



THE QUEST FOR MARKET SHARE

Why Companies Continue to Get It So Wrong

By Tom Nagle and Peter Walsh

STRATEGIC PRICING GROUP
A MEMBER OF MONITOR GROUP

Superior Profitability Drives Market Share, Not the Other Way Around

For most companies, market share is a key performance measure. But in too many companies, the pursuit of market share has become an obsession and can actually hurt profitability. Starting in the 1970's, several prestigious consulting firms unveiled insightful yet over-simplified frameworks that convinced executives that growth in market share led to growth in volume, resulting in superior profits. And while even the inventors of these frameworks have backed away from this approach, this dangerous mindset continues to run rampant inside organizations today. Most executives do understand that achieving profitable growth is more complicated than following the simple 2 X 2 frameworks, but even so, many senior and mid-level managers inside highly respected companies continue to make poor business decisions based on the pursuit of market share.

Take a look at your own company's strategic plan; more likely than not, you'll see aggressive market share targets by product line, geography, and customer segment. On top of that, your competitors will have similar targets in their plans, setting up a fight that no one can decisively win. If greater market share led to greater profits, then General Motors would be the most profitable car company, American the most profitable airline, and P&G the most

profitable consumer goods company – but all three are far from the top. In reality, superior profits are the driver of market share, not the other way around. The fundamental error most managers make is over-relying on market share as the key barometer of good business performance. Market share is not an end, nor is it a means to an end. Market share is simply the by-product of a well run company. And well run companies have a sustainable competitive advantage that allows them to reinvest profits to fuel future growth.

Sound Familiar?

The obsession with market share often happens subtly, with seemingly small decisions over time. There are several market share traps into which companies unknowingly fall. Without careful decision making and a willingness to confront issues early, it can also happen to you. Are you one of these companies?

Dominant leader pressured by Wall Street for results

The news is full of industry leading companies that wake up one day and realize their business is in trouble. Sears and Kmart are two recent examples of firms who tried everything to maintain volume and market share numbers, but must now join forces to compete against the stronger Wal-Mart. Companies usually begin to "buy" market share for two reasons, 1) they need to keep the quarterly results strong for Wall Street, and 2) they have a proud tradition of

success that prevents them from tackling business problems before they become critical. Instead of recognizing (and doing something about) Wal-Mart's advantages early in the fight, Sears and Kmart fought a market share war and tried to keep Wall Street happy, until it was too late.

Fast moving technology company fueling its own demise - The wireless phone industry is a classic example of this phenomenon. While the market was growing at double digit rates, many wireless providers myopically focused on growing market share. While new customers were flocking into the market, wireless providers kept lowering prices, hoping volume growth would eventually cover lower margins. However, most providers had to raise costs and "over invest" in infrastructure to keep up with competitors. These rising costs and lower prices had a devastating effect on profit for the entire industry.

Manufacturer beaten by procurement bullies - If you're selling into Wal-Mart or Home Depot, you know first hand the sophistication and strength of their negotiation power. For many suppliers, the quest for volume and market share prompts them to make deals with these industry powerhouses, often at razor thin margins. The good news: volume and market share usually increase dramatically after a deal is reached; the bad news: Wal-Mart or Home Depot want an even sweeter deal in year two of the contract. Many suppliers find themselves in the stranglehold of profitless growth today – damned if you do and damned if you don't.

Respected industry leader waiting for the "market" to return - Some companies make decisions to "buy" market share thinking it will help them in the short-term and they'll fix the problem later. Often, these companies simply don't understand (or are reacting slowly to) new structural changes in the marketplace. Costs may be rising, demand may be weak, or they may be trying to halt customer defections. Making an unprofitable deal today rarely makes sense as the market almost never returns in the way it was projected to.

What to Do if You're Caught in the Trap

Most companies don't realize they've fallen into the market share trap until they are firmly stuck in its grip. Like quicksand, market share obsession can be easy to get into and very difficult to get out. The first lesson for managers – don't let your company get caught. Be vigilant and vocal about market share directives that are not profitable. Challenge senior managers when they approve unprofitable deals with customers. Question the value propositions of new product introductions that don't increase revenue or decrease costs for customers. Question how much market share makes business sense before selling to less profitable customer segments. And if it's too late for preventive medicine, the following steps will get you back on track – although don't expect any quick fixes.

