4. Effective marketing strategies for a recession

A firm can survive turbulence and even prosper from it by developing an effective value marketing plan. Value marketing can be defined as meeting customer needs by providing as much value as possible in order to retain customer loyalty. With such loyal customers, a company should be able to weather economic turbulence. However, this is not a simple task as emerging or prevailing turbulence causes fluctuating and unpredictable customer needs and wants. Marketers therefore require a marketing strategy toolkit to enable them to be proactive in their marketing, allowing their companies to keep ahead of market changes and developments in such a way that they will not only survive, but also prosper. The following sections of this chapter provide a variety of strategic options available to marketers as ammunition against recessionary forces.

Effective pricing strategies

Determining how to price a product is one of the hardest decisions management has to make. If the price of a product is too high, then the company will lose out to the competition; if the price is too low, it is in danger of leaving money on the table for the customer, and is potentially denigrating the product by placing it beneath comparative products in the marketplace.

It is extremely risky for a company to raise or lower its prices without measuring demand elasticity in relation to price. From a marketing perspective, elasticity is important as an indicator of the

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competitive advantage or monopolistic power of a company, product or brand (Samli, 1993 p86).

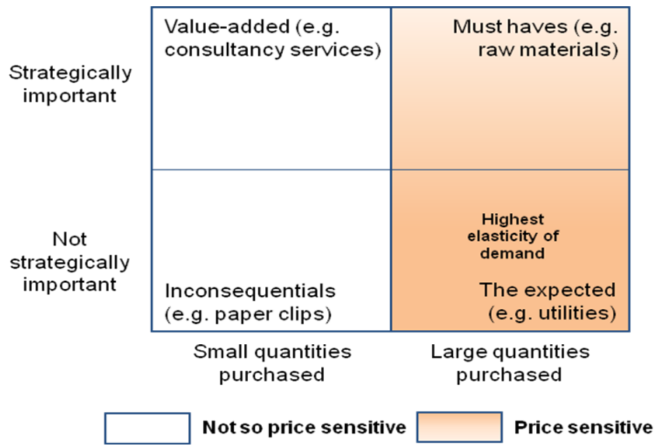
There are a number of factors that need to be taken into account in considering the price elasticity of demand:

Whether the market is in perfect or imperfect competition: In a general sense, and contrary to many consumer products, the elasticity of demand for most industrial products is low in cases where the market is in imperfect competition (for instance, where there is a monopoly, oligopoly, monopsony or oligopsony). In this context, if a company were to reduce or increase the price of a product, there would be no significant change in demand because the product is needed, regardless of changes to price.

The importance of the industrial product to the customer: A further factor to take into consideration is the importance of the industrial product to the customer. Demand is inelastic for products where the customer believes that neither the company nor the brand has close substitutes, and for products where there is urgency in need – both of which indicate the importance attached to the product.

Further factors associated with the importance of the product offering are those illustrated by Figure 4.1 overleaf which shows different types of product plotted on the matrix according to typical quantities purchased and strategic importance. The elasticity of demand varies for these different product groups, but demand is most elastic on the right hand side of the matrix where large quantities of the product are purchased. Hence demand elasticity is likely to be high for products that are taken for granted (classified as “the expected”, such as utilities or insurance, which are not strategically important) and it is likely to be relatively high for products considered to be “must haves” that are of strategic importance (such as raw materials and machinery). If prices are reduced for “value-added” products at the top left corner of the matrix, then the company could potentially denigrate its brand by devaluing its offering. Similarly if prices are reduced for inconsequentials, such as paper clips, the company is unlikely to stimulate sales given that customers in b2b markets normally only buy when they have a need. Thus it is for products that fall into the categories on the right hand side of the matrix where pricing strategies work best.

Figure 4.1 Elasticity Of Demand By Strategic Importance & Quantity Purchased



Inertia: In most b2b markets, many buyers and specifiers claim that they are sensitive to price and yet when they are asked how frequently they change suppliers, the reality is that they have seldom done so. There is huge inertia amongst industrial buyers. It is easier for them to carry on dealing with the same supplier than to switch suppliers. In the case of price increases, as a general rule many buyers in industrial markets will stick with their suppliers unless the price difference moves beyond 15% (or around 10% in a recession) of that of a competitor. In the case of price reductions and in times of adversity, demand is somewhat price inelastic as customers are unlikely to increase their purchases in spite of substantially lower prices (Samli, 1993 p88). Hence inertia is an important influence on the theory of elasticity in industrial markets and should be taken into account when considering the most appropriate strategy to adopt in a recession.

