers. Programs geared toward smaller customers provide a network of drop boxes, which allow for substantial discounts over letters and packages picked up at the shipper's place of business. United Parcel Service (UPS) conducts seminars to instruct exporters in the finer points of shipping overseas.[33]

Customer Profitability

What makes a customer profitable? A **profitable customer** is a person, household, or company that over time yields a revenue stream that exceeds by an acceptable amount the company's cost stream of attracting, selling, and servicing that customer. Note that the emphasis is on the lifetime stream of revenue and cost, not on the profit from a particular transaction.[34] Customer profitability can be assessed individually, by market segment, or by channel.

Although many companies measure customer satisfaction, most companies fail to measure individual customer profitability. Banks claim that this is a difficult task because a customer uses different banking services and the transactions are logged in different departments. However, banks that have succeeded in linking customer transactions have been appalled by the number of unprofitable customers in their customer base. Some banks report losing money on over 45 percent of their retail customers. There are only two solutions to handling unprofitable customers: Raise fees or reduce service support.[35]

CUSTOMER PROFITABILITY ANALYSIS A useful type of profitability analysis is shown in Figure 5.3.[36] Customers are arrayed along the columns and products along the rows. Each cell contains a symbol for the profitability of selling that product to that customer. Customer 1 is very profitable; he buys three profit-making products (P1, P2, and P4). Customer 2 yields a picture of mixed profitability; he buys one profitable product and one unprofitable product. Customer 3 is a losing customer because he buys one profitable product and two unprofitable products.

What can the company do about customers 2 and 3? (1) It can raise the price of its less profitable products or eliminate them, or (2) it can try to sell them its profit-making products. Unprofitable customers who defect should not concern the company. In fact, the company should encourage these customers to switch to competitors.

Customer profitability analysis (CPA) is best conducted with the tools of an accounting technique called Activity-Based Costing (ABC). The company estimates all revenue coming from the customer, less all costs. The costs should include not only the cost of making and distributing the products and services, but also such costs as taking phone calls from the customer, traveling to visit the customer, entertainment and gifts—all the company's resources that went into serving that customer. When this is done for each customer, it is possible to classify customers into different profit tiers: platinum customers (most profitable), gold customers (profitable), iron customers (low profitability but desirable), and lead customers (unprofitable and undesirable).

The company's job is to move iron customers into the gold tier and gold customers into the platinum tier, while dropping the lead customers or making them profitable by raising their prices or lowering the cost of serving them. More generally, marketers must segment customers into those worth pursuing versus those potentially less lucrative customers that should receive less attention, if any at all.

Dhar and Glazer make an interesting analogy between the individuals that make up the firm's customer portfolio for a firm and the stocks that make up an investment portfolio.[37] Just as with the latter, it is important to calculate the beta, or risk-reward value, for each customer and diversify the customer portfolio accordingly. From their perspective, firms

Customers

		C_1	C_2	C_3	
Products	P_1	+	+	+	Highly profitable product
	P_2	+			Profitable product
	P_3		–	–	Losing product
	P_4	+		–	Mixed-bag product
		High-profit customer	Mixed-bag customer	Losing customer	

FIG. 5.3

Customer–Product Profitability Analysis

should assemble portfolios of negatively correlated individuals so that the financial contributions of one offset the deficits of another to maximize the portfolio's risk-adjusted lifetime value.

COMPETITIVE ADVANTAGE Companies must not only be able to create high absolute value, but also high value relative to competitors at a sufficiently low cost. **Competitive advantage** is a company's ability to perform in one or more ways that competitors cannot or will not match. Michael Porter urged companies to build a sustainable competitive advantage.[38] But few competitive advantages are sustainable. At best, they may be leverageable. A *leverageable advantage* is one that a company can use as a springboard to new advantages, much as Microsoft has leveraged its operating system to Microsoft Office and then to networking applications. In general, a company that hopes to endure must be in the business of continuously inventing new advantages.

Any competitive advantage must be seen by customers as a *customer advantage*. For example, if a company delivers faster than its competitors, this will not be a customer advantage if customers do not value speed. Companies must focus on building customer advantages. Then they will deliver high customer value and satisfaction, which leads to high repeat purchases and ultimately to high company profitability.

Measuring Customer Lifetime Value

The case for maximizing long-term customer profitability is captured in the concept of customer lifetime value. **Customer lifetime value (CLV)** describes the net present value of the stream of future profits expected over the customer's lifetime purchases. The company must subtract from the expected revenues the expected costs of attracting, selling, and servicing that customer, applying the appropriate discount rate (e.g., 10%–20%, depending on cost of capital and risk attitudes). Various CLV estimates have been made for different products and services.

- Carl Sewell, in *Customers for Life* (with Paul Brown), estimated that a customer entering his car dealership for the first time represents a potential lifetime value of over $300,000.[39] If the satisfied customer brings in other customers, the figure would be higher. Similarly, General Motors estimates its lifetime customers to be worth $276,000 on average. These six-figure values are a graphic illustration of the importance of keeping the customer satisfied for the life of the automobile to better the chances of a repeat purchase.[40]
- Even though tacos may cost less than a dollar each, executives at Taco Bell have determined that a repeat customer is worth as much as $11,000. By sharing such estimates of customer lifetime value with its employees, Taco Bell's managers help employees understand the value of keeping customers satisfied.[41]
- Mark Grainer, former chairman of the Technical Assistance Research Programs Institute (TARP), estimated that a loyal supermarket customer is worth $3,800 annually.[42]


A GM customer shops the showroom at Hoskins Chevrolet in Elk Grove Village, Illinois. What GM wants is to satisfy him so he comes back to Hoskins and GM each time he needs a car.

We can work out an example of estimating CLV. Suppose a company analyzes its new-customer acquisition cost:

- Cost of average sales call (including salary, commission, benefits, and expenses): $300
- Average number of sales calls to convert an average prospect into a customer: 4
- Cost of attracting a new customer: $1,200

This is an underestimate because we are omitting the cost of advertising and promotion, plus the fact that only a fraction of all pursued prospects end up being converted into customers.

Now suppose the company estimates average customer lifetime value as follows:

- Annual customer revenue: $500
- Average number of loyal years: 20
- Company profit margin: .10
- Customer lifetime value: $1,000

This company is spending more to attract new customers than they are worth. Unless the company can sign up customers with fewer sales calls, spend less per sales call, stimulate higher new-customer annual spending, retain customers longer, or sell them higher-profit products, it is headed for bankruptcy. Of course, in addition to an average customer estimate, a company needs a way of estimating CLV for each individual customer to decide how much to invest in each customer.

CLV calculations provide a formal quantitative framework for planning customer investment and help marketers to adopt a long-term perspective. One challenge in applying CLV concepts, however, is to arrive at reliable cost and revenue estimates. Marketers who use CLV concepts must also be careful to not forget the importance of short-term, brand-building marketing activities that will help to increase customer loyalty.

Customer Equity

The aim of customer relationship management (CRM) is to produce high customer equity. **Customer equity** is the total of the discounted lifetime values of all of the firm's customers.[43] Clearly, the more loyal the customers, the higher the customer equity. Rust, Zeithaml, and Lemon distinguish three drivers of customer equity: value equity, brand equity, and relationship equity.[44]

- ***Value equity*** is the customer's objective assessment of the utility of an offering based on perceptions of its benefits relative to its costs. The sub-drivers of value equity are quality, price, and convenience. Each industry has to define the specific factors underlying each sub-driver in order to find programs to improve value equity. An airline passenger might define quality as seat width; a hotel guest might define quality as room size. Value equity makes the biggest contribution to customer equity when products are differentiated and when they are more complex and need to be evaluated. Value equity especially drives customer equity in business markets.
- ***Brand equity*** is the customer's subjective and intangible assessment of the brand, above and beyond its objectively perceived value. The sub-drivers of brand equity are customer brand awareness, customer attitude toward the brand, and customer perception of brand ethics. Companies use advertising, public relations, and other communication tools to affect these sub-drivers. Brand equity is more important than the other drivers of customer equity where products are less differentiated and have more emotional impact. We consider brand equity in detail in Chapter 9.
- ***Relationship equity*** is the customer's tendency to stick with the brand, above and beyond objective and subjective assessments of its worth. Sub-drivers of relationship equity include loyalty programs, special recognition and treatment programs, community-building programs, and knowledge-building programs. Relationship equity is especially important where personal relationships count for a lot and where customers tend to continue with suppliers out of habit or inertia.

This formulation integrates *value management*, *brand management*, and *relationship management* within a customer-centered focus. Companies can decide which driver(s) to strengthen for the best payoff. The researchers believe they can measure and compare the financial return of alternative investments to help choose strategies and actions based on which would provide the best return on marketing investments.

An alternative formulation to customer equity is provided by Blattberg, Getz, and Thomas. They view customer equity as driven by three components: acquisition, retention, and add-on selling.[45] Acquisition is affected by the number of prospects, the acquisition probability of a prospect, and acquisition spending per prospect. Retention is influenced by the retention rate and retention spending level. Add-on spending is a function of the efficiency of add-on selling, the number of add-on selling offers given to existing customers, and the response rate to new offers. Marketing activities can then be judged by how they affect these three components.

Customer equity represents a promising approach to marketing management. "Marketing Insight: Progress and Priorities in Customer Equity Management" highlights some recent academic thinking on the subject. Note too that customer equity notions can be extended. Mohan Sawhney defines the **relational equity** of the firm as the cumulative value of the firm's network of relationships with its customers, partners, suppliers, employees, and investors.[46] Relational equity depends on the company's ability to attract and retain talent, customers, investors, and partners.

::: Cultivating Customer Relationships

Maximizing customer value means cultivating long-term customer relationships. In the past, producers customized their offerings to each customer: The tailor fitted a suit and a cobbler made shoes for each individual. The Industrial Revolution ushered in an era of mass production. To maximize economies of scale, companies made standard goods in advance of orders and left it to individuals to fit into whatever was available. Producers moved from *built-to-order* marketing to *built-to-stock* marketing.

Companies are now moving away from wasteful mass marketing to more precision marketing designed to build strong customer relationships.[47] Today's economy is supported by information businesses. Information has the advantages of being easy to differentiate, customize, personalize, and dispatch over networks at incredible speed.

As companies have grown proficient at gathering information about individual customers and business partners (suppliers, distributors, retailers), and as their factories are designed more flexibly, they have increased their ability to individualize market offerings, messages, and media. **Mass customization** is the ability of a company to meet each customer's requirements—to prepare on a mass basis individually designed products, services, programs, and communications.[48] While Levi's and Lands' End were among the first clothing manufacturers to introduce custom jeans, now there are many players in the mass-customization market:

- Nike lets consumers customize athletic shoes for $10 more. A shopper with two different size feet can even get a nonmatching pair.
- At Reflect.com, the Web site for Procter & Gamble spin-off Reflect True Custom Beauty, consumers answer a set of questions and then get custom-blended foundation, moisturizer, shampoo, or other cosmetics and skin-care products.
- Interactive Custom Clothes, which began making made-to-order jeans and pants in 1996, has grown so fast that it had to stop taking orders in 2003. The company is now trying to find an apparel manufacturer or retailer partner to help ease the load.

Customer Relationship Management (CRM)

In addition to working with partners—called **partner relationship management (PRM)**—many companies are intent on developing stronger bonds with their customers—called **customer relationship management (CRM)**. This is the process of managing detailed information about individual customers and carefully managing all customer "touch points" to maximize customer loyalty. A *customer touch point* is any occasion on which a customer encounters the brand and product—from actual experience to personal or mass communications to casual observation. For a hotel, the touch points include reservations, check-in and check-out, frequent-stay programs, room service, business services, exercise facilities, laundry service, restaurants, and bars. For instance, the Four Seasons relies on personal touches, such as a staff that always addresses guests by name, high-powered employees who understand the needs of sophisticated business travelers, and at least one best-in-region facility, such as a premier restaurant or spa.[49]

Customer relationship management enables companies to provide excellent real-time customer service through the effective use of individual account information. Based on

MARKETING INSIGHT — PROGRESS AND PRIORITIES IN CUSTOMER EQUITY MANAGEMENT

Customer equity has roots in many different marketing concepts—direct marketing and database marketing, service quality, relationship marketing, brand equity. Its unique focus, however, is on understanding the value of the customer to the firm and how to manage the customer as a strategic asset to increase overall firm value for shareholders.

Customer equity can be seen as the expected lifetime value of a firm's existing customer base plus the expected future lifetime value of newly acquired customers. This basic CLV model can be modified to incorporate several other dimensions, such as individual customer risk, the social effects of the word of mouth, and competitive and environmental effects that can dampen customer retention rates.

A special issue of the *Journal of Service Research* devoted to articles on the topic of customer equity included contributions by top academics working on that topic. The papers covered a wide range of issues, among them how to implement customer equity management:

1. ***Assemble individual-level, industry-wide consumer data.*** Pooled customer information by all industry competitors can provide insight into crucial considerations such as an individual's share of requirements. The benefits of broad industry cooperation can offset the costs from the loss of company-specific knowledge.
2. ***Track marketing's effect on the balance sheet, not just the income statement.*** Accounting principles that recognize the customer asset are needed. The challenge is that CLV calculations depend on assumptions about a host of factors, such as the future income stream from a customer, appropriate cost allocations to a customer, discount factors, and the expected economic life of a customer.
3. ***Model future revenues appropriately.*** Decisions about the timing and probability of revenue flows have important implications.
4. ***Maximize (don't just measure) CLV.*** Marketers must implement marketing initiatives to maximize the value of the customer franchise (e.g., loyalty programs, customer reactivations, and cross-selling).
5. ***Align the organization with customer management activities.*** For example, some catalog retailers or credit card companies commonly separate the prospect acquisition team from a customer conversion team from those responsible for ongoing customer retention and servicing. Another team may even be assigned to work on reactivation of dormant accounts.
6. ***Respect the sensitivity of customer information.*** Consider decentralizing customer information storage and having data reside with the consumer, on personal computers or smart cards. Also, allow consumers the right to audit and contest the accuracy of their profiles.
7. ***Develop CRM from an efficiency tool into a service improvement tool.*** The most successful CRM implementations reevaluate and refine all customer-facing business processes; develop and motivate all service and support personnel; and select and tailor appropriate technologies.

Source: Special Issue on Customer Equity Management, *Journal of Services Research* 5, no.1 (August 2002).

what they know about each valued customer, companies can customize market offerings, services, programs, messages, and media. CRM is important because a major driver of company profitability is the aggregate value of the company's customer base.[50] A pioneer in the application of CRM techniques is Harrah's Entertainment.

HARRAH'S

In 1997, Harrah's Entertainment Inc., in Las Vegas, launched a pioneering loyalty program that pulled all customer data into a centralized warehouse and provided sophisticated analysis to better understand the value of the investments the casino makes in its customers. Harrah's now has fine-tuned its Total Rewards system to achieve near-real-time analysis: As customers interact with slot machines, check into casinos or buy meals, they receive reward offers based on the predictive analyses. The company has now identified hundreds of customer segments among its more than 25 million slot players. By targeting offers to highly specific customer segments, Harrah's boosted its market share by six percentage points and increased net income by 12.4 percent, even during the difficult post-9/11 market in 2002.[51]

Some of the groundwork for customer relationship management was laid by Don Peppers and Martha Rogers in a series of books.[52] Peppers and Rogers outline a four-step framework for one-to-one marketing that can be adapted to CRM marketing as follows:

- ***Identify your prospects and customers.*** Do not go after everyone. Build, maintain, and mine a rich customer database with information derived from all the channels and customer touch points.

Playing the slots at Harrah's Cherokee Casino in North Carolina. These customers are probably part of a sophisticated segmenting system that lets Harrah's target offers to hundreds of customer segments among its 25 million slot players.

- ***Differentiate customers in terms of (1) their needs and (2) their value to your company.*** Spend proportionately more effort on the most valuable customers (MVCs). Apply Activity Based Costing and calculate customer lifetime value. Estimate net present value of all future profits coming from purchases, margin levels, and referrals, less customer-specific servicing costs.
- ***Interact with individual customers to improve your knowledge about their individual needs and to build stronger relationships.*** Formulate customized offerings that are communicated in a personalized way.
- ***Customize products, services, and messages to each customer.*** Facilitate customer/company interaction through the company contact center and Web site.

Table 5.1 lists the main differences between mass marketing and one-to-one marketing.

A key driver of shareholder value is the aggregate value of the customer base. Winning companies improve the value of their customer base by excelling at strategies such as the following:

- ***Reducing the rate of customer defection.*** Whole Foods, the world's largest retailer of natural and organic foods, woos customers with a commitment to marketing the best foods and a team concept for employees. Selecting and training employees to be knowledgeable and friendly increases the likelihood that the inevitable shopping questions from customers will be answered satisfactorily.
- ***Increasing the longevity of the customer relationship.*** The more involved a customer is with the company, the more likely he or she is to stick around. Some companies treat their customers as partners—especially in business-to-business markets—soliciting their help in the design of new products or improving their customer service. Instant Web Companies (IWCO), a Chanhassen, Minnesota, direct-mail printer, launched a monthly Customer Spotlight program where guest companies provide an overview of their business and direct-mail programs and comment on IWCO practices, products, and services. IWCO's staff not only gains exposure to customers, but also develops a broader perspective on customers' business and marketing objectives and how to add value and identify options that help meet their customers' goals.[53]
- ***Enhancing the growth potential of each customer through "share-of-wallet," cross-selling, and up-selling.***[54] Harley-Davidson sells more than motorcycles and riding supplements (such as gloves, leather jackets, helmets, and sunglasses). Harley dealerships sell more than 3,000 items of clothing—some even have their own fitting rooms. Licensed goods sold by others range from the predictable (shot glasses, cue balls, and Zippo cigarette lighters) to the more surprising items (cologne, dolls, and cell phones). Harley-branded merchandise amounted to more than $211 million in company sales in 2003.
- ***Making low-profit customers more profitable or terminating them.*** To avoid the direct need for termination, unprofitable customers can be made to buy more or in larger quantities, forgo certain features or services, or pay higher amounts or fees. Banks, phone companies, and travel agencies are all now charging for once-free services to ensure minimum customer revenue levels.
- ***Focusing disproportionate effort on high-value customers.*** The most valuable customers can be treated in a special way. Thoughtful gestures such as birthday greetings, small gifts, or invitations to special sports or arts events can send a strong signal to the customer.

Attracting, Retaining, and Growing Customers

Customers are becoming harder to please. They are smarter, more price conscious, more demanding, less forgiving, and they are approached by many more competitors with equal or better offers. The challenge, according to Jeffrey Gitomer, is not necessarily to produce

TABLE 5.1

Mass Marketing Versus One-to-One Marketing

Mass Marketing	One-to-One Marketing
Average customer	Individual customer
Customer anonymity	Customer profile
Standard product	Customized market offering
Mass production	Customized production
Mass distribution	Individualized distribution
Mass advertising	Individualized message
Mass promotion	Individualized incentives
One-way message	Two-way messages
Economies of scale	Economies of scope
Share of market	Share of customer
All customers	Profitable customers
Customer attraction	Customer retention

Source: Adapted from Don Peppers and Martha Rogers, *The One-to-One Future* (New York: Doubleday/Currency, 1993). See their Web site www.1to1.com.

satisfied customers; several competitors can do this. The challenge is to produce delighted and loyal customers.[55]

Companies seeking to expand their profits and sales have to spend considerable time and resources searching for new customers. To generate leads, the company develops ads and places them in media that will reach new prospects; it sends direct mail and makes phone calls to possible new prospects; its salespeople participate in trade shows where they might find new leads; it purchases names from list brokers; and so on. All this activity produces a list of suspects. *Suspects* are people or organizations who might conceivably have an interest in buying the company's product or service, but may not have the means or real intention to buy. The next task is to identify which suspects are really good *prospects*—customers with the motivation, ability, and opportunity to make a purchase—by interviewing them, checking on their financial standing, and so on. Then it is time to send out the salespeople.

It is not enough, however, to attract new customers; the company must keep them and increase their business. Too many companies suffer from high **customer churn**—high customer defection. It is like adding water to a leaking bucket. Cellular carriers, for example, are plagued with "spinners," customers who switch carriers at least three times a year looking for the best deal. Many lose 25 percent of their subscribers each year at an estimated cost of $2 billion to $4 billion. Unfortunately, much marketing theory and practice centers on the art of attracting new customers, rather than on retaining and cultivating existing ones. The emphasis traditionally has been on making sales rather than building relationships; on preselling and selling rather than caring for the customer afterward.

There are two main ways to strengthen customer retention. One is to erect high switching barriers. Customers are less inclined to switch to another supplier when this would involve high capital costs, high search costs, or the loss of loyal-customer discounts. The better approach is to deliver high customer satisfaction. This makes it harder for competitors to offer lower prices or inducements to switch.

Some companies think they are getting a sense of customer satisfaction by tallying complaints, but 96 percent of dissatisfied customers don't complain; they just stop buying.[56] The best thing a company can do is to make it easy for the customer to complain. Suggestion forms, toll-free numbers, Web sites, and e-mail addresses allow for quick, two-way communication. The 3M Company claims that over two-thirds of its product improvement ideas come from listening to customer complaints.

Listening is not enough, however; the company must respond quickly and constructively to any complaint (see "Marketing Memo: How to Handle Customer Complaints"):

> Of the customers who register a complaint, between 54 and 70% will do business again with the organization if their complaint is resolved. The figure goes up to a staggering

MARKETING MEMO | HOW TO HANDLE CUSTOMER COMPLAINTS

No matter how perfectly designed and implemented a marketing program is, mistakes will happen. Given the potential downside of having an unhappy customer, it is critical that the negative experience be dealt with properly. As with any marketing crisis large or small, swiftness and sincerity are the key watchwords. Customers must feel an immediate sense that the company truly cares. Beyond that, the following procedures can help to recover customer goodwill:

1. Set up a 7-day, 24-hour toll-free "hotline" (by phone, fax, or e-mail) to receive and act on customer complaints.
2. Contact the complaining customer as quickly as possible. The slower the company is to respond, the more dissatisfaction may grow and lead to negative word of mouth.
3. Accept responsibility for the customer's disappointment; don't blame the customer.
4. Use customer service people who are empathic.
5. Resolve the complaint swiftly and to the customer's satisfaction. Some complaining customers are not looking for compensation so much as a sign that the company cares.

Source: Philip Kotler, *Kotler on Marketing* (New York: The Free Press, 1999), pp. 21–22.

95% if the customer feels that the complaint was resolved quickly. Customers who have complained to an organization and had their complaints satisfactorily resolved tell an average of five people about the good treatment they received.[57]

Dell Computer Corp. quickly yanked its corporate PC tech support out of India and placed it in a domestic call center when its U.S-based customers complained about the quality of help they received: rigid, "by-the-book" technicians who wasted their time wading through fixes they had already tried, problems with poor phone connections, and strongly accented English that was hard to understand.[58]

More companies now recognize the importance of satisfying and retaining customers. Satisfied customers constitute the company's *customer relationship capital*. If the company were to be sold, the acquiring company would have to pay not only for the plant and equipment and the brand name, but also for the delivered *customer base*, the number and value of the customers who would do business with the new firm. Here are some interesting facts that bear on customer retention:[59]

1. Acquiring new customers can cost five times more than the costs involved in satisfying and retaining current customers. It requires a great deal of effort to induce satisfied customers to switch away from their current suppliers.
2. The average company loses 10 percent of its customers each year.
3. A 5 percent reduction in the customer defection rate can increase profits by 25 percent to 85 percent, depending on the industry.
4. The customer profit rate tends to increase over the life of the retained customer.

Figure 5.4 shows the main steps in the process of attracting and keeping customers. The starting point is everyone who might conceivably buy the product or service (*suspects*). From these the company determines the most likely *prospects*, which it hopes to convert into *first-time customers*, and then into *repeat customers*, and then into *clients*—people to whom the company gives very special and knowledgeable treatment. The next challenge is to turn clients into *members* by starting a membership program that offers benefits to customers who join, and then into *advocates*, customers who enthusiastically recommend the company and its products and services to others. The ultimate challenge is to turn advocates into *partners*.

Markets can be characterized by their long-term buying dynamics and how easily and often customers can enter and leave.[60]

1. ***Permanent capture markets.*** Once a customer, always a customer (e.g., nursing homes, trust funds, and medical care).
2. ***Simple retention markets.*** Customers can permanently be lost after each period (e.g., telecom, cable, financial services, other services, subscriptions).
3. ***Customer migration markets.*** Customers can leave and come back (e.g., catalogs, consumer products, retail, and airlines).

Some customers inevitably become inactive or drop out. The challenge is to reactivate dissatisfied customers through win-back strategies. It is often easier to re-attract ex-customers (because the company knows their names and histories) than to find new ones. The key is to analyze the causes of customer defection through exit interviews and lost-customer surveys. The aim is to win back only those customers who have strong profit potential.

Building Loyalty

How much should a company invest in building loyalty so that the costs do not exceed the gains? We need to distinguish five different levels of investment in customer relationship building:

1. ***Basic marketing.*** The salesperson simply sells the product.
2. ***Reactive marketing.*** The salesperson sells the product and encourages the customer to call if he or she has questions, comments, or complaints.
3. ***Accountable marketing.*** The salesperson phones the customer to check whether the product is meeting expectations. The salesperson also asks the customer for any product or service improvement suggestions and any specific disappointments.
4. ***Proactive marketing.*** The salesperson contacts the customer from time to time with suggestions about improved product uses or new products.
5. ***Partnership marketing.*** The company works continuously with its large customers to help improve their performance. (General Electric, for example, has stationed engineers at large utilities to help them produce more power.)

Most companies practice only basic marketing when their markets contain many customers and their unit profit margins are small. Whirlpool is not going to phone each washing machine buyer to express appreciation. It may set up a customer hot line. In markets with few customers and high profit margins, most sellers will move toward partnership marketing. Boeing, for example, works closely with American Airlines to design airplanes that fully satisfy American's requirements. As Figure 5.5 shows, the likely level of relationship marketing depends on the number of customers and the profit margin level.

An increasingly essential ingredient for the best relationship marketing today is the right technology. Table 5.2 highlights five imperatives of CRM and where technology fits in. GE Plastics could not target its e-mail effectively to different customers if it were not for advances in database software. Dell Computer could not customize computer ordering for its global corporate customers without advances in Web technology. Companies are using e-mail, Web sites, call centers, databases, and database software to foster continuous contact between company and customer. Here is how one company used technology to build customer value:

AMERITRADE

The discount brokerage service Ameritrade provides detailed information to its customers, which helps to create strong bonds. It provides customized alerts to the device of the customer's choice, detailing stock movements and analysts' recommendations. The company's Web site permits online trading and provides access to a variety of research tools. Ameritrade developed an investing tutorial called Darwin, which it offered free on CD-ROM to its customers. Customers responded to this new focus on their needs: Ameritrade grew from fewer than 100,000 accounts in 1997 to 2.9 million in 2003.[61]

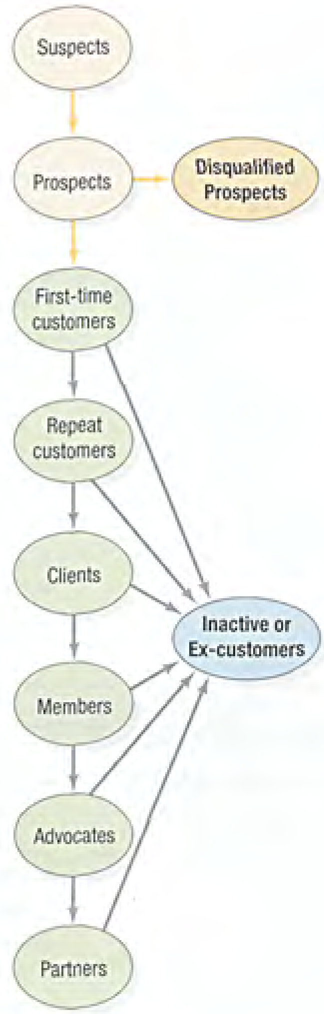


FIG. **5.4**

The Customer-Development Process

Source: See Jill Griffin, *Customer Loyalty: How to Earn It, How to Keep It* (New York: Lexington Books, 1995), p. 36. Also see Murray Raphel and Neil Raphel, *Up the Loyalty Ladder Turning Sometime Customers into Full-Time Advocates of Your Business* (New York: HarperBusiness, 1995).

	High Margin	Medium Margin	Low Margin
Many customers/ distributors	Accountable	Reactive	Basic or reactive
Medium number of customers/ distributors	Proactive	Accountable	Reactive
Few customers/ distributors	Partnership	Proactive	Accountable

FIG. **5.5**

Levels of Relationship Marketing

TABLE 5.2 Breaking Down Customer Relationship Management: What Customer Relationship Management Really Comprises

CRM Imperative				
Acquiring the right customer	Crafting the right value proposition	Instituting the best processes	Motivating employees	Learning to retain customers
You Get It When . . .				
■ You've identified your most valuable customers. ■ You've calculated your share of their wallet for your goods and services.	■ You've studied what products or services your customers need today and will need tomorrow. ■ You've surveyed what products or services your competitors offer today and will offer tomorrow. ■ You've spotted what products or services you should be offering.	■ You've researched the best way to deliver your products or services to customers, including the alliances you need to strike, the technologies you need to invest in, and the service capabilities you need to develop or acquire.	■ You know what tools your employees need to foster customer relationships. ■ You've identified the HR systems you need to institute in order to boost employee loyalty.	■ You've learned why customers defect and how to win them back. ■ You've analyzed what your competitors are doing to win your high-value customers. ■ Your senior management monitors customer defection metrics.
CRM Technology Can Help . . .				
■ Analyze customer revenue and cost data to identify current and future high-value customers. ■ Target your direct-marketing efforts better.	■ Capture relevant product and service behavior data. ■ Create new distribution channels. ■ Develop new pricing models. ■ Build communities.	■ Process transactions faster. ■ Provide better information to the front line. ■ Manage logistics and the supply chain more efficiently. ■ Catalyze collaborative commerce.	■ Align incentives and metrics. ■ Deploy knowledge management systems.	■ Track customer defection and retention levels. ■ Track customer service satisfaction levels.

Source: Darrel K. Rigby, Frederick F. Reichheld, and Phil Schefter, "Avoid the Four Perils of CRM," *Harvard Business Review* (February 2002): 106.

At the same time, online companies need to make sure their attempts to create relationships with customers don't backfire, as when customers are bombarded by computer-generated recommendations that consistently miss the mark. Buy a lot of baby gifts on Amazon, and your personalized recommendations suddenly don't look so personal. E-tailers need to recognize the limitations of online personalization at the same time that they try harder to find technology and processes that really work.[62]

Companies are also recognizing the importance of the personal component to CRM and what happens once customers make actual contact. As Stanford's business guru Jeffrey Pfeffer puts it, "the best companies build cultures in which front-line people are empowered to do what's needed to take care of the customer." He cites examples of firms like SAS, the Scandinavian airline, which engineered a turnaround in part based on the insight that a customer's impressions of a company are formed through a myriad of small interactions—checking in, boarding the plane, eating a meal, and so on.[63]

Reducing Customer Defection

There are five main steps a company can take to reduce the defection rate.

First, the company must define and measure its retention rate. For a magazine, the renewal rate is a good measure of retention. For a college, it could be the first- to second-year retention rate, or the class graduation rate.

Second, the company must distinguish the causes of customer attrition and identify those that can be managed better. (See "Marketing Memo: Asking Questions When Customers Leave.") The Forum Corporation analyzed the customers lost by 14 major companies for reasons other than leaving the region or going out of business: 15 percent switched because they found a better product; another 15 percent found a cheaper product; and 70 percent left because of poor or little attention from the supplier. Not much can be done about customers who leave the region or go out of business, but much can be done about those who leave because of poor service, shoddy products, or high prices.[64]

Third, the company needs to estimate how much profit it loses when it loses customers. In the case of an individual customer, the lost profit is equal to the customer's lifetime value—that is, the present value of the profit stream that the company would have realized if the customer had not defected prematurely—through some of the calculations outlined above.

Fourth, the company needs to figure out how much it would cost to reduce the defection rate. As long as the cost is less than the lost profit, the company should spend the money.

And finally, nothing beats listening to customers. Some companies have created an ongoing mechanism that keeps senior managers permanently plugged in to front-line customer feedback. MBNA, the credit card giant, asks every executive to listen in on telephone conversations in the customer service area or customer recovery units. Deere & Company, which makes John Deere tractors and has a superb record of customer loyalty—nearly 98 percent annual retention in some product areas—uses retired employees to interview defectors and customers.[65]

Forming Strong Customer Bonds

"Marketing Memo: Forming Strong Customer Bonds" offers some tips on connecting with customers. Berry and Parasuraman have identified three retention-building approaches:[66] adding financial benefits, adding social benefits, and adding structural ties.

ADDING FINANCIAL BENEFITS Two financial benefits that companies can offer are frequency programs and club marketing programs. **Frequency programs (FPs)** are designed to provide rewards to customers who buy frequently and in substantial amounts.[67] Frequency marketing is an acknowledgment of the fact that 20 percent of a company's customers might account for 80 percent of its business. Frequency programs are seen as a way to build long-term loyalty with these customers, potentially creating cross-selling opportunities in the process.

American Airlines was one of the first companies to pioneer a frequency program in the early 1980s, when it decided to offer free mileage credit to its customers. Hotels next adopted FPs, with Marriott taking the lead with its Honored Guest Program, followed by car rental firms. Then credit card companies began to offer points based on card usage level. Sears offers rebates to its Discover cardholders; and today most supermarket chains offer price club cards, which provide member customers with discounts on particular items.[68]

Typically, the first company to introduce an FP gains the most benefit, especially if competitors are slow to respond. After competitors respond, FPs can become a financial burden to all the offering companies, but some companies are more efficient and creative in

MARKETING MEMO | ASKING QUESTIONS WHEN CUSTOMERS LEAVE

To create effective retention programs, marketing managers need to identify customer defection patterns. This analysis should start with internal records, such as sales logs, pricing records, and customer survey results. The next step is to extend defection research to outside sources, such as benchmarking studies and statistics from trade associations. Some key questions to ask:

1. Do customers defect at different rates during the year?
2. Does retention vary by office, region, sales representative, or distributor?
3. What is the relationship between retention rates and changes in prices?
4. What happens to lost customers, and where do they usually go?
5. What are the retention norms for your industry?
6. Which company in your industry retains customers the longest?

Source: Reprinted from William A. Sherden, "When Customers Leave," *Small Business Reports* (November 1994): 45.

Pathmark Advantage Club cards: one for the wallet, one for the keyring.

managing FPs. For example, airlines run tiered loyalty programs in which they offer different levels of rewards to different travelers. They may offer one frequent-flier mile for every mile flown to occasional travelers and two frequent-flier miles for every mile flown to top customers.

Many companies have created club membership programs. Club membership can be open to everyone who purchases a product or service, or it can be limited to an affinity group or to those willing to pay a small fee. Although open clubs are good for building a database or snagging customers from competitors, limited membership clubs are more powerful long-term loyalty builders. Fees and membership conditions prevent those with only a fleeting interest in a company's products from joining. These clubs attract and keep

MARKETING MEMO | FORMING STRONG CUSTOMER BONDS

Companies that want to form strong customer bonds need to attend to the following basics:

- Get cross-departmental participation in planning and managing the customer satisfaction and retention process.
- Integrate the "Voice of the Customer" to capture their stated and unstated needs or requirements in all business decisions.
- Create superior products, services, and experiences for the target market.
- Organize and make accessible a database of information on individual customer needs, preferences, contacts, purchase frequency, and satisfaction.
- Make it easy for customers to reach appropriate company personnel and express their needs, perceptions, and complaints.
- Run award programs recognizing outstanding employees.

those customers who are responsible for the largest portion of business. Some highly successful clubs include the following:

APPLE

Apple encourages owners of its computers to form local Apple-user groups. By 2001, there were over 600 groups ranging in size from fewer than 25 members to over 1,000 members. The user groups provide Apple owners with opportunities to learn more about their computers, share ideas, and get product discounts. They sponsor special activities and events and perform community service. A visit to Apple's Web site will help a customer find a nearby user group.[69]

HARLEY-DAVIDSON

The world-famous motorcycle company sponsors the Harley Owners Group (H.O.G.), which now numbers 650,000 members in over 1,200 chapters. The first-time buyer of a Harley-Davidson motorcycle gets a free one-year membership. H.O.G. benefits include a magazine called *Hog Tales,* a touring handbook, emergency road service, a specially designed insurance program, theft reward service, discount hotel rates, and a Fly & Ride program enabling members to rent Harleys while on vacation. The company also maintains an extensive Web site devoted to H.O.G., which includes information on club chapters, events, and a special members-only section.[70]

ADDING SOCIAL BENEFITS Company personnel work on cementing social bonds with customers by individualizing and personalizing customer relationships. In essence, thoughtful companies turn their customers into clients. Donnelly, Berry, and Thompson draw this distinction:

> Customers may be nameless to the institution; clients cannot be nameless. Customers are served as part of the mass or as part of larger segments; clients are served on an individual basis. Customers are served by anyone who happens to be available; clients are served by the professional assigned to them.[71]

E-commerce companies looking to attract and retain customers are discovering that personalization goes beyond creating customized information.[72] For example, the Lands' End Live Web site offers visitors the opportunity to talk with a customer service representative. Nordstrom takes a similar approach with its Web site to ensure that online buyers are as satisfied with the company's customer service as the in-store visitors; and, with the click of a button, Eddie Bauer's e-commerce site connects shoppers to customer service representatives (CSRs) with a text-based chat feature.

A 2001 survey of 3,500 Web shoppers found that 77 percent of online shoppers have at least once selected an item for purchase but failed to complete the transaction.[73] Jupiter Media Metrix has reported that two-thirds of Web shoppers abandon shopping carts.[74] Worse, only 1.8 percent of visits to online retailers lead to sales, compared with 5 percent of visits to department stores. Analysts attribute this behavior partly to a general absence of interactive customer service in e-commerce. Customers looking for help are often sent to a text help file rather than a live sales representative. This can be frustrating and may prompt a customer to exit the site without buying. Another benefit of providing

Member of the Westsachsen, Germany, chapter of an H.O.G. club at a gathering in Hamburg to celebrate Harley-Davidson's 100th anniversary. Harley-Davidson uses its Web site to run one of the most successful club membership programs.

live sales assistance is the ability to sell additional items. When a representative is involved in the sale, the average amount per order is typically higher.

THE CONTAINER STORE

Dallas-based specialty chain The Container Store reaps the benefit of using live customer service personnel to augment its online orders. A Container Store representative speaks on the phone with each customer who submits an online request for custom closet planning. More importantly, phone calls don't end at the order initiation stage. An individual carefully reviews every Internet order before it is fulfilled. If it seems that certain parts of an order don't fit together, the customer representative calls to make sure that what is ordered is what the customer wants. In this way, The Container Store catches many mistakes that customers have made unknowingly long before orders are shipped. This both saves on returns and gives customers a more positive overall experience.[75]

Not all customer service features involve live personnel. Both Macys.com and gap.com offer prerecorded customer service information. Gap's Web site includes a "zoom" feature, which shoppers can use to get a close look at every detail of a garment, from elastic waistbands to fabric prints. Lands' End Live allows customers to "try on" clothes online using virtual models based on measurements supplied by customers.

ADDING STRUCTURAL TIES The company may supply customers with special equipment or computer links that help customers manage orders, payroll, and inventory. A good example is McKesson Corporation, a leading pharmaceutical wholesaler, which invested millions of dollars in EDI capabilities to help independent pharmacies manage inventory, order-entry processes, and shelf space. Another example is Milliken & Company, which provides proprietary software programs, marketing research, sales training, and sales leads to loyal customers.

Lester Wunderman, an astute observer of contemporary marketing, thinks talk about "loyalizing" customers misses the point.[76] People can be loyal to country, family, and beliefs, but less so to their toothpaste, soap, or even beer. The marketer's aim should be to increase the consumer's *proclivity to repurchase* the company's brand.

Here are his suggestions for creating structural ties with the customer:

1. ***Create long-term contracts.*** A newspaper subscription replaces the need to buy a newspaper each day. A 20-year mortgage replaces the need to re-borrow the money each year. A home heating oil agreement assures continuous delivery without renewing the order.
2. ***Charge a lower price to consumers who buy larger supplies.*** Offer lower prices to people who agree to be supplied regularly with a certain brand of toothpaste, detergent, or beer.
3. ***Turn the product into a long-term service.*** DaimlerChrysler could sell "miles of reliable transportation" instead of cars, with the consumer able to lease different cars at different times or for different occasions such as a station wagon for shopping and a convertible for the weekend. Gaines, the dog food company, could offer a Pet Care service that includes kennels, insurance, and veterinary care along with food.

::: Customer Databases and Database Marketing

Marketers must know their customers. And in order to know the customer, the company must collect information and store it in a database and do database marketing: A **customer database** is an organized collection of comprehensive information about individual customers or prospects that is current, accessible, and actionable for such marketing purposes as lead generation, lead qualification, sale of a product or service, or maintenance of customer relationships. **Database marketing** is the process of building, maintaining, and using customer databases and other databases (products, suppliers, resellers) for the purpose of contacting, transacting, and building customer relationships.

Customer Databases

As the former chief marketing officer of Amazon liked to point out, when you walk through the door at Macy's, the retailer has no idea who you are. When you log on to Amazon, however, you are greeted by name, presented a customized set of product purchase suggestions based on your past purchase choices, and offered an accompanying series of frank customer reviews. As you log off the site, you are also asked permission to be e-mailed special offers.[77]

Many companies confuse a customer mailing list with a customer database. A **customer mailing list** is simply a set of names, addresses, and telephone numbers. A customer database contains much more information, accumulated through customer transactions, registration information, telephone queries, cookies, and every customer contact.

Ideally, a customer database contains the consumer's past purchases, demographics (age, income, family members, birthdays), psychographics (activities, interests, and opinions), mediagraphics (preferred media), and other useful information. The catalog company Fingerhut possesses some 1,400 pieces of information about each of the 30 million households in its massive customer database.

Ideally, a **business database** would contain business customers' past purchases; past volumes, prices, and profits; buyer team member names (and ages, birthdays, hobbies, and favorite foods); status of current contracts; an estimate of the supplier's share of the customer's business; competitive suppliers; assessment of competitive strengths and weaknesses in selling and servicing the account; and relevant buying practices, patterns, and policies. For example, a Latin American unit of the Swiss pharmaceutical firm Novartis keeps data on 100,000 of Argentina's farmers, knows their crop protection chemical purchases, groups them by value, and treats each group differently.

Figure 5.6 displays a method for selectively gaining greater share of a customer's business, based on the presumption that the firm has gained a deep understanding of the customer.

Data Warehouses and Datamining

Savvy companies are capturing information every time a customer comes into contact with any of its departments. Touch points include a customer purchase, a customer-requested service call, an online query, or a mail-in rebate card. Banks and credit card companies, telephone companies, catalog marketers, and many other companies have a great deal of information about their customers, including not only addresses and phone numbers, but also their transactions and enhanced data on age, family size, income, and other demographic information.

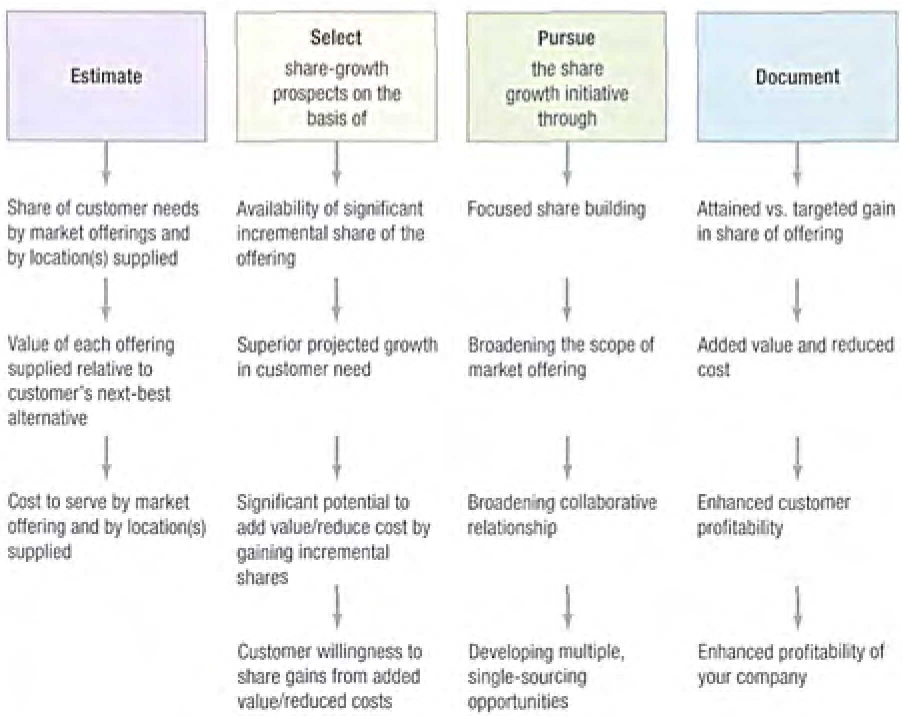


FIG. 5.6

Increasing Customer Share of Requirements

Source: James C. Anderson and James A. Narus, *MIT Sloan Management Review* (Spring 2003): 45.

These data are collected by the company's contact center and organized into a **data warehouse.** Company personnel can capture, query, and analyze the data. Inferences can be drawn about an individual customer's needs and responses. Telemarketers can respond to customer inquiries based on a total picture of the customer relationship.

Through **datamining,**[78] marketing statisticians can extract useful information about individuals, trends, and segments from the mass of data. Datamining involves the use of sophisticated statistical and mathematical techniques such as cluster analysis, automatic interaction detection, predictive modeling, and neural networking.[79]

Some observers believe that a proprietary database can provide a company with a significant competitive advantage. MCI Communications Corporation, the long-distance carrier, sifts through 1 trillion bytes of customer phoning data to craft new discount calling plans for different types of customers. Lands' End can tell which of its 2 million customers should receive special mailings of specific clothing items that would fit their wardrobe needs. (See Figure 5.7 for additional examples.)

USING THE DATABASE In general, companies can use their databases in five ways:

1. ***To identify prospects.*** Many companies generate sales leads by advertising their product or service. The ads generally contain a response feature, such as a business reply card or toll-free phone number. The database is built from these responses. The company sorts through the database to identify the best prospects, then contacts them by mail, phone, or personal call in an attempt to convert them into customers.
2. ***To decide which customers should receive a particular offer.*** Companies are interested in selling, up-selling, and cross-selling their products and services. Companies set up criteria describing the ideal target customer for a particular offer. Then they search their customer databases for those who most closely resemble the ideal type. By noting

FIG. 5.7

Examples of Database Marketing

Qwest Twice a year Qwest sifts through its customer list looking for customers that have the potential to be more profitable. The company's database contains as many as 200 observations about each customer's calling patterns. By looking at demographic profiles, plus the mix of local versus long-distance calls or whether a consumer has voice mail, Qwest can estimate potential spending. Next, the company determines how much of the customer's likely telecom budget is already coming its way. Armed with that knowledge, Qwest sets a cutoff point for how much to spend on marketing to this customer.

Royal Caribbean Royal Caribbean uses its database to offer spur-of-the-moment cruise packages to fill all the berths on its ships. It focuses on retired people and single people because they are more able to make quick commitments. Fewer empty berths mean maximized profits for the cruise line.

Fingerhut The skillful use of database marketing and relationship building has made catalog house Fingerhut one of the nation's largest direct-mail marketers. Not only is its database full of demographic details such as age, marital status, and number of children, but it also tracks customers' hobbies, interests, and birthdays. Fingerhut tailors mail offers based on what each customer is likely to buy. Fingerhut stays in continuous touch with customers through regular and special promotions, such as annual sweepstakes, free gifts, and deferred billing. Now the company has applied its database marketing to its Web sites.

Mars Mars is a market leader not only in candy, but also in pet food. In Germany, Mars has compiled the names of virtually every cat-owning family by contacting veterinarians and by advertising a free booklet titled "How to Take Care of Your Cat." Those who request the booklet fill out a questionnaire, so Mars knows the cat's name, age, and birthday. Mars now sends a birthday card to each cat each year, along with a new-cat-food sample or money-saving coupons for Mars brands.

