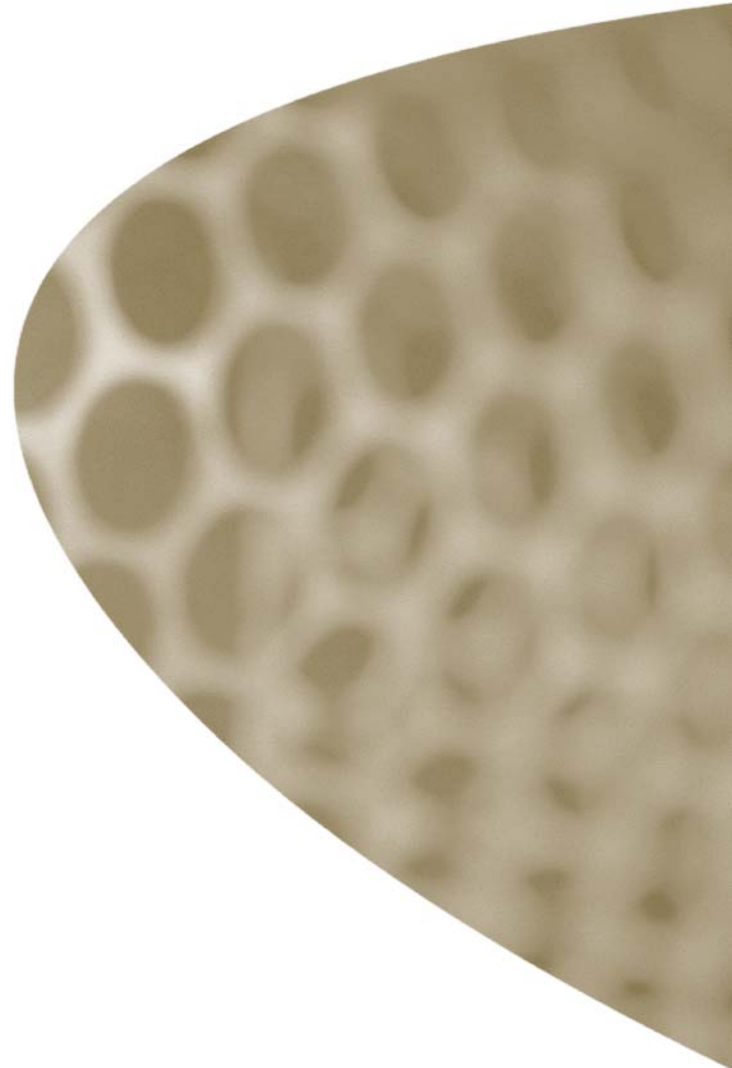


Handbook of Business Strategy

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Markets and marketing: How to build a great product

Susan E. Rau

President of Profit Solutions Associates



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How to build a great product

Susan E. Rau



Susan E. Rau is the President of Profit Solutions Associates.

Building a great product takes more than tweaking an old one. In fact, it takes a concerted effort on the part of the whole company to adopt and follow a winning strategy and to align all new products and services to fit that strategy. While successful strategies are as diverse as the companies they represent, research has found that winning companies adopt one of four focused strategies. This article outlines these four approaches and how they transform companies and the products they take to market into winners.

The marketplace is awash with “new” and “new and improved” products and services of all types. Building products that stand out in the crowd can be challenging unless the product development group at your company adopts a comprehensive and practical approach that ensures that your company’s products are winners.

Open any daily newspaper, drive along any suburban thoroughfare or surf the Web and you’ll quickly recognize that there is no shortage of product choices. Other than the signature colors, the clever jingle, the smart tag line, what really distinguishes one product from another? Unless a product or service breaks truly new ground (think FedEx at its inception), most products just cluster together in an undistinguishable heap of advertising, packaging and marketing. Seldom does the “new” or “new and improved” product scream competitive advantage the day it’s launched by the product development team.

So, how can your company break out from the pack of mediocrity? One way is to make the product itself bear some of the responsibility for customer acquisition and retention by creating products that really stand out and win in the marketplace.

Strategy – the starting point

The first step toward making great products is to decide how your company intends to be a winner and determine what role products and services are to play in that winning strategy. This sounds so simple, but our research suggests that this first crucial step is often what separates top performers from the rest of the pack.