Knowing what to do with pricing in volatile markets, especially those where there is high price elasticity in demand, is challenging as prices are under scrutiny and constantly changing. A selection of pricing strategies is discussed below.

Reducing prices

Many companies choose the option to reduce prices in order to stimulate sales and to remain competitive against their rivals who are also reducing prices. However, it is crucial to reduce prices with minimal effect to margins, for it is impossible to be profitable in the medium to long term if prices are slashed without consideration to profit margin. For most b2b marketers, finding the right price is a judgment which many get badly wrong – usually charging too little because they do not realise the value of their offerings.

As discussed above, reducing prices is most effective in markets where customers are sensitive to price. That said, it may well be that customers do not respond to price reductions, especially if all suppliers are reducing prices and there is little differentiation.

A way of seeking minimal effect to margins when reducing prices is to adjust the product offering to be aligned with the reduced price, or vice versa. Hart (2008 p71) suggests unbundling whereby features within a bundled package are stripped apart to enable the company to focus on its core offering, and to provide customers with only the specific components of the product offering that they require. Hart does not, however, acknowledge that bundling can enable a company to offer added value and to extract more value from the buyers of the bundled product, and so a company could be leaving money on the table by unbundling its offering. Whether a company pursues a strategy involving bundling or unbundling, it is vital to determine what trade-offs its customers really value and to segment its customers by needs, which is not an easy task but will nevertheless indicate how sales potential can be optimised from different customer segments.

Reducing prices is more of a short-term tactic than a medium- to long-term strategy. This is particularly the case with marginal pricing where prices are set above the average variable cost, but below the average total cost. Clearly not sustainable in the long term, it can nevertheless be successful in the short term, especially for filling excess capacity and shifting obsolescent and spoiled goods (Hart, 2008 p76). Similarly discounts, which are more common in consumer than b2b markets, can be successful in stimulating sales, but are also more of a tactic than a strategy given that they are launched to deal with a short-term threat or opportunity, rather than a long-term intention. Discounts should be used with caution in b2b markets for they should not set a precedent for customers to expect low prices, deals or negotiations on future purchases. Discounts can, however, be effective when used as one of many tactical manoeuvres under the strategic umbrella of the company's pricing strategy.

Raising prices

Raising prices enables companies to increase cash flow, but caution should be taken if there is no disciplined, long-term pricing strategy in place, for without this revenue can dry up extremely quickly, sometimes with fatal consequences. Mazda's CEO once increased prices across the board by 5% which led to demand falling by a significant 20% (idem p51). Once again, managers need to understand the price sensitivity of their market and have a feel for just how much they can change prices in order to generate more revenue and to maximise profits, without having the adverse effect.

As discussed earlier, the significant inertia in certain b2b markets offers opportunities for price increases given that many customers are unlikely to switch suppliers as a result of higher prices. In every industry sector, the majority of companies do not know what the optimum price points are of their products, meaning that endless opportunities are missed to extract more revenue. Raising prices to their optimal level (i.e. which the market will stand) can provide one of the fastest ways of increasing cash flow, so long as the loss of volume is offset by the rise in profit per unit. Thus if management does not know the price elasticity of demand for its products, it could quite clearly be missing a trick to maximise profits.

Many companies provide extraneous services which are either not acknowledged or appreciated by customers, or worse still, which customers are not paying for. Examples include delivery, invoicing the customer for non-warranty repairs on purchased equipment, fulfilling last-minute orders and late payment fees – all of which customers could be paying (more) for. In addition, more revenue could be generated by seeking to increase the minimum order size, obtaining a higher margin by using different mark-ups on different size products, incorporating re-ordering structures and charging extra for special orders (idem p67).

Presentation of prices

Particularly in a recession, customers need reassurance that they are obtaining value for money and companies need to seek new ways of making their products all the more attractive. Pricing using lifetime cost of ownership is an underused tool to illustrate that over the life of the product, the upfront payment made represents only a small percentage of the whole cost to the customer. Hence customers can be persuaded that life-time costs can be minimalised by purchasing a more expensive product.

A further powerful argument to support price increases is communicating the return on investment of the product, in that companies should show how their products can save or make their customers money. General Electric's Ecomagination programme, for instance, develops and markets environmentally-friendly products that are appealing to the market, not only because they are green, but also because they enable customers to reduce their own operational costs.