American Express It is no wonder that, at its secret location in Phoenix, security guards watch over American Express's 500 billion bytes of data on how its customers have used the company's 35 million green, gold, and platinum charge cards. Amex uses the database to include precisely targeted offers in its monthly mailing of millions of customer bills.

response rates, a company can improve its targeting precision over time. Following a sale, it can set up an automatic sequence of activities: One week later, send a thank-you note; five weeks later, send a new offer; ten weeks later (if customer has not responded), phone the customer and offer a special discount.

3. ***To deepen customer loyalty.*** Companies can build interest and enthusiasm by remembering customer preferences; by sending appropriate gifts, discount coupons, and interesting reading material.
4. ***To reactivate customer purchases.*** Companies can install automatic mailing programs (automatic marketing) that send out birthday or anniversary cards, Christmas shopping reminders, or off-season promotions. The database can help the company make attractive or timely offers.
5. ***To avoid serious customer mistakes.*** A major bank confessed to a number of mistakes that it had made by not using its customer database well. In one case, the bank charged a customer a penalty for late payment on his mortgage, failing to note that he headed a company that was a major depositor in this bank. He quit the bank. In a second case, two different staff members of the bank phoned the same mortgage customer offering a home equity loan at different prices. Neither knew that the other had made the call. In a third case, a bank gave a premium customer only standard service in another country.

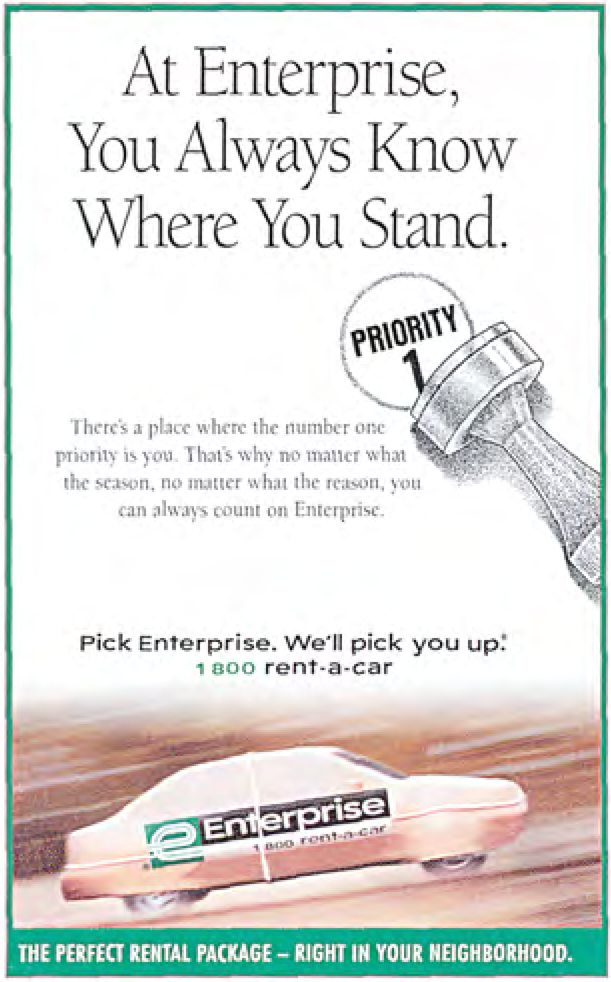
The Downside of Database Marketing and CRM

Having covered the good news about database marketing, we also have to cover the bad news. Four problems can deter a firm from effectively using CRM. The first is that building and maintaining a customer database requires a large investment in computer hardware, database software, analytical programs, communication links, and skilled personnel. It is difficult to collect the right data, especially to capture all the occasions of company interaction with individual customers. Building a customer database would not be worthwhile in the following cases: (1) where the product is a once-in-a-lifetime purchase (e.g., a grand piano); (2) where customers show little loyalty to a brand (i.e., there is lots of customer churn); (3) where the unit sale is very small (e.g., a candy bar); and (4) where the cost of gathering information is too high.

The second problem is the difficulty of getting everyone in the company to be customer-oriented and to use the available information. Employees find it far easier to carry on traditional transaction marketing than to practice customer relationship marketing. Effective database marketing requires managing and training employees as well as dealers and suppliers.

The third problem is that not all customers want a relationship with the company, and they may resent knowing that the company has collected that much personal information about them. Marketers must be concerned about customer attitudes toward privacy and security. American Express, long regarded as a leader on privacy issues, does not sell information on specific customer transactions. However, American Express found itself the target of consumer outrage when it announced a partnership with KnowledgeBase Marketing, Inc., that would have made data on 175 million Americans available to any merchant who accepts American Express cards. American Express killed the partnership. AOL, also targeted by privacy advocates, junked a plan to sell subscribers' telephone numbers. Online companies would be smart to explain their privacy policies, and give consumers the right not to have their information stored in a database. European countries do not look favorably upon database marketing. The European Union passed a law handicapping the growth of database marketing in its 15 member countries. Europeans are more protective of their private information than are U.S. citizens.

A fourth problem is that the assumptions behind CRM may not always hold true.[80] For example, it may not be the case that it costs less to serve more loyal customers. High-volume customers often know their value to a company and can leverage it to extract premium service and/or price discounts. Loyal customers may expect and demand more from the firm and resent any attempt by the firm to receive full or higher prices. They may also be jealous of attention lavished on other customers. When eBay began to chase big corporate customers such as IBM, Disney, and Sears, some small mom-and-pop businesses who helped to build the brand felt abandoned.[81] Loyal customers may not necessarily be the best ambassadors for the brand. One study found that customers who scored high on behavioral loyalty and bought a lot of a company' products were less active word-of-mouth



This Enterprise Rent-A-Car ad focuses on CRM: "There's a place where the number one priority is you."

marketers to others than customers who scored high on attitudinal loyalty and expressed greater commitment to the firm.

Thus, the benefits of database marketing do not come without heavy costs, not only in collecting the original customer data, but also in maintaining them and mining them. Yet, when it works, a data warehouse yields more than it costs. A 1996 study by DWI estimated that the average return on investment for a data warehouse over the course of three years is more than 400 percent, but the data have to be in good condition, and the discovered relationships must be valid. Consider the following cases were database marketing went awry:

CNA INSURANCE

At CNA Insurance, five programmers worked for nine months loading five years of claims data into a computer, only to discover that the data had been miscoded. Even if coded correctly, the data must be updated continuously because people move, drop out, or change their interests.

BRITISH COLUMBIA TELECOM

This company decided to invite 100 of its best customers to a Vancouver Grizzlies basketball game and selected customers who were heavy 900-number users. The invitations were already at the printer when the marketing staff discovered that heavy 900-number users included sex-line enthusiasts. They quickly added other criteria to search for a revised list of guests.

Database marketing is most frequently used by business marketers and service providers (hotels, banks, airlines; and insurance, credit card, and telephone companies) that normally and easily collect a lot of customer data. Other types of companies that are in the best position to invest in CRM are companies that do a lot of cross-selling and up-selling (e.g., GE and Amazon) or companies whose customers have highly differentiated needs and are of highly differentiated value to the company. It is used less often by packaged-goods retailers and consumer packaged-goods companies, though some companies (Kraft, Quaker Oats, Ralston Purina, and Nabisco) have built databases for certain brands. Businesses where the CLV is low, those who have high churn, and where there is no direct contact between the seller and ultimate buyer may not benefit as much from CRM. Some businesses cited as CRM successes include Enterprise Rent-A-Car, Pioneer Hi-bred Seeds, Fidelity Investments, Lexus, Intuit, and Capital One.[82]

Deloitte Consulting reported in 1999 that 70 percent of firms found little or no improvement through CRM implementation. The reasons are many: The system was poorly designed, it became too expensive, users didn't make much use of it or report much benefit, and collaborators ignored the system. One set of business commentators suggested the following as the four main perils of CRM:[83]

1. Implementing CRM before creating a customer strategy.
2. Rolling out CRM before changing organization to match.
3. Assuming more CRM technology is better.
4. Stalking, not wooing customers.

All this points to the need for each company to determine how much to invest in building and using database marketing to conduct its customer relationships. "Marketing Insight: Succeeding at CRM" provides some best-practice guidelines.

MARKETING **INSIGHT** | SUCCEEDING AT CRM

Based on a comprehensive survey of leading companies, Wharton's George Day concludes that superior CRM performance comes from integrating three components of the customer-relating capability: an organizational orientation that makes customer retention a priority and gives employees wide latitude to satisfy customers; information about relationships, including the quality of relevant customer data and the systems for sharing this information across the firm; and configuration, the alignment of the organization toward building customer relationships, achieved through incentives, metrics, organization structure, and accountabilities.

Configuration was the factor that most separated good firms from bad firms. Day observed that relatively few businesses in the survey emphasized customer satisfaction and retention in their incentives. An exception was Siebel Systems which tied 50 percent of management's incentive compensation and 25 percent of salespeople's compensation to measures of customer satisfaction. The real payoff, he notes, is when all the elements of a configuration—metrics, incentives, and structures—are properly aligned, citing General Electric Aircraft Engine Business Group's attempts to improve service for its jet engine customers. A study of customer needs led GE to assign a corporate vice president to each of the top 50 customers, putting leaders of its quality program on-site with customers, using the Internet to personalize delivery of parts, and incorporating customer service metrics into employee evaluation criteria.

Day also found that information was less important than orientation and configuration in distinguishing leaders from followers. He concluded that big investments in CRM technology were yielding negligible competitive advantages. He also concluded that one of the reasons many CRM failures occur is because companies concentrate on customer contact processes without making corresponding changes in internal structures and systems. His recommendation? Change the configuration before installing CRM: "Our survey results confirm that a superior customer relating capability has everything to do with how a business builds and manages its organization and not much to do with the CRM tools and technologies it employs."

Sources: George S. Day, "Creating a Superior Customer-Relating Capability," *Sloan Management Review* 44, no. 3 (2003): 77–82; George S. Day, "Creating a Superior Customer-Relating Capability," *MSI Report No. 03–101*, Marketing Science Institute, Cambridge, MA; "Why Some Companies Succeed at CRM (and Many Fail)," *Knowledge at Wharton*, http://knowledge.wharton.upenn.edu, January 15, 2003.

SUMMARY :::

1. Customers are value-maximizers. They form an expectation of value and act on it. Buyers will buy from the firm that they perceive to offer the highest customer-delivered value, defined as the difference between total customer value and total customer cost.
2. A buyer's satisfaction is a function of the product's perceived performance and the buyer's expectations. Recognizing that high satisfaction leads to high customer loyalty, many companies today are aiming for TCS—total customer satisfaction. For such companies,

customer satisfaction is both a goal and a marketing tool.

3. Losing profitable customers can dramatically affect a firm's profits. The cost of attracting a new customer is estimated to be five times the cost of keeping a current customer happy. The key to retaining customers is relationship marketing.
4. Quality is the totality of features and characteristics of a product or service that bear on its ability to satisfy stated or implied needs. Today's companies have no choice but to implement total quality management programs if they are to remain solvent and profitable.
5. Marketing managers have two responsibilities in a quality-centered company. First, they must participate in formulating strategies and policies designed to help the company win through total quality excellence. Second, they must deliver marketing quality alongside production quality.
6. Companies are also becoming skilled in Customer Relationship Management (CRM), which focuses on meeting the individual needs of valued customers. The skill requires building a customer database and doing datamining to detect trends, segments, and individual needs.

APPLICATIONS :::

Marketing Debate Online Versus Offline Privacy?

As more and more firms practice relationship marketing and develop customer databases, privacy issues are emerging as an important topic. Consumers and public interest groups are scrutinizing—and sometimes criticizing—the privacy policies of firms. Concerns are also being raised about potential theft of online credit card information or other potentially sensitive or confidential financial information. Others maintain that the online privacy fears are unfounded and that security issues are every bit as much a concern in the offline world. They argue that the opportunity to steal information exists virtually everywhere and that it is up to the consumer to protect his or her interests.

Take a position: (1) Privacy is a bigger issue in the online world than the offline world versus Privacy is no different online than offline. (2) Consumers on the whole receive more benefit than risk from marketers knowing their personal information.

Marketing Discussion

Consider the lifetime value of customers (CLV). Choose a business and show how you would go about developing a quantitative formulation that captures the concept. How would organizations change if they totally embraced the customer equity concept and maximized CLV?

MARKETING **SPOTLIGHT** DELL

"We have a tremendously clear business model," says Michael Dell. "There's no confusion about what the value proposition is, what the company offers, and why it's great for customers." Dell is now the number-one computer systems company.

Dell is extremely responsive. Buyers go on Dell's Web site and design their own computers. They give their payment authorization, which means that Dell receives the money in advance and can use the funds to pay for the supplies needed to build the computer. Because its computers are built-to-order, Dell carries an industry-leading four days of inventory. It takes delivery of components just minutes before they are needed. At its Austin, Texas, factories, a Dell System can in some cases be built, have the software installed, be tested, and be packed in eight hours. Dell's costs are lower, allowing it to price its computers lower than competitors' prices if it wishes.

Yet speed is only one part of the Dell equation. Service is the other. In fact, it was through veering away from its successful business model that Dell discovered the importance of customer service. In 1993, the company began trying to sell to retailers, mainly because everyone else was. Customers were disgruntled because of poor retail service. Dell ultimately abandoned the retail channel.

Most important, Michael Dell decided that "there would be more things we'd have to do besides build a PC." He knew his company had two kinds of customers, corporate and consumer. Whereas the consumer would buy mainly because of price, the corporate buyer needed a carefully developed relationship. Like most successful companies, Dell put the most resources into building relationships with its most profitable customers.

Corporate customers make up about 80 percent of Dell's business, and the company manages its corporate accounts with a top-notch sales team. Dell also installs custom software and keeps track of business customers' inventory for them. Through the use of Premier Dell.com, customized customer Web pages at the Dell site, the company has created a 24-hour order-entry system. Big customers can click on the site to see all kinds of information about their preferences and needs. The site can be accessed worldwide by any company subsidiary; and employees, not just purchasing agents, can use the Premier Dell.com to purchase computers according to an automated policy. "It's the ultimate network," Michael Dell says, "and a fabulous way for us to interact with our customers."

The normal practice of companies is to "build-to-stock." This is a guessing game that companies often lose by building too much or too little. In the auto industry, cars will sit unsold in dealers' lots for 60 days, tying up working capital. Why have auto and other companies not moved from the inefficient "build-to-stock" model of production to Dell's "build-to-order" model? Auto manufacturers have invited Michael Dell to speak to them on several occasions. The consensus seems to be that Dell works with 50 main suppliers to put together a $1,000 PC, but a car manufacturer may have to work with 900 suppliers to put together a $20,000 car. In addition to the technical challenge, the auto industry faces dealer and legislative hurdles.

Discussion Questions

1. What have been the key success factors for Dell?
2. Where is Dell vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should they be sure to do with its marketing?

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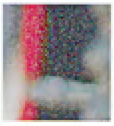


IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. How do consumer characteristics influence buying behavior?
2. What major psychological processes influence consumer responses to the marketing program?
3. How do consumers make purchasing decisions?
4. How do marketers analyze consumer decision making?

CHAPTER 6 ::: ANALYZING CONSUMER MARKETS

The aim of marketing is to meet and satisfy target customers' needs and wants better than competitors. **Consumer behavior** is the study of how individuals, groups, and organizations select, buy, use, and dispose of goods, services, ideas, or experiences to satisfy their needs and wants. Studying consumers provides clues for improving or introducing products or services, setting prices, devising channels, crafting messages, and developing other marketing activities. Marketers are always looking for emerging trends that suggest new marketing opportunities. The metrosexual is one:

In the summer of 2003, some marketing pundits proclaimed the existence of a new male market—the "metrosexual"—which was defined as straight urban men who enjoy such things as shopping and using grooming products and services. English soccer star David Beckham, with his carefully crafted fashion look, has been touted as the quintessential metrosexual icon. He's not afraid to wear either nail polish or sarongs (off the field, that is). One researcher estimated that 30 to 35 percent of young American men exhibited metrosexual tendencies, as evidenced in part by their purchase of products such as skin care cream and fragrances. Another study found "an emerging wave of men who chafe against the restrictions of traditional male roles and do what they want, buy what they want, enjoy what they want—regardless of whether some people might consider them unmanly." The emergence of this market has been a boon for >>>

British soccer star David Beckham is as well known for his style as he is for his playing.

men's grooming products, fueling the success of brands such as Unilever's Axe, a fragrant all-over body spray, The Body Shop's "For Men" line, and U.K. drugstore chain Boots' newly opened Men's Zones.[1]

Successful marketing requires that companies fully connect with their customers. Adopting a holistic marketing orientation means understanding consumers—gaining a 360-degree view of both their daily lives and the changes that occur during their lifetimes. Gaining a thorough, in-depth consumer understanding helps to ensure that the right products are marketed to the right consumers in the right way. This chapter explores individual consumer buying dynamics; the next chapter explores the buying dynamics of business buyers.

::: What Influences Consumer Behavior?

Marketers must fully understand both the theory and reality of consumer behavior. Table 6.1 includes some interesting facts about the American consumer in 2001, and "Marketing Insight: Consumer Trends for the Future" gives an idea of what marketers can expect to encounter in the year 2025.

A consumer's buying behavior is influenced by cultural, social, and personal factors. Cultural factors exert the broadest and deepest influence.

Cultural Factors

Culture, subculture, and social class are particularly important influences on consumer buying behavior. **Culture** is the fundamental determinant of a person's wants and behavior. The growing child acquires a set of values, perceptions, preferences, and behaviors through his or her family and other key institutions. A child growing up in the United States is exposed to the following values: achievement and success, activity, efficiency and practicality, progress, material comfort, individualism, freedom, external comfort, humanitarianism, and youthfulness.[2]

Each culture consists of smaller **subcultures** that provide more specific identification and socialization for their members. Subcultures include nationalities, religions, racial groups, and geographic regions. When subcultures grow large and affluent enough, companies often design specialized marketing programs to serve them. *Multicultural marketing* grew out of careful marketing research, which revealed that different ethnic and demographic niches did not always respond favorably to mass-market advertising.

Companies have capitalized on well-thought-out multicultural marketing strategies in recent years (see "Marketing Insight: Marketing to Cultural Market Segments"). For instance, many banks and life insurance companies are focusing on Hispanic Americans because although their income level is rising, the 40 million Hispanic Americans living in the United States have not yet become big consumers of financial services:

GE FINANCIAL

GE Financial has taken slow and careful steps to woo the Hispanic market. It spent more than two years researching and planning its Hispanic initiative, working closely with key people in the Hispanic community. It set up a Spanish-language call center, launched a Web site and tapped bilingual agents in key cities to sell GE products. It drafted financial commentator Julie Stav, a Latino personal finance guru, to make a series of information spots that run in English on GE's NBC station in Miami and in Spanish on Telemundo.[3]

TABLE 6.1

American Consumer Almanac

Personal Care

Amount spent per consumer unit on personal care products and services in 1999: **$408**

Food

Average annual expenditure on all food per household in 1999: **$5,031**

Number of eggs consumed per capita in 2000: **258**

Pounds of coffee (bean equivalent) consumed per capital 1999: **10**

Eating Out

Percentage of adults who eat out on a typical day: **44%**

Most popular month and day of the week to eat out: **August; Saturday**

Gum, Chocolate, and Candy

The average American chews **300** sticks of gum a year.

Wine (gallons per capita wine consumption)

France: **16.1** United States: **2.1**

Cars and Light Trucks

Median age of vehicles in operation in the U.S. in 2000: **Cars 8.3 years; Trucks 6.9 years**

Estimated percentage of U.S. households with three or more vehicles in 2000: **21%**

With 2 vehicles: **42%** With 1 vehicle: **31%** With no vehicles: **6%**

Travel and Lodging

Average annual number of trips per person of more than 100 miles: **3.9**

The number of nights the average traveler spends in a hotel, motel, or bed and breakfast annually: **3.3**

Leisure Time

Average number of times a U.S. adult goes out to a movie annually: **9**

Average number of times a U.S. adult attends a sporting event annually: **7**

Percentage of U.S. adults who visit an art museum, historical park, or monument or arts/crafts fair annually: **66%**

Consumer Electronics (percentage of household penetration)

VCR: **93%** Personal computer: **61%**

Wireless Phones

Percentage of U.S. drivers who usually have some type of wireless phone in their vehicle: **54%**

Percentage of U.S. households with cellular phones: **59%**

Of *those*, the percentage who report using their wireless phone while driving: **73%**

Virtually all human societies exhibit *social stratification*. Stratification sometimes takes the form of a caste system where the members of different castes are reared for certain roles and cannot change their caste membership. More frequently, it takes the form of **social classes**, relatively homogeneous and enduring divisions in a society, which are hierarchically ordered and whose members share similar values, interests, and behavior. One classic depiction of social classes in the United States defined seven ascending levels, as follows: (1) lower lowers, (2) upper lowers, (3) working class, (4) middle class, (5) upper middles, (6) lower uppers, and (7) upper uppers.[4]

Social classes have several characteristics. First, those within each class tend to behave more alike than persons from two different social classes. Social classes differ in dress, speech patterns, recreational preferences, and many other characteristics. Second, persons are perceived as occupying inferior or superior positions according to social class. Third,

MARKETING INSIGHT | CONSUMER TRENDS FOR THE FUTURE

What fundamental demographic trends will shape the consumer market over the next 25 years? To help answer that question, *American Demographics* teamed up with MapInfo, a Troy, New York–based market research firm, to create population projections to 2025. They found that the trends most likely to influence the business agendas of tomorrow are already gaining momentum today, and the smartest marketers have started developing strategies for the three largest and most likely demographic trends that will shape the marketplace of tomorrow:

America the Crowded

- More opportunity, more niche markets
- Environmental concerns moving front and center

By the year 2025, the U.S. population is expected to exceed 350 million people—an increase of about 70 million and a boost of 25 percent. Expect record-shattering growth to continue, as Americans live longer, birth rates hold steady, and immigration continues apace. However, this massive market does not herald a return to the mass market. As the population increases, niche markets may become unwieldy for businesses to target with a single marketing strategy. As a result, the niche market of today, such as Hispanic Americans, will become a mass market in its own right, segmented not only by nationality (i.e., Mexican, Guatemalan), but also by spending behavior and other psychographic characteristics. Of course, population growth will present some challenges. Natural resources will be stretched, so we can expect to see escalating conflicts at the local level over the use of land, water, and power. Products and services will be scrutinized more closely for their environmental impact.

The Mighty Mature Market

- The senior market gaining new allure
- Creating ageless, multigenerational brands

By 2025, as baby boomers age and life expectancy continues to increase, the number of seniors will double to more than 70 million people. The graying of America means that companies will have to do more than pay lip service to the idea of marketing to older people. Yet, businesses are not going to suddenly lose all interest in the 18 to 34 demographic. Instead, companies will have to learn to establish brands that attract older consumers without alienating younger ones. One example: A recent Pepsi commercial features a teenage boy in the middle of a mosh pit at a rock concert. He turns around to discover his father rocking out nearby. People at 50 aren't considered over the hill anymore. Smart marketers will capitalize on this knowledge and create the image of an ageless society where people define themselves more by the activities they're involved in than by their age. For instance, college students can be 20, 30, or 60 years old.

The Consumer Kaleidoscope

- Devising campaigns that appeal to many demographic segments
- Figuring out how to address the shrinking white majority

By 2025, the term "minority," as it's currently used, will be virtually obsolete. As the share of non-Hispanic whites falls to 60 percent from 70 percent today, the Hispanic population will almost double and the number of Asians in the United States will also double. As one executive at a trends consulting firm said, companies that have not yet developed a multicultural marketing strategy have to "wake up and smell the Thai tacos." Yet it's hard to know whether tomorrow's multicultural marketing strategies will continue to be segmented by race or whether an increasingly multicultural population prefers inclusive "fusion" strategies that attempt to encompass many different nationalities or racial identities in one campaign. Think Benetton and GAP for this latter strategy. To figure this out, companies will have to rely more heavily on ethnographic research. And yet, they can't ignore the dwindling white majority. If the current gap in wealth and income between white and nonwhite consumers holds for the next 25 years, businesses will have ample reason to target the nation's 210 million non-Hispanic white consumers.

Source: Adapted from Alison Stein Wellner, "The Next 25 Years," *American Demographics* (April 2003): 24–27.

social class is indicated by a cluster of variables—for example, occupation, income, wealth, education, and value orientation—rather than by any single variable. Fourth, individuals can move up or down the social-class ladder during their lifetimes. The extent of this mobility varies according to how rigid the social stratification is in a given society.

Social classes show distinct product and brand preferences in many areas, including clothing, home furnishings, leisure activities, and automobiles. Social classes differ in media preferences, with upper-class consumers often preferring magazines and books and lower-class consumers often preferring television. Even within a media category such as TV, upper-class consumers tend to prefer news and drama, and lower-class consumers tend to prefer soap operas and sports programs. There are also language differences among the social classes. Advertising copy and dialogue must ring true to the targeted social class.

Social Factors

In addition to cultural factors, a consumer's behavior is influenced by such social factors as reference groups, family, and social roles and statuses.

REFERENCE GROUPS A person's **reference groups** consist of all the groups that have a direct (face-to-face) or indirect influence on his/her attitudes or behavior. Groups having a direct influence on a person are called **membership groups**. Some membership groups are **primary groups**, such as family, friends, neighbors, and co-workers, those with whom the person interacts fairly continuously and informally. People also belong to **secondary groups**, such as religious, professional, and trade-union groups, which tend to be more formal and require less continuous interaction.

People are significantly influenced by their reference groups in at least three ways. Reference groups expose an individual to new behaviors and lifestyles, and influence attitudes and self-concept; they create pressures for conformity that may affect actual product and brand choices. People are also influenced by groups to which they do not belong. **Aspirational groups** are those a person hopes to join; **dissociative groups** are those whose values or behavior an individual rejects.

Manufacturers of products and brands where group influence is strong must determine how to reach and influence opinion leaders in these reference groups. An **opinion leader** is the person in informal, product-related communications who offers advice or information about a specific product or product category, such as which of several brands is best or how a particular product may be used.[5] Marketers try to reach opinion leaders by identifying demographic and psychographic characteristics associated with opinion leadership, identifying the media read by opinion leaders, and directing messages at opinion leaders.

NESTLÉ

Prior to the launch of its KitKat Kubes, a variant of the popular KitKat brand, Nestlé hired an agency to create a buzz among opinion leaders in the age 16 to 25 market. A database of about 20,000 was sent text messages and then this database was whittled down to 100 opinion leaders by a phone questionnaire. The opinion leaders were then sent a large box of KitKat Kubes. As one project manager at Nestlé Rowntree said: "It only takes 50 people to make a craze." But of course, it has to be the right fifty people.[6]

In Japan, high school girls have often been credited with creating the buzz that makes products such as Shiseido's Neuve nail polish a big hit.[7] In the United States, the hottest trends in teenage music, language, and fashion often start in the inner cities. Clothing companies like Hot Topic, which hope to appeal to the fickle and fashion-conscious youth market, have made a concerted effort to monitor urban opinion leaders' style and behavior.

HOT TOPIC

With 494 stores in malls in 49 states and Puerto Rico, Hot Topic has been hugely successful at using anti-establishment style in its fashions. Hot Topic's tagline, "everything about the music," reflects its operating premise: Music is the primary influence on teen fashion. Whether a teen is into rock, pop-punk, emo, acid rap, rave, or rockabilly—or even more obscure musical tastes—Hot Topic has the T-shirt for him or her. T-shirts featuring bands are the company's bread and butter. In order to keep up with music trends, all Hot Topic staffers, from the CEO to the lowliest store employee, regularly attend concerts by up-and-coming and established bands to scout who's wearing what. It's a perk for store clerks because they get reimbursed for concert tickets if they turn in a fashion write-up later. Hot Topic uses customer input too. Store managers keep comment cards near the till for shoppers to fill out. Hot Topic's Web site solicits e-mailed suggestions, and the CEO reads more than 1,000 customer comment cards and e-mails a month.[8]

FAMILY The family is the most important consumer buying organization in society, and family members constitute the most influential primary reference group.[9] We can distinguish between two families in the buyer's life. The **family of orientation** consists of parents and siblings. From parents a person acquires an orientation toward religion, politics, and economics, and a sense of personal ambition, self-worth, and love.[10] Even if the buyer no longer interacts very much with his or her parents, their influence on behavior can be significant. In countries where parents live with grown children, their influence can be substantial. A more direct influence on everyday buying behavior is the **family of procreation**—namely, one's spouse and children.

The makeup of the American family, however, has changed dramatically.[11] The U.S. Census Bureau's newest numbers show that married-couple households—the dominant

MARKETING INSIGHT | MARKETING TO CULTURAL MARKET SEGMENTS

Hispanic Americans

Expected to account for a quarter of the U.S. population by 2050, Hispanic Americans are the fastest-growing minority, and soon will be the largest minority in the country. Already with a population the same size as Canada, annual Hispanic American purchasing power in 2002 was $646 billion (total consumer spending by white Americans was $6.3 trillion). The Hispanic American segment can be difficult for marketers. Roughly two dozen nationalities can be classified as "Hispanic American," including Cuban, Mexican, Puerto Rican, Dominican, and other Central and South American groups. The Hispanic American group contains a mix of cultures, physical types, racial backgrounds, and aspirations.

Nickelodeon has been hugely successful in creating a "Pan-Latina" character, Dora the Explorer, that appeals to the increasing Hispanic preschool population in all these groups. The character is bilingual and the show displays aspects of many different Hispanic cultures. Dora's creators enlisted the help of a team of consultants with Latin American backgrounds. As a result, kids might see Dora up in the Andes or with a cocky, a frog that's an important part of Puerto Rican folklore. The research has paid off; the show is the most watched preschool show on commercial television, not only by Hispanic Americans but also by all preschoolers.

Yet despite their differences, Hispanic Americans often share strong family values, a need for respect, brand loyalty, and a strong interest in product quality. Marketers are reaching out to Hispanic Americans with targeted promotions, ads, or Web sites, but need to be careful to capture the nuances of cultural and market trends. For example, recognizing the fact that Hispanic consumers make twice as many trips to the grocery store per week and are less likely to eat out, Goya Foods has captured whole sections of large supermarkets, offering all the different goods Hispanic consumers might want. Other food companies have also introduced products targeting Hispanics, such as Frito-Lay with a lineup of spicy snacks sold in a rack emblazoned with the slogan "A Todo Sabor" (roughly, In Full Flavor).

African Americans

The purchasing power of the country's 34 million African Americans exploded during the prosperous 1990s. Based on survey findings, African Americans are the most fashion-conscious of all racial and ethnic groups. They also tend to be strongly motivated by quality and selection, and shop more at neighborhood stores. A telling testament to the growing power of African American consumers is their influence on white consumers, particularly those ages 12 to 34. Often fashion, dining, entertainment, sports, and music tastes emerge first from African American communities and make their way to the mainstream suburban mall. Think of rap- and hip-hop–inspired clothing, for instance.

Many companies have been successful at tailoring products to meet the needs of African Americans. In 1987, Hallmark Cards, Inc., launched its Afrocentric brand, Mahogany, with only 16 cards; it offers 800 cards today. Other companies offer more inclusive product lines within the same brand. Sara Lee Corporation's L'eggs discontinued its separate line of pantyhose for black women and now offers shades and styles popular among black women as half of the company's general-focus sub-brands. Finally, America's biggest packaged goods marketer, the Procter & Gamble Company, is teaming up its ad agencies specializing in campaigns aimed at African Americans with their general-market counterparts. By taking what used to be separate efforts through ethnic agencies and making them part of the company's core marketing effort, Procter & Gamble is moving the African American market from being largely an afterthought to being the name of the game.

Asian Americans

According to the U.S. Census Bureau, "Asian" refers to people having origins in any of the original peoples of the Far East, Southeast Asia, or the Indian subcontinent. Six countries represent 79 percent of the Asian U.S. population: China (21%), the Philippines (18%), India (11%), Vietnam (10%), Korea (10%), and Japan (9%).

Asian Americans tend to be more brand conscious than other minority groups, but yet are the least loyal to particular brands. Compared to other minority groups, they also tend to care more about what others think (e.g., whether their neighbors will approve). Asian Americans are the most wired and computer literate group too, and are more likely to use the Internet on a daily basis. Asian Americans often live with a larger extended family and may resonate to those types of depictions in advertising. Bank of America prospered by targeting Asians in San Francisco with separate TV campaigns aimed at Chinese, Korean, and Vietnamese consumers.

Sources: Rebecca Gardyn and John Fetto "The Way We Shop," *American Demographics* (February 2003): 33–34; Leon E. Wynter, "Business & Race: Hispanic Buying Habits Become More Diverse," *Wall Street Journal*, January 8, 1997, p. B1; Lisa A. Yorgey, "Hispanic Americans," *Target Marketing* (February 1998): 67; Carole Radice, "Hispanic Consumers: Understanding a Changing Market," *Progressive Grocer* (February 1997): 109–114; Alejandro Bianchi and Gabriel Sama, "Goya Foods Leads an Ethnic Sales Trend," *Wall Street Journal*, July 9, 2002, p. B2; Eduardo Porter and Betsy Mckay, "Frito-Lay Adds Spanish Accent to Snacks," *Wall Street Journal*, May 22, 2002, p. B3; Valerie Lynn Gray, "Going After Our Dollars," *Black Enterprise* (July 1997): 68–78; David Kiley, "Black Surfing," *Brandweek*, November 17, 1997, p. 36; Dana Canedy, "The Courtship of Black Consumers," *New York Times*, August 11, 1998, p. D1; Paula Lyon Andrus, "Mass Appeal: 'Dora' Translates Well," *Marketing News*, October 13, 2003, p. 8. Mindy Charski, "Old Navy to Tailor Message to Hispanics," *Adweek*, August 4, 2003, p. 9.

cohort since the country's founding—have slipped from nearly 80 percent in the 1950s to roughly 50 percent today. That means that the United States' 86 million single adults could soon define the new majority. Already, unmarrieds make up 42 percent of the workforce, 40 percent of homebuyers, 35 percent of voters, and one of the most powerful consumer groups on record. Marketers will have to pay attention not only to the buying habits of "singletons" who have delayed marriage, but also to families once considered on the fringe: cohabiting partners, divorced parents who share custody, single parents by choice, and same-sex couples who may or may not have children.

Marketers are interested in the roles and relative influence of family members in the purchase of a large variety of products and services. In the United States, husband–wife involvement has traditionally varied widely by product category. The wife has usually acted as the family's main purchasing agent, especially for food, sundries, and staple-clothing items. Now traditional purchasing roles are changing, and marketers would be wise to see both men and women as possible targets.

With expensive products and services like cars, vacations, or housing, the vast majority of husbands and wives engage in more joint decision making.[12] Given women's increasing wealth and income-generating ability, financial service firms such as Citigroup, Charles Schwab, and Merrill Lynch have expanded their efforts to attract women investors and business owners.[13] And marketers are realizing that men aren't the main buyers of high-tech gizmos and gadgets these days. Women actually buy more technology than men do, but consumer electronics stores have been slow to catch on to this fact. Some savvy electronics stores are starting to heed women's complaints of being ignored, patronized, or offended by salespeople. RadioShack Corp., a 7,000-store chain, began actively recruiting female store managers so that now a woman manages about one out of every seven stores.[14]

Nevertheless, men and women may respond differently to marketing messages.[15] One study showed that women valued connections and relationships with family and friends and placed a high priority on people. Men, on the other hand, related more to competition and placed a high priority on action. Marketers are taking more direct aim at women with new products such as Quaker's Nutrition for Women cereals and Crest Rejuvenating Effects toothpaste. Gillette Co. researched psychological issues specific to women and came out with an ergonomically designed razor, Venus, that fit more easily in a woman's hand. Sherwin-Williams recently designed a Dutch Boy easy-to-use "Twist and Pour" paint can targeted specifically at women.

Another shift in buying patterns is an increase in the amount of dollars spent and the direct and indirect influence wielded by children and teens.[16] Direct influence describes children's hints, requests, and demands—"I want to go to McDonald's." Direct influence of kids between the ages of 4 and 12 totaled around $275 billion in 1999. Their indirect influence on parental spending accounted for another $312 billion of household purchases.[17] Indirect influence means that parents know the brands, product choices, and preferences of their children without hints or outright requests. One research study showed that teenagers were playing a more active role than before in helping parents choose a car, audio/video equipment, or a vacation spot.[18]

Marketers use every possible channel of communication to reach kids, especially such popular media as Nickelodeon, Cartoon Network, or the Disney Channel on TV and magazines such as *Nickelodeon, Sports Illustrated for Kids*, and *Disney Adventures*.

DISNEY CHANNEL

After being considered an unprofitable stepchild of the Disney empire, the Disney Channel has become the company's cash cow solely from its ability to reach the underserved "tween market"—the 29 million 8 to 14-year-olds—and leverage its success through Disney's other divisions. In 2000, on the lookout for hip programming that would appeal to both tweens and their parents, the Disney Channel cast a then-obscure 12-year-old in the title role of a new weekly series, Lizzie McGuire. This sitcom about an everyday middle-schooler became a huge hit, and a year later Disney began running it on Saturday mornings on ABC, another Disney property. Then, in 2002, Disney unleashed a continuous stream of Lizzie spinoffs: Disney Press began publishing Lizzie books; its Buena Vista Music Group released the soundtrack for the series, which went platinum the following July; and Lizzie began airing every single day on the Disney Channel. That same year Disney's consumer products division began marketing everything from Lizzie dolls and sleeping bags to Lizzie pencils and notebooks. The Lizzie franchise has probably earned Disney about $100 million.[19]

Marketers are focusing more closely on women and their needs: This Dutch Boy "Twist and Pour" ad, which features a new, easy to use paint container, is targeted specifically at women.

The Lizzie McGuire juggernaut demonstrates how powerful television can be in reaching children, and marketers are using television to target children at younger ages than ever before. By the time children are around 2 years old, they can often recognize characters, logos, and specific brands. Marketers are tapping into that audience with product tie-ins, placed at a child's eye level, on just about everything—from Scooby Doo vitamins to Elmo juice and cookies.[20]

Today companies are also likely to use the Internet to show products to children and solicit marketing information from them. Millions of kids under the age of 17 are online. Marketers have jumped online with them, offering freebies in exchange for personal information. Many have come under fire for this practice and for not clearly differentiating ads from games or entertainment.

ROLES AND STATUSES A person participates in many groups—family, clubs, organizations. The person's position in each group can be defined in terms of role and status. A **role** consists of the activities a person is expected to perform. Each role carries a **status**. A senior vice president of marketing has more status than a sales manager, and a sales manager has more status than an office clerk. People choose products that reflect and communicate their role and actual or desired status in society. Company presidents often drive Mercedes, wear expensive suits, and drink expensive wines. Marketers must be aware of the status symbol potential of products and brands.

Personal Factors

A buyer's decisions are also influenced by personal characteristics. These include the buyer's age and stage in the life cycle; occupation and economic circumstances; personality and self-concept; and lifestyle and values. Because many of these characteristics have a very

MARKETING MEMO | THE AVERAGE AMERICAN CONSUMER QUIZ

Statements	Percent of consumers agreeing: % Men	Percent of consumers agreeing: % Women
1. A store's brand is usually a better buy than a nationally advertised brand.	______	______
2. I went fishing at least once in the past 12 months.	______	______
3. I am a homebody.	______	______
4. Information from advertising helps me make better buying decisions.	______	______
5. I like to pay cash for everything I buy.	______	______
6. A woman's place is in the home.	______	______
7. I am interested in spices and seasonings.	______	______
8. The father should be the boss in the house.	______	______
9. You have to use disinfectants to get things really clean.	______	______
10. I believe beings from other planets have visited Earth.	______	______

Note: Listed above are a series of statements that have been used in attitude surveys of American consumers. Only *married* U.S. men and women participated in these surveys. The people were selected because they were representative of a broad cross section of American consumers. The survey respondents were selected through a quota sample, balanced on age, income, geographical area, and population density. Consumers were asked whether they agreed or disagreed with each statement. For each statement, please estimate what percent of *married* American men and women agreed with each statement in 2004. Write a number between 0% and 100% in the columns to the right to indicate the percentage agreement. The correct answers can be found in the following footnote.*

* 1. M=57%, W=57%; 2. M=34%, W=24%; 3. M=64%, W=66%; 4. M=57%, W=61%; 5. M=60%, W=58%; 6. M=25%, W=23%; 7. M=70%, W=77%; 8. M=47%, W=29%; 9. M=58%, W=62%; 10. M=40%, W=35%. These numbers are based on DDB Life Style Study™. For an interesting application and analysis of the quiz, see Stephen J. Hoch, "Who Do We Know: Predicting the Interests and Opinions of the American Consumer," *Journal of Consumer Research*, 15 (December, 1998): 315–324.

direct impact on consumer behavior, it is important for marketers to follow them closely. See how well you do with "Marketing Memo: The Average American Consumer Quiz."

AGE AND STAGE IN THE LIFE CYCLE People buy different goods and services over a lifetime. Taste in food, clothes, furniture, and recreation is often age related. Consumption is also shaped by the *family life cycle* and the number, age, and gender of people in the household at any point in time. American households are increasingly fragmented—the traditional family of four with a husband, wife, and two kids makes up a much smaller percentage of total households than it once did. In addition, *psychological* life-cycle stages may matter. Adults experience certain "passages" or "transformations" as they go through life.[21]

Marketers should also consider *critical life events or transitions*—marriage, childbirth, illness, relocation, divorce, career change, widowhood—as giving rise to new needs. These should alert service providers—banks, lawyers, and marriage, employment, and bereavement counselors—to ways they can help.[22]

BANK OF AMERICA (BOA)

BOA is using "event-based triggers" to help its premier customers. BOA, using NCR's "Relationship Optimizer" solution, monitors large deposits, withdrawals, insufficient funds, and other events that deviate from a customer's normal behavior. Client managers are alerted to these events and phone the client to see if they can be of any assistance. For example, if a client has withdrawn a large sum of money to buy a home, the client manager offers to help the client find the best mortgage.

OCCUPATION AND ECONOMIC CIRCUMSTANCES Occupation also influences consumption patterns. A blue-collar worker will buy work clothes, work shoes, and lunchboxes. A company president will buy dress suits, air travel, and country club memberships. Marketers try to identify the occupational groups that have above-average interest in their products and services. A company can even tailor its products for certain occupational groups: Computer software companies, for example, design different products for brand managers, engineers, lawyers, and physicians.

Product choice is greatly affected by economic circumstances: spendable income (level, stability, and time pattern), savings and assets (including the percentage that is liquid), debts, borrowing power, and attitudes toward spending and saving. Luxury-goods makers such as Gucci, Prada, and Burberry can be vulnerable to an economic downturn. If economic indicators point to a recession, marketers can take steps to redesign, reposition, and reprice their products or introduce or increase the emphasis on discount brands so that they can continue to offer value to target customers.

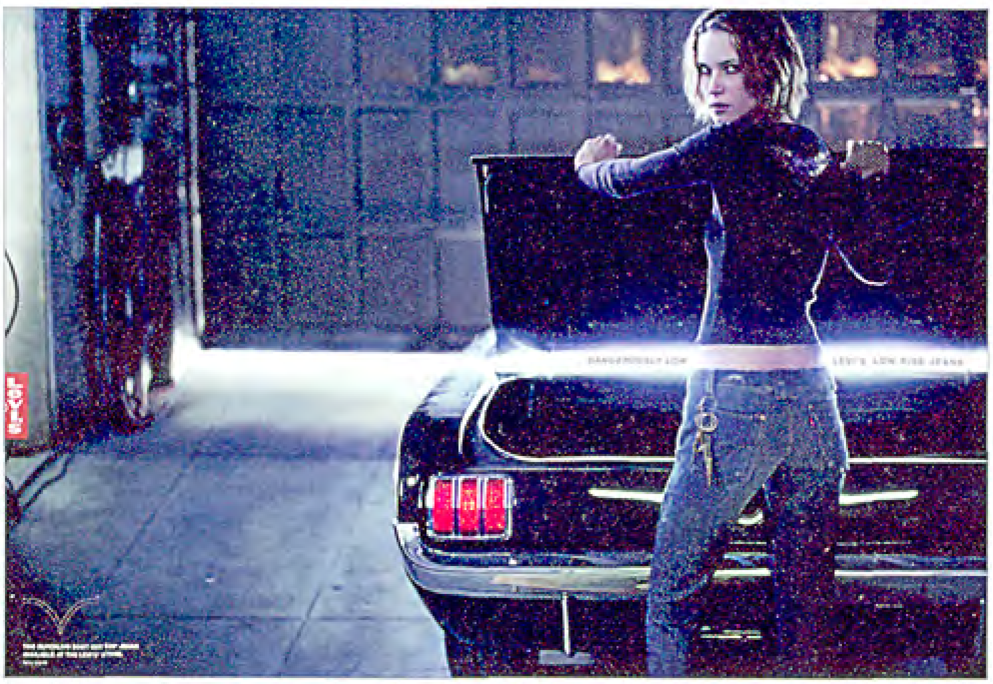
PERSONALITY AND SELF-CONCEPT Each person has personality characteristics that influence his or her buying behavior. By **personality**, we mean a set of distinguishing human psychological traits that lead to relatively consistent and enduring responses to environmental stimuli. Personality is often described in terms of such traits as self-confidence, dominance, autonomy, deference, sociability, defensiveness, and adaptability.[23] Personality can be a useful variable in analyzing consumer brand choices. The idea is that brands also have personalities, and consumers are likely to choose brands whose personalities match their own. We define **brand personality** as the specific mix of human traits that may be attributed to a particular brand.

Stanford's Jennifer Aaker conducted research into brand personalities and identified the following five traits:[24]

1. Sincerity (down-to-earth, honest, wholesome, and cheerful)
2. Excitement (daring, spirited, imaginative, and up-to-date)
3. Competence (reliable, intelligent, and successful)
4. Sophistication (upper-class and charming)
5. Ruggedness (outdoorsy and tough)

She proceeded to analyze some well-known brands and found that a number of them tended to be strong on one particular trait: Levi's with "ruggedness"; MTV with "excitement"; CNN with "competence"; and Campbell's with "sincerity." The implication is that these brands will attract persons who are high on the same personality traits. A brand personality may have several attributes: Levi's suggests a personality that is also youthful, rebellious, authentic, and American. The company utilizes product features, services, and image making to transmit the product's personality.

A Levi's ad expresses the brand personality: youthful, rebellious, authentic, American.



Consumers often choose and use brands that have a brand personality consistent with their own *actual self-concept* (how one views oneself), although in some cases the match may be based on the consumer's *ideal self-concept* (how one would like to view oneself) or even *others' self-concept* (how one thinks others see one) rather than actual self-image.[25] These effects may also be more pronounced for publicly consumed products as compared to privately consumed goods.[26] On the other hand, consumers who are high "self-monitors"—that is, sensitive to how others see them—are more likely to choose brands whose personalities fit the consumption situation.[27]

LIFESTYLE AND VALUES People from the same subculture, social class, and occupation may lead quite different lifestyles. A **lifestyle** is a person's pattern of living in the world as expressed in activities, interests, and opinions. Lifestyle portrays the "whole person" interacting with his or her environment. Marketers search for relationships between their products and lifestyle groups. For example, a computer manufacturer might find that most computer buyers are achievement-oriented. The marketer may then aim the brand more clearly at the achiever lifestyle. Marketers are always uncovering new trends in consumer lifestyles. Here's an example of one of the latest lifestyle trends businesses are currently targeting:

LOHAS

Consumers who worry about the environment, want products to be produced in a sustainable way, and spend money to advance their personal development and potential have been named "LOHAS." The name is an acronym standing for *lifestyles of health and sustainability.* The market for LOHAS products encompasses things like organic foods, energy-efficient appliances and sonar panels, as well as alternative medicine, yoga tapes, and ecotourism. Taken together, they accounted for a $230 billion market in 2000. Rather than looking at discrete product categories like cars or organic foods, it is more important to look at the common factors linking these product groups—for example, at cars, or energy and household products that are perceived as better for the environment and society.[28]

Lifestyles are shaped partly by whether consumers are *money-constrained* or *time-constrained.* Companies aiming to serve money-constrained consumers will create lower-cost products and services. By appealing to the money-constrained, Wal-Mart has become the largest company in the world. Its "everyday low prices" have wrung tens of billions of dollars out of the retail supply chain, passing the larger part of savings along to shoppers with rock-bottom bargain prices.[29]

Consumers who experience time famine are prone to **multitasking**, that is, doing two or more things at the same time. They will phone or eat while driving, or bicycle to work to get exercise. They will also pay others to perform tasks because time is more important than money. They may prefer bagels to breakfast cereals because they are quicker. Companies aiming to serve them will create convenient products and services for this group. Much of the wireless revolution is fueled by the multitasking trend. Texas Instruments recently unveiled a product design called WANDA, short for Wireless Any Network Digital Assistant, that allows users to talk on a cell phone while Web browsing over Wi-fi while conducting business via Bluetooth.