Successful strategies are as diverse as the companies they represent, but here again our research shows that companies that win big adopt one of four focused strategies:

- 1 *Product Leaders*. These companies spend most of their money on product innovation. This means more than just rewrapping a basic product and calling it a “new” product. Rather, the products introduced by Product Leaders forge new ground and are often copied and imitated by others. Mass marketing and brand identification are hallmarks of the Product Leader and achieving large market share is required to payback the big outlays for product development and marketing. Shareholder value is enhanced by dominance of product categories and brand recognition. Companies with winning Product Leader strategies include Proctor & Gamble, Frito Lay and ING.
- 2 *Distribution Giants*. These companies spend most of their money getting their products and services into the hands of their customers. Whether bricks and

mortar or e-commerce, the Distribution Giant seeks ubiquity. Often, these companies sell the products of others or private label; product innovation is not key to their strategy. However, pricing is a key strategic weapon and these giants with their massive distribution networks are frequently price discounters. Distribution Giants drive shareholder value through mass marketing, keeping up to the minute on sales production and running a tight financial ship. Winners that have adopted this strategy include Wal-Mart (a category killer!), Microsoft and Capital One.

- 3 *Innovation Superstars*. This winning strategy is, quite frankly, the hardest to pull off. The Innovation Superstar spends its money on fundamental scientific research, as contrasted with the applied research typical of Product Leaders. Companies that win based on innovation seldom build their own distribution networks and often partner with others to get their products to market. Patience and a long-term outlook drive shareholder value. The company must be adequately funded so as to be able to develop and innovate multiple initiatives at once, realizing that at least some projects will not pay off at all and only a very few will be “home runs”. Most pharmaceutical companies (e.g. Merck, Pfizer) win based on Innovation as do Boeing and 3M.
- 4 *Customer Lovers*. These companies take a long-term and very intense view of the relationship with their customers. But, unlike the Product Leader whose intensity is focused on the product and the Distribution Giant whose intensity is focused on ubiquity, the Customer Lover is focused uniquely on its customers. The Customer Lover’s products are nothing special; they rely on the caliber of their customer contact staff (and technology) to imprint the company’s products and services with a distinguishing “face” that causes the customer to differentiate between this company and a competitor. This customer entanglement approach requires a heavy investment in each customer and in ambience, allure and aura (the 3 As). Shareholder value is enhanced by long and deep customer relationships and high margins achieved through premium pricing. The best in bread Customer Lovers include Lexus, Disney and the Amex Black card.

In our research on publicly held companies, we find that companies that have the most focused and well developed strategies and execute those strategies well are the winners (as measured by share price and earnings per share).

Irrespective of their chosen strategy, winners need to have superior customer service and an excellent operating base. Thus, sad to tell, there is no strategy that, by itself, can succeed solely based on customer service and/or operational excellence. Rather, these critical attributes must play a strong supporting role to one of the four business strategy models if the company is to be a winner. The relationship of

service and operating effectiveness to strategy is shown graphically in Figure 1.

Understanding the role of products and services

Each of the winning strategy models puts a different emphasis on products and services. Not surprisingly, products and services take center stage for the Product Leader. Companies that select a Product Leadership strategy must be prepared to launch a constant stream of truly “new” and “new and improved” products into the market. These Product Leaders will need to carve out mass markets in order to generate enough sales volume to pay for the heavy investment in product development to drive this winning strategy.

Technology also plays a pivotal role for the Product Leader, both in the manufacture of the product and in its distribution (to limit delivery costs and boost operating leverage and profit margins). Big product development staffs, lots of product managers and significant outlays for market research and advertising are part of the cost burden that the Product Leader must bear. To make this effort financially viable, the products must be well researched, they must easily and reliably meet customer needs and effectively sell themselves.

The role of products and services for the Distribution Giant is quite different. Here, all the focus is on distribution outlets. Products have to be simple and cheap to produce since so much capital and expense is devoted to building and maintaining the distribution network (physical and virtual). Product innovation is not needed and, frankly, not wanted. The products need to be tried and true, reliable and thus able to sell themselves in order to contain sales costs and devote relatively larger outlays to the next 100 distribution outlets. Operating leverage is achieved through superb supply chain management and by maximizing scale economies in manufacturing, wholesale buying power and the application of technology to customer service, inventory control, packing, shipping and all aspects of expense management.