In b2b markets in particular, there is also a need for clarity in pricing. Industrial customers want to see exactly what they are paying for and so they prefer to see products and services unbundled and priced separately (Harvard Business School Working Knowledge, 3rd March 2008). Presenting a breakdown of prices to customers can also highlight value for money in terms of illustrating the many components of the product offering, so long as the company's pricing strategy is not transparent to its customers or competitors.

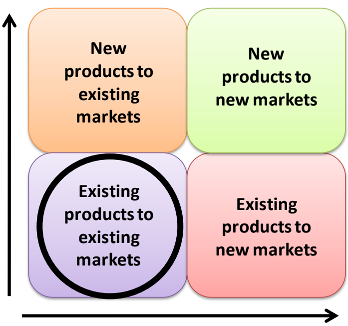
Finally, companies may need to adjust payment terms and pricing structures in order to accommodate the changing needs of customers who are also faced with recessionary pressures. Alternative pricing options, such as leasing versus up-front payments, are likely to attract certain customer segments and may prevent existing customers from defecting.

Effective strategies in the context of Ansoff – determining which products and which markets

In a downturn, managers tend to focus too much on managing threats and lose sight of seizing golden opportunities. A recent article in the Financial Times (22nd January 2009) encouraged managers to ask themselves the following questions:

- *Are competitors retreating from opportunities that we can seize?*
- *Should we double down in growth markets, such as BRIC economies, rather than retrenching to our core?*
- *Does our customers' or competitors' pain create an opportunity for us?*
- *Can we snap up key resources at bargain prices?*

It is necessary for managers to acknowledge that it is possible to seize the upside of a downturn by seeking opportunities, as well as by minimising threats. The following section discusses four effective marketing strategies in the context of Ansoff, as illustrated earlier in Figure 2.2.



Existing products to existing markets

As discussed earlier, it is important to retain existing customers in order to ensure survival through times of adversity. The top 20% of customers in a business may generate as much as 80% of the company's profits, half of which are lost serving the bottom 30% of unprofitable customers (Kotler and Keller, 2008). It is therefore necessary to focus on the existing customers that matter. This means that companies should be prepared to allow certain customers to defect.

Further, companies should accept that competitors will steal customers by offering lower prices. Certain customers could be worth more to these competitors than to other companies; they may have underestimated the true costs of serving these customers; or they may have a higher fixed cost structure which means sales at almost no marginal profit are still worthwhile to them. Retrenchment of this kind can be beneficial, for allowing the rotten apples to fall will enable the tree to focus its nutritional resources into its healthy and profit-maximising fruit.

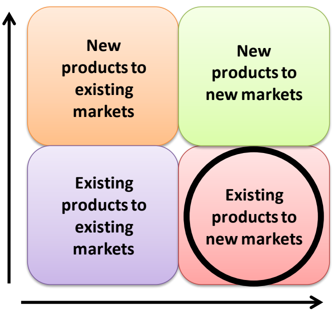
All good marketers need to closely target their offering against segments that value their offerings. In other words, they need to think carefully about segmentation and who they are aiming at. In a recession, there almost certainly will be groups of customers who are more resilient than others. That said, re-orientating a company such as a retailing group towards a segment takes time and most companies are ill-prepared for this. Indeed many reacted to this recession too slowly and too late as they did not see it coming or denied its severity.

Effective marketing strategies for a recession are not devised following the outbreak of a recession; rather effective marketing strategies for a recession are considered in advance of an economic downturn. It is the responsibility of management to deal with any of the company's weaknesses or threats prior to turbulence of any kind, for not doing so leaves the company vulnerable to recessionary pressures. This was the case for Woolworths which, with no differentiation and no unique selling point, collapsed in the recessionary storm.

In addition to rationalising the customer base, companies should also rationalise their product lines and focus on their core offering. Most firms have valuable assets such as certain customers, skills and an established brand identity. These should be protected so that they can weather the storm, as well as sharpened and strengthened in order that the company can remain resilient and competitive. This is what Google appears to have done as it pulled the plug on some of its products including SearchMash (a website to organise search results), Dodgeball (a mobile phone service) and Lively (a virtual world), explaining that it did so in order to prioritise its resources and to focus on its core search, ads and apps business (Wall Street Journal, 3rd December 2008). Charan (2009 p80) supports the rationalisation of product lines, encouraging companies to be "merciless in weeding out product lines and their myriad versions and extensions that create unnecessary complexity", and reinforces the 5 and 50 rule that 50% of parts in a company's inventory generate just 5% of its revenue.