In some categories, notably food processing, companies targeting time-constrained consumers need to be aware that these very same consumers seek the illusion that they are not operating within time constraints. The food processing industry has a name for those who seek both convenience and some involvement in the cooking process: the "convenience involvement segment."[30]

HAMBURGER HELPER

Launched in 1971 in response to tough economic times, the inexpensive pasta-and-powdered mix Hamburger Helper was designed to quickly and inexpensively stretch a pound of meat into a family meal. With an estimated 44 percent of evening meals prepared in under 30 minutes and strong competition from fast-food drive-through windows, restaurant deliveries, and precooked grocery store dishes, Hamburger Helper's days of prosperity might seem numbered. Market researchers found, however, that some consumers do not necessarily want the fastest microwaveable meal solution possible—they also want to feel good about how they prepare a meal. In fact, on average, they would prefer to use at least one pot or pan and 15 minutes of time. To remain attractive to the segment who want to spend less time in the kitchen without totally abandoning their traditional roles as family mealmakers, marketers of Hamburger Helper are always introducing new flavors to tap into the latest consumer taste trends.[31]

Consumer decisions are also influenced by **core values**, the belief systems that underlie consumer attitudes and behaviors. Core values go much deeper than behavior or attitude, and determine, at a basic level, people's choices and desires over the long term. Marketers who target consumers on the basis of their values believe that by appealing to people's inner selves, it is possible to influence their outer selves—their purchase behavior.

::: Key Psychological Processes

The starting point for understanding consumer behavior is the stimulus-response model shown in Figure 6.1. Marketing and environmental stimuli enter the consumer's consciousness. A set of psychological processes combine with certain consumer characteristics to result in decision processes and purchase decisions. The marketer's task is to understand what happens in the consumer's consciousness between the arrival of the outside marketing stimuli and the ultimate purchase decisions. Four key psychological processes—motivation, perception, learning, and memory—fundamentally influence consumer responses to the various marketing stimuli.

Motivation: Freud, Maslow, Herzberg

A person has many needs at any given time. Some needs are *biogenic;* they arise from physiological states of tension such as hunger, thirst, or discomfort. Other needs are *psychogenic;* they arise from psychological states of tension such as the need for recognition, esteem, or belonging. A need becomes a motive when it is aroused to a sufficient level of intensity. A **motive** is a need that is sufficiently pressing to drive the person to act.

Three of the best-known theories of human motivation—those of Sigmund Freud, Abraham Maslow, and Frederick Herzberg—carry quite different implications for consumer analysis and marketing strategy.

FREUD'S THEORY Sigmund Freud assumed that the psychological forces shaping people's behavior are largely unconscious, and that a person cannot fully understand his or her own motivations. When a person examines specific brands, he or she will react not only to their stated capabilities, but also to other, less conscious cues. Shape, size, weight, material, color, and brand name can all trigger certain associations and emotions. A technique called *laddering* can be used to trace a person's motivations from the stated instrumental ones to the more terminal ones. Then the marketer can decide at what level to develop the message and appeal.[32]

Motivation researchers often collect "in-depth interviews" with a few dozen consumers to uncover deeper motives triggered by a product. They use various *projective techniques* such as word association, sentence completion, picture interpretation, and role playing. Many of these techniques were pioneered by Ernest Dichter, a Viennese psychologist who settled in America.[33]

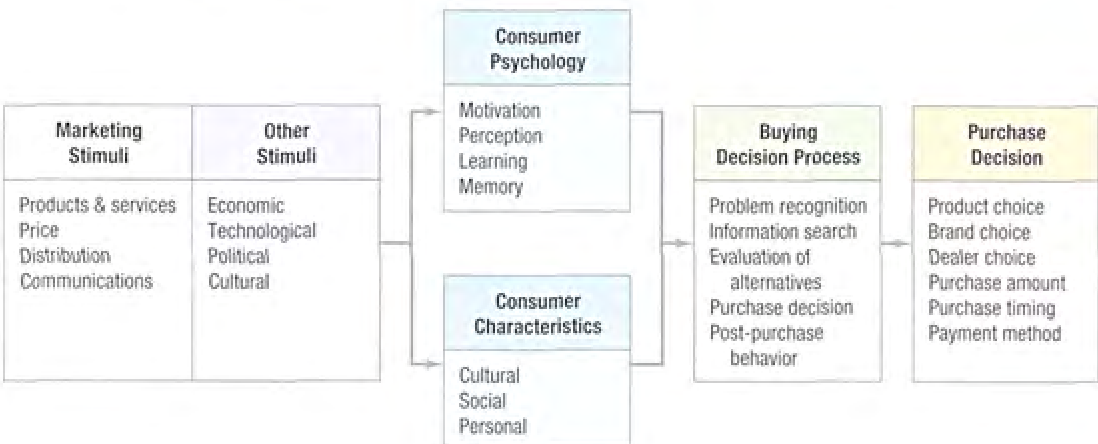


FIG. 6.1 Model of Consumer Behavior

Today motivational researchers continue the tradition of Freudian interpretation. Jan Callebaut identifies different motives a product can satisfy. For example, whisky can meet the need for social relaxation, status, or fun. Different whisky brands need to be motivationally positioned in one of these three appeals.[34] Another motivation researcher, Clotaire Rapaille, works on breaking the "code" behind a lot of product behavior. Research analyzing paper towels, according to Rapaille, revealed that its appeal to mothers is in how cleanliness plays into their instinctive desire to have their genes survive. "You are not just cleaning the table. You are saving the whole family," asserts the researcher.[35]

MASLOW'S THEORY Abraham Maslow sought to explain why people are driven by particular needs at particular times.[36] Why does one person spend considerable time and energy on personal safety and another on pursuing the high opinion of others? Maslow's answer is that human needs are arranged in a hierarchy, from the most pressing to the least pressing. In order of importance, they are physiological needs, safety needs, social needs, esteem needs, and self-actualization needs (see Figure 6.2). People will try to satisfy their most important needs first. When a person succeeds in satisfying an important need, he or she will then try to satisfy the next-most-important need. For example, a starving man (need 1) will not take an interest in the latest happenings in the art world (need 5), nor in how he is viewed by others (need 3 or 4), nor even in whether he is breathing clean air (need 2); but when he has enough food and water, the next-most-important need will become salient.

Maslow's theory helps marketers understand how various products fit into the plans, goals, and lives of consumers.

HERZBERG'S THEORY Frederick Herzberg developed a two-factor theory that distinguishes *dissatisfiers* (factors that cause dissatisfaction) and *satisfiers* (factors that cause satisfaction).[37] The absence of dissatisfiers is not enough; satisfiers must be present to motivate a purchase. For example, a computer that does not come with a warranty would be a dissatisfier. Yet the presence of a product warranty would not act as a satisfier or motivator of a purchase, because it is not a source of intrinsic satisfaction. Ease of use would be a satisfier.

Herzberg's theory has two implications. First, sellers should do their best to avoid dissatisfiers (for example, a poor training manual or a poor service policy). Although these things will not sell a product, they might easily unsell it. Second, the seller should identify the major satisfiers or motivators of purchase in the market and then supply them. These satisfiers will make the major difference as to which brand the customer buys.

Perception

A motivated person is ready to act. How the motivated person actually acts is influenced by his or her view or perception of the situation. **Perception** is the process by which an individual selects, organizes, and interprets information inputs to create a meaningful picture of

FIG. 6.2

Maslow's Hierarchy of Needs

Source: Motivation and Personality, 2nd ed., by A. H. Maslow, 1970. Reprinted by permission of Prentice Hall, Inc., Upper Saddle River, New Jersey.

the world.[38] Perception depends not only on the physical stimuli, but also on the stimuli's relation to the surrounding field and on conditions within the individual. The key point is that perceptions can vary widely among individuals exposed to the same reality. One person might perceive a fast-talking salesperson as aggressive and insincere; another, as intelligent and helpful. Each will respond differently to the salesperson.

In marketing, perceptions are more important than the reality, as it is perceptions that will affect consumers' actual behavior. People can emerge with different perceptions of the same object because of three perceptual processes: selective attention, selective distortion, and selective retention.

SELECTIVE ATTENTION It has been estimated that the average person may be exposed to over 1,500 ads or brand communications a day. Because a person cannot possibly attend to all of these, most stimuli will be screened out—a process called **selective attention**. Selective attention means that marketers have to work hard to attract consumers' notice. The real challenge is to explain which stimuli people will notice. Here are some findings:

1. ***People are more likely to notice stimuli that relate to a current need.*** A person who is motivated to buy a computer will notice computer ads; he or she will be less likely to notice DVD ads.
2. ***People are more likely to notice stimuli that they anticipate.*** You are more likely to notice computers than radios in a computer store because you do not expect the store to carry radios.
3. ***People are more likely to notice stimuli whose deviations are large in relation to the normal size of the stimuli.*** You are more likely to notice an ad offering $100 off the list price of a computer than one offering $5 off.

Although people screen out much of the surrounding stimuli, they are influenced by unexpected stimuli, such as sudden offers in the mail, over the phone, or from a salesperson. Marketers may attempt to promote their offers intrusively to bypass selective attention filters.

SELECTIVE DISTORTION Even noticed stimuli do not always come across in the way the senders intended. **Selective distortion** is the tendency to interpret information in a way that will fit our preconceptions. Consumers will often distort information to be consistent with prior brand and product beliefs.[39]

A stark demonstration of the power of consumer brand beliefs is the typical result of product sampling tests. In "blind" taste tests, one group of consumers samples a product without knowing which brand it is, whereas another group of consumers samples the product knowing which brand it is. Invariably, differences arise in the opinions of the two groups despite the fact that the two groups are *literally consuming exactly the same product*!

When consumers report different opinions between branded and unbranded versions of identical products, it must be the case that the brand and product beliefs, created by whatever means (e.g., past experiences, marketing activity for the brand, etc.), have somehow changed their product perceptions. Examples of branded differences can be found with virtually every type of product. For example, one study found that consumers were equally split in their preference for Diet Coke versus Diet Pepsi when tasting both on a blind basis.[40] When tasting the branded versions, however, consumers preferred Diet Coke by 65 percent and Diet Pepsi by only 23 percent (with the remainder seeing no difference).

Selective distortion can work to the advantage of marketers with strong brands when consumers distort neutral or ambiguous brand information to make it more positive. In other words, beer may seem to taste better, a car may seem to drive more smoothly, the wait in a bank line may seem shorter, and so on, depending on the particular brands involved.

SELECTIVE RETENTION People will fail to register much information to which they are exposed in memory, but will tend to retain information that supports their attitudes and beliefs. Because of **selective retention**, we are likely to remember good points about a product we like and forget good points about competing products. Selective retention again works to the advantage of strong brands. It also explains why marketers need to use repetition in sending messages to their target market—to make sure their message is not overlooked.

A Pepsi Challenge taste test in New York's Central Park. Companies like Pepsi often do taste tests of their products against other branded products to see if brand really makes a difference in customer preferences.

SUBLIMINAL PERCEPTION The selective perception mechanisms require active engagement and thought by consumers. A topic that has fascinated armchair marketers for ages is **subliminal perception.** The argument is that marketers embed covert, subliminal messages in ads or packages. Consumers are not consciously aware of these messages, but yet they affect their behavior. Although it is clear many subtle subconscious effects can exist with consumer processing,[41] no evidence supports the notion that marketers can systematically control consumers at that level.[42]

Learning

When people act, they learn. **Learning** involves changes in an individual's behavior arising from experience. Most human behavior is learned. Learning theorists believe that learning is produced through the interplay of drives, stimuli, cues, responses, and reinforcement.

A **drive** is a strong internal stimulus impelling action. **Cues** are minor stimuli that determine when, where, and how a person responds. Suppose you buy a Dell computer. If your experience is rewarding, your response to computers and Dell will be positively reinforced. Later on, when you want to buy a printer, you may assume that because Dell makes good computers, Dell also makes good printers. In other words, you *generalize* your response to similar stimuli. A countertendency to generalization is discrimination. **Discrimination** means that the person has learned to recognize differences in sets of similar stimuli and can adjust responses accordingly.

Learning theory teaches marketers that they can build demand for a product by associating it with strong drives, using motivating cues, and providing positive reinforcement. A new company can enter the market by appealing to the same drives that competitors use and by providing similar cue configurations, because buyers are more likely to transfer loyalty to similar brands (generalization); or the company might design its brand to appeal to a different set of drives and offer strong cue inducements to switch (discrimination).

Memory

All the information and experiences individuals encounter as they go through life can end up in their long-term memory. Cognitive psychologists distinguish between **short-term memory (STM)**—a temporary repository of information—and **long-term memory (LTM)**—a more permanent repository.

Most widely accepted views of long-term memory structure involve some kind of associative model formulation.[43] For example, the **associative network memory model** views LTM as consisting of a set of nodes and links. *Nodes* are stored information connected by *links* that vary in strength. Any type of information can be stored in the memory network, including information that is verbal, visual, abstract, or contextual. A spreading activation process from node to node determines the extent of retrieval and what information can actually be recalled in any given situation. When a node becomes activated because external information is being encoded (e.g., when a person reads or hears a word or phrase) or internal information is retrieved from LTM (e.g., when a person thinks about some concept), other nodes are also activated if they are sufficiently strongly associated with that node.

Consistent with the associative network memory model, consumer brand knowledge in memory can be conceptualized as consisting of a brand node in memory with a variety of linked associations. The strength and organization of these associations will be important determinants of the information that can be recalled about the brand. **Brand associations** consist of all brand-related thoughts, feelings, perceptions, images, experiences, beliefs, attitudes, and so on that become linked to the brand node.

Marketing can be seen as making sure that consumers have the right types of product and service experiences such that the right brand knowledge structures are created and maintained in memory.

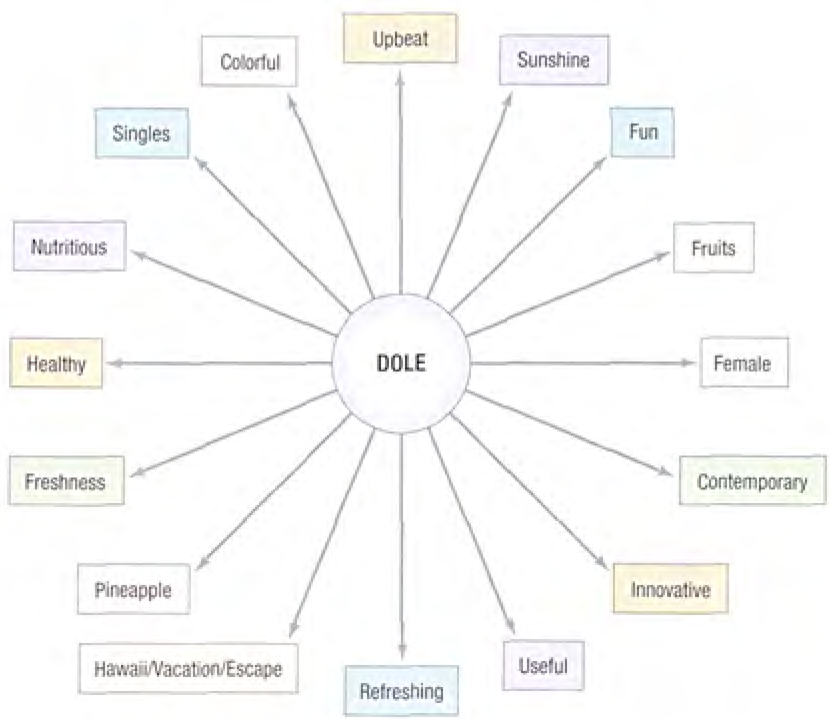
GODIVA CHOCOLATIER

Godiva Chocolatier's success is based on the appeal of emotional brand associations. In 1994, when the recession slowed sales of super premium goods, such as chocolates that sold for as much as $45 a pound, Godiva underwent a marketing makeover in its retail stores. The idea was to define, through store design, what the experience of eating chocolate felt like—sensual, indulgent, even sinful. In its multimillion-dollar redesign Godiva created elegant Art Noveau–style stores with bleached wood floors and wood and glass display cases. Customers were able to sample chocolates and find price lists instead of having to ask the salesperson the prices (which they might have found embarrassing). As redesigned "test" stores began to post significantly higher sales, Godiva rolled out the whole redesign and now the brand's associations of luxurious indulgence and sensuality have become ingrained in consumers' minds.[44]

Companies such as Procter & Gamble like to create mental maps of consumers that depict their knowledge of a particular brand in terms of the key associations that are likely to

FIG. 6.3

Hypothetical Dole Mental Map



be triggered in a marketing setting and their relative strength, favorability, and uniqueness to consumers. Figure 6.3 displays a very simple mental map highlighting brand beliefs for a hypothetical consumer for the Dole brand.

MEMORY PROCESSES: ENCODING **Memory encoding** refers to how and where information gets into memory. Memory encoding can be characterized according to the amount or quantity of processing that information receives at encoding (i.e., how much a person thinks about the information) and the nature or quality of processing that information receives at encoding (i.e., the manner in which a person thinks about the information). The quantity and quality of processing will be an important determinant of the strength of an association.[45]

In general, the more attention placed on the meaning of information during encoding, the stronger the resulting associations in memory will be.[46] When a consumer actively thinks about and "elaborates" on the significance of product or service information, stronger associations are created in memory. Another key determinant of the strength of a newly formed association will be the content, organization, and strength of existing brand associations in memory. It will be easier for consumers to create an association to new information when extensive, relevant knowledge structures already exist in memory. One reason why personal experiences create such strong brand associations is that information about the product is likely to be related to existing knowledge.

Consider the brand associations that might be created by a new TV ad campaign, employing a popular celebrity endorser, designed to create a new benefit association for a well-known brand. For example, assume Bruce Springsteen and his classic songs "Born in the USA" and "Born to Run" were jointly used to promote the "American heritage" and "Patriotic appeal" of New Balance athletic shoes, a Massachusetts-based company that

A Buick ad campaign features a popular celebrity endorser, the golfer Tiger Woods. Buick wants to appeal to younger drivers with a campaign designed to create a new benefit association for this well-known brand.

still manufactures in its local area. A number of different scenarios characterize how consumers might process such an ad:

1. Some consumers may barely notice the ads so that the amount of processing devoted to the ads is extremely low, resulting in weak to nonexistent brand associations.
2. The ads may catch the attention of other consumers, resulting in sufficient processing, but these consumers may devote most of the time during the ads thinking about the song and wondering why Springsteen decided to endorse New Balance (and whether he actually wore them), resulting in strong associations to Springsteen, but not to New Balance.
3. Another group of consumers may not only notice the ads but may think of how they had a wrong impression of New Balance and that it is "different" from the way they thought and that they would feel good about wearing the shoe. The endorsement by Springsteen in this case helped to transfer and create positive associations.

In addition to congruency or consistency with existing knowledge, the ease with which new information can be integrated into established knowledge structures clearly depends on the nature of that information, in terms of characteristics such as simplicity, vividness, and concreteness.

Repeated exposures to information provide greater opportunity for processing and thus the potential for stronger associations. Recent advertising research in a field setting, however, suggests that qualitative considerations and the manner or style of consumer processing engendered by an ad are generally more important than the cumulative total of ad exposures.[47] In other words, high levels of repetition for an uninvolving, unpersuasive ad is unlikely to have as much sales impact as lower levels of repetition for an involving, persuasive ad.

MEMORY PROCESSES: RETRIEVAL **Memory retrieval** refers to how information gets out of memory. According to the associative network memory model, the strength of a brand association increases both the likelihood that that information will be accessible and the ease with which it can be recalled by "spreading activation." Successful recall of brand information by consumers does not depend only on the initial strength of that information in memory. Three factors are particularly important.

First, the presence of *other* product information in memory can produce interference effects. It may cause the information to be either overlooked or confused. One challenge in a category crowded with many competitors—for example, airlines, financial services, and insurance companies—is that consumers may mix up brands.

TABLE 6.2

Understanding Consumer Behavior

Who buys our product or service?
Who makes the decision to buy the product?
Who influences the decision to buy the product?
How is the purchase decision made? Who assumes what role?
What does the customer buy? What needs must be satisfied?
Why do customers buy a particular brand?
Where do they go or look to buy the product or service?
When do they buy? Any seasonality factors?
How is our product perceived by customers?
What are customers' attitudes toward our product?
What social factors might influence the purchase decision?
Do customers' lifestyles influence their decisions?
How do personal or demographic factors influence the purchase decision?

Source: Based on list from George Belch and Michael Belch, *Advertising and Communication Management*, 6th ed. (Homewood, IL: Irwin, 2003).

Second, the time since exposure to information at encoding affects the strength of a new association—the longer the time delay, the weaker the association. The time elapsed since the last exposure opportunity, however, has been shown generally to produce only gradual decay. Cognitive psychologists believe that memory is extremely durable, so that once information becomes stored in memory, its strength of association decays very slowly.[48]

Third, information may be "available" in memory (i.e., potentially recallable) but may not be "accessible" (i.e., unable to be recalled) without the proper retrieval cues or reminders. The particular associations for a brand that "come to mind" depend on the context in which the brand is considered. The more cues linked to a piece of information, however, the greater the likelihood that the information can be recalled. The effectiveness of retrieval cues is one reason why marketing *inside* a supermarket or any retail store is so critical—in terms of the actual product packaging, the use of in-store mini-billboard displays, and so on. The information they contain and the reminders they provide of advertising or other information already conveyed outside the store will be prime determinants of consumer decision making.

FIG. 6.4

Five-Stage Model of the Consumer Buying Process

::: The Buying Decision Process: The Five-Stage Model

These basic psychological processes play an important role in understanding how consumers actually make their buying decisions. Marketers must understand every facet of consumer behavior. Table 6.2 provides a list of some key consumer behavior questions in terms of "who, what, when, where, how, and why." Smart companies try to fully understand the customers' buying decision process—all their experiences in learning, choosing, using, and even disposing of a product.[49]

Honda engineers took videos of shoppers loading groceries into car trunks to observe their frustrations and generate possible design solutions. Intuit, the maker of Quicken financial software, watched first-time buyers try to learn Quicken to sense their problems in learning how to use the product. Bissel developed its Steam n' Clean vacuum cleaner based on the product trial experiences of a local PTA group near corporate headquarters in Grand Rapids, Michigan. The result was a name change, color-coded attachments, and an infomercial highlighting its special features.[50]

Marketing scholars have developed a "stage model" of the buying decision process (see Figure 6.4). The consumer passes through five stages: problem recognition, information search, evaluation of alternatives, purchase decision, and postpurchase behavior. Clearly, the buying process starts long before the actual purchase and has consequences long afterward.[51]

But consumers do not always pass through all five stages in buying a product. They may skip or reverse some stages. A woman buying her regular brand of toothpaste goes directly from the need for toothpaste to the purchase decision, skipping information search and evaluation. The model in Figure 6.4 provides a good frame of reference, however, because it captures the full range of considerations that arise when a consumer faces a highly involving new purchase.[52]

Problem Recognition

The buying process starts when the buyer recognizes a problem or need. The need can be triggered by internal or external stimuli. With an internal stimulus, one of the person's normal needs—hunger, thirst, sex—rises to a threshold level and becomes a drive; or a need can be aroused by an external stimulus. A person may admire a neighbor's new car or see a television ad for a Hawaiian vacation, which triggers thoughts about the possibility of making a purchase. A believer in "retail theater," Krispy Kreme lights a neon "HOT NOW" sign to get attention—and purchase interest—each time a new batch of doughnuts is baked.

Marketers need to identify the circumstances that trigger a particular need by gathering information from a number of consumers. They can then develop marketing strategies that trigger consumer interest. This is particularly important with discretionary purchases such as luxury goods, vacation packages, and entertainment options. Consumer motivation may need to be increased so that a potential purchase is even given serious consideration.

Information Search

An aroused consumer will be inclined to search for more information. We can distinguish between two levels of arousal. The milder search state is called *heightened attention*. At this level a person simply becomes more receptive to information about a product. At the next

Triggering need: The "HOT NOW" sign is lit at this new Krispy Kreme store at Harrod's in London to signal the arrival of a batch of freshly baked doughnuts.

level, the person may enter an *active information search:* looking for reading material, phoning friends, going online, and visiting stores to learn about the product.

Of key interest to the marketer are the major information sources to which the consumer will turn and the relative influence each will have on the subsequent purchase decision. These information sources fall into four groups:

- ***Personal.*** Family, friends, neighbors, acquaintances
- ***Commercial.*** Advertising, Web sites, salespersons, dealers, packaging, displays
- ***Public.*** Mass media, consumer-rating organizations
- ***Experiential.*** Handling, examining, using the product

The relative amount and influence of these sources vary with the product category and the buyer's characteristics. Generally speaking, the consumer receives the most information about a product from commercial sources—that is, marketer-dominated sources. However, the most effective information often comes from personal sources or public sources that are independent authorities. More than 40 percent of all car shoppers consult *Consumer Reports,* making it the biggest single source of information.[53] Each information source performs a different function in influencing the buying decision. Commercial sources normally perform an information function, whereas personal sources perform a legitimizing or evaluation function. For example, physicians often learn of new drugs from commercial sources but turn to other doctors for evaluations.

The Internet has changed the process of information search. Today's marketplace is made up of traditional consumers (who do not shop online), cyber-consumers (who mostly shop online), and hybrid consumers (who do both).[54] Most consumers are hybrid: They shop in grocery stores but occasionally order from Peapod; they shop for books in Barnes & Noble bookstores but also sometimes order books from bn.com. People still like to squeeze the tomatoes, touch the fabric, smell the perfume, and interact with salespeople. They are motivated by more than shopping efficiency. Most companies will need a presence both offline and online to cater to these hybrid consumers.

ZAGAT

Based on the principle of organized word of mouth, husband and wife team Tim and Nina Zagat have recruited thousands of reviewers to rate restaurants in the world's top cities. These surveys were compiled into guidebooks that have sold millions. Now they have expanded their scope to include hotels, resorts, spas, and other services. Zagat's Web site has created an online community of reviewers, who are motivated in part by award prizes for the wittiest comments. Providing content online has actually helped sales of guidebooks offline. The New York guide has remained the number-one book sold in the city (with sales surpassing the Bible).[55]

Through gathering information, the consumer learns about competing brands and their features. The first box in Figure 6.5 shows the *total set* of brands available to the consumer. The individual consumer will come to know only a subset of these brands (*awareness set*). Some brands will meet initial buying criteria (*consideration set*). As the consumer gathers more information, only a few will remain as strong contenders (*choice set*). The consumer makes a final choice from this set.[56]

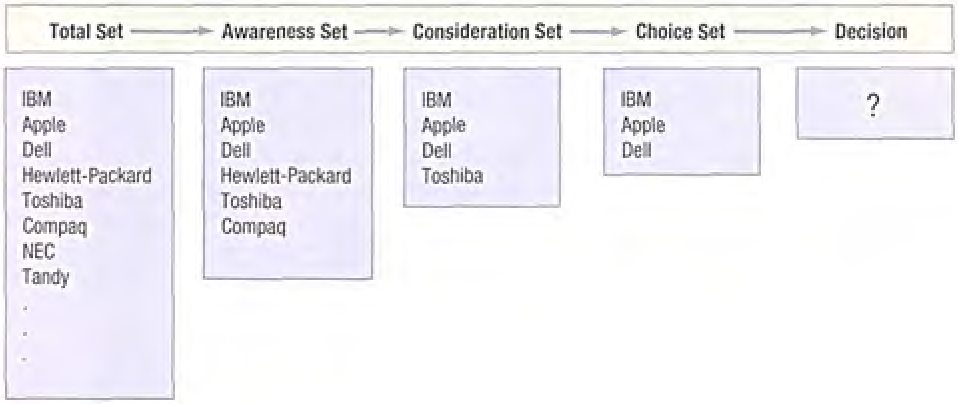


FIG. **6.5**

Successive Sets Involved in Consumer Decision Making

Figure 6.5 makes it clear that a company must strategize to get its brand into the prospect's awareness set, consideration set, and choice set. Food companies might work with supermarkets, for instance, in changing the way they display products. If a storeowner arranges yogurt first by brand (like Dannon and Yoplait) and then by flavor within each brand, consumers will tend to select their flavors from the same brand. However, if the products had been displayed with all the strawberry yogurts together, then all the vanilla yogurts and so forth, consumers would probably choose which flavors they wanted first, and then choose which brand name they would most like for that particular flavor. Australian supermarkets arrange meats by the way they might be cooked, and stores use more descriptive labels, like "a 10-minute herbed beef roast." The result is that Australians buy a greater variety of meats than Americans, who choose from meats laid out by animal type—beef, chicken, pork, and so on.[57]

The company must also identify the other brands in the consumer's choice set so that it can plan the appropriate competitive appeals. In addition, the company should identify the consumer's information sources and evaluate their relative importance. Consumers should be asked how they first heard about the brand, what information came later, and the relative importance of the different sources. The answers will help the company prepare effective communications for the target market.

Evaluation of Alternatives

How does the consumer process competitive brand information and make a final value judgment? No single process is used by all consumers or by one consumer in all buying situations. There are several processes, the most current models of which see the process as cognitively oriented. That is, they see the consumer as forming judgments largely on a conscious and rational basis.

Some basic concepts will help us understand consumer evaluation processes: First, the consumer is trying to satisfy a need. Second, the consumer is looking for certain benefits from the product solution. Third, the consumer sees each product as a bundle of attributes with varying abilities for delivering the benefits sought to satisfy this need. The attributes of interest to buyers vary by product—for example:

1. ***Cameras.*** Picture sharpness, camera speeds, camera size, price
2. ***Hotels.*** Location, cleanliness, atmosphere, price
3. ***Mouthwash.*** Color, effectiveness, germ-killing capacity, price, taste/flavor
4. ***Tires.*** Safety, tread life, ride quality, price

Consumers will pay the most attention to attributes that deliver the sought-after benefits. The market for a product can often be segmented according to attributes that are important to different consumer groups.

BELIEFS AND ATTITUDES Evaluations often reflect beliefs and attitudes. Through experience and learning, people acquire beliefs and attitudes. These in turn influence buying behavior. A **belief** is a descriptive thought that a person holds about something. People's beliefs about the attributes and benefits of a product or brand influence their buying decisions. Just as important as beliefs are attitudes. An **attitude** is a person's enduring favorable or unfavorable evaluation, emotional feeling, and action tendencies toward some object or idea.[58] People have attitudes toward almost everything: religion, politics, clothes, music, food.

Attitudes put people into a frame of mind: liking or disliking an object, moving toward or away from it. Attitudes lead people to behave in a fairly consistent way toward similar objects. Because attitudes economize on energy and thought, they can be very difficult to change. A company is well-advised to fit its product into existing attitudes rather than to try to change attitudes. Here is an example of an organization that used ad campaigns to remind consumers of their attitudes, with handsome results:

CALIFORNIA MILK PROCESSOR BOARD

After a 20-year decline in milk consumption among Californians, in 1993 milk processors from across the state formed the California Milk Processor Board (CMPB) with one goal in mind: to get people to drink more milk. The ad agency commissioned by the CMPB developed a novel approach to pitching milk's benefits. Research had shown that most consumers already believed milk was good for them. So the campaign would remind consumers of the inconvenience and annoyance of running out of milk, which became known as "milk deprivation." The "Got Milk?" tagline served to remind consumers to make sure they had milk in their refrigerators. In the year prior to the campaign's launch, California milk processors experienced a decline in sales volume of 1.67 percent. A year after the launch, sales volume increased 1.07 percent. In 1995, the "Got Milk?" campaign was licensed to the National Dairy Board. In 1998, the National Fluid Milk Processor Education Program, which had been using the "milk mustache" campaign since 1994 to boost sales, bought the rights to the "Got Milk?" tagline. The "Got Milk?" campaign continues to pay strong dividends. For 2002 and the first half of 2003, milk sales in California, where the ad campaign is centered, increased roughly 1.5 percent, whereas sales in the rest of the country remained flat.[59]

EXPECTANCY-VALUE MODEL The consumer arrives at attitudes (judgments, preferences) toward various brands through an attribute evaluation procedure.[60] He or she develops a set of beliefs about where each brand stands on each attribute. The **expectancy-value model** of attitude formation posits that consumers evaluate products and services by combining their brand beliefs—the positives and negatives—according to importance.

Suppose Linda Brown has narrowed her choice set to four laptop computers (A, B, C, D). Assume that she is interested in four attributes: memory capacity, graphics capability, size and weight, and price. Table 6.3 shows her beliefs about how each brand rates on the four attributes. If one computer dominated the others on all the criteria, we could predict that Linda would choose it. But, as is often the case, her choice set consists of brands that vary in their appeal. If Linda wants the best memory capacity, she should buy A; if she wants the best graphics capability, she should buy C; and so on.

TABLE 6.3

A Consumer's Brand Beliefs about Computers

Computer	Attribute			
	Memory Capacity	Graphics Capability	Size and Weight	Price
A	10	8	6	4
B	8	9	8	3
C	6	8	10	5
D	4	3	7	8

Note: Each attribute is rated from 0 to 10, where 10 represents the highest level on that attribute. Price, however, is indexed in a reverse manner, with a 10 representing the lowest price, because a consumer prefers a low price to a high price.

A "Got Milk" ad from the very successful campaign features Hong Kong star Zhang Ziyi from the film "Crouching Tiger, Hidden Dragon."

Most buyers consider several attributes in their purchase decision. If we knew the weights that Linda Brown attaches to the four attributes, we could more reliably predict her computer choice. Suppose Linda assigned 40 percent of the importance to the computer's memory capacity, 30 percent to graphics capability, 20 percent to size and weight, and 10 percent to price. To find Linda's perceived value for each computer, according to the expectancy-value model, we multiply her weights by her beliefs about each computer's attributes. This computation leads to the following perceived values:

$$\text{Computer A} = 0.4(8) + 0.3(9) + 0.2(6) + 0.1(9) = 8.0$$
$$\text{Computer B} = 0.4(7) + 0.3(7) + 0.2(7) + 0.1(7) = 7.0$$
$$\text{Computer C} = 0.4(10) + 0.3(4) + 0.2(3) + 0.1(2) = 6.0$$
$$\text{Computer D} = 0.4(5) + 0.3(3) + 0.2(8) + 0.1(5) = 5.0$$

An expectancy-model formulation would predict that Linda will favor computer A, which (at 8.0) has the highest perceived value.[61]

Suppose most computer buyers form their preferences the same way. Knowing this, a computer manufacturer can do a number of things to influence buyer decisions. The marketer of computer B, for example, could apply the following strategies to stimulate greater interest in brand B:

- ***Redesign the computer.*** This technique is called real repositioning.
- ***Alter beliefs about the brand.*** Attempting to alter beliefs about the brand is called psychological repositioning.
- ***Alter beliefs about competitors' brands.*** This strategy, called competitive depositioning, makes sense when buyers mistakenly believe a competitor's brand has more quality than it actually has.

MARKETING MEMO | APPLYING CUSTOMER VALUE ANALYSIS

A useful technique to gain consumer insight is customer value analysis. *Customer value analysis* assumes that customers choose between competitive brand offerings on the basis of which delivers the most customer value. Customer value is given by:

Customer Value = Customer Benefits − Customer Costs

Customer benefits include *product benefits, service benefits, personnel benefits,* and *image benefits.* Assume customers can judge the relative benefit level or worth of different brands. Suppose a customer is considering three brands, A, B, and C, and judges the customer benefits to be worth $150, $140, and $135, respectively. If the customer costs are the same, the customer would clearly choose brand A.

However, the costs are rarely the same. In addition to *purchase price,* costs include *acquisition costs, usage costs, maintenance costs, ownership costs,* and *disposal costs.* Often a customer will buy a more expensive brand because that particular brand will impose lower costs of other kinds. Consider Table 6.4. A, the highest-priced brand, also involves a lower total cost than lower-priced brands B and C. Clearly, supplier A has done a good job of reducing customers' other costs. Now we can compare the customer value of the three brands:

Customer value of A = $150 − $130 = $20

Customer value of B = $140 − $135 = $5

Customer value of C = $135 − $140 = −$5

The customer will prefer brand A both because the benefit level is higher and because the customer costs are lower, but this does not have to be the case. Suppose A decided to charge $120 instead of $100 to take advantage of its higher perceived benefit level. Then A's customer cost would have been $150 instead of $130 and just offset its higher perceived benefit. Brand A, because of its greed, would lose the sale to brand B.

Very often, managers conduct a **customer value analysis** to reveal the company's strengths and weaknesses relative to various competitors. The major steps in such an analysis are:

TABLE 6.4 | Customer Costs of Three Brands

	A	B	C
Price	$100	$ 90	$ 80
Acquisition costs	15	25	30
Usage costs	4	7	10
Maintenance costs	2	3	7
Ownership costs	3	3	5
Disposal costs	6	5	8
Total Cost	$130	$135	$140

1. ***Identify the major attributes customers value.*** Customers are asked what attributes and performance levels they look for in choosing a product and vendors.
2. ***Assess the quantitative importance of the different attributes.*** Customers are asked to rate the importance of the different attributes. If the customers diverge too much in their ratings, they should be clustered into different segments.
3. ***Assess the company's and competitors' performances on the different customer values against their rated importance.*** Customers describe where they see the company's and competitors' performances on each attribute.
4. ***Examine how customers in a specific segment rate the company's performance against a specific major competitor on an attribute-by-attribute basis.*** If the company's offer exceeds the competitor's offer on all important attributes, the company can charge a higher price (thereby earning higher profits), or it can charge the same price and gain more market share.
5. ***Monitor customer values over time.*** The company must periodically redo its studies of customer values and competitors' standings as the economy, technology, and features change.

- ***Alter the importance weights.*** The marketer could try to persuade buyers to attach more importance to the attributes in which the brand excels.
- ***Call attention to neglected attributes.*** The marketer could draw buyers' attention to neglected attributes, such as styling or processing speed.
- ***Shift the buyer's ideals.*** The marketer could try to persuade buyers to change their ideal levels for one or more attributes.[62]

"Marketing Memo: Applying Customer Value Analysis" describes a cost–benefit technique that provides additional insight into consumer decision making in a competitive setting.

Purchase Decisions

In the evaluation stage, the consumer forms preferences among the brands in the choice set. The consumer may also form an intention to buy the most preferred brand. In executing a purchase intention, the consumer may make up to five sub-decisions: *brand* (brand

A), *dealer* (dealer 2), *quantity* (one computer), *timing* (weekend), and *payment method* (credit card). Purchases of everyday products involve fewer decisions and less deliberation. For example, in buying sugar, a consumer gives little thought to vendor or payment method.

In some cases, consumers may decide not to formally evaluate each and every brand; in other cases, intervening factors may affect the final decision.

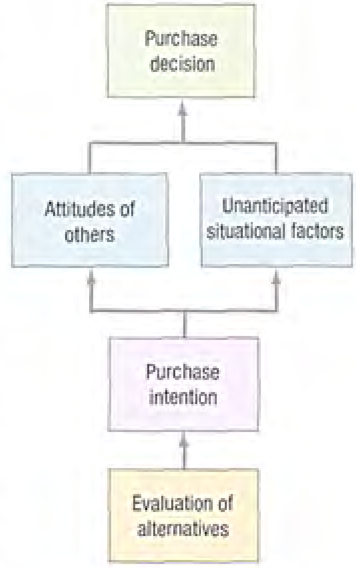


FIG. 6.6

Steps Between Evaluation of Alternatives and a Purchase Decision

NONCOMPENSATORY MODELS OF CONSUMER CHOICE The expectancy-value model is a compensatory model in that perceived good things for a product can help to overcome perceived bad things. But consumers may not want to invest so much time and energy to evaluate brands. They often take "mental shortcuts" that involve various simplifying *choice heuristics*.

With **noncompensatory models** of consumer choice, positive and negative attribute considerations do not necessarily net out. Evaluating attributes more in isolation makes decision making easier for a consumer, but also increases the likelihood that the person would have made a different choice if he or she had deliberated in greater detail. We highlight three such choice heuristics here.

1. With the **conjunctive heuristic**, the consumer sets a minimum acceptable cutoff level for each attribute and chooses the first alternative that meets the minimum standard for all attributes. For example, if Linda Brown decided that all attributes had to be rated at least a 7, she would choose computer B.
2. With the **lexicographic heuristic**, the consumer chooses the best brand on the basis of its perceived most important attribute. With this decision rule, Linda Brown would choose computer C.
3. With the **elimination-by-aspects heuristic**, the consumer compares brands on an attribute selected probabilistically—where the probability of choosing an attribute is positively related to its importance—and brands are eliminated if they do not meet minimum acceptable cutoff levels.

Characteristics of the person (e.g., brand or product knowledge), the purchase decision task and setting (e.g., number and similarity of brand choices and time pressure involved), and social context (e.g., need for justification to a peer or boss) all may affect if and how choice heuristics are used.[63]

Consumers do not necessarily adopt only one type of choice rule in making purchase decisions. In some cases, they adopt a phased decision strategy that combines two or more decision rules. For example, they might use a noncompensatory decision rule such as the conjunctive heuristic to reduce the number of brand choices to a more manageable number and then evaluate the remaining brands. Understanding if and how consumers screen brands can be critical. One reason for the runaway success of the Intel Inside campaign in the 1990s was that it made the brand the first cutoff for many consumers—they would only buy a PC which had an Intel microprocessor. PC makers such as IBM, Dell, and Gateway had no choice but to support Intel's marketing efforts.

INTERVENING FACTORS Even if consumers form brand evaluations, two general factors can intervene between the purchase intention and the purchase decision (Figure 6.6).[64] The first factor is the *attitudes of others*. The extent to which another person's attitude reduces the preference for an alternative depends on two things: (1) the intensity of the other person's negative attitude toward the consumer's preferred alternative and (2) the consumer's motivation to comply with the other person's wishes.[65] The more intense the other person's negativism and the closer the other person is to the consumer, the more the consumer will adjust his or her purchase intention. The converse is also true: A buyer's preference for a brand will increase if someone he or she respects favors the same brand strongly.

Related to the attitudes of others is the role played by infomediaries who publish their evaluations. Examples include *Consumer Reports*, which provides unbiased expert reviews of all types of products and services; J.D. Powers, which provides consumer-based ratings of cars, financial services, and travel products and services; professional movie, book, and music reviewers; customer reviews of books and music on Amazon.com; and the increasing number of chat rooms where people discuss products, services, and companies. Consumers are undoubtedly influenced by these evaluations, as evidenced by the success of a small-budget movie like *My Big Fat Greek Wedding*, which received a slew of favorable reviews by moviegoers on many Web sites.

The second factor is *unanticipated situational factors* that may erupt to change the purchase intention. Linda Brown might lose her job, some other purchase might become more urgent, or a store salesperson may turn her off. Preferences and even purchase intentions are not completely reliable predictors of purchase behavior.

A consumer's decision to modify, postpone, or avoid a purchase decision is heavily influenced by *perceived risk*.[66] There are many different types of risks that consumers may perceive in buying and consuming a product:

1. ***Functional risk*** – the product does not perform up to expectations.
2. ***Physical risk*** – the product poses a threat to the physical well-being or health of the user or others.
3. ***Financial risk*** – the product is not worth the price paid.
4. ***Social risk*** – the product results in embarrassment from others.
5. ***Psychological risk*** – the product affects the mental well-being of the user.
6. ***Time risk*** – the failure of the product results in an opportunity cost of finding another satisfactory product.

The amount of perceived risk varies with the amount of money at stake, the amount of attribute uncertainty, and the amount of consumer self-confidence. Consumers develop routines for reducing risk, such as decision avoidance, information gathering from friends, and preference for national brand names and warranties. Marketers must understand the factors that provoke a feeling of risk in consumers and provide information and support to reduce perceived risk.

Postpurchase Behavior

After the purchase, the consumer might experience dissonance that stems from noticing certain disquieting features or hearing favorable things about other brands, and will be alert to information that supports his or her decision. Marketing communications should supply beliefs and evaluations that reinforce the consumer's choice and help him or her feel good about the brand.

The marketer's job therefore does not end with the purchase. Marketers must monitor postpurchase satisfaction, postpurchase actions, and postpurchase product uses.

POSTPURCHASE SATISFACTION What determines customer satisfaction with a purchase? Satisfaction is a function of the closeness between expectations and the product's perceived performance.[67] If performance falls short of expectations, the consumer is *disappointed;* if it meets expectations, the consumer is *satisfied;* if it exceeds expectations, the consumer is *delighted.* These feelings make a difference in whether the customer buys the product again and talks favorably or unfavorably about it to others.

Consumers form their expectations on the basis of messages received from sellers, friends, and other information sources. The larger the gap between expectations and performance, the greater the dissatisfaction. Here the consumer's coping style comes into play. Some consumers magnify the gap when the product is not perfect, and they are highly dissatisfied; others minimize the gap and are less dissatisfied.[68]

The importance of postpurchase satisfaction suggests that product claims must truthfully represent the product's likely performance. Some sellers might even understate performance levels so that consumers experience higher-than-expected satisfaction with the product.

POSTPURCHASE ACTIONS Satisfaction or dissatisfaction with the product will influence subsequent behavior. If the consumer is satisfied, he or she will exhibit a higher probability of purchasing the product again. For example, data on automobile brand choice show a high correlation between being highly satisfied with the last brand bought and intention to buy the brand again. One survey showed that 75 percent of Toyota buyers were highly satisfied and about 75 percent intended to buy a Toyota again; 35 percent of Chevrolet buyers were highly satisfied and about 35 percent intended to buy a Chevrolet again. The satisfied customer will also tend to say good things about the brand to others. Marketers say: "Our best advertisement is a satisfied customer."[69]

Dissatisfied consumers may abandon or return the product. They may seek information that confirms its high value. They may take public action by complaining to the company, going to a lawyer, or complaining to other groups (such as business, private, or government

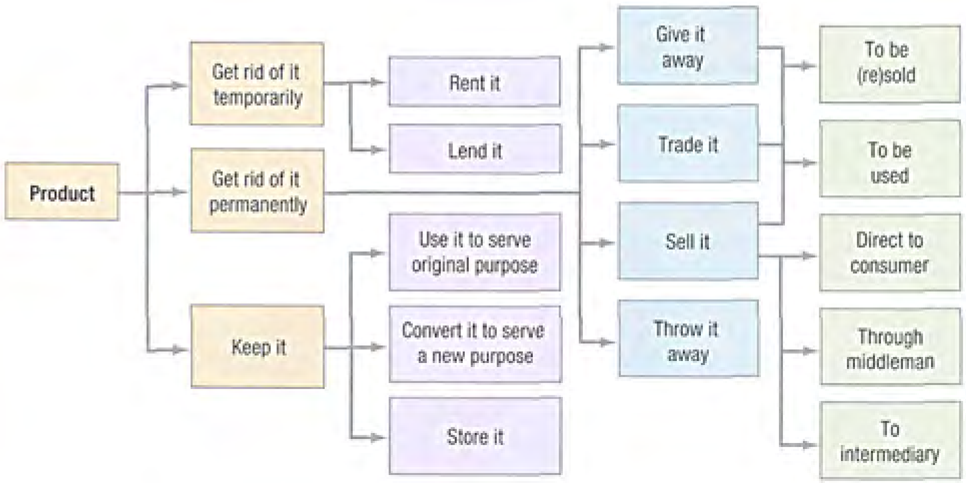


FIG. 6.7

How Customers Use or Dispose of Products

Source: From Jacob Jacoby, Carol K. Berning, and Thomas F. Dietvorst, "What about Disposition?" *Journal of Marketing* (July 1977): 23. Reprinted with permission of the American Marketing Association.

agencies). Private actions include making a decision to stop buying the product (*exit option*) or warning friends (*voice option*).[70] In all these cases, the seller has done a poor job of satisfying the customer.[71]

Chapter 5 described CRM programs designed to build long-term brand loyalty. Postpurchase communications to buyers have been shown to result in fewer product returns and order cancellations.[72] Computer companies, for example, can send a letter to new owners congratulating them on having selected a fine computer. They can place ads showing satisfied brand owners. They can solicit customer suggestions for improvements and list the location of available services. They can write intelligible instruction booklets. They can send owners a magazine containing articles describing new computer applications. In addition, they can provide good channels for speedy redress of customer grievances.

POSTPURCHASE USE AND DISPOSAL Marketers should also monitor how buyers use and dispose of the product (Figure 6.7). A key driver of sales frequency is product consumption rate—the more quickly buyers consume a product, the sooner they may be back in the market to repurchase it.