1. **Accurately diagnose your root cause problems** - This is easier said than done for most companies because, by definition, you're fighting against the internal dynamics that got you into trouble in the first place. That said, accurate diagnosis is critical because root cause problems often come from several sources. Unprofitable market share directives can stem from problems in your value proposition, pricing strategy, distribution channels, industry dynamics, business model, or any combination of these. For example, the previous Sears illustration has a very different "market share" problem than Verizon Wireless. To convince executives to change their thinking about market share, you'll need both quantitative and qualitative analysis on where the current problems are and where future opportunities lie. Relevant case examples of companies facing similar problems will also help to change the organizational mindset and paint new models of behavior.
2. **Find and focus on the right customers** - Far too many companies have a one-size-fits-all

strategy when it comes to customers, pricing, and product offerings. They focus on aggregate market share numbers instead of aggressively targeting the most profitable segments and leaving the unprofitable ones for competitors. Your marketing department may have developed a customer segment map, but for most companies, those segments based on attributes, demographics or psychographic profiles are exceedingly difficult for salespeople to use. The challenge is to identify the segments that drive your profitability and develop specific offers and pricing that map to these segments. Not all market share is good, so identify only the segments that drive your profitability and leave the rest. If you still need volume to drive your business model, make sure it is priced appropriately.

3. **Bite the bullet with Wall Street** - In the late 1990's, the Gillette Company had a problem. They had become so focused on market share and volume that they became addicted to "stuffing" their channels with low priced goods to induce distributors to buy in advance. The practice of stuffing only delayed (by a quarter or so) the inevitable decline in financial performance. Gillette went for years missing its numbers, shrinking its revenue and profit. To reverse this process, it took a new CEO who stopped the practice and basically told Wall Street that Gillette was no longer providing future guidance on financials. When companies get addicted to short-term actions that improve share and volume numbers, it's a treadmill that's hard to get off. The best advice, take no more than one year to fix the problem by systematically changing the people, processes, and systems.
4. **Use marketing and pricing strategy to outwit the procurement guerillas** - There is a way to grow profits and market

share when negotiating contracts with procurement giants like Home Depot, but it may require changing the rules of your current business. Instead of negotiating deals that deliver your highly valuable products at mind numbing discounts, think instead about subtracting value from your products and delivering a lower cost, lower value product that meets their financial objectives. John Deere is a good example of this approach. Instead of selling their best products to Home Depot and Lowes, they've developed a simplified product and brand at a lower price point for these channels, while continuing to sell their premium product through specialty dealers. In any negotiation with procurement guerillas, make sure to use the subtraction technique, taking valuable things out of the offer, when asked for a lower price. And if that means creating new products or capabilities to meet their needs, do that, instead of giving value away.

5. **Kill the mindless promotions that drive nothing but share** - We speak to many companies who profess that they are not driven by market share, but when we ask to see strategic plans or monthly reports, they are chock full of references to share and volume objectives. On top of that, their marketing departments continually generate promotional opportunities that drive share and volume. Promotions need to be targeted and offerings need to be structured and appropriately "fenced" to prevent undesired segments from accessing them. A one-sized approach to promotions typically misses the profits available at the high end of the market and attracts too much of the low end.

In Summary

Companies that leverage their operational prowess with marketing savvy are today's market share leaders. They use their profits

to make investments that drive growth and share. The key point to remember, more market share isn't always better. For those misguided companies that use precious resources to "buy" market share, they do so at a very high cost and its short-term improvements are rarely sustainable. While there is a relationship between market share and profitability, both are the results of a sustainable competitive advantage. They are the outputs of a well run company, not the inputs.



Tom Nagle and Peter Walsh are, respectively, Group Leader and Chief Marketing Officer in the Cambridge office of Strategic Pricing Group, a member of Monitor Group. They can be reached at tom_nagle@monitor.com and peter_walsh@monitor.com.

SPG *Insights* is a quarterly publication of Strategic Pricing Group, a member of Monitor Group. In each issue, we take an in-depth look at current value-based marketing challenges and provide practical solutions and insights for executives in marketing, sales and management. To register to receive SPG *Insights*, visit our website at www.strategicpricinggroup.com.