This same argument applies for certain parts of the service offering. For instance, resources can be freed by jettisoning superfluous activities, such as unnecessary face-to-face meetings with customers which could be conducted through more cost effective means (by telephone or online, for example).

A further strategy to consider is exploiting channels to market so as to extract more from existing products in existing markets. This appears to be Microsoft's strategy at this point in time as it is planning to open retail stores to improve the PC-buying experience and to boost revenues (New York Times, 13th February 2009). This strategy has additional benefits as it could introduce new customers to its offering, plus it could introduce existing and new customers to new products in its stores.



Existing products into new markets

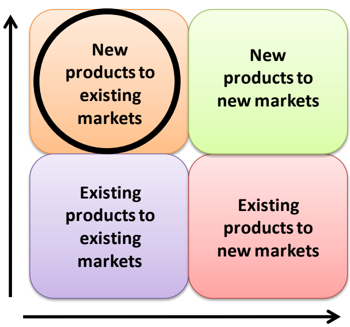
Against the backcloth of a gloomy recession, companies desperately attempt to maintain their position and steal market share in what has ultimately become a stagnant market. Entering new markets into which existing products can be sold – new industrial sectors or new geographical areas – offers opportunities to build cash flow, profits and market share.

Finding new customers is easier said than done. Some b2b companies are lethargic in seeking expansion in normal times; their capacity is full or nearly full and so they continue without change. A jolt from the recession could cause these companies to look towards markets which they would have otherwise eschewed. However, many companies fear change; they would rather stick with the stagnating old but familiar, than seek new opportunities that are challenging and risky.

Nevertheless, if market intelligence confirms that there is an opportunity in a new market, then there could be a significant return on investment if the company has the required resources to enter and establish itself in the new market. For example, Honeywell acknowledged that IBM was stronger in larger and more urban cities, so Honeywell attacked the more rural cities where it could penetrate the market easier and increase its market share (Hart, 2008 p120).

Some companies could consider targeting consumers as well as businesses. This is what the large automotive parts supplier Dana Corporation did to boost its sales. The company found that manufacturers of power transmission drives could charge consumer end users 25% more than they could OEMs because the replacement part is of more value to the end user than to the OEM which sees it as a major cost of the machine (idem p114).

There are often opportunities in new geographies, especially if the domestic market is saturated or stagnant. For example, HSBC recently announced plans to expand further into Vietnam, Laos and Cambodia (Wall Street Journal, 6th February 2009), and a portable electrocardiogram monitor that GE Healthcare developed in India to serve local rural markets has ultimately found markets in numerous other countries (Financial Times, 5th February). The BRIC countries in particular offer opportunities as many markets in these areas are still growing in spite of the global economic crisis – the biofuels and aluminium markets in Brazil; the marine market in Russia; the IT and telecoms market in India; and the market for tyres in China, to name but a few examples. Expanding into new markets requires market intelligence, considerable planning and ample and sustainable resources, but the payback can be considerable, enabling a company to survive and thrive through a recession.



New products into existing markets

The need to innovate to survive is often the mantra of those who are successful in business. This is because innovation by its very nature means doing things differently. In three years' time, if a company looks the same as it does today, it is likely to be dead in ten years. Every company needs to innovate to maintain a competitive edge, which is all the more important in turbulent markets.

Charan (2009 p88) argues that in downturns, most companies focus solely on research to improve *existing* products and that this is a mistake, stating:

> *"You will need to seize opportunities to make quantum leaps by focusing on new products [...] Your competitors are scared, may lack liquidity, and may be afraid of taking risks. That's a superb set of conditions for you to set up your company as a winner for decades to come. If you seize the opportunity, you can go from fourth or fifth in your industry to first or second when the downturn ends."*

The case is clear: product development should take place at all times and should not be neglected but rather embraced in times of adversity.

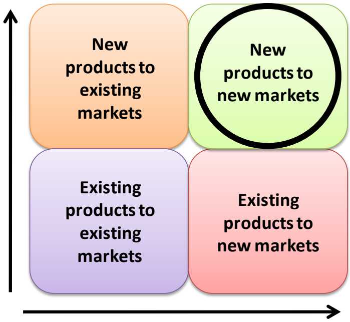
Market research can play an instrumental role in uncovering new product opportunities. A study by Eric von Hippel found that 80% of industrial innovations came from customers themselves (Hart, 2008 p99). Companies that do not actively listen to the market could, therefore, be closing their ears to new product opportunities.