One potential opportunity to increase frequency of product use is when consumers' perceptions of their usage differ from the reality. Consumers may fail to replace products with relatively short life spans in a timely manner because of a tendency to underestimate product life.[73] One strategy to speed up replacement is to tie the act of replacing the product to a certain holiday, event, or time of year.

For example, several brands have run promotions tied in with the springtime switch to daylight savings time (e.g., Oral-B toothbrushes). Another strategy might be to provide consumers with better information as to either: (1) when the product was first used or would need to be replaced or (2) the current level of performance. For example, batteries offer built-in gauges that show how much power they have left; toothbrushes have color indicators on their bristles to indicate when they are too worn; and so on. Perhaps the simplest way to increase usage is when actual usage of a product is less than optimal or recommended. In this case, consumers must be persuaded of the merits of more regular usage, and potential hurdles to increased usage must be overcome.

If consumers throw the product away, the marketer needs to know how they dispose of it, especially if it can damage the environment (as in the case with batteries, beverage containers, and disposable diapers). Increased public awareness of recycling and ecological concerns as well as consumer complaints about having to throw away beautiful bottles led French perfume maker Rochas to think about introducing a refillable fragrance line.

::: Other Theories of Consumer Decision Making

The consumer decision process may not always develop in a carefully planned fashion. It is important to understand other theories and approaches to how consumers make decisions and when they might apply.

Level of Consumer Involvement

The expectancy-value model assumes a high level of involvement on the part of the consumer. **Consumer involvement** can be defined in terms of the level of engagement and active processing undertaken by the consumer in responding to a marketing stimulus (e.g., from viewing an ad or evaluating a product or service).

ELABORATION LIKELIHOOD MODEL Richard Petty and John Cacioppo's *elaboration likelihood model*, an influential model of attitude formation and change, describes how consumers make evaluations in both low- and high-involvement circumstances.[74] There are two means of persuasion with their model: The central route, where attitude formation or change involves much thought and is based on a diligent, rational consideration of the most important product or service information; and the peripheral route, where attitude formation or change involves comparatively much less thought and is a consequence of the association of a brand with either positive or negative peripheral cues. Examples of peripheral cues for consumers might be a celebrity endorsement, a credible source, or any object that engendered positive feelings.

Consumers follow the central route only if they possess sufficient *motivation, ability,* and *opportunity.* In other words, consumers must want to evaluate a brand in detail, must have the necessary brand and product or service knowledge in memory, and must be given sufficient time and the proper setting to actually do so. If any one of those three factors is lacking, consumers will tend to follow the peripheral route and consider less central, more extrinsic factors in their decisions.

LOW-INVOLVEMENT MARKETING STRATEGIES Many products are bought under conditions of low involvement and the absence of significant brand differences. Consider salt. Consumers have little involvement in this product category. They go to the store and reach for the brand. If they keep reaching for the same brand, it is out of habit, not strong brand loyalty. There is good evidence that consumers have low involvement with most low-cost, frequently purchased products.

Marketers use four techniques to try to convert a low-involvement product into one of higher involvement. First, they can link the product to some involving issue, as when Crest toothpaste is linked to avoiding cavities. Second, they can link the product to some involving personal situation—for example, fruit juice makers began to include vitamins such as calcium to fortify their drinks. Third, they might design advertising to trigger strong emotions related to personal values or ego defense, as when cereal makers began to advertise the heart-healthy nature of cereals to adults and the importance of living a long time to enjoy family life. Fourth, they might add an important feature—for example, when GE light bulbs introduced "Soft White" versions. These strategies at best raise consumer involvement from a low to a moderate level; they do not necessarily propel the consumer into highly involved buying behavior.

If, regardless of what the marketer can do, consumers will have low involvement with a purchase decision, they are likely to follow the peripheral route. Marketers must pay special attention to giving consumers one or more positive cues that they can use to justify their brand choice. Brand familiarity can be important if consumers decide to just buy the brand about which they have heard or seen the most. Frequent ad repetition, visible sponsorships, and vigorous PR are all ways to enhance brand familiarity. Other peripheral cues can also be used. A beloved celebrity endorser, attractive packaging, or an appealing promotion all might tip the balance in favor of the brand.[75]

VARIETY-SEEKING BUYING BEHAVIOR Some buying situations are characterized by low involvement but significant brand differences. Here consumers often do a lot of brand switching. Think about cookies. The consumer has some beliefs about cookies, chooses a brand of cookies without much evaluation, and evaluates the product during consumption. Next time, the consumer may reach for another brand out of a wish for a different taste. Brand switching occurs for the sake of variety rather than dissatisfaction.

The market leader and the minor brands in this product category have different marketing strategies. The market leader will try to encourage habitual buying behavior by dominating the shelf space with a variety of related but different product versions, avoiding out-of-stock conditions, and sponsoring frequent reminder advertising. Challenger firms will encourage variety seeking by offering lower prices, deals, coupons, free samples, and advertising that tries to break the consumer's purchase and consumption cycle and presents reasons for trying something new.

Converting a low-involvement product to a higher-involvement product: Kellogg's now advertises its products as "healthy heart cereals" to make consumers aware that which cereal you eat matters.

Decision Heuristics and Biases

As the low-involvement and noncompensatory model discussions suggest, consumers do not always process information or make decisions in a deliberate, rational manner. Behavioral decision theory is a thriving area in consumer research. Behavioral decision theorists have identified many different heuristics and biases in everyday consumer decision making. **Heuristics** are rules of thumb or mental shortcuts in the decision process.

Heuristics can come into play when consumers forecast the likelihood of future outcomes or events.[76]

1. The **availability heuristic**: Consumers base their predictions on the quickness and ease with which a particular example of an outcome comes to mind. If an example comes to mind too easily, consumers might overestimate the likelihood of the outcome or event happening. For example, a recent product failure may lead a consumer to inflate the likelihood of a future product failure and make him or her more inclined to purchase a product warranty.
2. The **representativeness heuristic**: Consumers base their predictions on how representative or similar the outcome is to other examples. One reason that package appearances may be so similar for different brands in the same product category is that they want to be seen as representative of the category as a whole.
3. The **anchoring and adjustment heuristic**: Consumers arrive at an initial judgment and then make adjustments of that first impression based on additional information. For services marketers, it is critical to make a strong first impression to establish a favorable anchor so that subsequent experiences are interpreted in a more favorable light.

MARKETING MEMO | DECISION TRAPS

In *Decision Traps,* Jay Russo and Paul Schoemaker reveal the 10 most common mistakes managers make in their decisions.

1. ***Plunging In***—Beginning to gather information and reach conclusions without taking a few minutes to think about the crux of the issue you're facing or to think through how you believe decisions like this one should be made.
2. ***Frame Blindness***—Setting out to solve the wrong problem because you've created a mental framework for your decision, with little thought, that causes you to overlook the best options or lose sight of important objectives.
3. ***Lack of Frame Control***—Failing to consciously define the problem in more ways than one or being unduly influenced by the frames of others.
4. ***Overconfidence in Your Judgment***—Failing to collect key factual information because you are too sure of your assumptions and opinions.
5. ***Shortsighted Shortcuts***—Relying inappropriately on "rules of thumb" such as implicitly trusting the most readily available information or anchoring too much on convenient facts.
6. ***Shooting from the Hip***—Believing you can keep straight in your head all the information you've discovered, and therefore "winging it" rather than following a systematic procedure when making the final choice.
7. ***Group Failure***—Assuming that with many smart people involved, good choices will follow automatically, and therefore failing to manage the group decision-making process.
8. ***Fooling Yourself About Feedback***—Failing to interpret the evidence from past outcomes for what it really says, either because you are protecting your ego or because you are tricked by hindsight effects.
9. ***Not Keeping Track***—Assuming that experience will make its lessons available automatically, and therefore failing to keep systematic records to track the results of your decisions and failing to analyze these results in ways that reveal their key lessons.
10. ***Failure to Audit Your Decision Process***—Failing to create an organized approach to understanding your own decision making, so you remain constantly exposed to all the other nine decision traps.

Sources: J. Edward Russo and Paul J. H. Schoemaker, *Decision Traps: Ten Barriers to Brilliant Decision-Making and How to Overcome Them* (New York: Doubleday, 1990); see also, J. Edward Russo and Paul J. H. Schoemaker, *Winning Decisions: Getting It Right the First Time* (New York: Doubleday, 2001).

Note that marketing managers also may use heuristics and be subject to biases in their decision making. "Marketing Memo: Decision Traps" reveals 10 common mistakes managers make in their decisions.

Mental Accounting

Researchers have found that consumers use mental accounting when they handle their money.[77] **Mental accounting** refers to the manner by which consumers code, categorize, and evaluate financial outcomes of choices. Formally, it has been defined in terms of, "The tendency to categorize *funds* or items of value even though there is no logical *basis* for the categorization, e.g., individuals often segregate their savings into separate accounts to meet different goals even though funds from any of the accounts can be applied to any of the goals."[78]

For example, assume you spend $50 to buy a ticket to see a concert.[79] As you arrive at the show, you realize you've lost your ticket. You may be unsure about purchasing another ticket for $50. Assume, on the other hand, that you realized you had lost $50 on the way to buy the ticket. You might be much more likely to go ahead and buy the ticket anyway. Although the amount lost in each case was the same—$50—the reactions were very different. In the first case, you may have mentally allocated $50 for going to a concert. Buying another ticket would therefore exceed your mental concert budget. In the second case, the money that was lost did not belong to any account, so the mental concert budget had not yet been exceeded.

According to Chicago's Richard Thaler, mental accounting is based on a set of key core principles:

1. Consumers tend to *segregate gains.* When a seller has a product with more than one positive dimension, it is desirable to have each dimension evaluated separately. Listing multiple benefits of a large industrial product, for example, can make the sum of the parts seem greater than the whole.
2. Consumers tend to *integrate losses.* Marketers have a distinct advantage in selling something if its cost can be added to another large purchase. House buyers are more inclined to view additional expenditures favorably given the high price of buying a house.

3. Consumers tend to *integrate smaller losses with larger gains*. The "cancellation" principle might explain why withholding taxes taken from monthly paychecks are less aversive than large, lump-sum tax payments—they are more likely to be absorbed by the larger pay amount.
4. Consumers tend to *segregate small gains from large losses*. The "silver lining" principle might explain the popularity of rebates on big-ticket purchases such as cars.

The principles of mental accounting are derived in part from prospect theory. **Prospect theory** maintains that consumers frame decision alternatives in terms of gains and losses according to a value function. Consumers are generally loss averse. They tend to overweight very low probabilities and underweight very high probabilities.

Profiling the Customer Buying Decision Process

How can marketers learn about the stages in the buying process for their product? They can think about how they themselves would act (*introspective method*). They can interview a small number of recent purchasers, asking them to recall the events leading to their purchase (*retrospective method*). They can locate consumers who plan to buy the product and ask them to think out loud about going through the buying process (*prospective method*); or they can ask consumers to describe the ideal way to buy the product (*prescriptive method*). Each method yields a picture of the steps in the process.

Trying to understand the customer's behavior in connection with a product has been called mapping the customer's *consumption system*,[80] *customer activity cycle*,[81] or *customer scenario*.[82] This can be done for such activity clusters as doing laundry, preparing for a wedding, or buying a car. Buying a car, for example, involves a whole cluster of activities, including choosing the car, financing the purchase, buying insurance, buying accessories, and so on.

SUMMARY :::

1. Consumer behavior is influenced by three factors: cultural (culture, subculture, and social class); social (reference groups, family, and social roles and statuses); and personal (age, stage in the life cycle, occupation, economic circumstances, lifestyle, personality, and self-concept). Research into all these factors can provide marketers with clues to reach and serve consumers more effectively.
2. Four main psychological processes affect consumer behavior: motivation, perception, learning, and memory.
3. To understand how consumers actually make buying decisions, marketers must identify who makes and has input into the buying decision; people can be initiators, influencers, deciders, buyers, or users. Different marketing campaigns might be targeted to each type of person.
4. The typical buying process consists of the following sequence of events: problem recognition, information search, evaluation of alternatives, purchase decision, and postpurchase behavior. The marketers' job is to understand the behavior at each stage. The attitudes of others, unanticipated situational factors, and perceived risk may all affect the decision to buy, as will consumers' levels of postpurchase satisfaction and postpurchase actions on the part of the company.

APPLICATIONS :::

Marketing Debate Is Target Marketing Ever Bad?

As marketers increasingly develop marketing programs tailored to certain target market segments, some critics have denounced these efforts as exploitative. For example, the preponderance of billboards advertising cigarettes, alcohol, and other vices in low-income urban areas is seen as taking advantage of a vulnerable market segment. Critics can be especially harsh in evaluating marketing programs that target African Americans and other minority groups, claiming that they often employ clichéd stereotypes and inappropriate depictions. Others counter with the point of view that targeting and positioning is critical to marketing and that these marketing programs are an attempt to be relevant to a certain consumer group.

Take a position: Targeting minorities is exploitative versus Targeting minorities is a sound business practice.

Marketing Discussion What Are Your Mental Accounts?

What mental accounts do you have in your mind about purchasing products or services? Do you have any rules you employ in spending money? Are they different from what other people do? Do you follow Thaler's four principles in reacting to gains and losses?

MARKETING SPOTLIGHT | DISNEY

The Walt Disney Company, a $27 billion-a-year global entertainment giant, recognizes what its customers value in the Disney brand: a fun experience and homespun entertainment based on old-fashioned family values. Disney responds to these consumer preferences by leveraging the brand across different consumer markets. Say a family goes to see a Disney movie together. They have a great time. They want to continue the experience. Disney Consumer Products, a division of the Walt Disney Company, lets them do just that through product lines aimed at specific age groups.

Take the 2004 *Home on the Range* movie. In addition to the movie, Disney created an accompanying soundtrack album, a line of toys and kids' clothing featuring the heroine, a theme park attraction, and a series of books. Similarly, Disney's 2003 *Pirates of the Caribbean* had a theme park ride, merchandising program, video game, TV series, and comic books. Disney's strategy is to build consumer segments around each of its characters, from classics like Mickey Mouse and Snow White to new hits like Kim Possible. Each brand is created for a special age group and distribution channel. Baby Mickey & Co. and Disney Babies both target infants, but the former is sold through department stores and specialty gift stores whereas the latter is a lower-priced option sold through mass-market channels. Disney's Mickey's Stuff for Kids targets boys and girls, while Mickey Unlimited targets teens and adults.

On TV, the Disney Channel is the top primetime destination for kids age 6 to 14, and Playhouse Disney is Disney's preschool programming targeting kids age 2 to 6. Other products, like Disney's co-branded Visa card, target adults. Cardholders earn one Disney "dollar" for every $100 charged to the card, up to $75,000 annually, then redeem the earnings for Disney merchandise or services, including Disney's theme parks and resorts, Disney Stores, Walt Disney Studios, and Disney stage productions. Disney is even in Home Depot, with a line of licensed kids'-room paint colors with paint swatches in the signature mouse-and-ears shape.

Disney also has licensed food products with character brand tie-ins. For example, Disney Yo-Pals Yogurt features Winnie the Pooh and Friends. The four-ounce yogurt cups are aimed at preschoolers and have an illustrated short story under each lid that encourages reading and discovery. Keebler Disney Holiday Magic Middles are vanilla sandwich cookies that have an individual image of Mickey, Donald Duck, and Goofy imprinted in each cookie.

The integration of all the consumer product lines can be seen with Disney's "Kim Possible" TV program. The series follows the action-adventures of a typical high school girl who, in her spare time, saves the world from evil villains. The number-one-rated cable program in its time slot has spawned a variety of merchandise offered by the seven Disney Consumer Products divisions. The merchandise includes:

- Disney Hardlines—stationery, lunchboxes, food products, room decor.
- Disney Softlines—sportswear, sleepwear, daywear, accessories.
- Disney Toys—action figures, wigglers, beanbags, plush, fashion dolls, poseables.
- Disney Publishing—diaries, junior novels, comic books.
- Walt Disney Records—Kim Possible soundtrack.
- Buena Vista Home Entertainment—DVD/video.
- Buena Vista Games—GameBoy Advance.

"The success of Kim Possible is driven by action-packed storylines which translate well into merchandise in many categories," said Andy Mooney, chairman, Disney Consumer Products Worldwide. Rich Ross, president of entertainment, Disney Channel, added: "Today's kids want a deeper experience with their favorite television characters, like Kim Possible. This line of products extends our viewers' experience with Kim, Rufus, Ron and other show characters, allowing [kids] to touch, see and live the Kim Possible experience.

Walt Disney created Mickey Mouse in 1928 (Walt wanted to call his creation Mortimer until his wife convinced him Mickey Mouse was better). Disney's first feature-length musical animation, Snow White and the Seven Dwarfs, debuted in 1937. Today, the pervasiveness of Disney product offerings is staggering—all in all, there are over 3 billion entertainment-based impressions of Mickey Mouse received by children every year. But as Walt Disney said: "I only hope that we don't lose sight of one thing—that it was all started by a mouse."

Discussion Questions

1. What have been the key success factors for Disney?
2. Where is Disney vulnerable? What should it watch out for?
3. What recommendations would you make to their senior marketing executives going forward? What should it be sure to do with its marketing?

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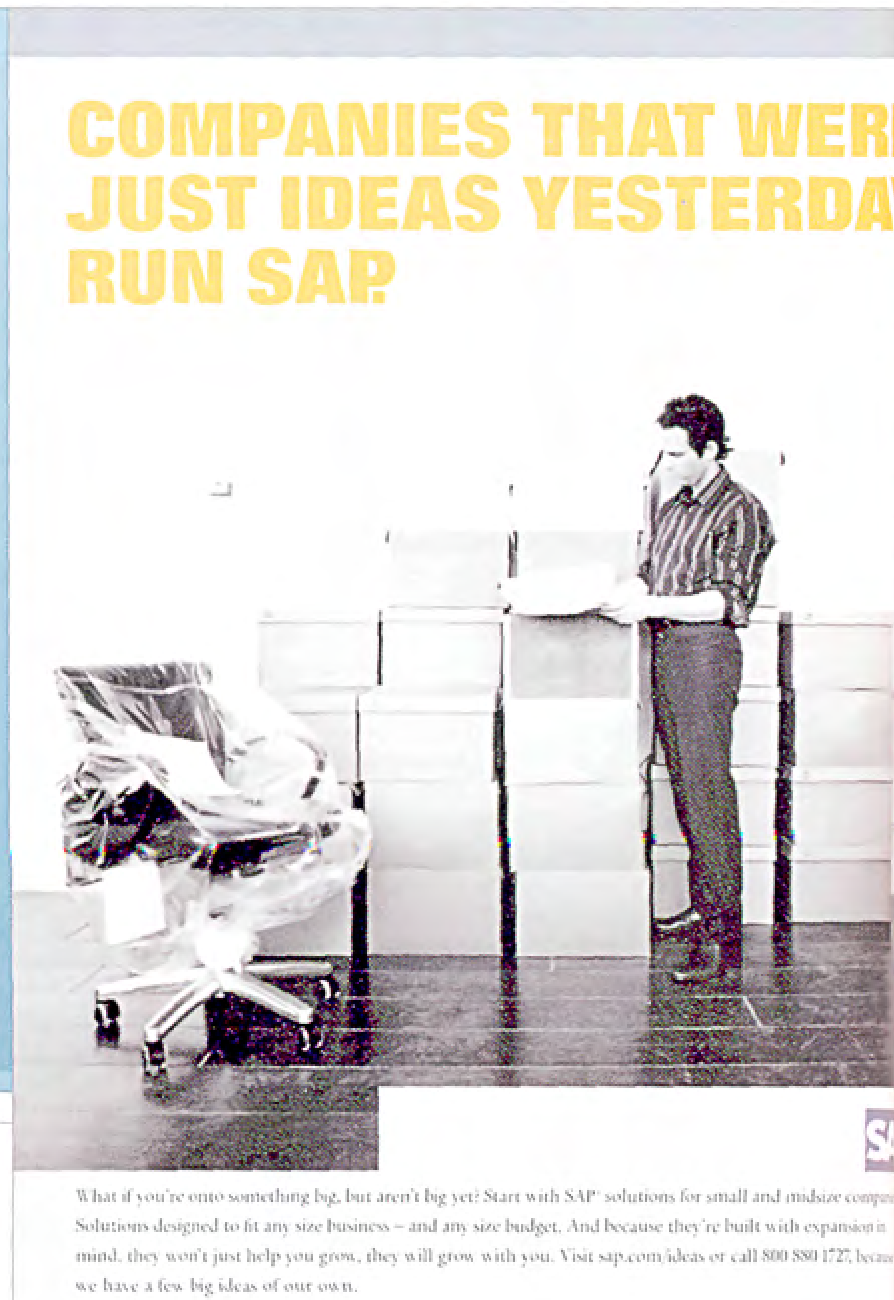
IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What is the business market, and how does it differ from the consumer market?
2. What buying situations do organizational buyers face?
3. Who participates in the business-to-business buying process?
4. How do business buyers make their decisions?
5. How can companies build strong relationships with business customers?
6. How do institutional buyers and government agencies do their buying?



CHAPTER 7 ::: ANALYZING BUSINESS MARKETS

seven

Business organizations do not only sell; they also buy vast quantities of raw materials, manufactured components, plant and equipment, supplies, and business services. There are over 13 million buying organizations in the United States alone. To create and capture value, sellers need to understand these organizations' needs, resources, policies, and buying procedures.

German software company SAP has become a leading seller to the business market by specializing in software to automate business functions, such as finance and factory management. It owns over half the market. SAP's leadership strategy is to focus carefully on what customers want, and show them how SAP's software applications can improve profits, raise revenue, or reduce costs. Partly through acquisitions, SAP offers IT customers one-stop shopping to standardize business processes.[1]

Some of the world's most valuable brands belong to business marketers: ABB, Caterpillar, DuPont, FedEx, GE, Hewlett-Packard, IBM, Intel, and Siemens. Much of basic marketing also applies to business marketers. They need to embrace holistic marketing principles, such as building strong relationships with their customers, just like any marketer. But there are some unique considerations in selling to other businesses.[2] In this chapter, we will highlight some of the crucial differences for marketing in business markets.

"The best run businesses run SAP": SAP's software helps businesses standardize processes and automate functions.

::: What Is Organizational Buying?

Webster and Wind define **organizational buying** as the decision-making process by which formal organizations establish the need for purchased products and services and identify, evaluate, and choose among alternative brands and suppliers.[3]

The Business Market Versus the Consumer Market

The **business market** consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others. The major industries making up the business market are agriculture, forestry, and fisheries; mining; manufacturing; construction; transportation; communication; public utilities; banking, finance, and insurance; distribution; and services.

More dollars and items are involved in sales to business buyers than to consumers. Consider the process of producing and selling a simple pair of shoes. Hide dealers must sell hides to tanners, who sell leather to shoe manufacturers, who sell shoes to wholesalers, who sell shoes to retailers, who finally sell them to consumers. Each party in the supply chain also has to buy many other goods and services.

Business markets have several characteristics that contrast sharply with those of consumer markets:

- *Fewer, larger buyers.* The business marketer normally deals with far fewer, much larger buyers than the consumer marketer does. The fate of Goodyear Tire Company and other

MARKETING INSIGHT | BIG SALES TO SMALL BUSINESS

Like millions of Americans, Ken Kantor likes to shop on eBay. However, he isn't looking for collectible Barbies, Batman cards, or gently used roller blades. Co-owner of a small audio design company, Intelligent Audio Systems, Kantor bids on business equipment, and he was pleased as punch to purchase some nearly new testing meters for $100 each, which would have easily gone for $4,700 retail.

Business owners like Kantor represent not only a sweet spot for eBay but also for behemoths such as IBM, American Express, and Microsoft. According to the Small Business Administration's Office of Advocacy, 550,000 small businesses opened in the United States in 2002. Those new ventures need capital equipment, technology, supplies, and services. Look beyond the United States to new ventures around the world and you have a huge new B2B growth market. Here's how some companies are reaching it:

- With its new suite of run-your-business software, **Microsoft** is counting on sales to 45 million small to midsize businesses worldwide to add $10 billion to annual revenue by 2010. Yet even with all its cash, Microsoft can't afford to send reps to all of them. Instead, Microsoft is unleashing an army of independent computer consulting companies—24,000 in all—known as value-added resellers. It has also added 300 sales managers to help educate and support both resellers and customers.
- **IBM** counts small to midsize businesses as 20 percent of its business and has launched Express, a line of hardware, software services, and financing, for this market. IBM sells through regional reps as well as independent software vendors and resellers, and it supports its small-midsize push with millions of dollars in advertising annually. Ads include TV spots and print ads in publications such as *American Banker* and *Inc.* The company also directly targets gay business owners with ads in *The Advocate* and *Out*. To reach other minority segments, such as African Americans and Hispanics, IBM partners with nonprofits.
- **American Express** has been steadily adding new features to its credit card for small business, which some small companies use to cover hundreds of thousands of dollars a month in cash needs. In addition to its credit card, American Express has been expanding its leading operations for small business. It has created a small business network called OPEN (www.openamericanexpress.com) to bring together various services, Web tools, and discount programs with other giants like ExxonMobil, Dell, FedEx, and Staples. With OPEN, American Express not only allows customers to save money on common expenses; it also encourages them to do much of their recordkeeping on its Web site.

Yet while small to midsize businesses present a huge opportunity, they also present huge challenges. The market is large and fragmented by industry, size, and number of years in operation. And once you reach them, it's hard to persuade them to buy. Small business owners are notably averse to long-range planning and have an "I'll buy it when I need it" decision-making style. Fortunately, however, those new to this market can tap into the growing body of experience from the likes of IBM, Microsoft, Hewlett-Packard, American Express, and others who have honed their small business marketing strategies.

Sources: Based on Barnaby J. Feder, "When Goliath Comes Knocking on David's Door," *New York Times*, May 6, 2003, p. G13; Jay Greene, "Small Biz: Microsoft's Next Big Thing?" *BusinessWeek*, April 21, 2003, pp. 72–73; Jennifer Gilbert, "Small but Mighty," *Sales& Marketing Management* (January 2004): 30–35; Verne Kopytoff, "Businesses Click on eBay," *San Francisco Chronicle*, July 28, 2003, p. E1; Matt Krantz, "Firms Jump on the eBay Wagon," *USA Today*, May 3, 2004, pp. 1B, 2B.

automotive part suppliers depends on getting contracts from a few major automakers. A few large buyers do most of the purchasing in such industries as aircraft engines and defense weapons. Although it should be noted that as a slowing economy has put a stranglehold on large corporations' purchasing departments, the small and midsize business market is offering new opportunities for suppliers.[4] See "Marketing Insight: Big Sales to Small Business," for more on this promising new B2B market, and see "Marketing Memo: Guidelines for Selling to Small Business" for some "do's and don'ts."

- ***Close supplier–customer relationship.*** Because of the smaller customer base and the importance and power of the larger customers, suppliers are frequently expected to customize their offerings to individual business customer needs. Business buyers often select suppliers who also buy from them. An example would be a paper manufacturer that buys chemicals from a chemical company that buys a considerable amount of its paper.

- ***Professional purchasing.*** Business goods are often purchased by trained purchasing agents, who must follow their organizations' purchasing policies, constraints, and requirements. Many of the buying instruments—for example, requests for quotations, proposals, and purchase contracts—are not typically found in consumer buying. Professional buyers spend their careers learning how to buy better. Many belong to the National Association of Purchasing Managers (NAPM), which seeks to improve professional buyers' effectiveness and status. This means that business marketers have to provide greater technical data about their product and its advantages over competitors' products.

- ***Several buying influences.*** More people typically influence business buying decisions. Buying committees consisting of technical experts and even senior management are common in the purchase of major goods. Business marketers have to send well-trained sales representatives and sales teams to deal with the well-trained buyers.

- ***Multiple sales calls.*** Because more people are involved in the selling process, it takes multiple sales calls to win most business orders, and some sales cycles can take years. A study by McGraw-Hill found that it takes four to four and a half calls to close an average industrial sale. In the case of capital equipment sales for large projects, it may take multiple attempts to fund a project, and the sales cycle—between quoting a job and delivering the product—is often measured in years.[5]

- ***Derived demand.*** The demand for business goods is ultimately derived from the demand for consumer goods. For this reason, the business marketer must closely monitor the buying patterns of ultimate consumers. For instance, the Big Three automakers in Detroit have been driving the boom in demand for steel-bar products. Much of that demand is derived from consumers' continued love affair with minivans and other light trucks, which consume far more steel than cars. Business buyers must also pay close attention to current and expected economic factors, such as the level of production, investment, consumer spending, and the interest rate. In a recession, business buyers reduce their investment in plant, equipment, and inventories. Business marketers can do little to stimulate total demand in this environment. They can only fight harder to increase or maintain their share of demand.

- ***Inelastic demand.*** The total demand for many business goods and services is inelastic—that is, not much affected by price changes. Shoe manufacturers are not going to buy much more leather if the price of leather falls, nor will they buy much less leather if the price rises, unless they can find satisfactory substitutes. Demand is especially inelastic in the short run because producers cannot make quick changes in production methods. Demand is also inelastic for business goods that represent a small percentage of the item's total cost, such as shoelaces.

- ***Fluctuating demand.*** The demand for business goods and services tends to be more volatile than the demand for consumer goods and services. A given percentage increase in consumer demand can lead to a much larger percentage increase in the demand for plant and equipment necessary to produce the additional output. Economists refer to this as the *acceleration effect.* Sometimes a rise of only 10 percent in consumer demand can cause as much as a 200 percent rise in business demand for products in the next period; a 10 percent fall in consumer demand may cause a complete collapse in business demand.

- ***Geographically concentrated buyers.*** More than half of U.S. business buyers are concentrated in seven states: New York, California, Pennsylvania, Illinois, Ohio, New Jersey, and Michigan. The geographical concentration of producers helps to reduce selling costs. At the same time, business marketers need to monitor regional shifts of certain industries.

- ***Direct purchasing.*** Business buyers often buy directly from manufacturers rather than through intermediaries, especially items that are technically complex or expensive (such as mainframes or aircraft).

Buying Situations

The business buyer faces many decisions in making a purchase. The number of decisions depends on the buying situation: complexity of the problem being solved, newness of the buying requirement, number of people involved, and time required. Patrick Robinson and others distinguish three types of buying situations: the straight rebuy, modified rebuy, and new task.[6]

STRAIGHT REBUY The purchasing department reorders on a routine basis (e.g., office supplies, bulk chemicals) and chooses from suppliers on an "approved list." The suppliers make an effort to maintain product and service quality and often propose automatic reordering systems to save time. "Out-suppliers" attempt to offer something new or to exploit dissatisfaction with a current supplier. Out-suppliers try to get a small order and then enlarge their purchase share over time.

MODIFIED REBUY The buyer wants to modify product specifications, prices, delivery requirements, or other terms. The modified rebuy usually involves additional participants on both sides. The in-suppliers become nervous and have to protect the account. The out-suppliers see an opportunity to propose a better offer to gain some business.

NEW TASK A purchaser buys a product or service for the first time (e.g., office building, new security system). The greater the cost or risk, the larger the number of participants and the greater their information gathering—and therefore the longer the time to a decision.[7]

MARKETING MEMO — GUIDELINES FOR SELLING TO SMALL BUSINESS

- ***Don't lump small and midsize businesses together.*** There's a big gap between $1 million in revenue and $50 million or between a start-up with 10 employees and a more mature business with 100. IBM customizes its small and midsize business portal (www-ibm.com/businesscenter/us) with call-me or text-chat buttons that are connected to products for different market segments.
- ***Don't waste their time.*** That means no cold calls, entertaining sales shows, or sales pitches over long, boozy lunches.
- ***Do keep it simple.*** This could be a corollary to "don't waste their time." Simplicity means one point of contact with a supplier for all service problems or one single bill for all services and products. AT&T corporation, which serves 3.9 million businesses with fewer than 100 employees, bundles data management, networking, and other abilities into convenient single packages for this market.
- ***Do use the Internet.*** In its research on buying patterns of small business owners, Hewlett-Packard found that these time-strapped decision makers prefer to buy, or at least research, products and services online. To that end, HP has designed a site targeted to small and midsize businesses and pulls business owners to the site through extensive advertising, direct mail, e-mail campaigns, catalogs, and events. IBM prospects via eBay by selling refurbished or phased-out equipment on its new B2B site. About 80 percent of IBM's equipment is sold to small businesses that are new to IBM—half of which have agreed to receive calls with other offers.
- ***Don't forget about direct contact.*** Even if a small business owner's first point of contact is via the Internet, you still need to offer phone or face time. Sprint connects with small businesses through its Sprint Experience Centers. Located in major metropolitan areas, these centers bring Sprint's products to life and serve as a place where Sprint reps or dealer reps can invite prospects and let them interact with the technologies.
- ***Do provide support after the sale.*** Small businesses want partners, not pitchmen. When The DeWitt Company, a 100-employee landscaping products business, purchased a large piece of machinery from Moeller, a German company, the company's president paid DeWitt's CEO a personal visit and stayed until the machine was up and running properly.
- ***Do your homework.*** The realities of small or midsize business management are different from those of a large corporation. Microsoft created a small, fictional executive research firm, Southridge, and baseball-style trading cards of its key decision makers in order to help Microsoft employees tie sales strategies to small business realities.

Sources: Based on Barnaby J. Feder, "When Goliath Comes Knocking on David's Door," *New York Times*, May 6, 2003, p. G13; Jay Greene, "Small Biz: Microsoft's Next Big Thing?" *BusinessWeek*, April 21, 2003, pp. 72–73; Jennifer Gilbert, "Small but Mighty," *Sales& Marketing Management* (January 2004): 30–35; Verne Kopytoff, "Businesses Click on eBay," *San Francisco Chronicle*, July 28, 2003, p. E1.

The business buyer makes the fewest decisions in the straight rebuy situation and the most in the new-task situation. Over time, new-buy situations become straight rebuys and routine purchase behavior. New-task buying passes through several stages: awareness, interest, evaluation, trial, and adoption.[8] The effectiveness of communication tools varies at each stage. Mass media are most important during the initial awareness stage; salespeople have their greatest impact at the interest stage; and technical sources are the most important during the evaluation stage.

In the new-task situation, the buyer has to determine product specifications, price limits, delivery terms and times, service terms, payment terms, order quantities, acceptable suppliers, and the selected supplier. Different participants influence each decision, and the order in which these decisions are made varies. This situation is the marketer's greatest opportunity and challenge. Because of the complicated selling involved, many companies use a *missionary sales force* consisting of their most effective salespeople. The brand promise and the manufacturer's brand name recognition will be important in establishing trust and the customer's willingness to consider change. The marketer also tries to reach as many key participants as possible and provide helpful information and assistance.

Once a customer is acquired, in-suppliers are continually seeking ways to add value to their market offer to facilitate rebuys. Often they do this by giving customers customized information:

ORICA LTD.

Orica Ltd., formerly ICI Australia, competes in the cutthroat commercial explosives business. Its customers are quarries that use explosives to blast solid rock face into aggregate of a specified size. Orica is constantly trying to minimize the cost of explosives. As a supplier, Orica realized it could create significant value by improving the efficiency of the blast. To do this, it established over 20 parameters that influenced the success of the blast and began collecting data from customers on the input parameters as well as the outcomes of individual blasts. By collating the data, Orica engineers came to understand the conditions that produced different outcomes. It then could offer customers a contract for "broken rock" that would almost guarantee the desired outcome. The success of Orica's approach—of managing the entire blast for the quarry rather than simply selling explosives—entrenched the company as the world's leading supplier of commercial explosives.[9]

Customers considering dropping six or seven figures on one transaction for big-ticket goods and services want all the information they can get. One way to entice new buyers is to create a customer reference program in which satisfied existing customers act in concert with the company's sales and marketing department by agreeing to serve as references. Companies that have such programs are Siebel Systems, J.D. Edwards, and Sun Microsystems:

J.D. EDWARDS

Denver-based software developer J.D. Edwards invites customers with a story that's "relevant to new customers" to join its reference program and specify the level at which they would like to participate. Customers might agree to take phone calls from potential customers, host a site visit, or simply lend their names or blurbs to press releases and other copy. J.D. Edwards' corporate communications director says that hearing other customers' stories is crucial for prospective buyers. The company evaluates the benefit of those customer references by tracking sales generated in the earlier stages of the prospect's contact with the program. For a seven-month period in 2002–2003, the reference program helped generate more than $35 million in software licensing fees.

Systems Buying and Selling

Many business buyers prefer to buy a total solution to a problem from one seller. Called *systems buying*, this practice originated with government purchases of major weapons and communications systems. The government would solicit bids from *prime contractors*, who assembled the package or system. The contractor who was awarded the contract would be responsible for bidding out and assembling the system's subcomponents from *second-tier contractors*. The prime contractor would thus provide a turnkey solution, so-called because the buyer simply had to turn one key to get the job done.

FORD

Ford has transformed itself from being mainly a car manufacturer to being mainly a car assembler. Ford relies primarily on a few major systems suppliers to provide seating systems, braking systems, door systems, and other major assemblies. In designing a new automobile, Ford works closely with (say) its seat manufacturer and creates a *black box specification* of the basic seat dimensions and performance that it needs, and then waits for the seat supplier to propose the most cost-effective design. When they agree, the seat supplier subcontracts with parts suppliers to produce and deliver the needed components.

Sellers have increasingly recognized that buyers like to purchase in this way, and many have adopted systems selling as a marketing tool. One variant of systems selling is *systems contracting*, where a single supplier provides the buyer with his or her entire requirement of MRO (maintenance, repair, operating) supplies. During the contract period, the supplier manages the customer's inventory. For example, Shell Oil manages the oil inventory of many of its business customers and knows when it requires replenishment. The customer benefits from reduced procurement and management costs and from price protection over the term of the contract. The seller benefits from lower operating costs because of a steady demand and reduced paperwork.

Systems selling is a key industrial marketing strategy in bidding to build large-scale industrial projects, such as dams, steel factories, irrigation systems, sanitation systems, pipelines, utilities, and even new towns. Project engineering firms must compete on price, quality, reliability, and other attributes to win contracts. Consider the following example.

JAPAN AND INDONESIA

The Indonesian government requested bids to build a cement factory near Jakarta. A U.S. firm made a proposal that included choosing the site, designing the cement factory, hiring the construction crews, assembling the materials and equipment, and turning over the finished factory to the Indonesian government. A Japanese firm, in outlining its proposal, included all of these services, plus hiring and training the workers to run the factory, exporting the cement through its trading companies, and using the cement to build roads and new office buildings in Jakarta. Although the Japanese proposal involved more money, it won the contract. Clearly, the Japanese viewed the problem not just as one of building a cement factory (the narrow view of systems selling) but as one of contributing to Indonesia's economic development. They took the broadest view of the customer's needs. This is true systems selling.

::: Participants in the Business Buying Process

Who buys the trillions of dollars' worth of goods and services needed by business organizations? Purchasing agents are influential in straight-rebuy and modified-rebuy situations, whereas other department personnel are more influential in new-buy situations. Engineering personnel usually have a major influence in selecting product components, and purchasing agents dominate in selecting suppliers.[10]

The Buying Center

Webster and Wind call the decision-making unit of a buying organization *the buying center*. It is composed of "all those individuals and groups who participate in the purchasing decision-making process, who share some common goals and the risks arising from the decisions."[11] The buying center includes all members of the organization who play any of seven roles in the purchase decision process.[12]

1. ***Initiators.*** Those who request that something be purchased. They may be users or others in the organization.
2. ***Users.*** Those who will use the product or service. In many cases, the users initiate the buying proposal and help define the product requirements.
3. ***Influencers.*** People who influence the buying decision. They often help define specifications and also provide information for evaluating alternatives. Technical personnel are particularly important influencers.
4. ***Deciders.*** People who decide on product requirements or on suppliers.
5. ***Approvers.*** People who authorize the proposed actions of deciders or buyers.

6. ***Buyers.*** People who have formal authority to select the supplier and arrange the purchase terms. Buyers may help shape product specifications, but they play their major role in selecting vendors and negotiating. In more complex purchases, the buyers might include high-level managers.
7. ***Gatekeepers.*** People who have the power to prevent sellers or information from reaching members of the buying center. For example, purchasing agents, receptionists, and telephone operators may prevent salespersons from contacting users or deciders.

Ford assembly line in action: Worker assembling autos at Ford Motor Company's St. Thomas Auto Plant in Ontario, Canada.

Several individuals can occupy a given role (e.g., there may be many users or influencers), and the individual may occupy multiple roles.[13] A purchasing manager, for example, often occupies the roles of buyer, influencer, and gatekeeper simultaneously: he or she can determine which sales reps can call on other people in the organization; what budget and other constraints to place on the purchase; and which firm will actually get the business, even though others (deciders) might select two or more potential vendors who can meet the company's requirements.

The typical buying center has a minimum of five or six members and often has dozens. The buying center may include people outside the target customer organization, such as government officials, consultants, technical advisors, and other members of the marketing channel.

Buying Center Influences

Buying centers usually include several participants with differing interests, authority, status, and persuasiveness. Each member of the buying center is likely to give priority to very different decision criteria. For example, engineering personnel may be concerned primarily with maximizing the actual performance of the product; production personnel may be concerned mainly with ease of use and reliability of supply; financial personnel may focus on the economics of the purchase; purchasing may be concerned with operating and replacement costs; union officials may emphasize safety issues, and so on.

Business buyers also respond to many influences when they make their decisions. Each buyer has personal motivations, perceptions, and preferences, which are influenced by the buyer's age, income, education, job position, personality, attitudes toward risk, and culture. Buyers definitely exhibit different buying styles. There are "keep-it-simple" buyers, "own-expert" buyers, "want-the-best" buyers, and "want-everything-done" buyers. Some younger, highly educated buyers are computer experts who conduct rigorous analyses of competitive proposals before choosing a supplier. Other buyers are "toughies" from the old school and pit the competing sellers against one another.

Webster cautions that ultimately, individuals, not organizations, make purchasing decisions.[14] Individuals are motivated by their own needs and perceptions in attempting to maximize the rewards (pay, advancement, recognition, and feelings of achievement) offered by the organization. Personal needs "motivate" the behavior of individuals but organizational needs "legitimate" the buying decision process and its outcomes. People are not buying "products." They are buying solutions to two problems: the organization's economic and strategic problem and their own personal "problem" of obtaining individual achievement and reward. In this sense, industrial buying decisions are both "rational" and "emotional," as they serve both the organization's and the individual's needs.[15]

Buying Center Targeting

To target their efforts properly, business marketers have to figure out: Who are the major decision participants? What decisions do they influence? What is their level of influence? What evaluation criteria do they use? Consider the following example:

A company sells nonwoven disposable surgical gowns to hospitals. The hospital personnel who participate in this buying decision include the vice president of purchasing, the operating-room administrator, and the surgeons. The vice president of purchasing analyzes whether the hospital should buy disposable gowns or reusable gowns. If the findings favor disposable gowns, then the operating-room administrator compares various competitors' products and prices and makes a choice. This administrator considers absorbency, antiseptic quality, design, and cost, and normally buys the brand that meets the functional requirements at the lowest cost. Surgeons influence the decision retroactively by reporting their satisfaction with the particular brand.

The business marketer is not likely to know exactly what kind of group dynamics take place during the decision process, although whatever information he or she can obtain about personalities and interpersonal factors is useful.

Small sellers concentrate on reaching the *key buying influencers*. Larger sellers go for *multilevel in-depth selling* to reach as many participants as possible. Their salespeople virtually "live" with high-volume customers. Companies will have to rely more heavily on their communications programs to reach hidden buying influences and keep current customers informed.[16]

SYMANTEC CORPORATION

Internet security provider Symantec Corporation has moved from being primarily a provider of consumer software (under the Norton name) to a provider of enterprise security solutions for financial services, health care, and utilities industries, as well as key accounts for the U.S. Department of Defense. To reach these new markets, Symantec had to restructure its sales force to develop high-level relationships. So Symantec launched the Executive Sponsorship Program in 2003. The 13 Symantec executives enrolled in the program are paired with vice presidents or C-level executives within 19 key customer organizations in industries ranging from banking to telecommunications and manufacturing. The goal of the program is to foster better understanding of Symantec's customers and their business concerns. So far the program has enabled Symantec to be seen as a valued partner and enabled the Symantec executives to gain insights into how they can develop products that fit customers' needs.[17]

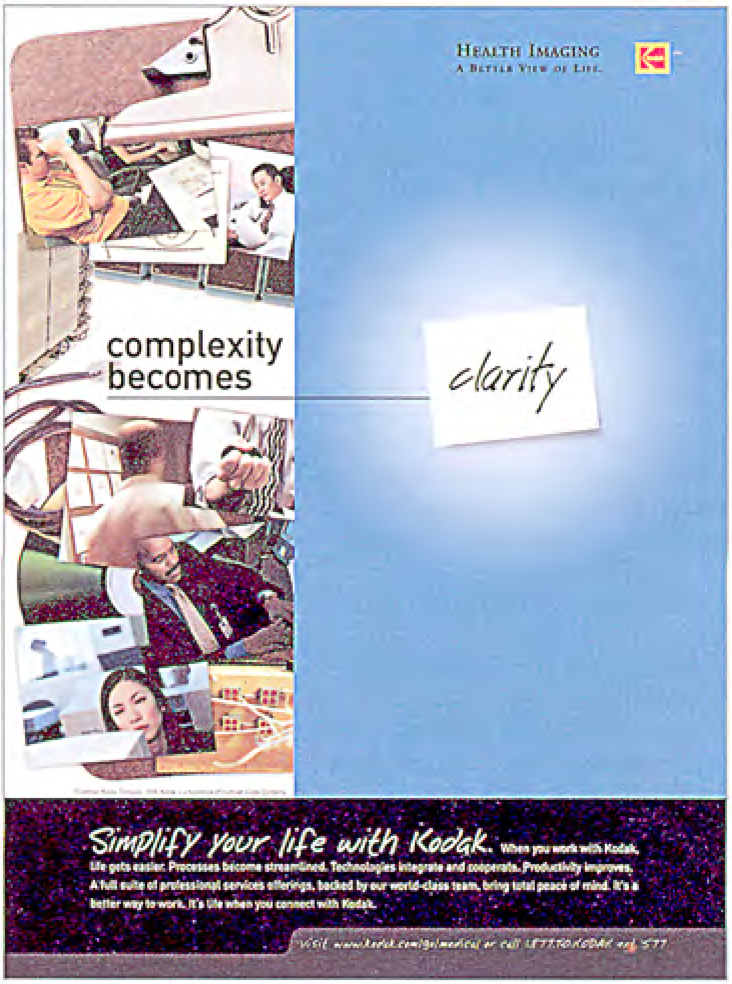
Business marketers must periodically review their assumptions about buying center participants. For years, Kodak sold X-ray film to hospital lab technicians. Kodak research indicated that professional administrators were increasingly making purchasing decisions. As a result, Kodak revised its marketing strategy and developed new advertising to reach out to these decision makers.

In defining target segments, four types of business customers can often be identified, with corresponding marketing implications.

1. ***Price-oriented customers*** (transactional selling). Price is everything.
2. ***Solution-oriented customers*** (consultative selling). They want low prices but will respond to arguments about lower total cost or more dependable supply or service.
3. ***Gold-standard customers*** (quality selling). They want the best performance in terms of product quality, assistance, reliable delivery, and so on.
4. ***Strategic-value customers*** (enterprise selling). They want a fairly permanent sole-supplier relationship with your company.

Some companies are willing to handle price-oriented buyers by setting a lower price, but establishing restrictive conditions: (1) limiting the quantity that can be purchased; (2) no refunds; (3) no adjustments; and (4) no services.[18]

- ***Cardinal Health*** set up a bonus dollars scheme at one time and gave points according to how much the business customer purchased. The points could be turned in for extra goods or free consulting.
- ***GE*** is installing diagnostic sensors in its airline engines and railroad engines. It is now compensated for hours of flight or railroad travel.
- ***IBM*** is now more of a service company aided by products than a product company aided by services. It may offer to sell computer power on demand (like video on demand) as an alternative to selling computers.



Kodak ad that targets hospital administrators by offering services that streamline processes, integrate technologies, and improve productivity.

Risk and gain sharing can be used to offset requested price reductions from customers. For example, say Medline, a hospital supplier, signs an agreement with Highland Park Hospital promising $350,000 in savings over the first 18 months in exchange for a tenfold increase in the hospitals' share of supplies. If Medline achieves less than this promised savings, it will make up the difference. If Medline achieves substantially more than this promise, it participates in the extra savings. To make such arrangements work, the supplier must be willing to help the customer to build a historical database, reach an agreement for measuring benefits and costs, and devise a dispute resolution mechanism.

Solution selling can also alleviate price pressure and comes in different forms. Here are three examples.[19]

- ***Solutions to Enhance Customer Revenues.*** Hendrix Voeders used its sales consultants to help farmers deliver an incremental animal weight gain of 5 to 10 percent over competitors.
- ***Solutions to Decrease Customer Risks.*** ICI Explosives formulated a safer way to ship explosives for quarries.
- ***Solutions to Reduce Customer Costs.*** W.W. Grainger employees work at large customer facilities to reduce materials-management costs.

::: The Purchasing/Procurement Process

Every organization has specific purchasing objectives, policies, procedures, organizational structures, and systems. In principle, business buyers seek to obtain the highest benefit package (economic, technical, service, and social) in relation to a market offering's costs. A business buyer's incentive to purchase will be greater in proportion to the ratio of perceived benefits to costs. The marketer's task is to construct a profitable offering that delivers superior customer value to the target buyers.

Purchasing Orientations

In the past, purchasing departments occupied a low position in the management hierarchy, in spite of often managing more than half the company's costs. Recent competitive pressures have led many companies to upgrade their purchasing departments and elevate administrators to vice presidential rank. Today's purchasing departments are staffed with MBAs who aspire to be CEOs—like Thomas Stallkamp, Chrysler's former executive vice president of procurement and supply, who cut costs and streamlined the automaker's manufacturing processes.[20]

These new, more strategically oriented purchasing departments have a mission to seek the best value from fewer and better suppliers. Some multinationals have even elevated them to "strategic supply departments" with responsibility for global sourcing and partnering. At Caterpillar, for example, purchasing, inventory control, production scheduling, and traffic have been combined into one department. Lockheed Martin is another firm that has improved its business buying practices.

LOCKHEED MARTIN

Defense contractor Lockheed Martin, which spends $13.2 billion annually, created a Strategic Sourcing Solutions Group to centralize the company's purchasing functions across divisions and consolidate redundancies. The group is comprised of 52 employees with cross-functional experience, and their mission is "to be an integrated, leading edge team that provides industry-recognized supply chain intelligence and innovative sourcing strategies, while fully optimizing customer value." As an example of the group's strategic focus, Lockheed Martin found it was spending roughly 25 to 40 percent more than it should on machining. A machining council was assigned to look into driving down the number of suppliers and consolidating among the preferred ones. The supply base was reduced by a combination of driving more business to preferred suppliers, increasing the frequency of negotiating, and introducing reverse auctions where appropriate.[21]

The upgrading of purchasing means that business marketers must upgrade their sales personnel to match the higher caliber of the business buyers. Formally, we can distinguish three company purchasing orientations:[22]

- ***Buying Orientation.*** The purchaser's focus is short term and tactical. Buyers are rewarded on their ability to obtain the lowest price from suppliers for the given level of quality and availability. Buyers use two tactics: *commoditization,* where they imply that the product is a commodity and care only about price; and *multisourcing,* where they use several sources and make them compete for shares of the company's purchases.
- ***Procurement Orientation.*** Here buyers simultaneously seek quality improvements and cost reductions. Buyers develop collaborative relationships with major suppliers and seek savings through better management of acquisition, conversion, and disposal costs. They encourage early supplier involvement in materials handling, inventory levels, just-in-time management, and even product design. They negotiate long-term contracts with major suppliers to ensure the timely flow of materials. They work closely with their manufacturing group on materials requirement planning (MRP) to make sure supplies arrive on time.
- ***Supply Chain Management Orientation.*** Here purchasing's role is further broadened to become a more strategic, value-adding operation. Purchasing executives at the firm work with marketing and other company executives to build a seamless supply chain management system from the purchase of raw materials to the on-time arrival of finished goods to the end users.

Types of Purchasing Processes

Marketers need to understand how business purchasing departments work. These departments purchase many types of products, and the purchasing process will vary depending on the types of products involved. Peter Kraljic distinguished four product-related purchasing processes:[23]

1. ***Routine products.*** These products have low value and cost to the customer and involve little risk (e.g., office supplies). Customers will seek the lowest price and emphasize routine ordering. Suppliers will offer to standardize and consolidate orders.
2. ***Leverage products.*** These products have high value and cost to the customer but involve little risk of supply (e.g., engine pistons) because many companies make them. The supplier knows that the customer will compare market offerings and costs, and it needs to show that its offering minimizes the customer's total cost.
3. ***Strategic products.*** These products have high value and cost to the customer and also involve high risk (e.g., mainframe computers). The customer will want a well-known and trusted supplier and be willing to pay more than the average price. The supplier should seek strategic alliances that take the form of early supplier involvement, co-development programs, and co-investment.
4. ***Bottleneck products.*** These products have low value and cost to the customer but they involve some risk (e.g., spare parts). The customer will want a supplier who can guarantee a steady supply of reliable products. The supplier should propose standard parts and offer a tracking system, delivery on demand, and a help desk.

Purchasing Organization and Administration

Most purchasing professionals describe their jobs as more strategic, technical, team-oriented, and involving more responsibility than ever before. "Purchasing is doing more cross-functional work than it did in the past," says David Duprey, a buyer for Anaren Microwave, Inc. Sixty-one percent of buyers surveyed said the buying group was more involved in new-product design and development than it was five years ago; and more than half of the buyers participate in cross-functional teams, with suppliers well represented.[24]

In multidivisional companies, most purchasing is carried out by separate divisions. Some companies, however, have started to centralize purchasing. Headquarters identifies materials purchased by several divisions and buys them centrally, thereby gaining more purchasing clout. The individual divisions can buy from another source if they can get a better deal, but in general, centralized purchasing produces substantial savings. For the business marketer, this development means dealing with fewer and higher-level buyers and using a national account sales group to deal with large corporate buyers.

At the same time, companies are decentralizing some purchasing operations by empowering employees to purchase small-ticket items such as special binders, coffeemakers, or Christmas trees. This has come about through the availability of corporate purchasing cards issued by credit card organizations. Companies distribute the cards to foremen, clerks, and secretaries; the cards incorporate codes that set credit limits and restrict where they can be used. National Semiconductor's purchasing chief has noted that the cards have cut processing costs from $30 an order to a few cents. The additional benefit is that buyers and suppliers now spend less time on paperwork.

::: Stages in the Buying Process

At this point we are ready to describe the general stages in the business buying decision process. Robinson and Associates have identified eight stages and called them *buyphases*.[25] The stages are shown in Table 7.1. This model is called the *buygrid* framework.

Table 7.1 describes the buying stages involved in a new-task buying situation. In modified-rebuy or straight-rebuy situations, some stages are compressed or bypassed. For example, in a straight-rebuy situation, the buyer normally has a favorite supplier or a ranked list of suppliers. Thus the supplier search and proposal solicitation stages would be skipped.

The eight-stage buyphase model describes the major steps in the business buying process. Tracing out a buyflow map can provide many clues to the business marketer. A buyflow map for the purchase of a packaging machine in Japan is shown in Figure 7.1. The numbers within the icons are defined at the right. The italicized numbers between icons show the flow of events. Over 20 people in the purchasing company were involved, including the production

TABLE 7.1

Buygrid Framework: Major Stages (Buyphases) of the Industrial Buying Process in Relation to Major Buying Situations (Buyclasses)

		Buyclasses		
		New Task	Modified Rebuy	Straight Rebuy
	1. Problem recognition	Yes	Maybe	No
	2. General need description	Yes	Maybe	No
	3. Product specification	Yes	Yes	Yes
BUYPHASES	4. Supplier search	Yes	Maybe	No
	5. Proposal solicitation	Yes	Maybe	No
	6. Supplier selection	Yes	Maybe	No
	7. Order-routine specification	Yes	Maybe	No
	8. Performance review	Yes	Yes	Yes

manager and staff, new-product committee, company laboratory, marketing department, and the department for market development. The entire decision-making process took 121 days. There are important considerations in each of the eight stages.

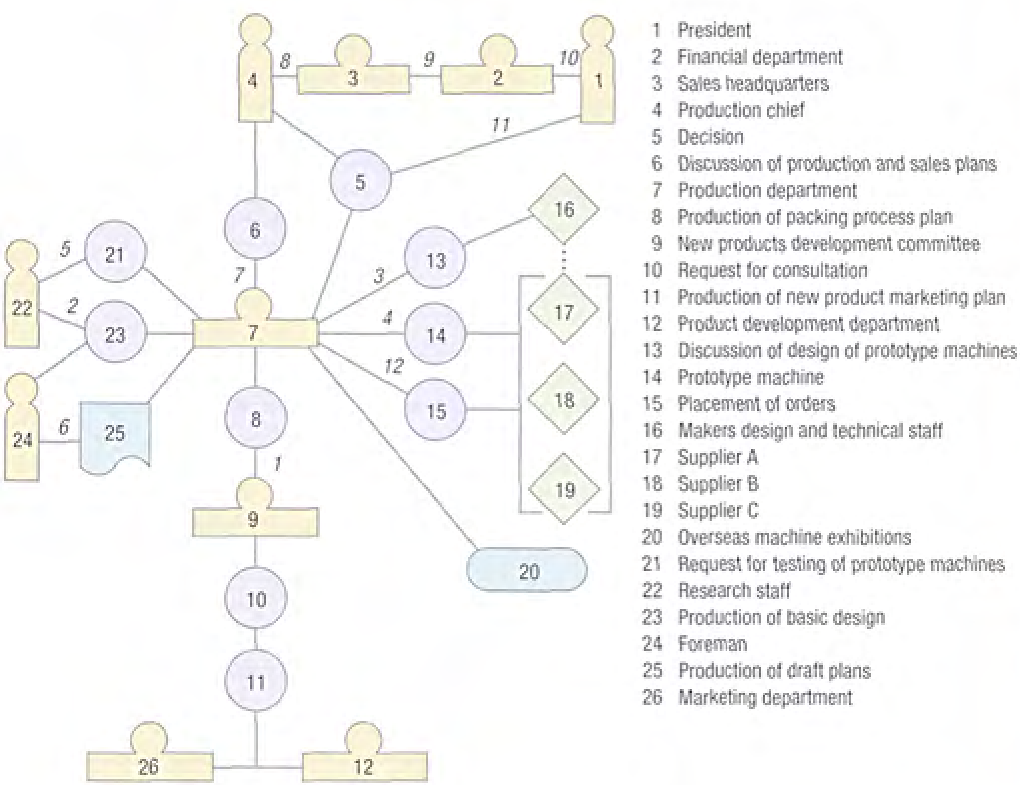
Problem Recognition

The buying process begins when someone in the company recognizes a problem or need that can be met by acquiring a good or service. The recognition can be triggered by internal or external stimuli. Internally, some common events lead to problem recognition. The company decides to develop a new product and needs new equipment and materials. A machine breaks down and requires new parts. Purchased material turns out to be unsatisfactory, and

FIG. 7.1

Organizational Buying Behavior in Japan: Packaging-Machine Purchase Process

Source: "Japanese Firms Use Unique Buying Behavior," *The Japan Economic Journal*, December 23, 1980, p. 29. Reprinted by permission.



the company searches for another supplier. A purchasing manager senses an opportunity to obtain lower prices or better quality. Externally, the buyer may get new ideas at a trade show, see an ad, or receive a call from a sales representative who offers a better product or a lower price. Business marketers can stimulate problem recognition by direct mail, telemarketing, and calling on prospects.

General Need Description and Product Specification

Next, the buyer determines the needed item's general characteristics and required quantity. For standard items, this is simple. For complex items, the buyer will work with others—engineers, users—to define characteristics like reliability, durability, or price. Business marketers can help by describing how their products meet or even exceed the buyer's needs. Here is an example of how a supplier is using value-added services to gain a competitive edge.

HEWLETT-PACKARD

Hewlett-Packard's marketing division has developed a concept called "trusted advisor." The marketers felt HP needed to move beyond selling systems to selling itself as an advisor and offering specific solutions to unique problems. What HP discovered is that some companies want a partner and others simply want a product that works. HP assumes an advisory role when it sells complex products like a network computer system. HP estimates that the new way of selling has contributed to a 60 percent growth of the high-end computer business. The company has increased its consulting business and is working on enterprise-wide projects through a series of partnerships with systems integrators and software companies.[26]

One of a series of Hewlett Packard ads with the theme "+ hp = everything is possible" that focus on its consulting and advisory capabilities. Through a joint venture with the Hong Kong Special Administrative Region government, hp created a Web portal that gives Hong Kong's citizens 24-hour access to government services.

The buying organization now develops the item's technical specifications. Often, the company will assign a product-value-analysis engineering team to the project. *Product value analysis (PVA)* is an approach to cost reduction in which components are studied to determine if they can be redesigned or standardized or made by cheaper methods of production. The PVA team will examine the high-cost components in a given product. The team will also identify overdesigned components that last longer than the product itself. Tightly written specifications will allow the buyer to refuse components that are too expensive or that fail to meet specified standards. Suppliers can use product value analysis as a tool for positioning themselves to win an account.

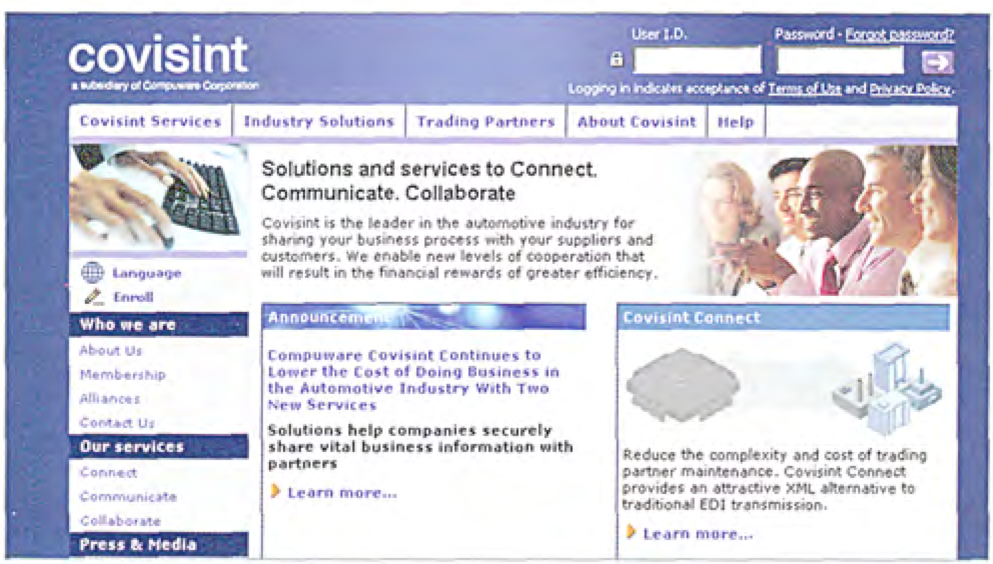
Supplier Search

The buyer next tries to identify the most appropriate suppliers through trade directories, contacts with other companies, trade advertisements, and trade shows. Business marketers also put products, prices, and other information on the Internet.[27] While B2B electronic commerce has not delivered on its early promise, it still far outstrips B2C commerce. According to market research firm eMarketer, U.S. businesses spent about $482 billion on online transactions with other businesses in 2002—up 242 percent from $141 billion spent two years earlier. By comparison, consumers spent only $71 billion on goods and services online in 2002.[28] The move to Internet purchasing has far-reaching implications for suppliers and will change the shape of purchasing for years to come. (See "Marketing Insight: The Business-to-Business Cyberbuying Bazaar.")

E-Procurement

Web sites are organized around two types of e-hubs: *vertical hubs* centered on industries (plastics, steel, chemicals, paper) and *functional hubs* (logistics, media buying, advertising, energy management). In addition to using these Web sites, companies can do e-procurement in other ways:

- ***Direct extranet links to major suppliers.*** A company can set up extranet links to its major suppliers. For example, it can set up a direct e-procurement account at Dell or Office Depot, and its employees can make their purchases this way.
- ***Buying alliances.*** Coca-Cola, Sara Lee, Kraft, PepsiCo, Gillette, P&G, and several other companies joined forces to form a buying alliance called Transora to use their combined leverage to obtain lower prices for raw materials. Transora members also share data on less expensive ways to ship products and track inventory. Several auto companies (GM, Ford, DaimlerChrysler) formed Covisint for the same reason. They believe they can save as much as $1,200 per car.



Covisint's home page: "Solutions and services to . . . Connect. Communicate. Collaborate."

MARKETING INSIGHT | THE BUSINESS-TO-BUSINESS (B2B) CYBERBUYING BAZAAR

With the growth of consumer online shopping, it is easy to lose sight of one of the most significant trends in e-commerce: the growth of business-to-business e-procurement. In addition to posting their own Web pages on the Internet, companies have established intranets for employees to communicate with one another, and extranets to link a company's communications and data with regular suppliers and distributors.

So far, most of the products that businesses are buying electronically are MRO materials (maintenance, repair, and operations) and travel and entertainment services. MRO materials make up 30 percent of business purchases, and the transaction costs for order processing are high, which means there is a huge incentive to streamline the process. Here are some examples: Los Angeles County purchases everything from chickens to condoms over the Internet. National Semiconductor has automated almost all of the company's 3,500 monthly requisitions to buy materials ranging from the sterile booties worn in its fabrication plants to state-of-the-art software. GE buys not only general operating supplies, but also industrial supplies online. Now that GE Information Services (GEIS) has opened its buying site to other companies, the company is well on its way to creating a vast electronic clearinghouse. Hundreds of thousands of firms will exchange trillions of dollars of industrial inputs—with GEIS running the show.

Many brick-and-mortar companies have expanded their online presence by building their business-to-business operations and targeting small businesses, which account for 98 percent of all U.S. employers. The 54 percent of companies that now purchase over the Internet are utilizing electronic marketplaces that are popping up in several forms:

- ***Catalog sites.*** Companies can order thousands of items through electronic catalogs distributed by e-procurement software, such as Grainger's.
- ***Vertical markets.*** Companies buying industrial products such as plastics, steel, or chemicals, or services such as logistics or media can go to specialized Web sites (called e-hubs). For example, Plastics.com allows plastics buyers to search for the best prices from the thousands of plastics sellers.
- ***"Pure Play" auction sites.*** These are online marketplaces such as eBay and Freemarkets.com that could not have been realized without the Internet and for which no business model existed before their formation. Freemarkets.com provides online auctions for buyers and sellers of industrial parts, raw materials, commodities, and services in over 50 product categories, and has facilitated over $40 billion worth of commerce since 1995.
- ***Spot (or exchange) markets.*** On spot electronic markets, prices change by the minute. ChemConnect.com is an exchange for buyers and sellers of bulk chemicals such as benzine and is a B2B success in an arena littered with failed online exchanges. First to market, it is now the biggest online exchange for chemical trading, with volume of $8.8 billion in 2002. Customers like Vanguard Petroleum Corp. in Houston conduct about 15 percent of their spot purchases and sales of natural gas liquids on ChemConnect's commodities trading site.
- ***Private exchanges.*** Hewlett-Packard, IBM, and Wal-Mart operate private exchanges to link with specially invited groups of suppliers and partners over the Web.
- ***Barter markets.*** In these markets, participants offer to trade goods or services.
- ***Buying alliances.*** Several companies buying the same goods join together to form purchasing consortia and gain deeper discounts on volume purchases (Transora, Covisint).

Online business buying offers several advantages: It shaves transaction costs for both buyers and suppliers, reduces time between order and delivery, consolidates purchasing systems, and forges more intimate relationships between partners and buyers. On the downside, it may help to erode supplier–buyer loyalty and create potential security problems. Businesses also face a technological dilemma because no single system yet dominates.

Sources: Robert Yoegel, "The Evolution of B-to-B Selling on the 'Net,'" *Target Marketing* (August 1998): 34; Andy Reinhardt, "Extranets: Log On, Link Up, Save Big," *BusinessWeek*, June 22, 1998, p. 134; "To Byte the Hand that Feeds," *The Economist*, June 17, 1998, pp. 61–62; John Evan Frook, "Buying Behemoth—By Shifting $5B in Spending to Extranets, GE Could Ignite a Development Frenzy," *Internetweek*, August 17, 1998, p. 1; Nicole Harris, "'Private Exchanges' May Allow B-to-B Commerce to Thrive After All," *Wall Street Journal*, March 16, 2001, pp. B1, B4; Olga Kharif, "B2B, Take 2," *BusinessWeek*, November 25, 2003; George S. Day, Adam J. Fein, and Gregg Ruppersberger, "Shakeouts in Digital Markets: Lessons from B2B Exchanges," *California Management Review* 45, no. 2 (Winter 2003): 131–151; Julia Angwin, "Top Online Chemical Exchange Is Unlikely Success Story," *Wall Street Journal*, January 8, 2004, p. A15.

- ***Company buying sites.*** General Electric formed the Trading Process Network (TPN) where it posts *requests for proposals (RFPs)*, negotiates terms, and places orders.

Moving into e-procurement involves more than acquiring software; it requires changing purchasing strategy and structure. However, the benefits are many: Aggregating purchasing across multiple departments gains larger, centrally negotiated volume discounts. There is less buying of substandard goods from outside the approved list of suppliers, and a smaller purchasing staff is required.

OWENS-CORNING

In 2001, the Owens-Corning purchasing organization set a goal of wiping out 80 percent of its paper invoices by the end of 2004. The strategic objectives underlying this goal were cost reduction, supply chain visibility, business process integration, and a common standardized process for all suppliers. To accomplish these objectives, Owens-Corning signed on with Advanced Data Exchange (ADX), an outsourced provider of EDI and XML, which takes whatever suppliers have to work with and effectively translates it into a usable electronic format for Owens-Corning. The electronic invoicing initiative worked with the company's use of e-auctions. Starting in 2004, all suppliers participating in e-auctions were told that as part of online auction bids they must agree to exchange invoices and purchase orders electronically if they are awarded the contract. With a $3 billion annual spending budget, Owens-Corning has the kind of clout to ensure suppliers get online.[29]

The supplier's task is to get listed in major online catalogs or services, develop a strong advertising and promotion program, and build a good reputation in the marketplace. This often means creating a well-designed and easy-to-use Web site.

HEWLETT-PACKARD

In 2003, Hewlett-Packard Co. was named number one in *BtoB* magazine's annual ranking of the top B-to-B Web sites. The site (www.hp.com) was launched after HP's merger with Compaq Computer and has 2.5 million pages and roughly 1,900 site areas. The challenge for HP was to integrate this enormous amount of information and present it coherently. Upon entering the site, users can click directly into their customer segment and search for information by product or by solution or click into a product category. The site allows companies to create customized catalogs for frequently purchased products, set up automatic approval routing for orders, and conduct end-to-end transaction processing. To further build relationships with customers, HP.com features Flash demos that show how to use the site, e-newsletters, live chats with sales reps, online classes, and real-time customer support. HP's Web efforts are paying off big: roughly 55 percent of the company's total sales come from the Web site.[30]

Suppliers who lack the required production capacity or suffer from a poor reputation will be rejected. Those who qualify may be visited by the buyer's agents, who will examine the suppliers' manufacturing facilities and meet their personnel. After evaluating each company, the buyer will end up with a short list of qualified suppliers. Many professional buyers have forced suppliers to change their marketing to increase their likelihood of making the cut.

CUTLER-HAMMER

Pittsburgh-based Cutler-Hammer supplies circuit breakers, motor starters, and other electrical equipment to industrial manufacturers such as Ford Motor Company. In response to the growing complexity and proliferation of its products, C-H developed "pods" of salespeople focused on a particular geographic region, industry, or market concentration. Each person brings a degree of expertise about a product or service. Now the salespeople can leverage the knowledge of co-workers to sell to increasingly sophisticated buying teams instead of working in isolation.[31]

Proposal Solicitation

The buyer invites qualified suppliers to submit proposals. If the item is complex or expensive, the buyer will require a detailed written proposal from each qualified supplier. After evaluating the proposals, the buyer will invite a few suppliers to make formal presentations.

Business marketers must be skilled in researching, writing, and presenting proposals. Written proposals should be marketing documents that describe value and benefits in customer terms. Oral presentations should inspire confidence, and position the company's capabilities and resources so that they stand out from the competition.

Consider the hurdles that Xerox has set up in qualifying suppliers.

XEROX

Xerox qualifies only suppliers who meet the ISO 9000 quality standards, but to win the company's top award—certification status—a supplier must first complete the Xerox Multinational Supplier Quality Survey. The survey requires the supplier to issue a quality assurance manual, to adhere to continuous improvement principles, and to demonstrate effective systems implementation. Once qualified, a supplier must participate in Xerox's Continuous Supplier Involvement process: The two companies work together to create specifications for quality, cost, delivery times, and process capability. The final step toward certification requires a supplier to undergo additional, rigorous quality training and an evaluation based on the same criteria as the Malcolm Baldridge National Quality Award. Not surprisingly, only 176 suppliers worldwide have achieved the 95 percent rating required for certification as a Xerox supplier.[32]

Supplier Selection

Before selecting a supplier, the buying center will specify desired supplier attributes and indicate their relative importance. To rate and identify the most attractive suppliers, buying centers often use a supplier-evaluation model such as the one shown in Table 7.2.

Business marketers need to do a better job of understanding how business buyers arrive at their valuations.[33] Anderson, Jain, and Chintagunta conducted a study of the main methods business marketers use to assess customer value and found eight different *customer value assessment (CVA)* methods. Companies tended to use the simpler methods, although the more sophisticated ones promise to produce a more accurate picture of customer perceived value. (See "Marketing Memo: Methods of Assessing Customer Value.")

The choice and importance of different attributes varies with the type of buying situation.[34] Delivery reliability, price, and supplier reputation are important for routine-order products. For procedural-problem products, such as a copying machine, the three most important attributes are technical service, supplier flexibility, and product reliability. For political-problem products that stir rivalries in the organization (such as the choice of a computer system), the most important attributes are price, supplier reputation, product reliability, service reliability, and supplier flexibility.

TABLE 7.2

An Example of Vendor Analysis

Attributes	Rating Scale				
	Importance Weights	Poor (1)	Fair (2)	Good (3)	Excellent (4)
Price	.30				x
Supplier reputation	.20			x	
Product reliability	.30				x
Service reliability	.10		x		
Supplier flexibility	.10			x	
Total score: .30(4) + .20(3) + .30(4) + .10(2) + .10(3) = 3.5					

MARKETING MEMO — METHODS OF ASSESSING CUSTOMER VALUE

1. ***Internal engineering assessment.*** Company engineers use laboratory tests to estimate the product's performance characteristics. Weakness: Ignores the fact that in different applications, the product will have different economic value.
2. ***Field value-in-use assessment.*** Customers are interviewed about cost elements associated with using the new-product offering compared to an incumbent product. The task is to assess how much each element is worth to the buyer.
3. ***Focus-group value assessment.*** Customers in a focus group are asked what value they would put on potential market offerings.
4. ***Direct survey questions.*** Customers are asked to place a direct dollar value on one or more changes in the market offering.
5. ***Conjoint analysis.*** Customers are asked to rank their preference for alternative market offerings or concepts. Statistical analysis is used to estimate the implicit value placed on each attribute.
6. ***Benchmarks.*** Customers are shown a "benchmark" offering and then a new-market offering. They are asked how much more they would pay for the new offering or how much less they would pay if certain features were removed from the benchmark offering.
7. ***Compositional approach.*** Customers are asked to attach a monetary value to each of three alternative levels of a given attribute. This is repeated for other attributes. The values are then added together for any offer configuration.
8. ***Importance ratings.*** Customers are asked to rate the importance of different attributes and the supplier firms' performance on these attributes.

Source: James C. Anderson, Dipak C. Jain, and Pradeep K. Chintagunta, "A Customer Value Assessment in Business Markets: A State-of-Practice Study," *Journal of Business-to-Business Marketing* 1, no. 1 (1993): 3–29.

The buying center may attempt to negotiate with preferred suppliers for better prices and terms before making the final selection. Despite moves toward strategic sourcing, partnering, and participation in cross-functional teams, buyers still spend a large chunk of their time haggling with suppliers on price. In 1998, 92 percent of buyers responding to a *Purchasing* magazine survey cited negotiating price as one of their top responsibilities. Nearly as many respondents said price remains a key criterion they use to select suppliers.[35]

Marketers can counter the request for a lower price in a number of ways. They may be able to show evidence that the "total cost of ownership," that is, the "life-cycle cost" of using their product is lower than that of competitors' products. They can also cite the value of the services the buyer now receives, especially if those services are superior to those offered by competitors.

Other approaches may also be used to counter intense price pressure. Consider the following example.

LINCOLN ELECTRIC

Lincoln Electric has a decades-long tradition of working with its customers to reduce costs through its Guaranteed Cost Reduction Program. When a customer insists that a Lincoln distributor lower prices to match Lincoln's competitors, the company and the particular distributor may guarantee that, during the coming year, they will find cost reductions in the customer's plant that meet or exceed the price difference between Lincoln's products and the competition's. If an independent audit at the end of the year does not reveal the promised cost savings, Lincoln Electric and the distributor compensate the customer for the difference. In all the years the program has been in existence, Lincoln has only had to write a check once or twice.[36]

As part of the buyer selection process, buying centers must decide how many suppliers to use. Companies are increasingly reducing the number of suppliers. Ford, Motorola, and Honeywell have cut the number of suppliers by anywhere from 20 to 80 percent. These companies want their chosen suppliers to be responsible for a larger component system; they want them to achieve continuous quality and performance improvement and at the same time lower the supply price each year by a given percentage. These companies expect their suppliers to work closely with them during product development, and they value their suggestions. There is even a trend toward single sourcing.

Companies that use multiple sources often cite the threat of a labor strike as the biggest deterrent to single sourcing. Another reason companies may be reluctant to use a single source is that they fear they will become too comfortable in the relationship and lose their competitive edge.

Order-Routine Specification

After selecting suppliers, the buyer negotiates the final order, listing the technical specifications, the quantity needed, the expected time of delivery, return policies, warranties, and so on. Many industrial buyers lease heavy equipment like machinery and trucks. The lessee gains a number of advantages: conserving capital, getting the latest products, receiving better service, and some tax advantages. The lessor often ends up with a larger net income and the chance to sell to customers who could not afford outright purchase.

In the case of maintenance, repair, and operating items, buyers are moving toward blanket contracts rather than periodic purchase orders. A blanket contract establishes a long-term relationship in which the supplier promises to resupply the buyer as needed, at agreed-upon prices, over a specified period of time. Because the stock is held by the seller, blanket contracts are sometimes called *stockless purchase plans*. The buyer's computer automatically sends an order to the seller when stock is needed. This system locks suppliers in tighter with the buyer and makes it difficult for out-suppliers to break in unless the buyer becomes dissatisfied with the in-supplier's prices, quality, or service.

Companies that fear a shortage of key materials are willing to buy and hold large inventories. They will sign long-term contracts with suppliers to ensure a steady flow of materials. DuPont, Ford, and several other major companies regard long-term supply planning as a major responsibility of their purchasing managers. For example, General Motors wants to buy from fewer suppliers who are willing to locate close to its plants and produce high-quality components. In addition, business marketers are using the Internet to set up extranets with important customers to facilitate and lower the cost of transactions. The customers enter orders directly on the computer, and these orders are automatically transmitted to the supplier. Some companies go further and shift the ordering responsibility to their suppliers in systems called *vendor-managed inventory*. These suppliers are privy to the customer's inventory levels and take responsibility to replenish it automatically through *continuous replenishment programs*.

"OTIFNE" is a term that summarizes three desirable outcomes of a B-to-B transaction:

- OT—deliver on time
- IF—in full
- NE—no error

All three matter. If a supplier achieves on-time compliance of only 80 percent, in-full compliance of 90 percent, and no error compliance of 70 percent, overall performance computes at 80% × 90% × 70%—only 50%!

Performance Review

The buyer periodically reviews the performance of the chosen supplier(s). Three methods are commonly used. The buyer may contact the end users and ask for their evaluations; the buyer may rate the supplier on several criteria using a weighted score method; or the buyer might aggregate the cost of poor performance to come up with adjusted costs of purchase, including price. The performance review may lead the buyer to continue, modify, or end a supplier relationship.

Many companies have set up incentive systems to reward purchasing managers for good buying performance, in much the same way that sales personnel receive bonuses for good selling performance. These systems are leading purchasing managers to increase pressure on sellers for the best terms.

MARKETING INSIGHT | ESTABLISHING CORPORATE TRUST AND CREDIBILITY

Strong bonds and relationships between firms depend on their perceived credibility. *Corporate credibility* refers to the extent to which customers believe that a firm can design and deliver products and services that satisfy their needs and wants. Corporate credibility relates to the reputation that a firm has achieved in the marketplace and is the foundation for a strong relationship. It is difficult for a firm to develop strong ties with another firm unless it is seen as highly credible.

Corporate credibility, in turn, depends on three factors:

- ***Corporate expertise***—the extent to which a company is seen as able to make and sell products or conduct services.
- ***Corporate trustworthiness***—the extent to which a company is seen as motivated to be honest, dependable, and sensitive to customer needs.
- ***Corporate likability***—the extent to which a company is seen as likable, attractive, prestigious, dynamic, and so on.

In other words, a credible firm is seen as being good at what it does; it keeps its customers' best interests in mind and is enjoyable to work with.

Trust is a particularly important determinant of credibility and a firm's relationships with other firms. Trust is reflected in the willingness and confidence of a firm to rely on a business partner. A number of interpersonal and interorganizational factors affect trust in a business-to-business relationship, such as the perceived competence, integrity, honesty, and benevolence of the firm. Trust will be affected by personal interactions between employees of a firm as well as opinions about the company as a whole, and perceptions of trust will evolve with more experience with a company.

Trust can be especially tricky in online settings, and firms often impose more stringent requirements on their online business partners. Business buyers worry that they won't get products of the right quality delivered to the right place at the right time. Sellers worry about getting paid on time—or at all—and how much credit they should extend. Some firms, such as transportation and supply chain management company Ryder System, are using tools such as automated credit-checking applications and online trust services to help determine the credibility of trading partners.

Sources: Robert M. Morgan and Shelby D. Hunt, "The Commitment–Trust Theory of Relationship Marketing," *Journal of Marketing* 58, no. 3 (1994): 20–38; Christine Moorman, Rohit Deshpande, and Gerald Zaltman, "Factors Affecting Trust in Market Research Relationships," *Journal of Marketing* 57 (January 1993): 81–101; Kevin Lane Keller and David A. Aaker, "Corporate-Level Marketing: The Impact of Credibility on a Company's Brand Extensions," *Corporate Reputation Review* 1 (August 1998): 356–378; Bob Violino, "Building B2B Trust," *Computerworld*, June 17, 2002, p. 32; Richard E. Plank, David A. Reid, and Ellen Bolman Pullins, "Perceived Trust in Business-to-Business Sales: A New Measure," *Journal of Personal Selling and Sales Management* 19, no. 3 (Summer 1999): 61–72.

::: Managing Business-to-Business Customer Relationships

To improve effectiveness and efficiency, business suppliers and customers are exploring different ways to manage their relationships. Closer relationships are driven in part by trends related to supply chain management, early supplier involvement, purchasing alliances, and so on.[37] Cultivating the right relationships with business is paramount with any holistic marketing program.

The Benefits of Vertical Coordination

Much research has advocated greater vertical coordination between buying partners and sellers so that they transcend mere transactions to engage in activities that create more value for both parties. Building trust between parties is often seen as one prerequisite to healthy long-term relationships.[38] "Marketing Insight: Establishing Corporate Trust and Credibility" identifies some key dimensions of those concepts. Consider the mutual benefits from the following arrangement.

MOTOMAN INC. AND STILLWATER TECHNOLOGIES

Motoman Inc., a leading supplier of industry robotic systems, and Stillwater Technologies, a contract tooling and machinery company and a key supplier to Motoman, are tightly integrated. Not only do they occupy office and manufacturing space in the same facility, but their telephone and computer systems are linked, and they share a common lobby, conference room, and employee cafeteria. Philip V. Morrison, chairman and

CEO of Motoman, says it is like "a joint venture without the paperwork." Short delivery distances are just one benefit of the unusual partnership. Also key is the fact that employees of both companies have ready access to one another and can share ideas on improving quality and reducing costs. This close relationship has opened the door to new opportunities. Both companies had been doing work for Honda Motor Company, and Honda suggested that they work together on systems projects. The integration makes the two bigger than they are individually.[39]

One historical study of four very different business-to-business relationships found that several factors, by affecting partner interdependence and/or environmental uncertainty, influenced the development of a relationship between business partners.[40] The relationship between advertising agencies and clients illustrates these findings:

1. ***In the relationship formation stage, one partner experienced substantial market growth.*** Manufacturers capitalizing on mass-production techniques developed national brands, which increased the importance and amount of mass-media advertising.
2. ***Information asymmetry between partners was such that a partnership would generate more profits than if the partner attempted to invade the other firm's area.*** Advertising agencies had specialized knowledge that their clients would have had difficulty obtaining.
3. ***At least one partner had high barriers to entry that would prevent the other partner from entering the business.*** Advertising agencies could not easily become national manufacturers, and for years, manufacturers were not eligible to receive media commissions.
4. ***Dependence asymmetry existed such that one partner was more able to control or influence the other's conduct.*** Advertising agencies had control over media access.
5. ***One partner benefited from economies of scale related to the relationship.*** Ad agencies gained by providing the same market information to multiple clients.

Cannon and Perreault found that buyer–supplier relationships differed according to four factors: availability of alternatives; importance of supply; complexity of supply; and supply market dynamism. Based on these four factors, they classified buyer–supplier relationships into eight different categories:[41]

1. ***Basic buying and selling*** – relatively simple, routine exchanges with moderately high levels of cooperation and information exchange.
2. ***Bare bones*** – similar to basic buying and selling but more adaptation by the seller and less cooperation and information exchange.
3. ***Contractual transaction*** – generally low levels of trust, cooperation, and interaction; exchange is defined by formal contract.
4. ***Customer supply*** – traditional custom supply situation where competition rather than cooperation is the dominant form of governance.
5. ***Cooperative systems*** – although coupled closely in operational ways, neither party demonstrates structural commitment through legal means or adaptation approaches.
6. ***Collaborative*** – much trust and commitment leading to true partnership.
7. ***Mutually adaptive*** – much relationship-specific adaptation for buyer and seller, but without necessarily strong trust or cooperation.
8. ***Customer is king*** – although bonded by a close, cooperative relationship, the seller adapts to meet the customer's needs without expecting much adaptation or change on the part of the customer in exchange.

Some firms find that their needs can be satisfied with fairly basic supplier performance. They do not want or require a close relationship with a supplier. Alternatively, some suppliers may not find it worth their while to invest in customers with limited growth potential. One study found that the closest relationships between customers and suppliers arose when the supply was important to the customer and when there were procurement obstacles such as complex purchase requirements and few alternative suppliers.[42] Another study suggested that greater vertical coordination between buyer and seller through information exchange and planning is usually necessary only when high environmental uncertainty exists and specific investments are modest.[43]

Business Relationships: Risks and Opportunism

Buvik and John note that in establishing a customer–supplier relationship, there is tension between safeguarding and adaptation. Vertical coordination can facilitate stronger customer–seller ties but at the same time may increase the risk to the customer's and supplier's specific investments. *Specific investments* are those expenditures tailored to a particular company and value chain partner (e.g., investments in company-specific training, equipment, and operating procedures or systems).[44] Specific investments help firms grow profits and achieve their positioning.[45] For example, Xerox has worked closely with its suppliers to develop customized processes and components that reduced its copier-manufacturing costs by 30 to 40 percent. In return, suppliers received sales and volume guarantees, an enhanced understanding of their customer needs, and a strong position with Xerox for future sales.[46]

Specific investments, however, also entail considerable risk to both customer and supplier. Transaction theory from economics maintains that because these investments are partially sunk, they lock in the firms that make the investments to a particular relationship. Sensitive cost and process information may need to be exchanged. A buyer may be vulnerable to holdup because of switching costs; a supplier may be more vulnerable to holdup in future contracts because of dedicated assets and/or expropriation of technology/knowledge. In terms of the latter risk, consider the following example.[47]

An automobile component manufacturer wins a contract to supply an under-hood component to an original equipment manufacturer (OEM). A one-year, sole-source contract safeguards the supplier's OEM-specific investments in a dedicated production line. However, the supplier may also be obliged to work (noncontractually) as a partner with the OEM's internal engineering staff (using linked computing facilities) to exchange detailed engineering information and coordinate frequent design and manufacturing changes over the term of the contract. These interactions could reduce costs and/or increase quality by improving the firm's responsiveness to marketplace changes. Such interactions could also potentially magnify the threat to the supplier's intellectual property.

When buyers cannot easily monitor supplier performance, the supplier might shirk or cheat and not deliver the expected value. *Opportunism* can be thought of as "some form of cheating or undersupply relative to an implicit or explicit contract."[48] It may involve blatant self-interest and deliberate misrepresentation that violates contractual agreements. In creating the 1996 version of the Ford Taurus, Ford Corporation chose to outsource the whole process to one supplier, Lear Corporation. Lear committed to a contract that, for various reasons, it knew it was unable to fulfill. According to Ford, Lear missed deadlines, failed to meet weight and price objectives, and furnished parts that did not work.[49] A more passive form of opportunism might involve a refusal or unwillingness to adapt to changing circumstances.

Opportunism is a concern because firms must devote resources to control and monitoring that otherwise could be allocated to more productive purposes. Contracts may become inadequate to govern supplier transactions when supplier opportunism becomes difficult to detect; as firms make specific investments in assets that cannot be used elsewhere; and as contingencies are harder to anticipate. Customers and suppliers are more likely to form a joint venture (versus a simple contract) when the supplier's degree of asset specificity is high, monitoring the supplier's behavior is difficult, and the supplier has a poor reputation.[50] When a supplier has a good reputation, for example, it is more likely to avoid opportunism to protect this valuable intangible asset.

The presence of a significant future time horizon and/or strong solidarity norms so that customers and suppliers are willing to strive for joint benefits can cause a shift in the effect of specific investments, from expropriation (increased opportunism on the receiver's part) to bonding (reduced opportunism).[51]

::: Institutional and Government Markets

Our discussion has concentrated largely on the buying behavior of profit-seeking companies. Much of what we have said also applies to the buying practices of institutional and government organizations. However, we want to highlight certain special features of these markets.

The **institutional market** consists of schools, hospitals, nursing homes, prisons, and other institutions that must provide goods and services to people in their care. Many of these organizations are characterized by low budgets and captive clienteles. For example, hospitals have to decide what quality of food to buy for patients. The buying objective here is not profit, because the food is provided as part of the total service package; nor is cost minimization the sole objective, because poor food will cause patients to complain and hurt the hospital's reputation. The hospital purchasing agent has to search for institutional-food vendors whose quality meets or exceeds a certain minimum standard and whose prices are low. In fact, many food vendors set up a separate division to sell to institutional buyers because of these buyers' special needs and characteristics. Heinz produces, packages, and prices its ketchup differently to meet the requirements of hospitals, colleges, and prisons. Aramark Corp., has a competitive advantage when it comes to providing food for the nation's prisons, a direct result of refining its purchasing practices and its supply chain management:

ARAMARK CORP.

Where Aramark once merely selected products from lists provided by potential suppliers, it now collaborates with suppliers to develop products that Aramark customizes to meet the needs of individual segments. In the corrections segment, quality has historically been sacrificed to meet food costs operators outside that market would find impossible to work with. "When you go after business in the corrections field, you are making bids that are measured in hundredths of a cent," says John Zillmer, president of Aramark's Food & Support Services, "So any edge we can gain on the purchasing side is extremely valuable." Aramark took a series of protein products and sourced them with unique partners at price points it never could have imagined before. It was able to drive costs down by working with partners who understood the chemistry of proteins and knew how to do things to lower the price but which could still create a product very acceptable to Aramark's customers. Then Aramark replicated this process with 163 different items formulated exclusively for corrections. Rather than reduce food costs by increments of a penny or so a meal, which was the previous norm for this market, Aramark succeeded in taking 5 to 9 cents off a meal—while maintaining or even improving quality.[52]

Being a supplier of choice for the nation's schools or hospitals means big business:

CARDINAL HEALTH

A spinoff of Baxter Healthcare Corporation, Cardinal Health has become the largest supplier of medical, surgical, and laboratory products in the United States. The company's stockless inventory program, known as ValueLink, was cited as a "best practice" by Arthur Andersen's business consulting practice. Currently in service at over 150 acute-care hospitals in the United States, this program supplies hospital personnel with the products they need when and where they need them. An integrated system meets the needs of customers who deal with life-and-death situations every minute. In the old system, an 18-wheeler simply dropped off a week's or a month's worth of supplies at the back door of a hospital. It inevitably turned out that the items most in demand were the ones in short supply, whereas the ones the hospital never used were available in great number. Cardinal Health estimates that its ValueLink system saves customers an average of $500,000 or more each year.[53]

In most countries, government organizations are a major buyer of goods and services. Government organizations typically require suppliers to submit bids, and normally they award the contract to the lowest bidder. In some cases, the government unit will make allowance for the supplier's superior quality or reputation for completing contracts on time. Governments will also buy on a negotiated contract basis, primarily in the case of complex projects involving major R&D costs and risks and in cases where there is little competition. Government organizations tend to favor domestic suppliers. A major complaint of multinationals operating in Europe was that each country showed favoritism toward its nationals in spite of superior offers available from foreign firms. The European Union is removing this bias.

Because their spending decisions are subject to public review, government organizations require considerable paperwork from suppliers, who often complain about excessive paperwork, bureaucracy, regulations, decision-making delays, and frequent shifts in procurement personnel. Given all the red tape, why would any firm want to do business

Cardinal Health ad directed to pharmacists that focuses on its ability to partner with customers to help them manage inventory, drug utilization, and medication safety issues.

with the U.S. government? Here is how Paul E. Goulding, a Washington, DC–based consultant who has helped clients obtain more than $30 billion in government contracts, answers that question:[54]

> When I hear that question, I tell the story of the businessman who buys a hardware store after moving to a small town. He asks his new employees who the biggest hardware customer in town is. He is surprised to learn that the customer isn't doing business with his store. When the owner asks why not, his employees say the customer is difficult to do business with and requires that a lot of forms be filled out. I point out that the same customer is probably very wealthy, doesn't bounce his checks, and usually does repeat business when satisfied. That's the type of customer the federal government can be.

The U.S. government buys goods and services valued at $200 billion. That makes Uncle Sam the largest customer in the world. It is not just the dollar figure that is large, but the number of individual acquisitions. According to the General Sources Administration Procurement Data Center, over 20 million individual contract actions are processed every year. Although most items purchased are between $2,500 and $25,000, the government also makes purchases in the billions, many of them in technology. But government decision makers often think that technology vendors have not done their homework. In addition, vendors do not pay enough attention to cost justification, which is a major activity for government procurement professionals. Companies hoping to be government contractors need to help government agencies see the bottom-line impact of products.

Just as companies provide government agencies with guidelines on how best to purchase and use their products, governments provide would-be suppliers with detailed guidelines describing how to sell to the government. Not following the guidelines properly and filling out forms and contracts incorrectly can create a legal nightmare.[55] Suppliers have to master the system and try to find ways to cut through the red tape. Goulding says that it requires an investment of time, money, and resources not unlike what is required for entering a new market overseas.

ADI TECHNOLOGY

The federal government has always been ADI Technology Corporation's most important client: Federal contracts account for about 90 percent of its nearly $6 million in annual revenues. Yet managers at this professional services company often shake their heads at all the work that goes into winning the coveted government contracts. A comprehensive bid proposal will run from 500 to 700 pages because of federal paperwork requirements. The company's president estimates that the firm has spent as much as $20,000, mostly in worker hours, to prepare a single bid proposal.

Fortunately for businesses of all sizes, the federal government has been trying to simplify the contracting procedure and make bidding more attractive. Some reforms place more emphasis on buying commercial off-the-shelf items instead of items built to the government's specs; online communication with vendors to eliminate the massive paperwork; and a "debriefing" from the appropriate government agency for vendors who lose a bid, enabling them to increase their chances of winning the next time around.[56] The government's goal is to get all purchases online. To do this, the government is likely to bet on Web-based forms, digital signatures, and electronic procurement cards (P-cards).[57]

Several federal agencies that act as purchasing agents for the rest of the government have launched Web-based catalogs that allow authorized defense and civilian agencies to buy everything from medical and office supplies to clothing online. "Marketing Memo: Selling Tech to the Government" provides some tips for attacking that multibillion-dollar market. The General Services Administration, for example, not only sells stocked merchandise through its Web site, but also creates direct links between buyers and contract suppliers.