Another study has shown that over three quarters of companies in the 2001 downturn used customer segmentation and surveys in developing new product offerings (idem p97). In fact many companies underestimate the importance of segmenting the market by needs. They stop at segmenting their customers by firmographics such as industry segment, geographical location or customer size. If a company segments the market by needs, it will not only better serve its customers by tailoring its offering according to what each segment values (and therefore extract more value from these segments), but it will also discover opportunities for new products in accordance with what the market wants.

Product development can be a costly and lengthy process, but there are means of obtaining speedier cost efficiencies in a recession, such as new product development through substitution.

Substitutes allow companies to circumvent entry barriers erected by former market leaders, making the new product strategy easier, quicker and cheaper to implement in a downturn.

New product opportunities can cover intangibles such as the service offering, as services can be faster, and in many cases cheaper, to get out into the marketplace than new products. Moreover, a new service may have more of an impact on customers than a new product and could strengthen the customer value proposition, thereby providing companies with increased competitive strength to survive and prosper in the recession.



New products into new markets

This final quadrant of the Ansoff matrix is where companies seek to find new opportunities in new businesses either by acquisition or by greenfield development. It is very risky, especially in a recession given that considerable investment is required (at a time when most companies want to conserve cash) and that new products take time to grow organically (and time is of the essence when the boat is sinking).

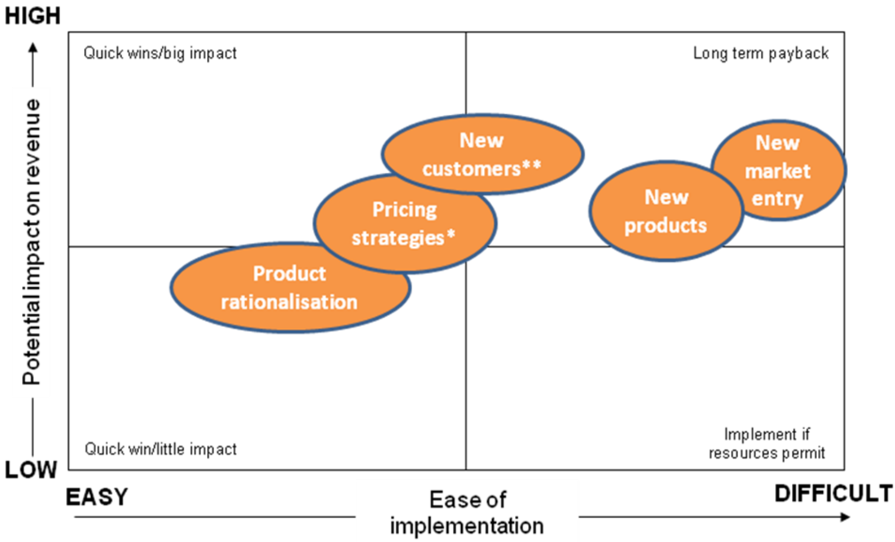
Nevertheless, there are examples of companies pursuing this strategy in this recession, such as Procter & Gamble which recently acquired car wash franchises, explaining that it was looking for growth opportunities which are not limited to its current business model (Wall Street Journal, 5th February 2009). Acquisition can be particularly attractive in a recession when distressed sellers are under pressure to dispose of valuable assets at low prices.

Devising a strategy around new products into new markets goes beyond the marketer's remit as acquisition is more of a business than marketing strategy. Such a strategy is to be avoided if a company is seeking a quick-win solution with minimum risk.

Summary

Numerous strategies have been explored in this chapter, all of which can be effective in a recession if they are appropriate for the market and if they can be implemented by the company (for example, if the company has the necessary resources required, such as R&D expertise to develop new products). The main strategies discussed can be summarised according to their ease of implementation and potential to generate revenue (see Figure 4.2). In considering which strategy to pursue, marketers need to determine whether they require a quick-win but lower cost and less risky strategy (the left-hand side of the matrix below), or whether they need a long-term strategy which involves a larger investment but which provides a more substantial return over time (the right-hand side of the matrix).

Figure 4.2 Main Marketing Strategies According To Ease Of Implementation & Potential Revenue



* Including raising prices, reducing prices and pricing alternatives such as leasing versus up-front payments
** Seeking new customers in existing markets; not to be confused with new industrial sectors or new geographies with new market entry

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