In spite of these reforms, for a number of reasons many companies that sell to the government have not used a marketing orientation. The government's procurement policies have traditionally emphasized price, leading suppliers to invest considerable effort in bringing costs down. Where product characteristics are carefully specified, product differentia-

MARKETING MEMO | SELLING TECH TO THE GOVERNMENT

The U.S. government is projected to spend $65.9 billion on IT in fiscal year 2006. A large chunk of this U.S. government business, however, isn't contracted out at all. Through the General Services Administration (GSA) and other government organizations, companies can sell directly to agencies without having to go to formal bidding. Here are three tips for how to tap into that market.

1. ***Get in the Government IT Catalog.*** The GSA runs an online catalog of goods and services for government agencies. About 28 percent of federal spending flows through the catalog's Schedule 70, which includes more than 2000 tech vendors. Getting a business listed can be important. Applications can be done electronically. Remember to spell out pricing structure carefully.
2. ***Work Your Way In.*** Small businesses—especially those owned by women and minorities—are often needed by large businesses to satisfy small business set-asides. To maximize that probability:
   - ***Make sure contractors can find you.*** Get listed on the Small Business Administration's Subcontracting Network (wed.sba.gov/subnet) or use the U.S. Chamber of Commerce Web site.
   - ***Stay on top of key contracts.*** Several Web sites provide updates for the latest deals that might provide opportunities (www.fedbizopps.gov; www.dodbusopps.com; prod.nais.nasa.gov/pub/fedproc/home.hml).
   - ***Work the angles.*** Meet with prospective bidders and explain your qualifications.
3. ***Network Actively.*** Attend one of the large trade shows, such as FOSE, GSA Expo, or E-Gov.

Source: Owen Thomas, "How to Sell Tech to the Feds," *Business 2.0*, March 2003, pp. 111–112.

tion is not a marketing factor; nor are advertising and personal selling of much consequence in winning bids. Some companies have pursued government business by establishing separate government marketing departments.

Companies such as Gateway, Rockwell, Kodak, and Goodyear anticipate government needs and projects, participate in the product specification phase, gather competitive intelligence, prepare bids carefully, and produce strong communications to describe and enhance their companies' reputations.

SUMMARY :::

1. Organizational buying is the decision-making process by which formal organizations establish the need for purchased products and services, then identify, evaluate, and choose among alternative brands and suppliers. The business market consists of all the organizations that acquire goods and services used in the production of other products or services that are sold, rented, or supplied to others.
2. Compared to consumer markets, business markets generally have fewer and larger buyers, a closer customer–supplier relationship, and more geographically concentrated buyers. Demand in the business market is derived from demand in the consumer market and fluctuates with the business cycle. Nonetheless, the total demand for many business goods and services is quite price-inelastic. Business marketers need to be aware of the role of professional purchasers and their influencers, the need for multiple sales calls, and the importance of direct purchasing, reciprocity, and leasing.
3. The buying center is the decision-making unit of a buying organization. It consists of initiators, users, influencers, deciders, approvers, buyers, and gatekeepers. To influence these parties, marketers must be aware of environmental, organizational, interpersonal, and individual factors.
4. The buying process consists of eight stages called buyphases: (1) problem recognition, (2) general need description, (3) product specification, (4) supplier search, (5) proposal solicitation, (6) supplier selection, (7) order-routine specification, and (8) performance review.
5. Business marketers must form strong bonds and relationships with their customers and provide them added value. Some customers, however, may prefer more of a transactional relationship.
6. The institutional market consists of schools, hospitals, nursing homes, prisons, and other institutions that provide goods and services to people in their care. Buyers for government organizations tend to require a great deal of paperwork from their vendors and to favor open bidding and domestic companies. Suppliers must be prepared to adapt their offers to the special needs and procedures found in institutional and government markets.

APPLICATIONS :::

Marketing Debate How Different is Business-to-Business Marketing?

Many business-to-business marketing executives lament the challenges of business-to-business marketing, maintaining that many traditional marketing concepts and principles do not apply. For a number of reasons, they assert that selling products and services to a company is fundamentally different from selling to individuals. Others disagree, claiming that marketing theory is still valid and only involves some adaptation in the marketing tactics.

Take a position: Business-to-business marketing requires a special, unique set of marketing concepts and principles versus Business-to-business marketing is really not that different and the basic marketing concepts and principles apply.

Marketing Discussion

Consider some of the consumer behavior topics from Chapter 6. How might you apply them to business-to-business settings? For example, how might noncompensatory models of choice work?

MARKETING SPOTLIGHT | GENERAL ELECTRIC

GE is an amazingly large company made up of 11 major divisions that operate in areas as diverse as home appliances, jet engines, security systems, wind turbines, and financial services. The company is so large (2003 revenues of $134 billion) that even if each of its 11 business units were ranked separately, all would appear on the *Fortune* 500 list. If GE were its own country, it would be one of the 50 largest and would rank ahead of Finland, Israel, and Ireland.

GE became the acknowledged pioneer in business-to-business marketing in the 1950s and 1960s. Back then, GE's tagline was "Live Better Electrically." As the company diversified its product lines, it created new campaigns, including "Progress for People" and "We bring good things to life."

In 2003, the company faced a new challenge: how to promote its brand globally with a unified message. GE launched a major new campaign, "Imagination at Work," which earned it the 2003 B2B Best Award for a top integrated campaign. The purpose of the campaign was not simply to create warm feelings for the company, but to achieve real business results. The campaign promoted GE's B2B units such as GE Aircraft Engines, GE Medical Systems, and GE Plastics. The goal was to unify these divisions under the GE brand while giving them a voice. The new campaign highlights the breadth of GE's product offerings.

GE spends some $150 million on corporate advertising—a large sum, but a sum that gains efficiencies by focusing on the core GE brand. The challenge with creating a unified message was that each GE business had to fit with that brand image. GE chose "Imagination at Work" because it portrayed the innovation inherent in all its wide-ranging products.

The new integrated campaign got results. "Research indicates GE is now being associated with attributes such as being high-tech, leading-edge, innovative, contemporary and creative," said Judy Hu, GE's general manager for global advertising and branding. Just as encouraging, market research found that respondents still associate GE with some of its traditional attributes, such as being trustworthy and reliable.

"We believe 'Imagination at Work' has proven to be a strong global message for us," said GE's chief marketing officer Beth Comstock. "Our goal is to be more present around the world and more consistent. To do it more broadly and faster. Going forward, you'll see medical and health care as the face of GE."

While the campaign unites all the GE business units, GE's success rests on its ability to understand the business market and the business buying process. GE puts itself in the shoes of its business customers. Consider, for example, its approach to pricing its aircraft engines. One would expect GE to charge a particular price for a particular engine type. But GE is aware that for the customer, purchasing an aircraft engine is a multimillion-dollar expenditure ($21 million for each large engine). And the expenditure doesn't end with the purchase of the engine—customers (airlines) face substantial maintenance costs to meet FAA guidelines and ensure the reliability of engines. So in 1999, GE pioneered a new pricing option. The concept, called "Power by the Hour," gives its customers an opportunity to pay a fixed fee each time they run the engine. In return, GE performs all of the maintenance and guarantees the reliability of the engine. GE gives its customers a lower cost of ownership of the GE aircraft engine.

Business buyers value this option because it shifts risk away from them. In times of uncertain air travel, buying new jet engines for new airliners is a major financial risk. "Power by the Hour" lets the airlines pay only when they use the engine. Moreover, airlines do not have to worry about unexpected high maintenance costs. Buyers are assured a low, predictable cost of ownership through the preset pricing.

This kind of B2B savvy has helped GE cement its top position in the *Financial Times* World's Most Respected Companies survey. Chief executives from 20 countries have given GE the top spot in the survey for 6 years.

GE's understanding of the business markets, its way of doing business, and its brand marketing have kept GE's brand equity growing. Indeed, its brand equity was valued at $53.6 billion by Corebrand in the fourth quarter of 2003.

"The GE brand is what connects us all and makes us so much better than the parts," Chief Marketing Officer Comstock said.

Discussion Questions

1. What have been the key success factors for GE?
2. Where is GE vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should they be sure to do with its marketing?

Sources: Michael Skapinker, "Brand Strength Proves Its Worth," *Financial Times*, January 20, 2004; Sean Callahan, "Exclusive: Microsoft, GE Top Brand Equity Study," *BtoB*, January 19, 2004; "Marketer of the Year Special Report," *BtoB*, December 8, 2003, pp. 16, 22; "More Imagination," *Delaney Report*, October 20, 2003, p. 1; Sean Callahan, "BtoB Q&A: New GE CMO Taps 'Imagination'," *BtoB*, August 11, 2003; <www.ge.com>.

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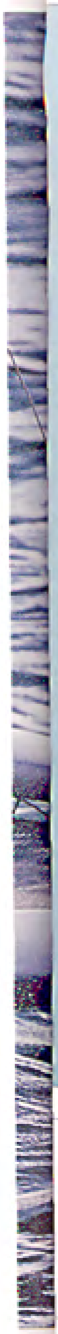
IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What are the different levels of market segmentation?
2. How can a company divide a market into segments?
3. How should a company choose the most attractive target markets?
4. What are the requirements for effective segmentation?

CHAPTER 8 ::: IDENTIFYING MARKET SEGMENTS AND TARGETS

Markets are not homogeneous. A company cannot connect with all customers in large, broad, or diverse markets. Consumers vary on many dimensions and often can be grouped according to one or more characteristics. A company needs to identify which market segments it can serve effectively. Such decisions require a keen understanding of consumer behavior and careful strategic thinking. Marketers sometimes mistakenly pursue the same market segment as many other firms and overlook some potentially more lucrative segments.

The magnitude and wealth of older consumers, for example, should be important to many different marketers.[1] The population of mature consumers, those 50 and older, will swell to 115 million in the next 25 years. Yet, not only have youth-obsessed marketers traditionally neglected this huge market, they have also turned them off with stereotypes of grandmas and grandpas living on fixed incomes.[2] "To young product managers, everyone over 45 is lumped into a category called old," says Lori Bitter, partner at J. Walter Thompson's Mature Marketing Group. "They want to put swing music in the background of an ad targeted at 50-year-olds. We have to say, 'No, let's try Sting'." Seniors, particularly boomers-turned-seniors, often make buying decisions based on lifestyle, not age. But don't expect them to remain loyal once they've made a decision. Although highly brand-conscious and brand-aware, baby boomers are not necessarily as brand loyal as traditionally was the case >>>



A rapidly growing target market: Mature consumers who live active lives and who make buying decisions based not on age, but on lifestyle.

with older consumers.[3] With their allegiances potentially up for grabs, astute markets would be wise to keep their eyes on them.[4]

To compete more effectively, many companies are now embracing target marketing. Instead of scattering their marketing effort (a "shotgun" approach), they focus on those consumers they have the greatest chance of satisfying (a "rifle" approach).

Effective target marketing requires that marketers:

1. Identify and profile distinct groups of buyers who differ in their needs and preferences (market segmentation).
2. Select one or more market segments to enter (market targeting).
3. For each target segment, establish and communicate the distinctive benefit(s) of the company's market offering (market positioning).

This chapter will focus on the first two steps. Chapter 10 discusses brand and market positioning.

::: Levels of Market Segmentation

The starting point for discussing segmentation is **mass marketing**. In mass marketing, the seller engages in the mass production, mass distribution, and mass promotion of one product for all buyers. Henry Ford epitomized this strategy when he offered the Model-T Ford in one color, black. Coca-Cola also practiced mass marketing when it sold only one kind of Coke in a 6.5-ounce bottle.

The argument for mass marketing is that it creates the largest potential market, which leads to the lowest costs, which in turn can lead to lower prices or higher margins. However, many critics point to the increasing splintering of the market, which makes mass marketing more difficult. The proliferation of advertising media and distribution channels is making it difficult and increasingly expensive to reach a mass audience. Some claim that mass marketing is dying. Most companies are turning to *micromarketing* at one of four levels: segments, niches, local areas, and individuals.

Segment Marketing

A market segment consists of a group of customers who share a similar set of needs and wants. Thus we distinguish between car buyers who are primarily seeking low-cost basic transportation, those seeking a luxurious driving experience, and those seeking driving thrills and performance. We must be careful not to confuse a *segment* and a *sector*. A car company might say that it will target young, middle-income car buyers. The problem is that young, middle-income car buyers will differ about what they want in a car. Some will want a low-cost car and others will want an expensive car. Young, middle-income car buyers are a sector, not a segment.

The marketer does not create the segments; the marketer's task is to identify the segments and decide which one(s) to target. Segment marketing offers key benefits over mass marketing. The company can presumably better design, price, disclose and deliver the product or service to satisfy the target market. The company also can fine-tune the marketing program and activities to better reflect competitors' marketing.

The Model T: Henry Ford was the first to mass-market automobiles. Ford mass-produced by assembly line, mass-distributed through dealers, and mass-promoted one product for all buyers in ads like these.

However, even a segment is partly a fiction, in that not everyone wants exactly the same thing. Anderson and Narus have urged marketers to present flexible market offerings to all members of a segment.[5]

A **flexible market offering** consists of two parts: a *naked solution* containing the product and service elements that all segment members value, and *discretionary options* that some segment members value. Each option might carry an additional charge. For example, Delta Airlines offers all economy passengers a seat and soft drinks. It charges economy passengers extra for alcoholic beverages. Siemens Electrical Apparatus Division sells metal-clad boxes to small manufacturers whose price includes free delivery and a warranty, but also offers installation, tests, and communication peripherals as extra-cost options.

Market segments can be defined in many different ways. One way to carve up a market is to identify *preference segments*. Suppose ice cream buyers are asked how much they value sweetness and creaminess as two product attributes. Three different patterns can emerge.

1. ***Homogeneous preferences*** – Figure 8.1(a) shows a market where all the consumers have roughly the same preferences. The market shows no natural segments. We would predict that existing brands would be similar and cluster around the middle of the scale in both sweetness and creaminess.
2. ***Diffused preferences*** – At the other extreme, consumer preferences may be scattered throughout the space (Figure 8.1[b]), indicating that consumers vary greatly in their preferences. The first brand to enter the market is likely to position itself to appeal to the most people. A second competitor could locate next to the first brand and fight for market share, or it could locate in a corner to attract a customer group that was not satisfied with the center brand. If several brands are in the market, they are likely to position themselves throughout the space and show real differences to match differences in consumer preference.

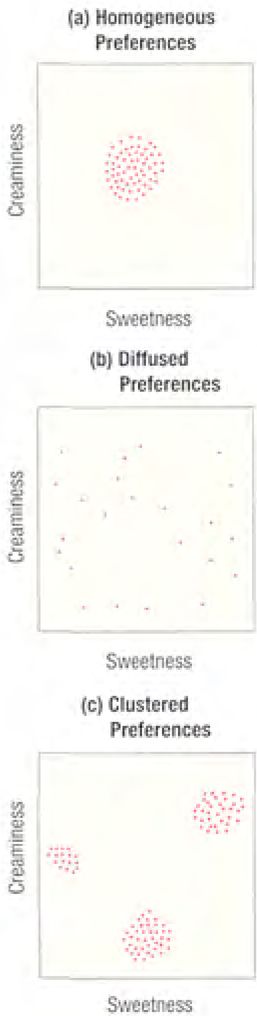


FIG. 8.1

Basic Market-Preference Patterns

3. ***Clustered preferences*** – The market might reveal distinct preference clusters, called *natural market segments* (Figure 8.1[c]). The first firm in this market has three options. It might position in the center, hoping to appeal to all groups. It might position in the largest market segment (*concentrated marketing*). It might develop several brands, each positioned in a different segment. If the first firm developed only one brand, competitors would enter and introduce brands in the other segments.

Later in this chapter, we will consider various ways to segment and compete in a market.

Niche Marketing

A niche is a more narrowly defined customer group seeking a distinctive mix of benefits. Marketers usually identify niches by dividing a segment into subsegments. For example, Progressive, a Cleveland auto insurer, sells "nonstandard" auto insurance to risky drivers with a record of auto accidents, charges a high price for coverage and makes a lot of money in the process.

An attractive niche is characterized as follows: The customers in the niche have a distinct set of needs; they will pay a premium to the firm that best satisfies their needs; the niche is not likely to attract other competitors; the nicher gains certain economies through specialization; and the niche has size, profit, and growth potential. Whereas segments are fairly large and normally attract several competitors, niches are fairly small and normally attract only one or two.

ENTERPRISE

Enterprise Rent-A-Car has challenged Hertz's supremacy in the rental car market by tailoring its marketing program to a relatively neglected target market.[6] While Hertz, Avis, Alamo, and others specialize in airport rental cars for business and leisure travelers, Enterprise has attacked the low-budget, insurance-replacement market by primarily renting to customers whose cars have been wrecked or stolen. Enterprise charges low rental rates by avoiding expensive airport and downtown locations, by only opening for daylight hours, and by holding on to its fleet of cars for a longer period of time before replacing them. Enterprise also distinguishes itself, in part, by offering to pick up customers. Enterprise has a limited advertising budget, relying more on a grassroots marketing push based on referrals from insurance agents and adjusters, car dealers, body shops, and garages. By creating unique associations to low cost and convenience in an overlooked niche market, Enterprise has been highly profitable.

Larger companies, such as IBM, have lost pieces of their market to nichers: This confrontation has been labeled "guerrillas against gorillas."[7] Some large companies have even turned to niche marketing. Hallmark commands a 55 percent share of the $7.8 billion global greeting card market by rigorously segmenting its greeting card business. In addition to popular sub-branded card lines like the humorous Shoebox Greetings, Hallmark has introduced lines targeting specific market segments. Fresh Ink targets 18- to 39-year-old women, Hallmark En Espanol targets Hispanic card givers, and Out of the Blue targets those who want inexpensive cards that can be sent for no reason.[8]

Niche marketers presumably understand their customers' needs so well that the customers willingly pay a premium. Tom's of Maine all-natural personal care products sometimes commands a 30 percent premium on its toothpaste because its unique, environmentally friendly products and charitable donation programs appeal to consumers who have been turned off by big businesses.[9] As marketing efficiency increases, niches that were seemingly too small may become more profitable.[10]

In the world of pharmaceuticals, biotech company Genentech stands out for developing drugs that target tiny niche markets instead of going after blockbusters like Pfizer's Lipitor or Merck's Zocor, cholesterol medications that rack up billions of dollars in sales:

GENENTECH

San Francisco–based Genentech pursues "targeted therapies," drugs aimed at relatively small subsets of patients. The drugs produce the same kind of dramatic benefit doctors get when they identify the specific type of bacteria causing an infection and slam it with the right antibiotic. A few years ago, the company launched the first highly targeted therapy—Herceptin, a breast-cancer drug that is prescribed only to the

Niche marketer Tom's of Maine makes environmentally friendly products and participates in a number of environmental action programs, like the Tom's of Maine National Rivers Awareness Program™

25 percent or so of patients whose tumors harbor a particular genetic quirk—and it hasn't looked back. Genentech's targeted therapies make economic sense because the company is small, doesn't need to sell billions of dollars of drugs each year to support an army of sales reps or marketing executives, and can charge premium prices because its anti-cancer drugs really work. Genentech's revenues were $3.3 billion in 2003, up 24 percent from 2001.[11]

Globalization has facilitated niche marketing. For example, the German economy has more than 300,000 small and midsize companies (known as *the Mittelstand*). Many enjoy over 50 percent market share in well-defined global niches. Hermann Simon dubbed these global niche leaders "hidden champions."[12] Here are some examples:

- Tetra Food supplies 80 percent of the food for feeding pet tropical fish.
- Hohner has 85 percent of the world harmonica market.
- Becher has 50 percent of the world's oversized umbrella market.
- Steiner Optical has 80 percent of the world's military field glasses market.

These hidden champions tend to be found in stable markets, are typically family owned or closely held, and are long lived. They are dedicated to their customers and offer superior performance, responsive service, and punctual delivery (rather than low price) as well as customer intimacy. Senior management emphasizes continuous innovation and stays in direct and regular contact with top customers.

The low cost of setting up shop on the Internet has also led to many small business start-ups aimed at niches. The recipe for Internet niching success: Choose a hard-to-find product that customers do not need to see and touch. This "Webpreneur" followed the recipe with astonishing results:[13]

OSTRICHESONLINE.COM

Whereas Internet giants like Amazon.com struggled to realize a profit, Steve Warrington is earning a six-figure income selling ostriches—and every product derived from them—online (www.ostrichesonline.com). Since the site was launched for next to nothing in 1996, Warrington's business has sold to over 20,000 clients in over 125 countries from a catalog of more than 17,500 ostrich-related products. Visitors to the site can buy ostrich meat, feathers, leather jackets, videos, eggshells, and subscribe to a newsletter devoted to ostriches.[14]

Local Marketing

Target marketing is leading to marketing programs tailored to the needs and wants of local customer groups (trading areas, neighborhoods, even individual stores). Citibank provides different mixes of banking services in its branches, depending on neighborhood demographics. Kraft helps supermarket chains identify the cheese assortment and shelf positioning that will optimize cheese sales in low-, middle-, and high-income stores, and in different ethnic neighborhoods.

AMERICAN DRUG

American Drug, one of the largest U.S. drugstore retailers, had its marketing team assess shopping patterns at hundreds of its Osco and Sav-on Drug Stores on a market-by-market basis. Using scanned data, the company fine-tuned the stores' product mix, revamped store layout, and refocused marketing efforts to more closely align with local consumer demand. Depending on the local demographics, each store unit varies the amount and type of merchandise in such categories as hardware, electrical supplies, automotive supplies, cookware, over-the-counter drugs, and convenience goods.[15]

Local marketing reflects a growing trend called grassroots marketing. Marketing activities concentrate on getting as close and personally relevant to individual customers as possible. Much of Nike's initial success has been attributed to the ability to engage target consumers through grassroots marketing such as sponsorship of local school teams, expert-conducted clinics, and provision of shoes, clothing, and equipment.

A large part of local, grassroots marketing is experiential marketing, which promotes a product or service not just by communicating its features and benefits, but by also connecting it with unique and interesting experiences. One marketing commentator describes experiential marketing this way: "The idea is not to sell something, but to demonstrate how a brand can enrich a customer's life."[16] "Marketing Insight: Experiential Marketing" describes the concept of Customer Experience Management.

Holiday Inn Hotels and Resorts is trying to recharge its faded brand image through experiential marketing aimed not only at creating new customer experiences, but also at getting customers to kindle nostalgia for their own childhood experiences with the brand:

HOLIDAY INN HOTELS AND RESORTS

The chain that grew up with the Interstate System and defined the overnight roadside experience is trying to push itself back into Americans' consciousness. The marketing push is geared at evoking the good old days when its popularity was reflected in stolen towels—the chain claims it still loses 560,000 towels annually. So in 2003, Holiday Inn designated August 28 as "National Towel Amnesty Day." Extending through Labor Day weekend, each Holiday Inn distributed 50 limited edition towels that read, "100 percent cotton, 100 percent guilt-free, 100 percent yours." In addition, the chain created an Internet site at www.holiday-inn.com/towels where visitors could share towel stories. For each story collected, $1 was donated to a charity benefiting children with life-threatening diseases who wish to visit central Florida attractions. By getting customers involved in swapping stories, the hotel chain hopes to play up the emotional connection many Americans still have with its simple, dependable, white-bread image.[17]

Pine and Gilmore, who are pioneers on the topic, have argued that we are on the threshold of the "Experience Economy," a new economic era in which all businesses must orchestrate memorable events for their customers.[18] They assert:

- If you charge for stuff, then you are in the *commodity business.*
- If you charge for tangible things, then you are in the *goods business.*
- If you charge for the activities you perform, then you are in the *service business.*
- If you charge for the time customers spend with you, then and only then are you in the *experience* business.

Citing examples of a range of companies from Disney to AOL, they maintain that salable experiences come in four varieties: entertainment, education, esthetic, and escapist. VANS, which pioneered slip-on sneakers for skateboarding, has succeeded in that market with an offbeat marketing mix of events, sponsorships, and even a documentary film, all celebrating the skateboard culture.[19] VANS' CEO Gary Schoenfeld proclaims, "Our vision is not to hit our

MARKETING INSIGHT | EXPERIENTIAL MARKETING

Through several books and papers, Columbia University's Bernd Schmitt has developed the concept of *Customer Experience Management (CEM)*—the process of strategically managing a customer's entire experience with a product or company. According to Schmitt, brands can help to create five different types of experiences: (1) Sense, (2) Feel, (3) Think, (4) Act, (5) Relate. In each case, Schmitt distinguishes between hard-wired and acquired experiential response levels. He maintains that marketers can provide experiences for customers through a set of experience providers.

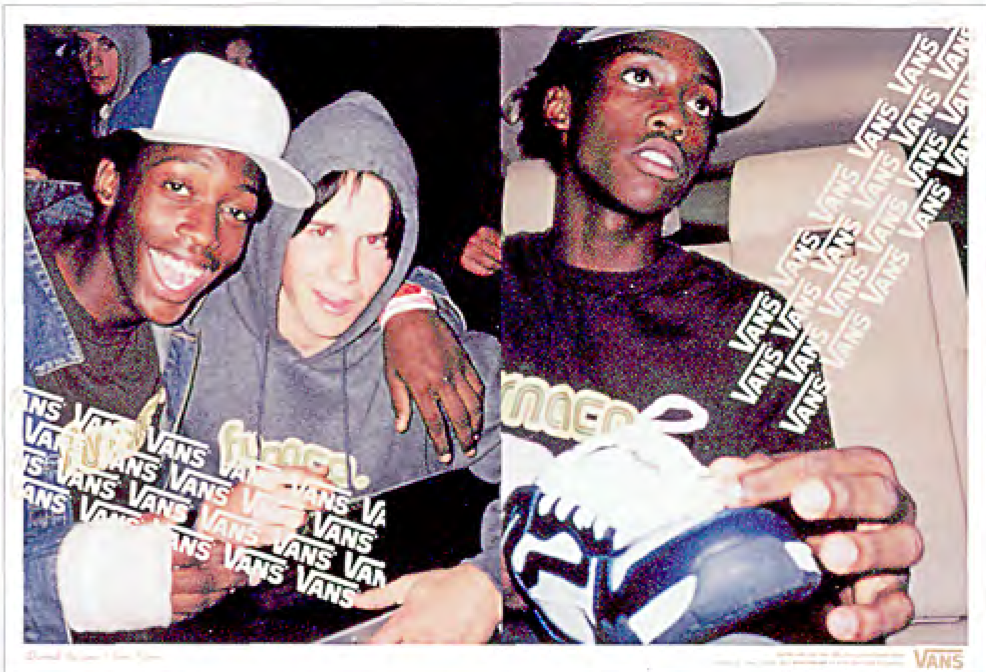
1. ***Communications:*** advertising, public relations, annual reports, brochures, newsletters, and magalogs.
2. ***Visual/verbal identity:*** names, logos, signage, and transportation vehicles.
3. ***Product presence:*** product design, packaging, and point-of-sale displays.
4. ***Co-branding:*** event marketing and sponsorships, alliances and partnerships, licensing, and product placement in movies or TV.
5. ***Environments:*** retail and public spaces, trade booths, corporate buildings, office interiors, and factories.
6. ***Web sites and electronic media:*** corporate sites, product or service sites, CD-ROMs, automated e-mails, online advertising, and intranets.
7. ***People:*** salespeople, customer service representatives, technical support or repair providers, company spokepersons, and CEOs and other executives.

The CEM framework is made up of five basic steps:

1. ***Analyzing the experiential world of the customer:*** gaining insights into the sociocultural context of consumers or the business context of business customers.
2. ***Building the experiential platform:*** developing a strategy that includes the positioning for the kind of experience the brand stands for ("what"), the value proposition of what relevant experience to deliver ("why"), and the overall implementation theme that will be communicated ("how").
3. ***Designing the brand experience:*** implementing their experiential platform in the look and feel of logos and signage, packaging, and retail spaces, in advertising, collaterals, and online.
4. ***Structuring the customer interface:*** implementing the experiential platform in the dynamic and interactive interfaces including face-to-face, in stores, during sales visits, at the check-in desk of a hotel, or the e-commerce engine of a Web site.
5. ***Engaging in continuous innovation:*** implementing the experiential platform in new-product development, creative marketing events for customers, and fine-tuning the experience at every point of contact.

Schmitt cites Pret A Manger, the U.K.-based sandwich company, as an example of a company that provides an attractive brand experience, customer interface, and ongoing innovation: "The Pret A Manger brand is about great tasting, handmade, natural products served by amazing people who are passionate about their work. The sandwiches and stores look appealing and attractive. The company hires only 5% of those who apply and only after they have worked for a day in the shop. This process ensures good fit and good teamwork." He also offers Singapore Airlines, Starbucks, and Amazon.com as outstanding providers of customer experiences.

Sources: www.exgroup.com; Bernd Schmitt, *Customer Experience Management: A Revolutionary Approach to Connecting with Your Customers* (New York: John Wiley and Sons, 2003); Bernd Schmitt, David L. Rogers, and Karen Vrotsos, *There's No Business That's Not Show Business: Marketing in an Experience Culture* (Upper Saddle River, NJ: Prentice Hall, 2003); Bernd Schmitt, *Experiential Marketing: How to Get Companies to Sense, Feel, Think, Act, and Relate to Your Company and Brands* (New York: Free Press, 1999); Bernd Schmitt and Alex Simonson, *Marketing Aesthetics: The Strategic Management of Brands, Identity and Image* (New York: Free Press, 1997).



Pro skateboarders Darrell Stanton and Scott Kane in a VANS ad. Both Stanton and Kane are part of a VANS-sponsored team.

target audience over the head with our ads, but to integrate ourselves into the places they are most likely to be."

Those who favor localized marketing see national advertising as wasteful because it is too "arm's length" and fails to address local needs. Those against local marketing argue that it drives up manufacturing and marketing costs by reducing economies of scale. Logistical problems are magnified. A brand's overall image might be diluted if the product and message are different in different localities.

Customerization

The ultimate level of segmentation leads to "segments of one," "customized marketing," or "one-to-one marketing."[20]

Today customers are taking more individual initiative in determining what and how to buy. They log onto the Internet; look up information and evaluations of product or service offers; dialogue with suppliers, users, and product critics; and in many cases, design the product they want. More online companies today are offering customers a Choiceboard, an interactive online system that allows individual customers to design their own products and services by choosing from a menu of attributes, components, prices, and delivery options. The customer's selections send signals to the supplier's manufacturing system that set in motion the wheels of procurement, assembly, and delivery.[21]

Wind and Rangaswamy see the Choiceboard as a movement toward "customerizing" the firm.[22] **Customerization** combines operationally driven mass customization with customized marketing in a way that empowers consumers to design the product and service offering of their choice. The firm no longer requires prior information about the customer, nor does the firm need to own manufacturing. The firm provides a platform and tools and "rents" out to customers the means to design their own products. A company is customerized when it is able to respond to individual customers by customizing its products, services, and messages on a one-to-one basis.[23]

Each business unit will have to decide whether it would gain more by designing its business system to create offerings for *segments* or for *individuals*. Companies that favor segmentation see it as more efficient, as requiring less customer information, and as permitting more standardization of market offerings. Those who favor individual marketing claim that segments are a fiction, that individuals within so-called segments differ greatly, and that marketers can achieve much more precision and effectiveness by addressing individual needs.

Customization is certainly not for every company: It may be very difficult to implement for complex products such as automobiles. Customization can raise the cost of goods by

Acumins Internet-based vitamin company Acumins blends vitamins, herbs, and minerals according to a customer's instructions, compressing up to 95 ingredients into three to five "personalized pills." The Acumins premise is simple and attractive: Why swallow dozens of pills when you can take three pills with dozens of ingredients of your choosing?

Paris Miki The Japanese company Paris Miki, one of the largest eyeglass retailers in the world, uses a design tool that takes a digital picture of the customer's face. The customer describes the style he or she wants—sports, elegant, traditional—and the system displays alternatives on the computerized photograph. After selecting the frame, the customer also chooses nosepieces, hinges, and arms. The glasses are ready within an hour.

DeBeers With DeBeers' Design Your Own Ring program, customers can design their own diamond rings by choosing from any of 189 unique combinations of center stone and side stone shapes and weights and band metal, as well as connect with a local jeweler who can help them buy it.

Andersen Windows Andersen Windows of Bayport, Minnesota, the home-building industry's leading window and patio door manufacturer, has developed an interactive computer version of its catalogs for distributors and retailers that is linked directly to the factory. With this system, now in 650 showrooms, salespeople can help customers customize each window, check the design for structural soundness, and generate a price quote. From there Andersen went on to develop a "batch of one" manufacturing process in which every window and door part is made to order, thus reducing its finished parts inventory (a major cost to the company).

ChemStation Based in Dayton, Ohio, ChemStation offers customized soap formulas to its industrial customers, who range from car washes to the U.S. Air Force. What cleans a car will not clean an airplane or equipment in a mine shaft. Salespeople visit customer sites to gather information. All the data from the company's chemical lab and its field studies are kept in a central database called Tank Management System (TMS). TMS is linked directly to both the lab and the company's 40 plants across the country, where computer-operated machines mix each customer's special formula.

FIG. 8.2

Examples of Marketing Customization

Sources: "Creating Greater Customer Value May Require a Lot of Changes," *Organizational Dynamics* (Summer 1998): 26; Erick Schonfeld, "The Customized, Digitized, Have-It-Your-Way Economy," *Fortune*, September 28, 1998, pp. 115–124; Jim Barlow, "Individualizing Mass Production," *Houston Chronicle*, April 13, 1997, p. E1; Sarah Schafer, "Have It Your Way," *Inc.*, November 18, 1997, pp. 56–64; Jim Christie, "Mass Customization: The New Assembly Line?" *Investor's Daily*, February 25, 2000.

more than the customer is willing to pay. Some customers do not know what they want until they see actual products. Customers cannot cancel the order after the company has started to work on the product. The product may be hard to repair and have little sales value. In spite of this, customization has worked well for some products. Figure 8.2 shows examples of companies that employ customization.

Segmenting Consumer Markets

Two broad groups of variables are used to segment consumer markets. Some researchers try to form segments by looking at descriptive characteristics: geographic, demographic, and psychographic. Then they examine whether these customer segments exhibit different needs or product responses. For example, they might examine the differing attitudes of "professionals," "blue collars," and other groups toward, say, "safety" as a car benefit.

Other researchers try to form segments by looking at "behavioral" considerations, such as consumer responses to benefits, use occasions, or brands. Once the segments are formed, the researcher sees whether different characteristics are associated with each consumer-response segment. For example, the researcher might examine whether people who want "quality" rather than "low price" in buying an automobile differ in their geographic, demographic, and psychographic makeup.

Regardless of which type of segmentation scheme is employed, the key is that the marketing program can be profitably adjusted to recognize customer differences. The major segmentation variables—geographic, demographic, psychographic, and behavioral segmentation—are summarized in Table 8.1.

Geographic Segmentation

Geographic segmentation calls for dividing the market into different geographical units such as nations, states, regions, counties, cities, or neighborhoods. The company can operate in one or a few areas, or operate in all but pay attention to local variations. For example, Hilton Hotels customizes rooms and lobbies according to location. Northeastern hotels are sleeker and more cosmopolitan. Southwestern hotels are more rustic. Major retailers such as Wal-Mart, Sears, Roebuck & Co., and Kmart all allow local managers to stock products that suit the local community.[24]

TABLE 8.1

Major Segmentation Variables for Consumer Markets

Geographic region	Pacific, Mountain, West North Central, West South Central, East North Central, East South Central, South Atlantic, Middle Atlantic, New England
City or metro size	Under 5,000; 5,000–20,000; 20,000–50,000; 50,000–100,000; 100,000–250,000; 250,000–500,000; 500,000–1,000,000; 1,000,000–4,000,000; 4,000,000 or over
Density	Urban, suburban, rural
Climate	Northern, southern
Demographic age	Under 6, 6–11, 12–19, 20–34, 35–49, 50–64, 65+
Family size	1-2, 3-4, 5+
Family life cycle	Young, single; young, married, no children; young, married, youngest child under 6; young, married, youngest child 6 or over; older, married, with children; older, married, no children under 18; older, single; other
Gender	Male, female
Income	Under \$10,000; \$10,000–\$15,000; \$15,000–\$20,000; \$20,000–\$30,000; \$30,000–\$50,000; \$50,000–\$100,000; \$100,000 and over
Occupation	Professional and technical; managers, officials, and proprietors; clerical sales; craftspeople; forepersons; operatives; farmers; retired; students; homemakers; unemployed
Education	Grade school or less; some high school; high school graduate; some college; college graduate
Religion	Catholic, Protestant, Jewish, Muslim, Hindu, other
Race	White, Black, Asian, Hispanic
Generation	Baby boomers, Generation Xers
Nationality	North American, South American, British, French, German, Italian, Japanese
Social class	Lower lowers, upper lowers, working class, middle class, upper middles, lower uppers, upper uppers
Psychographic lifestyle	Culture-oriented, sports-oriented, outdoor-oriented
Personality	Compulsive, gregarious, authoritarian, ambitious
Behavioral occasions	Regular occasion, special occasion
Benefits	Quality, service, economy, speed
User status	Nonuser, ex-user, potential user, first-time user, regular user
Usage rate	Light user, medium user, heavy user
Loyalty status	None, medium, strong, absolute
Readiness stage	Unaware, aware, informed, interested, desirous, intending to buy
Attitude toward product	Enthusiastic, positive, indifferent, negative, hostile

BED BATH & BEYOND

Home furnishing retailer Bed Bath & Beyond's ability to cater to local tastes has fueled its phenomenal growth. Bed Bath & Beyond's managers pick 70 percent of their own merchandise, and this fierce local focus has helped the chain evolve from one that began selling little more than bed linens to the "beyond" part—products ranging from picture frames and pot holders to imported olive oil and designer door mats. In Manhattan stores, for instance, managers are beginning to stock wall paint. You won't find paint in suburban stores where customers can go to Home Depot or Lowe's. One Bed Bath manager says that several customers have been surprised when they found out that the store is part of a national chain and not a mom-and-pop operation. That's the ultimate compliment.[25]

More and more, regional marketing means marketing right down to a specific zip code.[26] Many companies use mapping software to show the geographic locations of their customers. The software may show a retailer that most of his customers are within only a 10-mile radius of his store, and further concentrated with certain zip+4 areas. By mapping the densest areas, the retailer can resort to *customer cloning*, assuming that the best prospects live where most of his customers come from.

Some approaches combine geographic data with demographic data to yield even richer descriptions of consumers and neighborhoods. Claritas, Inc., has developed a geoclustering approach called PRIZM (Potential Rating Index by Zip Markets) that classifies over half a million U.S. residential neighborhoods into 15 distinct groups and 66 distinct lifestyle segments called PRIZM Clusters.[27] The groupings take into consideration 39 factors in 5 broad categories: (1) education and affluence, (2) family life cycle, (3) urbanization, (4) race and ethnicity, and (5) mobility. The neighborhoods are broken down by zip code, zip+4, or census tract and block group. The clusters have descriptive titles such as *Blue Blood Estates, Winner's Circle, Hometown Retired, Latino America, Shotguns and Pickups,* and *Back Country Folks.* The inhabitants in a cluster tend to lead similar lives, drive similar cars, have similar jobs, and read similar magazines. Here are four new PRIZM clusters:[28]

- ***Young Digerati.*** Couples or single-headed households, most of them with kids, who have decided to stay in urban centers rather than flee to the suburbs. This sector includes a high proportion of affluent, tech-savvy, 20-somethings, who tend to hold master's degrees and live in fashionable neighborhoods on the urban fringe. They are staking out territory in once-forgotten neighborhoods in cities such as New York, Chicago, and Atlanta.
- ***Beltway Boomers.*** Now in their forties and fifties, these college-educated, upper-middle-class homeowners married late and are still raising children. They live in comfortable suburban subdivisions and are still pursuing kid-centered lifestyles.
- ***The Cosmopolitans.*** Continued gentrification of the nation's cities has resulted in the emergence of this segment, concentrated in America's fast-growing metro areas such as Las Vegas, Miami, and Albuquerque. These households feature older homeowners, empty nesters, and college graduates who enjoy leisure-intensive lifestyles.
- ***Old Milltowns.*** Just as America's once thriving factory towns have aged, so have their residents. Old Milltowns reflects the decline of these small, once-industrial communities, now filled with retired singles and couples living quietly on fixed incomes. These home-centered residents make up one of the top segments for daytime television.

Marketers can use PRIZM to answer such questions as these: Which geographic areas (neighborhoods or zip codes) contain our most valuable customers? How deeply have we already penetrated these segments? Which distribution channels and promotional media work best in reaching our target clusters in each area? Geoclustering captures the increasing diversity of the American population. Upscale sportswear retailer Eddie Bauer has used geoclustering information to better locate stores and serve customers. Based on a successful pilot with *Veggie Tales* concerts, Clear Channel Communications is using geoclustering information to send targeted e-mails to prospects for national tours in all entertainment venues.[29] Marketing to microsegments has become accessible even to small organizations as database costs decline, PCs proliferate, software becomes easier to use, data integration increases, and the Internet grows.[30]

Demographic Segmentation

In demographic segmentation, the market is divided into groups on the basis of variables such as age, family size, family life cycle, gender, income, occupation, education, religion, race, generation, nationality, and social class. There are several reasons for the popularity of demographic variables to distinguish customer groups. One reason is that consumer needs, wants, and usage rates and product and brand preferences are often associated with demographic variables. Another is that demographic variables are easier to measure. Even when the target market is described in nondemographic terms (say, a personality type), the link back to demographic characteristics may be needed in order to estimate the size of the market and the media that should be used to reach it efficiently.

Here is how certain demographic variables have been used to segment markets.

AGE AND LIFE-CYCLE STAGE Consumer wants and abilities change with age. Toothpaste brands such as Crest and Colgate offer three main lines of products to target kids, adults, and older consumers. Age segmentation can be even more refined. Pampers divides its market into prenatal, newborn (0–1 month), infant (2–5 months), cruiser (6–12 months), toddler (13–18 months), explorer (19–23 months), and preschooler (24 months+).

Nevertheless, age and life cycle can be tricky variables.[31] In some cases, the target market for products may be the psychologically young. For example, Honda tried to target 21-year-olds with its boxy Element, which company officials described as a "dorm room on wheels." So many baby boomers were attracted to the car's ads depicting sexy college kids partying near the car at a beach, however, that the average age of buyers turned out to be 42! Nostalgia can also play a role. Chrysler had a young target market in mind for the PT Cruiser, but found that lots of older consumers were reminded of hot rods from their youth. Toyota has been more successful with its younger pitch for Scion.[32]

SCION

Named for wealthy offspring, Scion is an attempt by Toyota to attract the Gen Y audience, which might see Toyota as their parents' brand. The Scion has a hip look and feel—and an industrial strength stereo—and is sold in chrome and black showrooms tucked inside Toyota dealerships. Priced at under $15,000 and sold on a fixed price basis (no haggling), the marketing strategy is to go underground and link the brand to up-and-coming entertainment and events, allowing the youthful target to "discover" the brand.

LIFE STAGE Persons in the same part of the life cycle may differ in their life stage. **Life stage** defines a person's major concern, such as going through a divorce, going into a second marriage, taking care of an older parent, deciding to cohabit with another person, deciding to buy a new home, and so on. These life stages present opportunities for marketers who can help people cope with their major concerns.

NEWLYWEDS

It has been estimated that newlyweds in the United States spend a total of $70 billion on their households in the first year after marriage—and they buy more in the first six months of marriage than an established household does in five years! Marketers know that marriage often means that two sets of shopping habits and brand preferences have to be blended into one. Companies such as Procter & Gamble, Clorox, and Colgate-Palmolive include their products in "Newlywed Kits" that are distributed when couples apply for their marriage license. JC Penney has identified "Starting Outs" as one of its two major customer groups. Marketers pay companies a premium for name lists to assist their direct marketing because, as one marketer noted, newlywed names "are like gold."[33]

GENDER Men and women tend to have different attitudinal and behavioral orientations, based partly on genetic makeup and partly on socialization. For example, women tend to be more communal-minded and men tend to be more self-expressive and goal-directed; women tend to take in more of the data in their immediate environment; men tend to focus on the part of the environment that helps them achieve a goal. A research study examining how men and women shop found that men often need to be invited to touch a product, while women are likely to pick it up without prompting. Men often like to read product information; women may relate to a product on a more personal level.[34]

Gender differentiation has long been applied in clothing, hairstyling, cosmetics, and magazines. Avon has built a $6 billion-plus business selling beauty products to women. Some products have been positioned as more masculine or feminine. Gillette's Venus is the most successful female shaving line ever, with over 70 percent of the market, and has appropriate product design, packaging, and advertising cues to reinforce a female image; Camel Cigarettes emphasizes men and surrounds the brand with more masculine, rugged cues.

Media have emerged to facilitate gender targeting. Women can be more easily reached on Lifetime, Oxygen, and WE television networks and through scores of women's magazines; men are more likely to be found at ESPN, Comedy Central, Fuel, and Spike TV channels, and reading magazines such as *Maxim* and *Men's Health*.[35]

Some traditionally more male-oriented markets, such as the automobile industry, are beginning to recognize gender segmentation, and are changing how they design and sell cars. For example, armed with research suggesting that 80 percent of home improvement projects are now initiated by women, Lowe's designed its stores with wider aisles—to make it easier for shopping carts to get around—and to include more big-ticket appliances and high-margin home furnishings. Half of its clientele is now female, forcing its more traditional competitor, Home Depot, to introduce "Ladies Night at the Depot" to appeal to women.[36] Many others are recognizing the opportunities to target women.

An ad for financial services firm Paine Webber features a picture of two women: one clearly the mother, the other her 20-something-year-old daughter. The copy reads, "You're psyched about the future. You're full of new ideas. You're looking to start a business. You're the one on the right." The one on the right is the older woman. Paine Webber is one of a handful of companies—including Chico's, the hugely successful women's clothing chain, and New Balance sneakers—that are targeting one of the biggest, richest, most lucrative and most ignored markets: boomer women. Women control or influence 80 percent of both consumer and business goods and services. They have sole or joint ownership of 87 percent of homes and account for over 60 percent of all home improvement, home computer, and health care services purchases. And they start 70 percent of all new businesses. In short, women are spending the money and boomer women have more of it to spend.

INCOME Income segmentation is a long-standing practice in such product and service categories as automobiles, clothing, cosmetics, financial services, and travel.

WACHOVIA CORP.

Like many banks, Wachovia is trying to determine who its "sweet spot" clients are and deliver specialized services for those individuals. Wachovia's wealth management unit has determined that executives and professionals with between $2.5 million and $15 million of assets are the bank's most attractive customers. These customers are not the affluent or "ultra-wealthy" and, by and large, did not inherit their wealth. The bank plans to become extremely focused on this segment, with the idea of helping them move from creating wealth to leveraging that wealth and then, finally, to preserving it.[37]

However, income does not always predict the best customers for a given product. Blue-collar workers were among the first purchasers of color television sets; it was cheaper for them to buy these sets than to go to movies and restaurants.

Increasingly, companies are finding that their markets are "hourglass-shaped" as middle-market Americans migrate toward more premium products.[38] When Whirlpool launched a pricey Duet washer line, sales doubled forecasts in a weak economy, due primarily to middle-class shoppers who traded up. Michael Silverstein, a senior vice president and director for the Boston Consulting Group, and former BCG partner Neil Fiske have been studying this phenomenon, which they call "trading up." Their new book, *Trading Up: The New American Luxury*, documents their investigation into the forces driving the trend and points out companies that have cracked the code for success in this market:[39]

PANERA BREAD

While lunch at Panera's bakery cafés costs twice as much as at Burger King, customers don't mind paying because the cafés deliver all three benefits that Silverstein and Fiske say are common to successful new-luxury goods: *technical benefits* (how a product is engineered), *functional benefits* (the experience it provides the customer), and *emotional benefits* (how it makes the customer feel). Getting a smoked turkey breast with chipotle mayonnaise on Asiago cheese focaccia and a chai latte in a pleasing café atmosphere is the kind of satisfying experience "trading-up" customers crave. And being able to deliver that experience quickly and relatively inexpensively has spurred the growth of Panera and others in the so-called "fast casual" dining segment.

According to Silverstein and Fiske, companies that make a concerted effort to reinvent their products and come up with something genuinely better will find a huge potential market. The trading-up universe generally begins with households earning at least $50,000. In the United States, more than 47 million households have that kind of spending power. Of course, if companies miss out on this new market, they risk being "trapped in the middle" and seeing their market share steadily decline. General Motors was caught in the middle, between highly engineered German imports in the luxury market and high-value Japanese and Korean models in the economy class.[40]

GENERATION Each generation is profoundly influenced by the times in which it grows up—the music, movies, politics, and defining events of that period. Demographers call these groups *cohorts*. Members of a cohort share the same major cultural, political, and economic

FIG. 8.3

Profiling American Generations

Source: Bonnie Tsui, "Generation Next," *Advertising Age*, January 15, 2001, pp. 14–16.

GI generation (16 million people)
Born 1901–1924
Shaped by hard times and the Great Depression, financial security is one of their core values. Conservative spenders and civic-minded, they are team-oriented and patriotic.

Silent Generation (35 million people)
Born 1925–1945
Trusting conformists who value stability, they are now involved in civic life and extended families.

Baby Boomers (78 million people)
Born 1946–1964
Great acquisitors, they are value- and cause-driven despite indulgences and hedonism.

Generation X (57 million people)
Born 1965–1977
Cynical and media-savvy, they are more alienated and individualistic.

Generation Y (60 million)
Born 1978–1994
Edgy, focused on urban style, they are more idealistic than Generation X.

Millennials (42 million people)
Born 1995–2002
Multicultural, they will be tech-savvy, educated, grow up in affluent society, and have big spending power.

experiences. They have similar outlooks and values. Marketers often advertise to a cohort group by using the icons and images prominent in their experiences. Figure 8.3 depicts six well-established cohort groups. "Marketing Insight: Marketing to Generation Y" provides insight into that key age cohort. "Marketing Memo: Cheat Sheet for 21-Year-Olds" provides insights into a key part of Gen Y.

Yet, while distinctions can be made between different cohorts, generational cohorts also influence each other. For instance, because so many members of Generation Y—"Echo Boomers"—are living with their boomer parents, the parents are being influenced and exhibiting what demographers are calling a "boom-boom effect." The same products that appeal to 21-year-olds are appealing to youth-obsessed baby boomers. Boomer parents are watching MTV's *The Osbournes*, the reality show based on heavy-metal rocker Ozzy Osbourne and his family, right alongside their children.

Meredith, Schewe, and Karlovich developed a framework called The Lifestage Analytic Matrix, which combines information on cohorts, life stages, physiographics, emotional effects, and socioeconomics in analyzing a segment or individual.[41] For example, two individuals from the same cohort may differ in their *life stages* (having a divorce, getting remarried), *physiographics* (coping with hair loss, menopause, arthritis, or osteoporosis), *emotional effects* (nostalgia for the past, wanting experiences instead of things), or *socioeconomics* (losing a job, receiving an inheritance). The authors believe this analysis will lead to more efficient targeting and messages.

SOCIAL CLASS Social class has a strong influence on preference in cars, clothing, home furnishings, leisure activities, reading habits, and retailers. Many companies design products and services for specific social classes. The tastes of social classes change with the years. The 1990s were about greed and ostentation for the upper classes. Affluent tastes now run more conservatively, although luxury goods makers such as Coach, Tiffany, Burberry, TAG Heuer, and Louis Vuitton still successfully sell to those seeking the good life.[42]

Psychographic Segmentation

Psychographics is the science of using psychology and demographics to better understand consumers. In *psychographic segmentation*, buyers are divided into different groups on the basis of psychological/personality traits, lifestyle, or values. People within the same demographic group can exhibit very different psychographic profiles.

One of the most popular commercially available classification systems based on psychographic measurements is SRI Consulting Business Intelligence's (SRIC-BI) VALS™ framework. VALS classifies U.S. adults into eight primary groups based on personality traits and key demographics. The segmentation system is based on responses to a questionnaire featuring 4 demographic and 35 attitudinal questions. The VALS system is continually updated with new data from more than 80,000 surveys per year (see Figure 8.4).[43]

MARKETING INSIGHT | MARKETING TO GENERATION Y

They're dubbed "Echo Boomers" or "Generation Y." They grew up during times of economic abundance followed by years of economic recession. Their world was defined by long years of national calm and peace disrupted by events like Columbine and 9/11. They have been "wired" almost from birth—playing computer games, navigating the World Wide Web, downloading music, connecting with friends via instant messaging and mobile phones. They have a sense of entitlement and abundance from having grown up during the economic boom and being pampered by their boomer parents. They are selective, confident, and also impatient. They "want what they want when they want it"—and they often get it by using plastic. The average 21-year-old is carrying almost $3,000 in credit card debt (see "Marketing Memo: A Cheat Sheet for 21-Year-Olds" for more fast facts about 21-year-olds within the Gen Y cohort).

The influences that have shaped the Gen Y cohort are incredibly important to marketers because Generation Y is the force that will shape consumer and business markets for years to come. Born between 1977 and 1994, Generation Y is three times the size of Generation X. Roughly 78 million Americans belong to this group, the largest generational cohort in American history. Their spending power is estimated at $187 billion annually. If you take that $187 billion, factor in career growth, household and family formation, and multiply by another 53 years of life expectancy, you're in the $10 trillion range in consumer spending over the life span of today's 21-year-olds.

It's not surprising, then, that market researchers and advertisers are racing to get a bead on Gen Y's buying behavior. Because they are often turned off by overt branding practices and a "hard sell," marketers have tried many different approaches to reach and persuade Generation Y.[70]

1. ***Online buzz***—Rock band Foo Fighters created a digital street team that sends targeted e-mail blasts to members who "get the latest news, exclusive audio/video sneak previews, tons of chances to win great Foo Fighters prizes, and become part of the Foo Fighters Family."
2. ***Student ambassadors***—Red Bull enlists college students as Red Bull Student Brand Managers to distribute samples, research drinking trends, design on-campus marketing initiatives, and write stories for student newspapers.
3. ***Unconventional sports***—Dodge automobiles sponsors the World Dodgeball Association, which is taking the sport "to a new level by emphasizing teamwork, strategy, and skill."
4. ***Cool events***—The U.S. Open of Surfing attracted sponsors such as Honda, Philips Electronics and, of course, O'Neill Clothing, originators of the first wet suit. Spring break in Florida has been the place for the launch of such products as Old Spice Cool Contact Refreshment Towels and Calvin Klein's CK swimwear line.
5. ***Computer games***—Product placement is not restricted to movies or TV: Mountain Dew, Oakley, and Harley-Davidson all made deals to put logos on Tony Hawk's Pro Skater 3 from Activision.
6. ***Videos***—Burton snowboards ensures that its boards and riders are clearly visible in any videos that are shot.
7. ***Street teams***—As part of an anti-smoking crusade, The American Legacy hires teens as the "Truth Squad" to hand out T-shirts, bandanas, and dog tags at teen-targeted events

Sources: J. M. Lawrence, "Trends: X-ed Out: Gen Y Takes Over," *Boston Herald*, February 2, 1999, p. 243; Martha Irvine, "Labels Don't Fit Us, Gen Y Insists," *Denver Post*, April 19, 2001, p. A9; Anonymous, "Gen Y and the Future of Mall Retailing," *American Demographics* (December 2002/January 2003): J1–J4; Michael J. Weiss, "To Be about to Be," *American Demographics* (September 2003): 28–36; John Leo, "The Good-News Generation," *U.S. News & World Report*, November 3, 2003, p. 60; Kelly Pate, "Not 'X,' but 'Y' Marks the Spot: Young Generation a Marketing Target," *Denver Post*, August 17, 2003, p. K1; Bruce Horovitz, "Gen Y: A Tough Crowd to Sell," *USA Today*, April 22, 2002, pp. 1B–2B; Bruce Horovitz, "Marketers Revel with Spring Breakers," *USA Today*, March 12, 2002, p. 3B.

MARKETING MEMO | CHEAT SHEET FOR 21-YEAR-OLDS

In 2003, 4.1 million Americans turned 21. Here are some facts you need to know about them.

41%—Share of 21-year-olds who currently live with mom and/or dad.

60%—Share of college students who plan to move back home after graduation.

1-in-4—Odds that a 21-year-old was raised by a single parent.

70%—Share of 21-year-olds who have a full- or part-time job.

47%—Share of 21-year-olds who own a mobile phone.

23 million—Number of ad impressions received thus far by the average 21-year-old.

$2,241,141—Amount the average 21-year-old will spend between now and the end of his or her life.

$3,000—Credit card debt of the average 21-year-old.

5.8—Years until the average 21-year-old man marries for the first time.

4.1—Years until the average 21-year-old woman marries for the first time.

10—Years until the average 21-year-old buys his or her first vacation home.

43%—Share of 21-year-olds who have a tattoo or a body piercing.

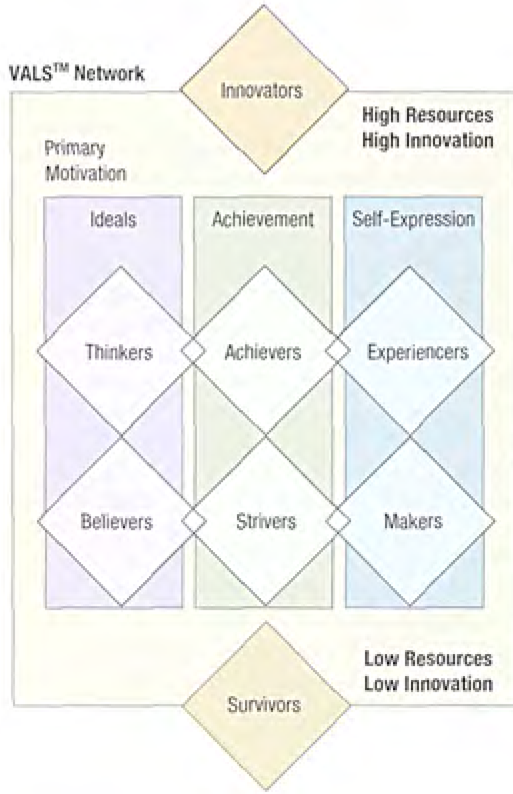
62%—Share of 21-year-olds who are non-Hispanic whites.

Source: John Fetto, "Twenty-One, and Counting . . . ," *American Demographics* (September 2003): 48.

FIG. 8.4

The VALS Segmentation System: An 8-Part Typology

Source: © 2004 by SRI Consulting Business Intelligence. All rights reserved. Printed by permission.



The major tendencies of the four groups with higher resources are:

1. ***Innovators*** – Successful, sophisticated, active, "take-charge" people with high self-esteem. Purchases often reflect cultivated tastes for relatively upscale, niche-oriented products and services.
2. ***Thinkers*** – Mature, satisfied, and reflective people who are motivated by ideals and value order, knowledge, and responsibility. Favor durability, functionality, and value in products.
3. ***Achievers*** – Successful goal-oriented people who focus on career and family. Favor premium products that demonstrate success to their peers.
4. ***Experiencers*** – Young, enthusiastic, impulsive people who seek variety and excitement. Spend a comparatively high proportion of income on fashion, entertainment, and socializing.

The major tendencies of the four groups with lower resources are:

1. ***Believers*** – Conservative, conventional, and traditional people with concrete beliefs. Favor familiar, American products and are loyal to established brands.
2. ***Strivers*** – Trendy and fun-loving people who are resource-constrained. Favor stylish products that emulate the purchases of those with greater material wealth.
3. ***Makers*** – Practical, down-to-earth, self-sufficient people who like to work with their hands. Favor American-made products with a practical or functional purpose.
4. ***Survivors*** – Elderly, passive people who are concerned about change. Loyal to their favorite brands.

You can find out which VALS type you are by going to SRIC-BI's Web site (www.sric-bi.com).

Psychographic segmentation schemes are often customized by culture. The Japanese version of VALS, Japan VALS™, divides society into 10 consumer segments on the basis of two key consumer concepts: life orientation (traditional ways, occupations, innovation, and self-expression) and attitudes to social change (sustaining, pragmatic, adapting, and innovating).

Behavioral Segmentation

In behavioral segmentation, buyers are divided into groups on the basis of their knowledge of, attitude toward, use of, or response to a product.

Once cranberries were used only for holiday dinner at Thanksgiving and Christmas. Ocean Spray cranberry-based juice drinks have given the company a year-round market for its product.

DECISION ROLES It is easy to identify the buyer for many products. In the United States, men normally choose their shaving equipment, and women choose their pantyhose; but even here marketers must be careful in making their targeting decisions, because buying roles change. When ICI, the giant British chemical company, discovered that women made 60 percent of the decisions on the brand of household paint, it decided to advertise its DuLux brand to women.

People play five roles in a buying decision: *Initiator, Influencer, Decider, Buyer, User.* For example, assume a wife initiates a purchase by requesting a new treadmill for her birthday. The husband may then seek information from many sources, including his best friend who has a treadmill and is a key influencer in what models to consider. After presenting the alternative choices to his wife, he then purchases her preferred model which, as it turns out, ends up being used by the entire family. Different people are playing different roles, but all are crucial in the decision process and ultimate consumer satisfaction.

BEHAVIORAL VARIABLES Many marketers believe that behavioral variables—occasions, benefits, user status, usage rate, loyalty status, buyer-readiness stage, and attitude—are the best starting points for constructing market segments.

Occasions Occasions can be defined in terms of the time of day, week, month, year, or in terms of other well-defined temporal aspects of a consumer's life. Buyers can be distinguished according to the occasions when they develop a need, purchase a product, or use a product. For example, air travel is triggered by occasions related to business, vacation, or family. Occasion segmentation can help firms expand product usage. For example, the Florida Citrus Growers ran an ad campaign—"Orange Juice. It's Not Just For Breakfast Anymore"— to expand its usage to other day parts. During the 1960s and 1970s, Ocean Spray Cranberries, Inc., was essentially a single-purpose, single-usage product: Consumption of cranberries was almost entirely confined to the serving of cranberry sauce as a side dish with Thanksgiving and Christmas holiday dinners. After a pesticide scare one Thanksgiving drastically cut sales and almost put growers out of business, the cooperative embarked on a program to diversify and create a year-round market by producing cranberry-based juice drinks and other products.[44]

Marketers also can try to extend activities associated with certain holidays to other times of the year. For instance, while Christmas, Mother's Day, and Valentine's Day are the three major gift-giving holidays, these and other holidays account for just over half of the gifters' budgets. That leaves the rest available throughout the year for occasion-driven gift-giving: birthdays, weddings, anniversaries, housewarming, and new babies.[45]

Benefits Buyers can be classified according to the benefits they seek. Even car drivers who want to stop for gas may seek different benefits. Through its research, Mobil identified five different benefit segments and their sizes:

1. ***Road Warriors*** – premium products and quality service. (16%)
2. ***Generation F*** – fast fuel, fast service, and fast food. (27%)
3. ***True Blues*** – branded products and reliable service. (16%)
4. ***Home Bodies*** – convenience. (21%)
5. ***Price Shoppers*** – low price. (20%)

Surprisingly, although gasoline is largely a commodity, price shoppers constituted only 20 percent of the buyers. Mobil decided to focus on the less price-sensitive segments, and rolled out *Friendly Serve:* cleaner property, bathrooms, better lighting, well-stocked stores, and friendlier personnel. Although Mobil charged 2 cents per gallon more than its competitors, sales increased by 20 to 25 percent.[46]

User Status Markets can be segmented into nonusers, ex-users, potential users, first-time users, and regular users of a product. Blood banks cannot rely only on regular donors to supply blood; they must also recruit new first-time donors and contact ex-donors. Each will require a different marketing strategy. Included in the potential user group are consumers who will become users in connection with some life stage or life event. Mothers-to-be are potential users who will turn into heavy users. Producers of infant products and services learn their names and shower them with products and ads to capture a share of their future purchases. Market-share leaders tend to focus on attracting potential users because they have the most to gain. Smaller firms focus on trying to attract current users away from the market leader.

Usage Rate Markets can be segmented into light, medium, and heavy product users. Heavy users are often a small percentage of the market but account for a high percentage of total consumption. For example, heavy beer drinkers account for 87 percent of the beer consumed—almost seven times as much as the light beer drinkers. Marketers would rather attract one heavy user than several light users. A potential problem, however, is that heavy users often either are extremely loyal to one brand, or never stay loyal to a brand and are always looking for the lowest price.

Buyer-Readiness Stage A market consists of people in different stages of readiness to buy a product. Some are unaware of the product, some are aware, some are informed, some are interested, some desire the product, and some intend to buy. The relative numbers make a big difference in designing the marketing program. Suppose a health agency wants to encourage women to have an annual Pap test to detect possible cervical cancer. At the beginning, most women may be unaware of the Pap test. The marketing effort should go into awareness-building advertising using a simple message. Later, the advertising should dramatize the benefits of the Pap test and the risks of not taking it. A special offer of a free health examination might motivate women to actually sign up for the test.

Loyalty Status Buyers can be divided into four groups according to brand loyalty status:

1. ***Hard-core loyals*** – Consumers who buy only one brand all the time.
2. ***Split loyals*** – Consumers who are loyal to two or three brands.

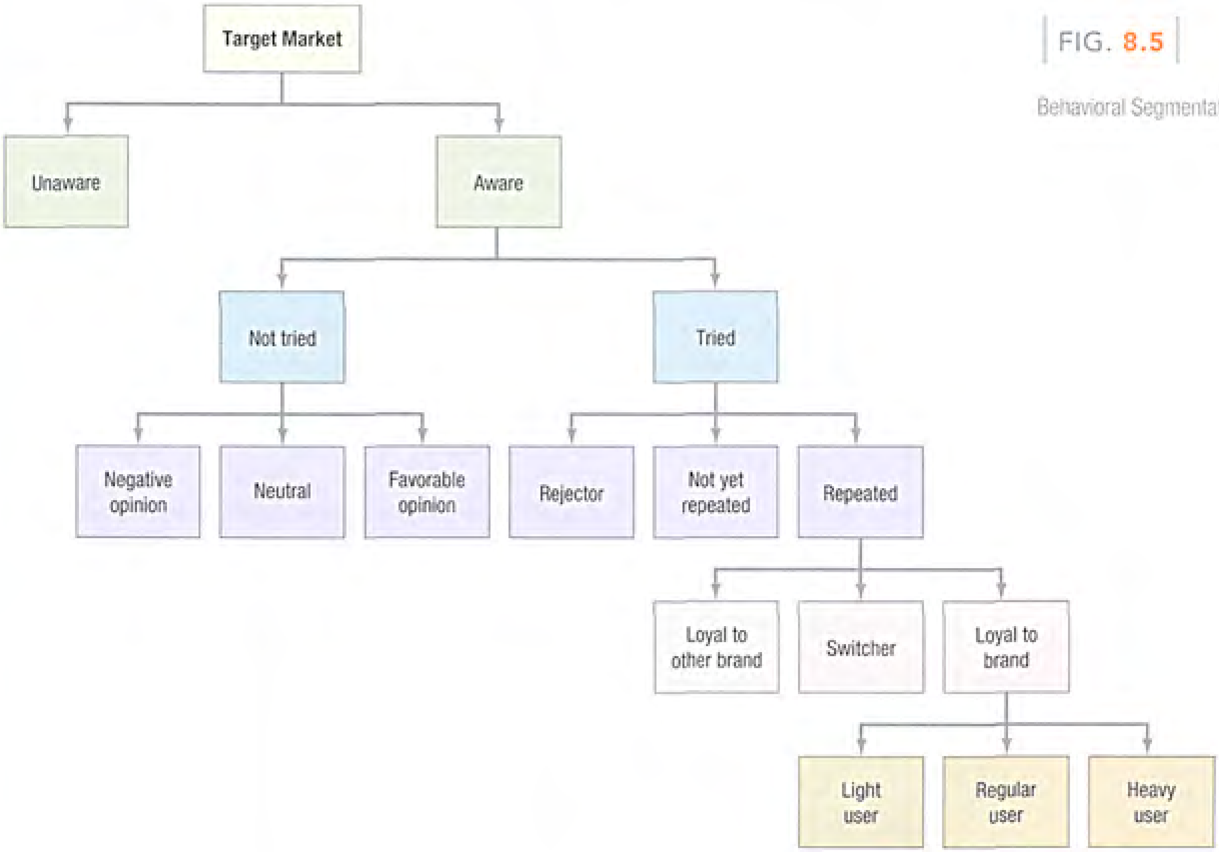


FIG. 8.5

Behavioral Segmentation Breakdown

3. ***Shifting loyals*** – Consumers who shift loyalty from one brand to another.
4. ***Switchers*** – Consumers who show no loyalty to any brand.[47]

A company can learn a great deal by analyzing the degrees of brand loyalty: (1) By studying its hard-core loyals, the company can identify its products' strengths. (2) By studying its split loyals, the company can pinpoint which brands are most competitive with its own. (3) By looking at customers who are shifting away from its brand, the company can learn about its marketing weaknesses and attempt to correct them.

Companies selling in a market dominated by switchers may have to rely more on price-cutting. If mistreated, they can also turn on the company. One caution: What appear to be brand-loyal purchase patterns may reflect habit, indifference, a low price, a high switching cost, or the nonavailability of other brands.

Attitude Five attitude groups can be found in a market: enthusiastic, positive, indifferent, negative, and hostile. Door-to-door workers in a political campaign use voter attitude to determine how much time to spend with that voter. They thank enthusiastic voters and remind them to vote; they reinforce those who are positively disposed; they try to win the votes of indifferent voters; they spend no time trying to change the attitudes of negative and hostile voters.

Combining different behavioral bases can help to provide a more comprehensive and cohesive view of a market and its segments. Figure 8.5 depicts one possible way to break down a target market by various behavioral segmentation bases.

THE CONVERSION MODEL The Conversion Model has been developed to measure the strength of the psychological commitment between brands and consumers and their openness to change.[48] To determine the ease with which a consumer can be converted to another choice, the model assesses commitment based on factors such as consumer attitudes toward and satisfaction with current brand choices in a category and the importance of the decision to select a brand in the category.[49]

The model segments *users* of a brand into four groups based on strength of commitment, from low to high, as follows:

1. Convertible (users who are most likely to defect).
2. Shallow (consumers who are uncommitted to the brand and could switch—some are actively considering alternatives).
3. Average (consumers who are also committed to the brand they are using, but not as strongly—they are unlikely to switch brands in the short term).
4. Entrenched (consumers who are strongly committed to the brand they are currently using—they are highly unlikely to switch brands in the foreseeable future).

The model also classifies *nonusers* of a brand into four other groups based on their "balance of disposition" and openness to trying the brand, from low to high, as follows:

1. Strongly Unavailable (nonusers who are unlikely to switch to the brand—their preference lies strongly with their current brands).
2. Weakly Unavailable (nonusers who are not available to the brand because their preference lies with their current brand, although not strongly).
3. Ambivalent (nonusers who are as attracted to the brand as they are to their current brands).
4. Available (nonusers of the brand who are most likely to be acquired in the short run).

In an application of the Conversion Model, Lloyds TSB bank discovered that the profitability of its clients who had been identified as "least committed" had fallen by 14 percent in a 12-month period, whereas those that were "most committed" had increased by 9 percent. Those who were "committed" were 20 percent more likely to increase the number of products they held during the 12-month period. As a result, the bank took action to attract and retain high-value committed customers, which resulted in increased profitability.

::: Bases for Segmenting Business Markets

Business markets can be segmented with some of the same variables used in consumer market segmentation, such as geography, benefits sought, and usage rate, but business marketers also use other variables. Bonoma and Shapiro proposed segmenting the business market with the variables shown in Table 8.2. The demographic variables are the most important, followed by the operating variables—down to the personal characteristics of the buyer.

The table lists major questions that business marketers should ask in determining which segments and customers to serve. A rubber-tire company should first decide which industries it wants to serve. It can sell tires to manufacturers of automobiles, trucks, farm tractors, forklift trucks, or aircraft. Within a chosen target industry, a company can further segment by company size. The company might set up separate operations for selling to large and small customers. Consider how Dell is organized.

DELL

Dell is divided into two direct sales divisions: One sells to consumers and small businesses; another manages the company's corporate accounts. Three key segments are included under the corporate accounts umbrella: the enterprise group (*Fortune* 500 companies), large corporate accounts (multinational companies in what would be the *Fortune* 501 to 2000 range), and preferred accounts (medium businesses with 200 to 2,000 employees).

Marketing to Small Businesses

Small businesses, in particular, have become a Holy Grail for business marketers.[50] In the United States, small businesses are now responsible for 50 percent of the gross national product, according to the U.S. Small Business Administration, and this segment is growing at 11 percent annually, three percentage points higher than the growth of large companies. Here are two examples of companies focusing on small businesses.

TABLE 8.2

Major Segmentation Variables for Business Markets

Demographic

1. *Industry:* Which industries should we serve?
2. *Company size:* What size companies should we serve?
3. *Location:* What geographical areas should we serve?

Operating Variables

4. *Technology:* What customer technologies should we focus on?
5. *User or nonuser status:* Should we serve heavy users, medium users, light users, or nonusers?
6. *Customer capabilities:* Should we serve customers needing many or few services?

Purchasing Approaches

7. *Purchasing-function organization:* Should we serve companies with highly centralized or decentralized purchasing organizations?
8. *Power structure:* Should we serve companies that are engineering dominated, financially dominated, and so on?
9. *Nature of existing relationships:* Should we serve companies with which we have strong relationships or simply go after the most desirable companies?
10. *General purchase policies:* Should we serve companies that prefer leasing? Service contracts? Systems purchases? Sealed bidding?
11. *Purchasing criteria:* Should we serve companies that are seeking quality? Service? Price?

Situational Factors

12. *Urgency:* Should we serve companies that need quick and sudden delivery or service?
13. *Specific application:* Should we focus on certain applications of our product rather than all applications?
14. *Size of order:* Should we focus on large or small orders?

Personal Characteristics

15. *Buyer-seller similarity:* Should we serve companies whose people and values are similar to ours?
16. *Attitudes toward risk:* Should we serve risk-taking or risk-avoiding customers?
17. *Loyalty:* Should we serve companies that show high loyalty to their suppliers?

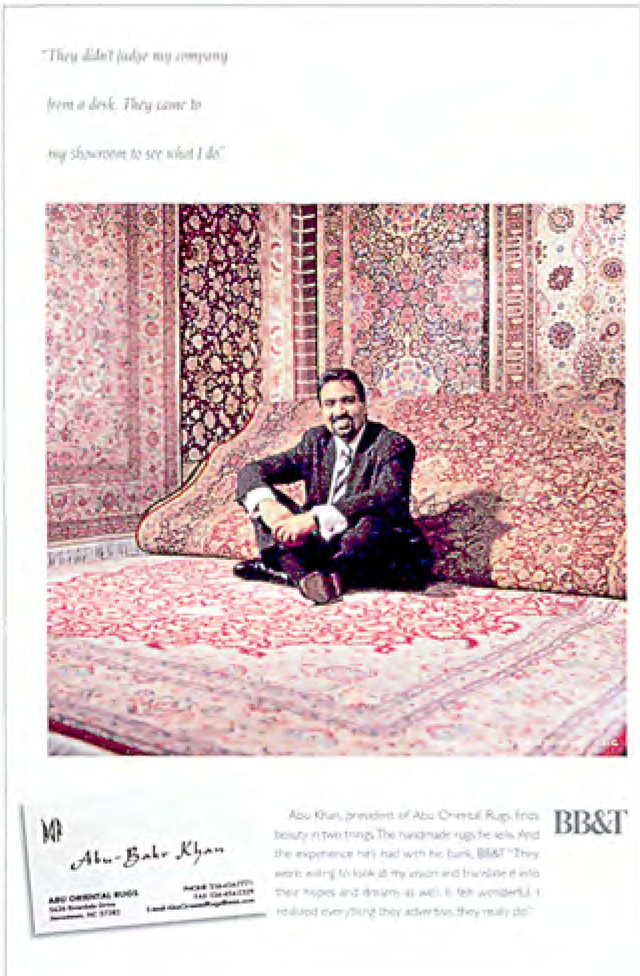
Source: Adapted from Thomas V. Bonoma and Benson P. Shapiro, *Segmenting the Industrial Market* (Lexington, MA: Lexington Books, 1983).

BB&T

BB&T Corporation, headquartered in Winston-Salem, North Carolina, is positioning itself as a powerful local bank with a down-home approach. It launched a business-to-business (B2B) advertising campaign depicting various Carolina businesses and their owners. Each entrepreneur is a BB&T small business customer, and the ads reinforce the bank's commitment to small business.[51]

PENN NATIONAL INSURANCE

With 82 percent of its commercial business coming from small businesses, Penn National Insurance decided it needed to identify the different classes of business that offer the greatest opportunity for profit. Working with a commercial insurance database, the company was able to categorize such key information as exposure data, growth, and employment information by business classification, size, and location. Beyond making it easier for agents to pinpoint prospects, the segmentation scheme also helped Penn National diversify beyond its concentration in the construction business. Overall, some 244 small business segments (based on SIC codes) were identified.[52]



One of North Carolina BB&T bank's B to B ads featuring local businesses and their owners: "They didn't judge my company from a desk. They came to my showroom to see what I do."

Within a given target industry and customer size, a company can segment by purchase criteria. For example, government laboratories need low prices and service contracts for scientific equipment; university laboratories need equipment that requires little service; and industrial laboratories need equipment that is highly reliable and accurate.

Sequential Segmentation

Business marketers generally identify segments through a sequential process. Consider an aluminum company: The company first undertook macrosegmentation. It looked at which end-use market to serve: automobile, residential, or beverage containers. It chose the residential market, and needed to determine the most attractive product application: semifinished material, building components, or aluminum mobile homes. Deciding to focus on building components, it considered the best customer size and chose large customers. The second stage consisted of microsegmentation. The company distinguished among customers buying on price, service, or quality. Because the aluminum company had a high-service profile, it decided to concentrate on the service-motivated segment of the market.

Business buyers seek different benefit bundles based on their stage in the purchase decision process:[53]

1. ***First-time prospects*** – Customers who have not yet purchased but want to buy from a vendor who understands their business, who explains things well, and whom they can trust.
2. ***Novices*** – Customers who are starting their purchasing relationship want easy-to-read manuals, hot lines, a high level of training, and knowledgeable sales reps.
3. ***Sophisticates*** – Established customers want speed in maintenance and repair, product customization, and high technical support.

These segments may also have different channel preferences. First-time prospects would prefer to deal with a company salesperson instead of a catalog or direct-mail channel, because the latter provides too little information. Sophisticates, on the other hand, may want to conduct more of their buying over electronic channels.

One proposed segmentation scheme classifies business buyers into three groups, each warranting a different type of selling:[54]

- ***Price-oriented customers (transactional selling).*** They want value through lowest price.
- ***Solution-oriented customers (consultative selling).*** They want value through more benefits and advice.
- ***Strategic-value customers (enterprise selling).*** They want value through the supplier co-investing and participating in the customer's business.

The authors cite several cases of mismanagement by companies that did not understand the business buyer:

- A packaging manufacturer decided to upgrade and rename sales reps as packaging consultants at a cost of $10 million, but 90 percent of its customers bought transactionally. The company failed and was acquired by a major competitor who reintroduced a transactional selling effort.
- A consulting firm replaced its long-term consultants with salespeople to sell quick consulting projects. They acquired many new clients but lost most of their old clients, who wanted consultative selling.
- A container manufacturer selling consultatively to a major food company was asked to join in some risk and gain sharing involving co-development of radically new packaging approaches. It refused and lost the account.

::: Market Targeting

Once the firm has identified its market-segment opportunities, it has to decide how many and which ones to target. Marketers are increasingly combining several variables in an effort to identify smaller, better-defined target groups. Thus, a bank may not only identify a group of wealthy retired adults, but within that group distinguish several segments depending on current income, assets, savings, and risk preferences. This has led some market researchers to advocate a *needs-based market segmentation approach*. Roger Best proposed the seven-step approach shown in Table 8.3.

TABLE 8.3

Steps in the Segmentation Process

	Description
1. Needs-Based Segmentation	Group customers into segments based on similar needs and benefits sought by customer in solving a particular consumption problem.
2. Segment Identification	For each needs-based segment, determine which demographics, lifestyles, and usage behaviors make the segment distinct and identifiable (actionable).
3. Segment Attractiveness	Using predetermined segment attractiveness criteria (such as market growth, competitive intensity, and market access), determine the overall attractiveness of each segment.
4. Segment Profitability	Determine segment profitability.
5. Segment Positioning	For each segment, create a "value proposition" and product-price positioning strategy based on that segment's unique customer needs and characteristics.
6. Segment "Acid Test"	Create "segment storyboards" to test the attractiveness of each segment's positioning strategy.
7. Marketing-Mix Strategy	Expand segment positioning strategy to include all aspects of the marketing mix: product, price, promotion, and place.

Source: Adapted from Robert J. Best, *Market-Based Management* (Upper Saddle River, NJ: Prentice Hall, 2000).

Effective Segmentation Criteria

Not all segmentation schemes are useful. For example, table salt buyers could be divided into blond and brunette customers, but hair color is undoubtedly irrelevant to the purchase of salt. Furthermore, if all salt buyers buy the same amount of salt each month, believe all salt is the same, and would pay only one price for salt, this market would be minimally segmentable from a marketing point of view.

To be useful, market segments must rate favorably on five key criteria:

- ***Measurable.*** The size, purchasing power, and characteristics of the segments can be measured.
- ***Substantial.*** The segments are large and profitable enough to serve. A segment should be the largest possible homogeneous group worth going after with a tailored marketing program. It would not pay, for example, for an automobile manufacturer to develop cars for people who are under four feet tall.
- ***Accessible.*** The segments can be effectively reached and served.
- ***Differentiable.*** The segments are conceptually distinguishable and respond differently to different marketing-mix elements and programs. If married and unmarried women respond similarly to a sale on perfume, they do not constitute separate segments.
- ***Actionable.*** Effective programs can be formulated for attracting and serving the segments.

Evaluating and Selecting the Market Segments

In evaluating different market segments, the firm must look at two factors: the segment's overall attractiveness and the company's objectives and resources. How well does a potential segment score on the five criteria? Does a potential segment have characteristics that make it generally attractive, such as size, growth, profitability, scale economies, and low risk? Does investing in the segment make sense given the firm's objectives, competencies, and resources? Some attractive segments may not mesh with the company's long-run objectives, or the company may lack one or more necessary competencies to offer superior value.

After evaluating different segments, the company can consider five patterns of target market selection, shown in Figure 8.6.

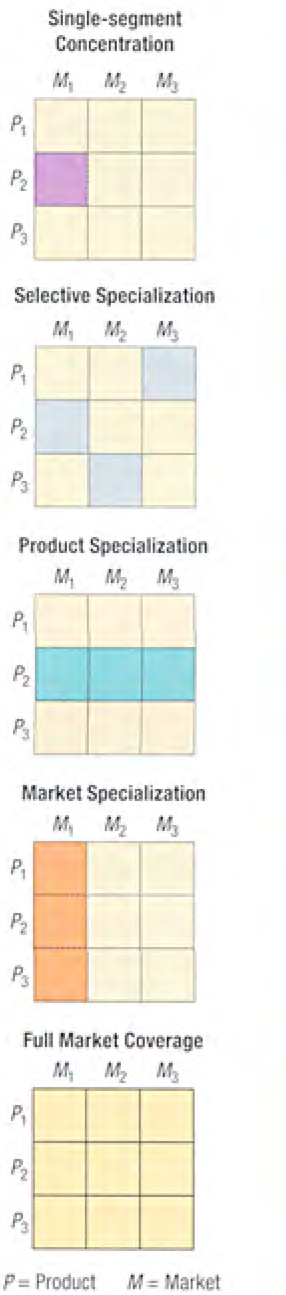


FIG. 8.6

Five Patterns of Target Market Selection

Source: Adapted from Derek F. Abell, *Defining the Business: The Starting Point of Strategic Planning* (Upper Saddle River, NJ: Prentice Hall, 1980), ch. 8, pp. 192–196.

SINGLE-SEGMENT CONCENTRATION Volkswagen concentrates on the small-car market and Porsche on the sports car market. Through concentrated marketing, the firm gains a strong knowledge of the segment's needs and achieves a strong market presence. Furthermore, the firm enjoys operating economies through specializing its production, distribution, and promotion. If it captures segment leadership, the firm can earn a high return on its investment.

However, there are risks. A particular market segment can turn sour or a competitor may invade the segment: When digital camera technology took off, Polaroid's earnings fell sharply. For these reasons, many companies prefer to operate in more than one segment. If selecting more than one segment to serve, a company should pay close attention to segment interrelationships on the cost, performance, and technology side. A company carrying fixed costs (sales force, store outlets) can add products to absorb and share some costs. The sales force will sell additional products, and a fast-food outlet will offer additional menu items. Economies of scope can be just as important as economies of scale.

Companies can try to operate in supersegments rather than in isolated segments. A **supersegment** is a set of segments sharing some exploitable similarity. For example, many symphony orchestras target people who have broad cultural interests, rather than only those who regularly attend concerts.

SELECTIVE SPECIALIZATION A firm selects a number of segments, each objectively attractive and appropriate. There may be little or no synergy among the segments, but each promises to be a moneymaker. This multisegment strategy has the advantage of diversifying the firm's risk. When Procter & Gamble launched Crest Whitestrips, initial target segments included newly engaged women and brides-to-be as well as gay males.

PRODUCT SPECIALIZATION The firm makes a certain product that it sells to several different market segments. An example would be a microscope manufacturer who sells to university, government, and commercial laboratories. The firm makes different microscopes for the different customer groups and builds a strong reputation in the specific product area. The downside risk is that the product may be supplanted by an entirely new technology.

MARKET SPECIALIZATION The firm concentrates on serving many needs of a particular customer group. An example would be a firm that sells an assortment of products only to university laboratories. The firm gains a strong reputation in serving this customer group and becomes a channel for additional products the customer group can use. The downside risk is that the customer group may suffer budget cuts or shrink in size.

FULL MARKET COVERAGE The firm attempts to serve all customer groups with all the products they might need. Only very large firms such as IBM (computer market), General Motors (vehicle market), and Coca-Cola (nonalcoholic beverage market) can undertake a full market coverage strategy. Large firms can cover a whole market in two broad ways: through undifferentiated marketing or differentiated marketing.

In *undifferentiated marketing*, the firm ignores segment differences and goes after the whole market with one offer. It designs a product and a marketing program that will appeal to the broadest number of buyers. It relies on mass distribution and advertising. It aims to endow the product with a superior image. Undifferentiated marketing is "the marketing counterpart to standardization and mass production in manufacturing."[55] The narrow product line keeps down costs of research and development, production, inventory, transportation, marketing research, advertising, and product management. The undifferentiated advertising program keeps down advertising costs. Presumably, the company can turn its lower costs into lower prices to win the price-sensitive segment of the market.

In *differentiated marketing*, the firm operates in several market segments and designs different products for each segment. Cosmetics firm Estée Lauder markets brands that appeal to women (and men) of different tastes: The flagship brand, the original Estée Lauder, appeals to older consumers; Clinique caters to middle-aged women; M.A.C. to youthful hipsters; Aveda to aromatherapy enthusiasts; and Origins to ecoconscious consumers who want cosmetics made from natural ingredients.[56]

EMMIS BROADCASTING

Emmis Communications owns three different radio stations in New York with three different distinct targets and positions: WQHT-FM ("Hot 97") proclaims that it plays "blazin' hip-hop (urban street music) and R&B," and is popular with listeners in the under-25 crowd. WRKS-FM (98.7 KISS-FM) describes itself as "offering the best variety of old school and today's R&B [rhythm and blues]," and appeals to older listeners. WQCD-FM (CD 101.9) is the country's largest smooth jazz radio station and targets adults age 25 to 54, who want a radio station to relax to and to listen to at work.[57] If one of the formats falls out of fashion, the fact that the other stations tap into different market segments provides a potential buffer to ratings and sales.

MANAGING MULTIPLE SEGMENTS The best way to manage multiple segments is to appoint segment managers with sufficient authority and responsibility for building the segment's business. At the same time, segment managers should not be so focused as to resist cooperating with other groups in the company. Consider the following situation.

BAXTER

Baxter operates several divisions selling different products and services to hospitals. Each division sends out its own invoices. Some hospitals complain about receiving as many as seven different Baxter invoices each month. Baxter's marketers finally convinced the separate divisions to send the invoices to headquarters so that Baxter could send one invoice a month to its customers.

Differentiated marketing: Emmis Broadcasting's WRKS (98.7 KISS-FM) appeals to older listeners with old school and today's R&B; its other stations in the New York market target under-25s with hip-hop (WQHT-FM) and adults 25-54 with smooth jazz (CD 101.9).

DIFFERENTIATED MARKETING COSTS Differentiated marketing typically creates more total sales than undifferentiated marketing. However, it also increases the costs of doing business. The following costs are likely to be higher:

- ***Product modification costs.*** Modifying a product to meet different market-segment requirements usually involves R&D, engineering, and special tooling costs.
- ***Manufacturing costs.*** It is usually more expensive to produce 10 units of 10 different products than 100 units of one product. The longer the production setup time and the smaller the sales volume of each product, the more expensive the product becomes. However, if each model is sold in sufficiently large volume, the higher setup costs may be quite small per unit.
- ***Administrative costs.*** The company has to develop separate marketing plans for each market segment. This requires extra marketing research, forecasting, sales analysis, promotion, planning, and channel management.
- ***Inventory costs.*** It is more costly to manage inventories containing many products.
- ***Promotion costs.*** The company has to reach different market segments with different promotion programs. The result is increased promotion-planning costs and media costs.

Because differentiated marketing leads to both higher sales and higher costs, nothing general can be said regarding the profitability of this strategy. Companies should be cautious about oversegmenting their markets. If this happens, they may want to turn to *countersegmentation* to broaden the customer base. For example, Johnson & Johnson broadened its target market for its baby shampoo to include adults. Smith Kline Beecham launched its Aquafresh toothpaste to attract three benefit segments simultaneously: those seeking fresh breath, whiter teeth, and cavity protection.

Additional Considerations

Three other considerations must be taken into account in evaluating and selecting segments: segment-by-segment invasion plans, updating segmentation schemes, and ethical choice of market targets.

SEGMENT-BY-SEGMENT INVASION PLANS A company would be wise to enter one segment at a time. Competitors must not know to what segment(s) the firm will move next.

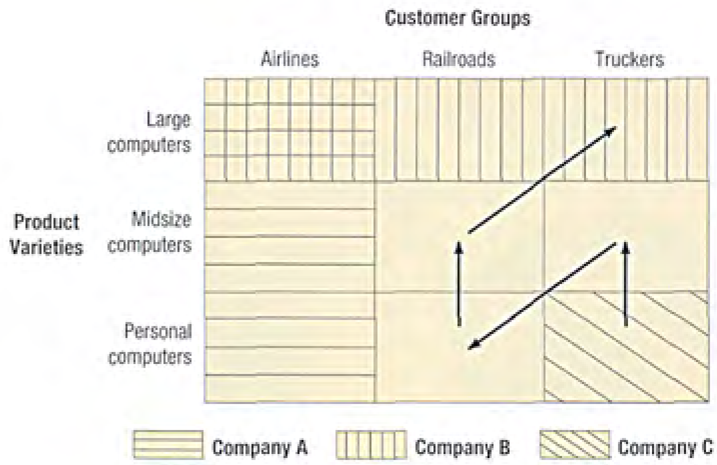


FIG. 8.7

Segment-by-Segment Invasion Plan

Segment-by-segment invasion plans are illustrated in Figure 8.7. Three firms, A, B, and C, have specialized in adapting computer systems to the needs of airlines, railroads, and trucking companies. Company A meets all the computer needs of airlines. Company B sells large computer systems to all three transportation sectors. Company C sells personal computers to trucking companies.

Where should company C move next? Arrows have been added to the chart to show the planned sequence of segment invasions. Company C will next offer midsize computers to trucking companies. Then, to allay company B's concern about losing some large computer business with trucking companies, C's next move will be to sell personal computers to railroads. Later, C will offer midsize computers to railroads. Finally, it may launch a full-scale attack on company B's large computer position in trucking companies. Of course, C's hidden planned moves are provisional in that much depends on competitors' segment moves and responses.

Unfortunately, too many companies fail to develop a long-term invasion plan. PepsiCo is an exception. It first attacked Coca-Cola in the grocery market, then in the vending-machine market, then in the fast-food market, and so on. Japanese firms also plot their invasion sequence. They first gain a foothold in a market, then enter new segments with products. Toyota began by introducing small cars (Tercel, Corolla), then expanded into midsize cars (Camry, Avalon), and finally into luxury cars (Lexus).

A company's invasion plans can be thwarted when it confronts blocked markets. The invader must then figure out a way to break in. The problem of entering blocked markets calls for a megamarketing approach. **Megamarketing** is the strategic coordination of economic, psychological, political, and public relations skills, to gain the cooperation of a number of parties in order to enter or operate in a given market. Pepsi used megamarketing to enter the Indian market.

PEPSICO

After Coca-Cola left India, Pepsi worked with an Indian business group to gain government approval for its entry, over the objections of domestic soft drink companies and anti-multinational legislators. Pepsi offered to help India export some agricultural products in a volume that would more than cover the cost of importing soft-drink concentrate. Pepsi also promised to help rural areas in their economic development. It further offered to transfer food-processing, packaging, and water-treatment technology to India. Pepsi's bundle of benefits won the support of various Indian interest groups.

Once in, a multinational must be on its best behavior. This calls for well-thought-out *civic positioning*.

A Pepsi ad from India. To enter the Indian market, Pepsi used megamarketing: With the aid of an Indian business group, it offered a package of benefits that gained it acceptance.

HEWLETT-PACKARD

Hewlett-Packard positions itself as a company implementing "e-inclusion,"— the attempt to help bring the benefits of technology to the poor. Toward that end, HP has begun a three-year project designed to create jobs, improve education, and provide better access to government services in the Indian state of Kuppam. Working with the local government, as well as a branch of HP Labs based in India, the company is helping to provide the rural poor with access to government records, schools, health information, crop prices, and so forth. Its hope is to stimulate small, tech-based businesses. Not only does this build goodwill and the HP brand in India, but it will also help the company discover new, profitable lines of business.[58]

UPDATING SEGMENTATION SCHEMES Market segmentation analysis must be done periodically because segments change. At one time the personal computer industry segmented its products purely on speed and power. Later, PC marketers recognized an emerging "Soho" market, named for "small office and home office." Mail-order companies such as Dell and Gateway appealed to this market's requirement for high performance coupled with low price and user-friendliness. Shortly thereafter, PC makers began to see Soho as comprised of smaller segments. "Small-office needs might be very different from home-office needs," says one Dell executive.[59]

One way to discover new segments is to investigate the hierarchy of attributes consumers examine in choosing a brand if they use phased decision strategies. This process is called **market partitioning**. Years ago, most car buyers first decided on the manufacturer and then on one of its car divisions (*brand-dominant hierarchy*). A buyer might favor General Motors cars and, within this set, Pontiac. Today, many buyers decide first on the nation from which they want to buy a car (*nation-dominant hierarchy*). Buyers may first decide they want to buy a Japanese car, then Toyota, and then the Corolla model of Toyota. Companies must monitor potential shifts in consumers' hierarchy of attributes and adjust to changing priorities.

The hierarchy of attributes can reveal customer segments. Buyers who first decide on price are price dominant; those who first decide on the type of car (e.g., sports, passenger, station wagon) are type dominant; those who first decide on the car brand are brand dominant. Those who are type/price/brand dominant make up a segment; those who are quality/service/type dominant make up another segment. Each segment may have distinct demographics, psychographics, and mediagraphics.[60]

ETHICAL CHOICE OF MARKET TARGETS Market targeting sometimes generates public controversy.[61] The public is concerned when marketers take unfair advantage of vulnerable groups (such as children) or disadvantaged groups (such as inner-city poor people), or promote potentially harmful products. The cereal industry has been heavily criticized for marketing efforts directed toward children. Critics worry that high-powered appeals presented through the mouths of lovable animated characters will overwhelm children's defenses and lead them to want sugared cereals or poorly balanced breakfasts. Toy marketers have been similarly criticized. McDonald's and other chains have drawn criticism for pitching their high-fat, salt-laden fare to low-income, inner-city residents.

Internal documents from R. J. Reynolds and Brown & Williamson Tobacco Corporation (marketer of the Kool brand) have revealed the extent to which these companies targeted black youths age 16 to 25, particularly with their menthol brands.[62] G. Heileman Brewing drew fire when it extended its Colt 45 malt liquor line with Powermaster, a new high-test malt (5.9 alcohol). Malt liquor is consumed primarily by blacks, and by targeting blacks extensively Heileman was itself targeted by federal officials, industry leaders, black activists, and the media.[63]

Not all attempts to target children, minorities, or other special segments draw criticism. Colgate-Palmolive's Colgate Junior toothpaste has special features designed to get children to brush longer and more often. Other companies are responding to the special needs of minority segments. Black-owned ICE theaters noticed that although moviegoing by blacks has surged, there were few inner-city theaters. Starting in Chicago, ICE partnered with the black communities in which it operates theaters, using local radio stations to promote films and featuring favorite food items at concession stands.[64] Thus the issue is not who is targeted, but rather, how and for what. Socially responsible marketing calls for targeting that serves not only the company's interests, but also the interests of those targeted.

Socially responsible marketing: Colgate Junior Toothpaste ads promote special features designed to get children to brush more often.

This is the case being made by many companies marketing to the nation's preschoolers. With nearly 4 million youngsters attending some kind of organized child care, the potential market—including both kids and parents—is too great to pass up. So in addition to stocking the usual standards like art easels, gerbil cages, and blocks, the nation's preschools are likely to have Care Bear worksheets, Pizza Hut reading programs, and Nickelodeon magazines.

NICKELODEON, PIZZA HUT, FORD MOTOR CORP.

Cable TV station Nickelodeon was one of the first companies to capitalize on the preschool market when it launched *Nick Jr.* family magazine in 1999. It distributes half of the magazine's 1 million copies to preschools free and makes no bones about the fact that it is trying to sell parents on Nickelodeon shows and licensed products. In contrast, other corporations insist that their preschool products are designed purely to meet a social need. Pizza Hut is one. Its preschool program offers each student a certificate for a personal pizza if his or her teacher spends at least 60 minutes a week reading to the class for four consecutive weeks. In 2002, 1.6 million preschoolers in 33,800 child-care facilities participated. Likewise, automaker Ford says it sends posters to 100,000 preschools, child-care centers, and kindergarten classes to encourage children ages 2 to 5 to think about safety. The poster is an alphabet of safety tips with, not surprisingly, A for automobile (but no F for Ford).

Teachers and parents are divided in their feelings about the ethics of this increasing preschool marketing push. Some side with groups like Stop Commercial Exploitation of Children who feel that preschoolers are incredibly susceptible to advertising and that schools' endorsements of products make children believe the product is good for them—no matter what it is. Yet, many preschools and day care centers operating on tight budgets welcome the free resources.[65]

SUMMARY :::

1. Target marketing involves three activities: market segmentation, market targeting, and market positioning.
2. Markets can be targeted at four levels: segments, niches, local areas, and individuals. Market segments are large, identifiable groups within a market. A niche is a more narrowly defined group. Marketers appeal to local markets through grassroots marketing for trading areas, neighborhoods, and even individual stores.
3. More companies now practice individual and mass customization. The future is likely to see more self-marketing, a form of marketing in which individual consumers take the initiative in designing products and brands.
4. There are two bases for segmenting consumer markets: consumer characteristics and consumer responses. The major segmentation variables for consumer markets are geographic, demographic, psychographic, and behavioral. These variables can be used singly or in combination.
5. Business marketers use all these variables along with operating variables, purchasing approaches, and situational factors.
6. To be useful, market segments must be measurable, substantial, accessible, differentiable, and actionable.
7. A firm has to evaluate the various segments and decide how many and which ones to target: a single segment, several segments, a specific product, a specific market, or the full market. If it serves the full market, it must choose between differentiated and undifferentiated marketing. Firms must also monitor segment relationships, and seek economies of scope and the potential for marketing to supersegments. They should develop segment-by-segment invasion plans.
8. Marketers must choose target markets in a socially responsible manner.

APPLICATIONS :::

Marketing Debate Is Mass Marketing Dead?

With marketers increasingly adopting more and more refined market segmentation schemes—fueled by the Internet and other customization efforts—some critics claim that mass marketing is dead. Others counter that there will always be room for large brands that employ marketing programs targeting the mass market.

Take a position: Mass marketing is dead versus Mass marketing is still a viable way to build a profitable brand.

Marketing Discussion

Descriptive versus Behavioral Market Segmentation Schemes Think of various product categories. How would you classify yourself in terms of the various segmentation schemes? How would marketing be more or less effective for you depending on the segment involved? How would you contrast demographic versus behavioral segment schemes? Which ones do you think would be most effective for marketers trying to sell to you?

MARKETING SPOTLIGHT | HSBC

HSBC is known as the "world's local bank." Originally called the Hong Kong and Shanghai Banking Corporation Limited, HSBC was established in 1865 to finance the growing trade between China and the United Kingdom. HSBC is now the second-largest bank in the world, serving 100 million customers through 9,500 branches in 79 countries. The company is organized by business line (personal financial services; consumer finance; commercial banking; corporate investment banking and markets; private banking), as well as by geographic segment (Asia-Pacific, U.K./Eurozone, North America/NAFTA, South America, Middle East).

Despite operating in 79 different countries, the bank works hard to maintain a local feel and local knowledge in each area. HSBC's fundamental operating strategy is to remain close to its customers. As HSBC chairman Sir John Bond said in November 2003, "Our position as the world's local bank enables us to approach each country uniquely, blending local knowledge with a world-wide operating platform."

For example, consider HSBC's local marketing efforts in New York City. To prove to jaded New Yorkers that the London-based financial behemoth was "the world's local bank," HSBC held a "New York City's Most Knowledgeable Cabbie" contest. The winning cabbie gets paid to drive full-time for HSBC for the year, and HSBC customers win, too. Any customer showing an HSBC bankcard, checkbook, or bank statement can get a free ride in the HSBC-branded Bankcab. The campaign demonstrates HSBC's local knowledge. "In order to make New Yorkers believe you're local, you have to act local," said Renegade Marketing Group's CEO Drew Neisser.

Across the world in Hong Kong, HSBC undertook a different campaign. In the region hit hard by the Severe Acute Respiratory Syndrome (SARS) outbreak, HSBC launched a program to revitalize the local economy. HSBC "plowed back interest payments" to customers who worked in industries most affected by SARS (cinemas, hotels, restaurants, and travel agencies). The program eased its customers' financial burden. The bank also promoted Hong Kong's commercial sector by offering discounts and rebates for customers who use an HSBC credit card when shopping and dining out, to help businesses affected by the downturn. More than 1,500 local merchants participated in the promotion.

In addition to local marketing, HSBC does niche marketing. For example, it found a little-known product area that was growing at 125 percent a year: pet insurance. In December 2003 it announced that it will distribute nationwide pet insurance through its HSBC Insurance agency, making the insurance available to its depositors.

HSBC also segments demographically. In the United States, the bank will target the immigrant population, particularly Hispanics, now that it has acquired Bital in Mexico, where many migrants to the United States deposit money.

Overall, the bank has been consciously pulling together its worldwide businesses under a single global brand with the "world's local bank" slogan. The aim is to link its international size with close relationships in each of the countries in which it operates. The company spends $600 million annually on global marketing and will likely consolidate and use fewer ad agencies. HSBC will decide who gets the account by giving each agency a "brand-strategy exercise." Agencies will be vying for the account by improving on HSBC's number 37 global brand ranking.

Discussion Questions

1. What have been the key success factors for HSBC?
2. Where is HSBC vulnerable? What should it watch out for?
3. What recommendations would you make to senior marketing executives going forward? What should they be sure to do with its marketing?

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PART

4

BUILDING STRONG BRANDS

IN THIS CHAPTER, WE WILL ADDRESS THE FOLLOWING QUESTIONS:

1. What is a brand and how does *branding work*?
2. What is brand equity?
3. How is brand equity built, measured, and managed?
4. What are the important decisions in developing a branding strategy?

Building a strong brand requires careful planning and a great deal of long-term investment. At the heart of a successful brand is a great product or service, backed by creatively designed and executed marketing. One of the hottest brands around is Google:

Founded in 1998 by two Stanford University Ph.D. students, search engine Google's name is a play on the word googol—the number represented by a 1 followed by 100 zeroes—a reference to the huge amount of data online. With 200 million search requests daily, the company has turned a profit by focusing on searches alone and not adding other services, as was the case with many other portals. By focusing on plain text, avoiding ads, and using sophisticated search algorithms, Google provides fast and reliable service. Google makes money from paid listings relevant to a searcher's query, and by licensing its technology to firms such as AOL and the Washington Post. *In perhaps the ultimate sign of success, the brand is now often used as a verb—"to google" is to search online. Based on a public poll of the brand that had made the most impact in their lives, Google was named "Brand of the Year" in 2002 by Interbrand branding consultants. This success has not gone unnoticed, however, and has led to strong competitive responses from industry giants Yahoo! and Microsoft.*[1]

>>>

Google founders Larry Page and Sergey Brin.

Perhaps the most distinctive skill of professional marketers is their ability to create, maintain, enhance, and protect brands. Branding has become a marketing priority. Successful brands such as Starbucks, Sony, and Nike command a price premium and elicit much loyalty. New brands such as Krispy Kreme, Red Bull, and JetBlue capture the imagination of consumers and the financial community alike. Marketers of successful twenty-first-century brands must excel at the strategic brand management process. *Strategic brand management* involves the design and implementation of marketing activities and programs to build, measure, and manage brands to maximize their value. The strategic brand management process involves four main steps:

- Identifying and establishing brand positioning.
- Planning and implementing brand marketing.
- Measuring and interpreting brand performance.
- Growing and sustaining brand value.

Chapter 10 deals with brand positioning. The remaining topics are discussed in this chapter. Chapter 11 reviews important concepts dealing with competition.

::: What Is Brand Equity?

The American Marketing Association defines a **brand** as "a name, term, sign, symbol, or design, or a combination of them, intended to identify the goods or services of one seller or group of sellers and to differentiate them from those of competitors." A brand is thus a product or service that adds dimensions that differentiate it in some way from other products or services designed to satisfy the same need. These differences may be functional, rational, or tangible—related to product performance of the brand. They may also be more symbolic, emotional or intangible—related to what the brand represents.

Branding has been around for centuries as a means to distinguish the goods of one producer from those of another.[2] The earliest signs of branding in Europe were the medieval guilds' requirement that craftspeople put trademarks on their products to protect themselves and consumers against inferior quality. In the fine arts, branding began with artists signing their works. Brands today play a number of important roles that improve consumers' lives and enhance the financial value of firms.

The Role of Brands

Brands identify the source or maker of a product and allow consumers—either individuals or organizations—to assign responsibility to a particular manufacturer or distributor. Consumers may evaluate the identical product differently depending on how it is branded. Consumers learn about brands through past experiences with the product and its marketing program. They find out which brands satisfy their needs and which ones do not. As consumers' lives become more complicated, rushed, and time-starved, the ability of a brand to simplify decision making and reduce risk is invaluable.[3]

Brands also perform valuable functions for firms.[4] First, they simplify product handling or tracing. Brands help to organize inventory and accounting records. A brand also offers the firm legal protection for unique features or aspects of the product.[5] The brand name can be protected through registered trademarks; manufacturing processes can be protected through patents; and packaging can be protected through copyrights and designs. These intellectual property rights ensure that the firm can safely invest in the brand and reap the benefits of a valuable asset.

MARKETING MEMO — THE BRAND REPORT CARD

The world's strongest brands share 10 attributes:

1. ***The brand excels at delivering the benefits consumers truly desire.*** Do you focus relentlessly on maximizing customers' product and service experiences?
2. ***The brand stays relevant.*** Are you in touch with your customers' tastes, current market conditions, and trends?
3. ***The pricing strategy is based on consumer perceptions of value.*** Have you optimized price, cost, and quality to meet or exceed customer expectations?
4. ***The brand is properly positioned.*** Have you established necessary and competitive points of parity with competitors? Have you established desirable and deliverable points of difference?
5. ***The brand is consistent.*** Are you sure that your marketing programs are not sending conflicting messages?
6. ***The brand portfolio and hierarchy makes sense.*** Can the corporate brand create a seamless umbrella for all the brands in the portfolio? Do you have a brand hierarchy that is well thought out and well understood?
7. ***The brand makes use of and coordinates a full repertoire of marketing activities to build equity.*** Have you capitalized on the unique capabilities of each communication option while ensuring that the meaning of the brand is consistently represented?
8. ***The brand's managers understand what the brand means to consumers.*** Do you know what customers like and do not like about your brand? Have you created detailed, research-driven portraits of your target customers?
9. ***The brand is given proper, sustained support.*** Are the successes or failures of marketing programs fully understood before they are changed? Is the brand given sufficient R&D support?
10. ***The company monitors sources of brand equity.*** Have you created a brand charter that defines the meaning and equity of the brand and how it should be treated? Have you assigned explicit responsibility for monitoring and preserving brand equity?

Source: Adapted from Kevin Lane Keller, "The Brand Report Card," *Harvard Business Review* (January 1, 2000): 147–157

Brands can signal a certain level of quality so that satisfied buyers can easily choose the product again.[6] Brand loyalty provides predictability and security of demand for the firm and creates barriers to entry that make it difficult for other firms to enter the market. Loyalty also can translate into a willingness to pay a higher price—often 20 to 25 percent more.[7] Although competitors may easily duplicate manufacturing processes and product designs, they cannot easily match lasting impressions in the minds of individuals and organizations from years of marketing activity and product experience. In this sense, branding can be seen as a powerful means to secure a competitive advantage.[8]

To firms, brands thus represent enormously valuable pieces of legal property that can influence consumer behavior, be bought and sold, and provide the security of sustained future revenues to their owner.[9] Large earning multiples have been paid for brands in mergers or acquisitions, starting with the boom years of the mid-1980s. The price premium is often justified on the basis of assumptions of the extra profits that could be extracted and sustained from the brands, as well as the tremendous difficulty and expense of creating similar brands from scratch. Wall Street believes that strong brands result in better earnings and profit performance for firms, which, in turn, creates greater value for shareholders. Much of the recent interest in brands by senior management has been a result of these bottom-line financial considerations. "Marketing Memo: The Brand Report Card" lists 10 key characteristics based on a review of the world's strongest brands.[10]

The Scope of Branding

How then do you "brand" a product? Although firms provide the impetus to brand creation through marketing programs and other activities, ultimately a brand is something that resides in the minds of consumers. A brand is a perceptual entity that is rooted in reality but reflects the perceptions and perhaps even the idiosyncrasies of consumers.

Branding is endowing products and services with the power of a brand. Branding is all about creating differences. To brand a product, it is necessary to teach consumers "who" the product is—by giving it a name and using other brand elements to help identify it—as well as "what" the product does and "why" consumers should care. Branding involves creating mental structures and helping consumers organize their knowledge about products and services in a way that clarifies their decision making and, in the process, provides value to the firm.

For branding strategies to be successful and brand value to be created, consumers must be convinced that there are meaningful differences among brands in the product or service category. The key to branding is that consumers must not think that all brands in the category are the same.

Brand differences often are related to attributes or benefits of the product itself. Gillette, Merck, Sony, 3M, and others have been leaders in their product categories for decades due, in part, to continual innovation. Other brands create competitive advantages through non-product-related means. Coca-Cola, Calvin Klein, Gucci, Tommy Hilfiger, Marlboro, and others have become leaders in their product categories by understanding consumer motivations and desires and creating relevant and appealing images around their products.

Branding can be applied virtually anywhere a consumer has a choice. It is possible to brand a physical good (Campbell's soup, Pantene shampoo, or Ford Mustang automobiles), a service (Singapore Airlines, Bank of America, or BlueCross/BlueShield medical insurance), a store (Nordstrom department store, Foot Locker specialty store, or Safeway supermarket), a person (Tom Clancy, Britney Spears, or Andre Agassi), a place (the city of Sydney, state of Texas, or country of Spain), an organization (UNICEF, American Automobile Association, or The Rolling Stones), or an idea (abortion rights, free trade, or freedom of speech).

Defining Brand Equity

Brand equity is the added value endowed to products and services. This value may be reflected in how consumers think, feel, and act with respect to the brand, as well as the prices, market share, and profitability that the brand commands for the firm. Brand equity is an important intangible asset that has psychological and financial value to the firm.

Marketers and researchers use various perspectives to study brand equity.[11] Customer-based approaches view brand equity from the perspective of the consumer—either an individual or an organization.[12] The premise of customer-based brand equity models is that the power of a brand lies in what customers have seen, read, heard, learned, thought, and felt about the brand over time. In other words, the power of a brand lies in the minds of existing or potential customers and what they have experienced directly and indirectly about the brand.[13]

Branding a place: ad for Australia tourism focusing on the city of Sydney with its signature opera house.

Customer-based brand equity can be defined as the differential effect that brand knowledge has on consumer response to the marketing of that brand.[14] A brand is said to have positive customer-based brand equity when consumers react more favorably to a product and the way it is marketed when the brand is identified as compared to when it is not. A brand is said to have negative customer-based brand equity if consumers react less favorably to marketing activity for the brand under the same circumstances.

There are three key ingredients to this definition. First, brand equity arises from differences in consumer response. If no differences occur, then the brand name product can essentially be classified as a commodity or generic version of the product. Competition would then probably be based on price.

Second, these differences in response are a result of consumer's knowledge about the brand. **Brand knowledge** consists of all the thoughts, feelings, images, experiences, beliefs, and so on that become associated with the brand. In particular, brands must create strong, favorable, and unique brand associations with customers, as has been the case with Volvo (*safety*), Hallmark (*caring*), and Harley-Davidson (*adventure*). Third, the differential response by consumers that makes up the brand equity is reflected in perceptions, preferences, and behavior related to all aspects of the marketing of a brand. Table 9.1 summarizes some of these key benefits of brand equity.

The challenge for marketers in building a strong brand is therefore ensuring that customers have the right type of experiences with products and services and their marketing programs to create the desired brand knowledge structures for the brand.

APPLE COMPUTER

Apple Computer is recognized as a master at building a strong brand that resonates with customers across generations and national boundaries. Named "2003 Marketer of the Year" by *Advertising Age* magazine, Apple achieves incredible brand loyalty largely by delivering on its mission as defined by CEO Steven Jobs: "To create great things that change people's lives." It has created an army of Apple evangelists not just because of its great advertising but also because it focuses on the consumer in everything it does. Some of its biggest buzz campaigns don't even originate with the company: In a trendy club in Manhattan's meatpacking district, two DJs host Tuesday night "Open iPod DJ Parties." Yet, the company doesn't rely on customers to do its marketing. Apple spent $293 million to create 73 retail stores to fuel excitement for the brand, including a store in New York's SoHo that drew over 14 million visitors in 2003. The rationale behind the move to retail is that the more people can see and touch Apple products—and see what Apple can do for them—the more likely Apple is to increase its market share, which is still a tiny slice of the PC market.[15]

Consumer knowledge is what drives the differences that manifest themselves in brand equity. In an abstract sense, brand equity can be seen as providing marketers with a vital strategic "bridge" from their past to their future.

TABLE 9.1

Marketing Advantages of Strong Brands

Improved Perceptions of Product Performance
Greater Loyalty
Less Vulnerability to Competitive Marketing Actions
Less Vulnerability to Marketing Crises
Larger Margins
More Inelastic Consumer Response to Price Increases
More Elastic Consumer Response to Price Decreases
Greater Trade Cooperation and Support
Increased Marketing Communications Effectiveness
Possible Licensing Opportunities
Additional Brand Extension Opportunities

Brand Equity as a Bridge

From the perspective of brand equity, all the marketing dollars spent each year on products and services should be thought of as investments in consumer brand knowledge. The *quality* of the investment in brand building is the critical factor, not necessarily the *quantity*, beyond some minimal threshold amount.

It is actually possible to "overspend" on brand building if money is not spent wisely. In the beverage category, brands such as Michelob, Miller Lite, and 7Up saw sales decline in the 1990s despite sizable marketing support, arguably because of poorly targeted and delivered marketing campaigns. And there are numerous examples of brands that amass a great deal of brand equity by spending on marketing activities that create valuable, enduring memory traces in the consumers' minds. Despite being outspent by such beverage brand giants as Coca-Cola, Pepsi, and Budweiser, the California Milk Processor Board was able to reverse a decades-long decline in consumption of milk in California partly through its well-designed and executed "Got Milk?" campaign.

At the same time, the brand knowledge created by these marketing investments dictates appropriate future directions for the brand. Consumers will decide, based on what they think and feel about the brand, where (and how) they believe the brand should go and grant permission (or not) to any marketing action or program. New products such as Crystal Pepsi, Levi's Tailored Classic suits, Fruit of the Loom laundry detergent, and Cracker Jack cereal failed because consumers found them inappropriate.

A brand is essentially a marketer's promise to deliver predictable product or service performance. A **brand promise** is the marketer's vision of what the brand must be and do for consumers. At the end of the day, the true value and future prospects of a brand rest with consumers, their knowledge about the brand, and their likely response to marketing activity as a result of this knowledge. Understanding consumer brand knowledge—all the different things that become linked to the brand in the minds of consumers—is thus of paramount importance because it is the foundation of brand equity.

Virgin, the brainchild of England's flamboyant Richard Branson, vividly illustrates the power enjoyed and responsibility assumed by a strong brand.[16]

VIRGIN

Starting with Virgin Music, Branson's Virgin Group Ltd., now spans three continents and 200 businesses, including Virgin Atlantic Airways, Virgin Mobile (cell phones), Virgin Energy, Virgin Rail, Virgin Direct (insurance, mortgages, and investment funds), and Virgin Hotels. Clearly, Branson can create interest in almost any business he wants by simply attaching the name "Virgin" to it. Virgin Mobile exemplifies this strategy. Branson supplies the brand, a small initial investment, and takes a majority control while big-name partners come up with the cash. Some marketing and financial critics point out that he is diluting the brand, that it covers too many businesses. Branson has had some fumbles: Virgin Cola, Virgin Cosmetics, and Virgin Vodka have all but disappeared. But Branson replies: "We have a strategy of using the credibility of our brand to challenge the dominant players in a range of industries where we believe the consumer is not getting value for money. . . . If the consumer benefits, I see no reason why we should be frightened about launching new products." One of Branson's newest ventures: He's jumping into the fiercely competitive discount airline business in the United States with Virgin USA in 2005.

Brand Equity Models

Although there is agreement about basic principles, a number of models of brand equity offer some different perspectives. Here we briefly highlight four of the more established ones.

BRAND ASSET VALUATOR Advertising agency Young and Rubicam (Y&R) developed a model of brand equity called Brand Asset Valuator (BAV). Based on research with almost 200,000 consumers in 40 countries, BAV provides comparative measures of the brand equity of thousands of brands across hundreds of different categories. There are four key components—or pillars—of brand equity, according to BAV:

- ***Differentiation*** measures the degree to which a brand is seen as different from others.
- ***Relevance*** measures the breadth of a brand's appeal.

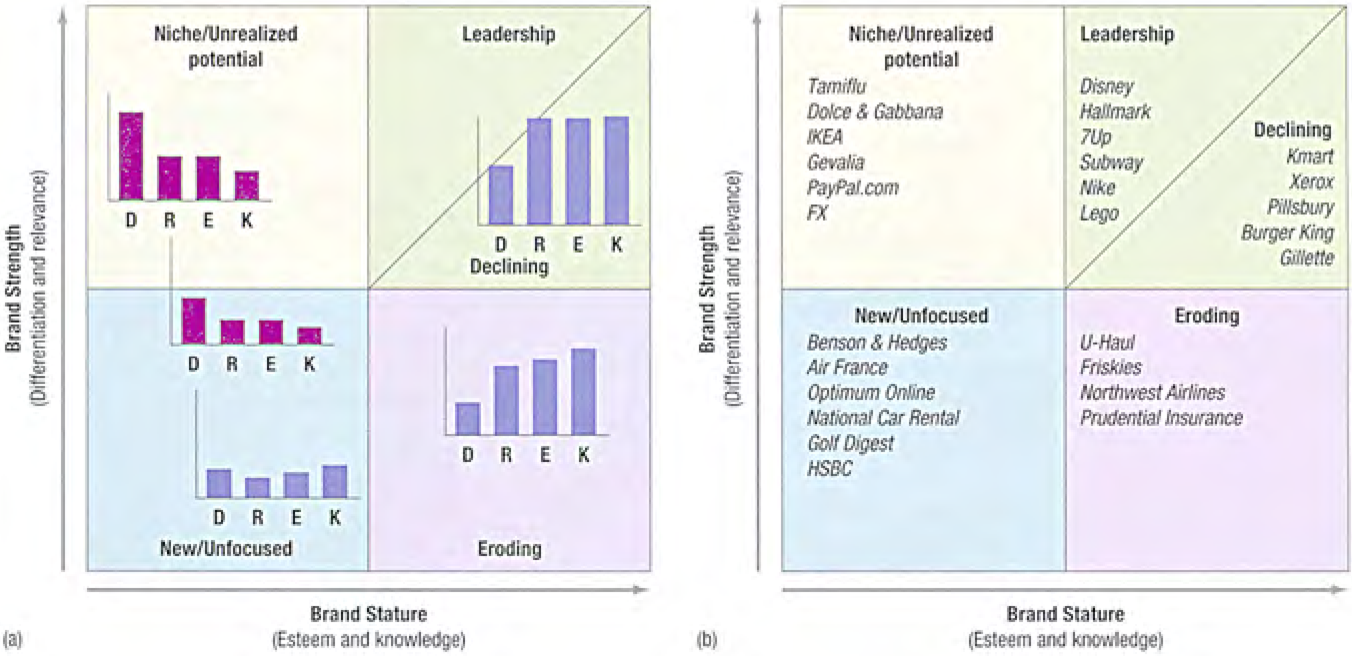


FIG. 9.1

BAV Power Grid

- ***Esteem*** measures how well the brand is regarded and respected.
- ***Knowledge*** measures how familiar and intimate consumers are with the brand.

Differentiation and Relevance combine to determine *Brand Strength*. These two pillars point to the brand's future value, rather than just reflecting its past. Esteem and Knowledge together create *Brand Stature*, which is more of a "report card" on past performance.

Examining the relationships among these four dimensions—a brand's "pillar pattern"—reveals much about its current and future status. Brand Strength and Brand Stature can be combined to form a Power Grid that depicts the stages in the cycle of brand development—each with its characteristic pillar patterns—in successive quadrants (see Figure 9.1). New brands, just after they are launched, show low levels on all four pillars. Strong new brands tend to show higher levels of Differentiation than Relevance, while both Esteem and Knowledge are lower still. Leadership brands show high levels on all four pillars. Finally, declining brands show high Knowledge—evidence of past performance—relative to a lower level of Esteem, and even lower Relevance and Differentiation.

AAKER MODEL Former UC-Berkeley marketing professor David Aaker views brand equity as a set of five categories of brand assets and liabilities linked to a brand that add to or subtract from the value provided by a product or service to a firm and/or to that firm's customers. These categories of brand assets are: (1) brand loyalty, (2) brand awareness, (3) perceived quality, (4) brand associations, and (5) other proprietary assets such as patents, trademarks, and channel relationships.

According to Aaker, a particularly important concept for building brand equity is *brand identity*—the unique set of brand associations that represent what the brand stands for and promises to customers.[17] Aaker sees brand identity as consisting of 12 dimensions organized around 4 perspectives: *brand-as-product* (product scope, product attributes, quality/value, uses, users, country of origin); *brand-as-organization* (organizational attributes, local versus global); *brand-as-person* (brand personality, brand–customer relationships); and *brand-as-symbol* (visual imagery/metaphors and brand heritage).

Aaker also conceptualizes brand identity as including a core and an extended identity. The core identity—the central, timeless essence of the brand—is most likely to remain constant as the brand travels to new markets and products. The extended identity includes various brand identity elements, organized into cohesive and meaningful groups. If we apply this approach to Saturn, the newest General Motors car division might yield the following:[18]

- ***Core Identity.*** A world-class car with employees who treat customers with respect and as friends.
- ***Extended Identity.*** U.S. subcompact with Spring Hill, Tennessee, plant; no pressure, no haggling, informative retail experience; thoughtful, friendly, down-to-earth, youthful and lively personality; committed employees and loyal users.

BRANDZ Marketing research consultants Millward Brown and WPP have developed the BRANDZ model of brand strength, at the heart of which is the BrandDynamics pyramid. According to this model, brand building involves a sequential series of steps, where each step is contingent upon successfully accomplishing the previous step. The objectives at each step, in ascending order, are as follows:

- ***Presence.*** Do I know about it?
- ***Relevance.*** Does it offer me something?
- ***Performance.*** Can it deliver?
- ***Advantage.*** Does it offer something better than others?
- ***Bonding.*** Nothing else beats it.

Research has shown that bonded consumers, those at the top level of the pyramid, build stronger relationships with the brand and spend more of their category expenditures on the brand than those at lower levels of the pyramid. More consumers, however, will be found at the lower levels. The challenge for marketers is to develop activities and programs that help consumers move up the pyramid.

BRAND RESONANCE The brand resonance model also views brand building as an ascending, sequential series of steps, from bottom to top: (1) ensuring identification of the brand with customers and an association of the brand in customers' minds with a specific product class or customer need; (2) firmly establishing the totality of brand meaning in the minds of customers by strategically linking a host of tangible and intangible brand associations; (3) eliciting the proper customer responses in terms of brand-related judgment and feelings; and (4) converting brand response to create an intense, active loyalty relationship between customers and the brand. According to this model, enacting the four steps involves establishing six "brand building blocks" with customers. These brand building blocks can be assembled in terms of a brand pyramid, as illustrated in Figure 9.2. The model emphasizes the duality of brands—the rational route to brand building is the left-hand side of the pyramid, whereas the emotional route is the right-hand side.[19]

MasterCard is an example of a brand with duality, as it emphasizes both the rational advantage to the credit card, through its acceptance at establishments worldwide, and the emotional advantage through its award-winning "priceless" advertising campaign, which shows people buying items to reach a certain goal. The goal itself—a feeling, an accomplishment, or other intangible—is "priceless" ("There are some things money can't buy, for everything else, there's MasterCard.").

The creation of significant brand equity involves reaching the top or pinnacle of the brand pyramid, and will occur only if the right building blocks are put into place.

- ***Brand salience*** relates to how often and easily the brand is evoked under various purchase or consumption situations.
- ***Brand performance*** relates to how the product or service meets customers' functional needs.
- ***Brand imagery*** deals with the extrinsic properties of the product or service, including the ways in which the brand attempts to meet customers' psychological or social needs.
- ***Brand judgments*** focus on customers' own personal opinions and evaluations.
- ***Brand feelings*** are customers' emotional responses and reactions with respect to the brand.
- ***Brand resonance*** refers to the nature of the relationship that customers have with the brand and the extent to which customers feel that they are "in sync" with the brand.

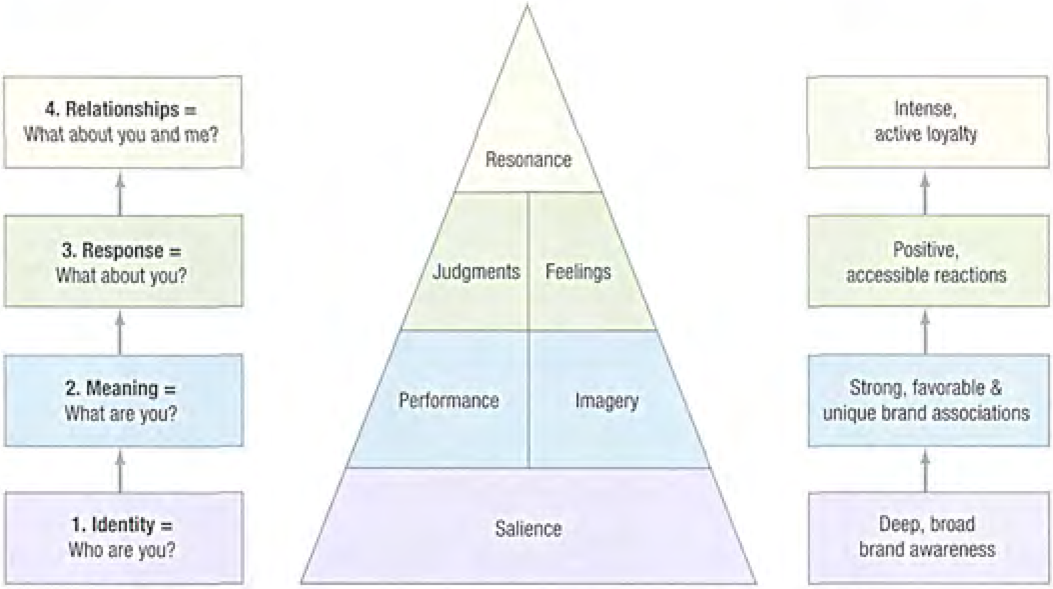


FIG. 9.2 Brand Resonance Pyramid

Resonance is characterized in terms of the intensity or depth of the psychological bond customers have with the brand, as well as the level of activity engendered by this loyalty. Examples of brands with high resonance include Harley-Davidson, Apple, and eBay.

::: Building Brand Equity

Marketers build brand equity by creating the right brand knowledge structures with the right consumers. This process depends on *all* brand-related contacts—whether marketer-initiated or not. From a marketing management perspective, however, there are three main sets of *brand equity drivers:*

1. ***The initial choices for the brand elements or identities making up the brand (e.g., brand names, URLs, logos, symbols, characters, spokespeople, slogans, jingles, packages, and signage).*** Old Spice uses bright-red packaging and its familiar ocean schooner to reinforce its nautical theme while also launching deodorant and antiperspirant extensions adding the High Endurance and Red Zone brand names.[20]
2. ***The product and service and all accompanying marketing activities and supporting marketing programs.*** Joe Boxer made its name selling colorful underwear with its signature yellow smiley face, Mr. Licky, in a hip, fun way. The company spent almost zero on advertising; clever stunts and events garnered publicity and word of mouth. An exclusive deal with Kmart has generated strong retail support.[21]
3. ***Other associations indirectly transferred to the brand by linking it to some other entity (e.g., a person, place, or thing).*** Subaru used the rugged Australian Outback and actor Paul Hogan of *Crocodile Dundee* movie fame in ads to help craft the brand image of the Subaru Outback line of sports utility wagons.

Choosing Brand Elements

Brand elements are those trademarkable devices that serve to identify and differentiate the brand. Most strong brands employ multiple brand elements. Nike has the distinctive "swoosh" logo, the empowering "Just Do It" slogan, and the mythological "Nike" name based on the winged goddess of victory.

Brand elements can be chosen to build as much brand equity as possible. The test of the brand-building ability of these elements is what consumers would think or feel about the product *if* they only knew about the brand element. A brand element that provides a positive contribution to brand equity, for example, would be one where consumers assumed or inferred certain valued associations or responses. Based on its name alone, a consumer might expect ColorStay lipsticks to be long-lasting and SnackWell to be healthful snack foods.

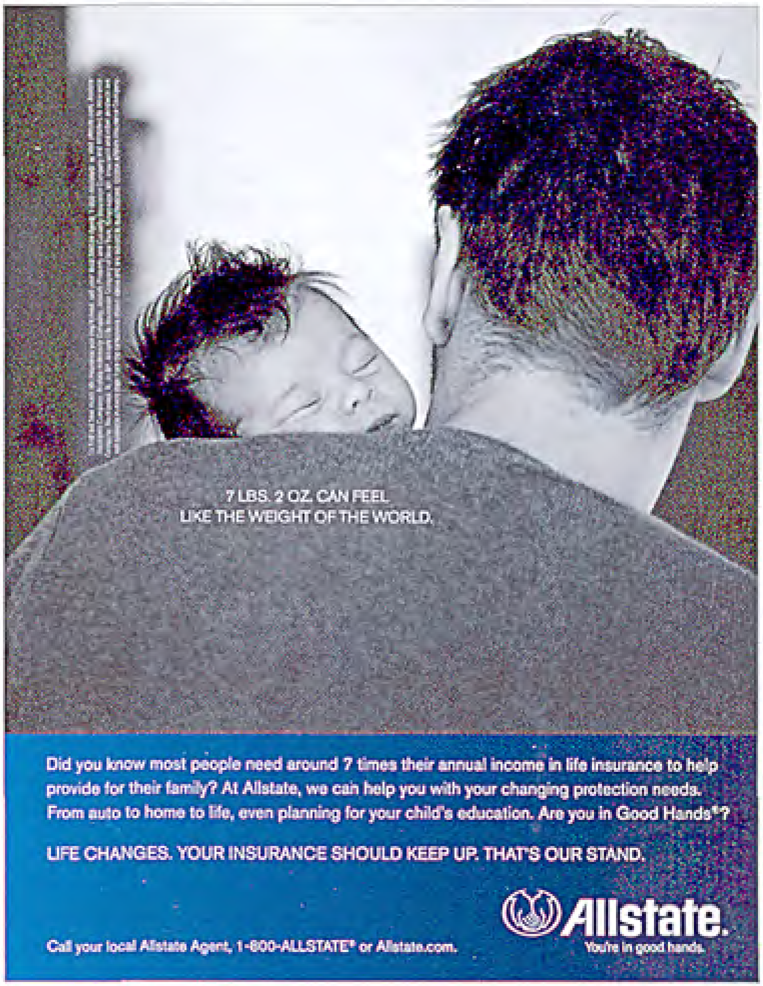
BRAND ELEMENT CHOICE CRITERIA There are six criteria in choosing brand elements (as well as more specific choice considerations in each case). The first three (memorable, meaningful, and likable) can be characterized as "brand building" in terms of how brand equity can be built through the judicious choice of a brand element. The latter three (protectable, adaptable, and transferable) are more "defensive" and are concerned with how the brand equity contained in a brand element can be leveraged and preserved in the face of different opportunities and constraints.

1. ***Memorable.*** How easily is the brand element recalled? How easily recognized? Is this true at both purchase and consumption? Short brand names such as Tide, Crest, and Puffs can help.
2. ***Meaningful.*** To what extent is the brand element credible and suggestive of the corresponding category? Does it suggest something about a product ingredient or the type of person who might use the brand? Consider the inherent meaning in names such as DieHard auto batteries, Mop & Glo floor wax, and Lean Cuisine low-calorie frozen entrees.
3. ***Likeability.*** How aesthetically appealing do consumers find the brand element? Is it inherently likable visually, verbally, and in other ways? Concrete brand names such as Sunkist, Spic and Span, and Firebird evoke much imagery.
4. ***Transferable.*** Can the brand element be used to introduce new products in the same or different categories? To what extent does the brand element add to brand equity across geographic boundaries and market segments? Volkswagen chose to name its new SUV, Touareg, after a tribe of colorful Saharan nomads. Unfortunately, historically they were also notorious slave owners, which created a negative press backlash in the United States.[22]
5. ***Adaptable.*** How adaptable and updatable is the brand element? Betty Crocker has received over eight makeovers through the years—although she is over 75 years old, she doesn't look a day over 35!
6. ***Protectible.*** How legally protectible is the brand element? How competitively protectible? Can it be easily copied? It is important that names that become synonymous with product categories—such as Kleenex, Kitty Litter, Jell-O, Scotch Tape, Xerox, and Fiberglass—retain their trademark rights and not become generic.

DEVELOPING BRAND ELEMENTS In creating a brand, marketers have many choices of brand elements to identify their products. Before, companies chose brand names by generating a list of possible names, debating their merits, eliminating all but a few, testing them with target consumers, and making a final choice.[23] Today, many companies hire a marketing research firm to develop and test names. These companies use human brainstorming sessions and vast computer databases, cataloged by association, sounds, and other qualities. Name-research procedures include *association tests* (What images come to mind?), *learning tests* (How easily is the name pronounced?), *memory tests* (How well is the name remembered?), and *preference tests* (Which names are preferred?). Of course, the firm must also conduct searches to make sure the chosen name has not already been registered.

Brand elements can play a number of brand-building roles. If consumers do not examine much information in making their product decisions, brand elements should be easily recognized and recalled and inherently descriptive and persuasive. Memorable or meaningful brand elements can reduce the burden on marketing communications to build awareness and link brand associations. The different associations that arise from the likeability and appeal of brand elements may also play a critical role in the equity of a brand. The Keebler elves reinforce home-style baking quality and a sense of magic and fun for their line of cookies. Ads featuring the Buddy Lee doll character for Lee's Jeans helped to make the brand popular with a younger audience that had not yet connected to the brand.

Brand names are not the only important brand element. Often, the less concrete brand benefits are, the more important it is that brand elements capture the brand's intangible



Building a brand with elements that capture the brand's intangible characteristics: An Allstate ad, with the graphic symbol of cupped hands and the tagline, "You're in good hands."

characteristics. Many insurance firms use symbols of strength (the Rock of Gibraltar for Prudential and the stag for Hartford), security (the "good hands" of Allstate, Traveller's umbrella, and the hard hat of Fireman's Fund), or some combination of the two (the castle for Fortis).

A powerful—but sometimes overlooked—brand element is slogans. Like brand names, slogans are an extremely efficient means to build brand equity. Slogans can function as useful "hooks" or "handles" to help consumers grasp what the brand is and what makes it special. They are an indispensable means of summarizing and translating the intent of a marketing program. Think of the inherent brand meaning in slogans such as, "Like a Good Neighbor, State Farm is There," "Nothing Runs Like a Deere," and "Help is Just Around the Corner. Tru Value Hardware."

AVIS GROUP HOLDINGS INC.

A classic case of a company using a slogan to build brand equity is that of Avis's 41-year-old "We Try Harder" ad campaign. In 1963, when the campaign was developed, Avis was losing money and widely considered the number-two car rental company next to market leader Hertz. When account executives from DDB ad agency met with Avis managers, they asked: "What can you do that we can say you do better than your competitors?" An Avis manager replied, "We try harder because we have to." Someone at DDB wrote this down and it became the heart of the campaign. Avis was hesitant to air the campaign because of its blunt, break-the-rules honesty, but also because the company had to deliver on that promise. Yet, by creating buy-in on "We Try Harder" from all Avis employees, especially its front-line employees at the rental desks, the company was able to create a company culture and brand image from an advertising slogan.[24]

Designing Holistic Marketing Activities

Although the judicious choice of brand elements and secondary associations can make important contributions to building brand equity, the primary input comes from the product or service and supporting marketing activities.

Brands are not built by advertising alone. Customers come to know a brand through a range of contacts and touch points: personal observation and use, word of mouth, interactions with company personnel, online or telephone experiences, and payment transactions. A **brand contact** can be defined as any information-bearing experience a customer or prospect has with the brand, the product category, or the market that relates to the marketer's product or service.[25] Any of these experiences can be positive or negative. The company must put as much effort into managing these experiences as it does in producing its ads.[26]

The strategy and tactics behind marketing programs have changed dramatically in recent years.[27] Marketers are creating brand contacts and building brand equity through many avenues, such as clubs and consumer communities, trade shows, event marketing, sponsorship, factory visits, public relations and press releases, and social cause marketing. To market its cereals, General Mills supplemented traditional advertising and promotion with, among other things, a family-themed, entertainment-based retail destination, Cereal Adventure, inside Minneapolis's Mall of America, the world's largest shopping mall.[28] Chupa Chups has developed an extensive marketing program.

CHUPA CHUPS

Who says lollipops are just for kids? Not Spanish Chupa Chups, the world's largest maker of lollipops. In order to extend the Chupa Chups brand beyond children, Chupa Chups is taking a truly holistic approach, which includes savvy—and totally free—product placement, fresh marketing ideas, and even its own line of retail boutiques. An internal task force, dubbed 4C for Chupa Chups Corporate Communications, is charged with raising brand awareness among fashion-conscious and media-saturated teens and youth. One example: When he learned that the coach of Barcelona's soccer team was struggling to quit smoking, a 4C sports fan sent him a complimentary box of Chupa Chups. For the rest of the season, the coach was rarely seen on the sidelines without a lollipop in his mouth. Chupa Chups sales in soccer-crazed Catalonia doubled that year. The company also gains visibility at high-profile awards ceremonies. When A-list stars come out at such events as the Venice Film Festival or the Grammys, a scantily clad "Chupa Chick" in a lollipop-studded bra top is there to greet them. So far Chupa's "celebrity suckers"—those caught on camera sucking a Chupa Chups—include Jerry Seinfeld, Elton John, Georgio Armani, Sheryl Crow, and Magic Johnson. Once Chupa Chups has caught teens' attention via these "nonendorser endorsers," they can point them to Chupa Chups packed in makeup kits or to clothing, eyewear, motorcycle helmets, and other items bearing the brand name.[29]

Regardless of the particular tools or approaches they choose, holistic marketers emphasize three important new themes in designing brand-building marketing programs: personalization, integration, and internalization.

PERSONALIZATION The rapid expansion of the Internet has created opportunities to personalize marketing.[30] Marketers are increasingly abandoning the mass-market practices that built brand powerhouses in the 1950s, 1960s, and 1970s for new approaches that are in fact a throwback to marketing practices from a century ago, when merchants literally knew their customers by name. To adapt to the increased consumer desire for personalization, marketers have embraced concepts such as experiential marketing, one-to-one marketing, and permission marketing. Chapter 5 summarized some of these concepts; "Marketing Insight: Applying Permission Marketing" highlights key principles with that particular approach.

From a branding point of view, these concepts are about getting consumers more actively involved with a brand by creating an intense, active relationship. *Personalizing marketing* is about making sure that the brand and its marketing are as relevant as possible to as many customers as possible—a challenge, given that no two customers are identical.

JONES SODA

Peter van Stolk founded Jones Soda on the premise that Gen Y consumers would be more accepting of a new soft-drink brand if they felt they discovered it themselves. Jones Soda initially was sold only in shops that sell surfboards, snowboards, and skateboards. The Jones Soda Web site encourages fans to send in personal photos for possible use on Jones Soda labels. Although only maybe 40 or so are picked annually from the tens of thousands of entries, the approach helps to create relevance and an emotional connection.[31]

INTEGRATION One implication of these new marketing approaches is that the traditional "marketing-mix" concept and the notion of the "4 Ps" may not adequately describe modern marketing programs. **Integrating marketing** is about mixing and matching marketing activities to maximize their individual and collective effects.[32] As part of integrated marketing, marketers need a variety of different marketing activities that reinforce the brand promise. The Olive Garden has become the second-largest casual dining restaurant chain in the United States, with $2 billion in sales and over 500 restaurants, in part through a fully integrated marketing program.

THE OLIVE GARDEN

The Olive Garden brand promise is "the idealized Italian family meal" characterized by "fresh, simple delicious Italian food," "complimented by a great glass of wine," "welcomed by people who treat you like family," "in a comfortable home-like setting." To live up to that brand promise, The Olive Garden sends select managers and servers on cultural immersion trips to Italy; launched the Culinary Institute of Tuscany in Italy to inspire new dishes; conducts wine training workshops for employees and in-restaurant wine sampling for customers; and remodeled restaurants to give them a Tuscan farmhouse look. Communications include in-store, employee, and mass-media messages that all reinforce the brand promise and ad slogan, "When You're Here, You're Family."[33]

MARKETING INSIGHT | APPLYING PERMISSION MARKETING

Permission marketing, the practice of marketing to consumers only after gaining their express permission, is a tool companies can use to break through clutter and build customer loyalty. With the help of large databases and advanced software, companies can store gigabytes of customer data and send targeted, personalized marketing messages to customers.

Seth Godin, a pioneer in the technique, estimates that each American receives about 3,000 marketing messages daily. He maintains that marketers can no longer use "interruption marketing" via mass-media campaigns. Marketers can develop stronger consumer relationships by respecting consumers' wishes and sending messages only when they express a willingness to become more involved with the brand. According to Godin, effective permission marketing works because it is "anticipated, personal, and relevant."

Godin identifies five steps to effective permission marketing:

1. Offer the prospect an incentive to volunteer (e.g., free sample, sales promotion, or contest).
2. Offer the interested prospect a curriculum over time that teaches the consumer about the product or service.
3. Reinforce the incentive to guarantee that the prospect maintains the permission.
4. Offer additional incentives to get more permission from the consumer.
5. Over time, leverage the permission to change consumer behavior toward profits.

Permission marketing does have drawbacks. One is that it presumes consumers to some extent "know what they want." But in many cases, consumers have undefined, ambiguous, or conflicting preferences. In applying permission marketing, consumers may need to be given assistance in forming and conveying their preferences. "Participatory marketing" may be a more appropriate concept because marketers and consumers need to work together to find out how the firm can best satisfy consumers.

Sources: Seth Godin, *Permission Marketing: Turning Strangers into Friends, and Friends into Customers* (New York: Simon & Schuster, 1999); Susan Fournier, Susan Dobscha, and David Mick, "Preventing the Premature Death of Relationship Marketing," *Harvard Business Review* (January–February, 1998): 42–51.