The Customer Lover strategy also relies on simple products; however these are wrapped in a unique customer experience as the way to differentiate the products of one company from another and to impart value to the customer. Products are usually quite simple and are enhanced by ambiance, allure and aura added at the point of sale. The Customer Lover's product development efforts make sure that each customer feels that the product/service considers his/her unique needs. Pricing is a key component of the product strategy for Customer Lovers; the customer experience must be supported by premium pricing to recoup the significant costs of delivery and ongoing customer service.

Thus, a boutique private bank with a focus on the business owner and a Customer Lover strategy will "construct" loan and cash management products for the business while the same bank's wealth management area will assemble an investment portfolio which includes private placements and closed end funds as well as tax advantaged strategies for preserving wealth for the next generation. The bank will charge a premium price for assembling the products and for providing advice on how to use them to meet the business owner's goals and objectives. Discrete forums for clients with top-notch speakers add to the allure and aura.

Figure 2 shows the very different roles that products and services play in each winning strategy.

Building a great product

It is reasonably easy to make products that meet one or more clearly identified needs of a specific target market; making great products that are really valuable to the customer and stand out

from the competition is much more difficult. One of the reasons that so many products look alike and that so many customers are unimpressed is that marketers tend to confuse what the product does and how it works (product features) with meeting customer needs (product benefits). This is pretty basic, but many companies are at a loss as to how to make the connection to the customer in a way that clearly strikes a response cord and results in a sale.

Link product development to strategy

The first step toward building a great product is to forge a strong link between the product development function and the company's chosen winning strategy. Returning to Figure 2, it would be a mistake, for example, to devote significant resources to product R&D if the company intends to win as a Customer Lover. The result would be over-engineered products and a confused customer who cannot see why he or she is being asked to pay a premium price when the product does so much that the staff and customer experience becomes superfluous. With this misguided approach to product development, profit margins will be strained as the company makes big investments in product innovation product costs and then layers on a very expensive value-added delivery.

Product building blocks

The linkage between product development, strategy and meeting customer needs is more readily understood when we look closely at three related factors:

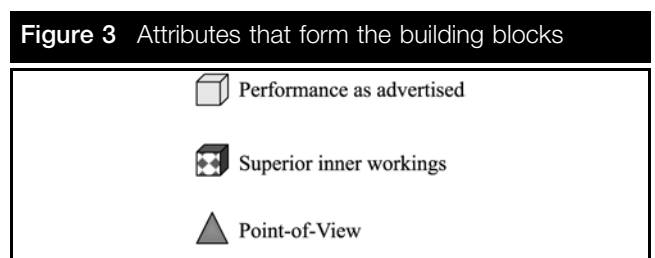
- 1 Properly defining the company's products.
- 2 Ensuring firm linkages between product development and corporate strategy.
- 3 Winning by meeting customer needs reliably, regularly and profitably.

The construct of each product or service that the company offers includes one or more of three attributes that form the building blocks of product development (see Figure 3).

In theory, all products should perform as advertised and be reliable and credible. In reality, many do not. Ever bounced a check because the overdraft protection feature just did not kick in? Ever spent hours on the phone when your bar-coded luggage mysteriously disappears between Duluth and Dayton?

Figure 2 Product/strategy linkages

Product Attribute	Winning Strategy			
	Product	Distribution	Innovation	Customer
	Leader	Giant	Superstar	Lover
Innovation	████	█	██████	█
R & D	████	█	██████	█
Product Complexity	☆☆	☆	☆☆☆	☆
Assembled/Disassembled	☆☆☆	☆☆☆	☆☆	☆
Customer Experience	☺	☺☺	☺☺	☺☺☺☺
Sales Complexity	YY	Y	YYY	YYY
Marketing Costs	YYY	YY	YYY	YYYY
Price	\$\$	\$	\$\$\$	\$\$\$\$



It is not at all surprising that the most frequently mentioned negative in customer satisfaction surveys is that the product just does not perform as advertised. This is a major irritant to consumers and business customers alike and the negative impact last a long, long time making it very challenging to regain the trust and loyalty of the customer who has been burned by a product or service that does not perform reliably.

For Product Leaders, any lack of product reliability hits at the core of the strategy and tarnishes the brand. For Distribution Giants, products that do not perform as advertised become a major distraction as time is chewed up trying to figure out how to fix the problem, time that could and should be devoted to maximizing each outlet by making new sales and attracting new customers. Companies whose strategy is to win as Customer Lovers can be especially hard hit when products fail to live up to expectations and the precious customer experience rings hollow. It is tough to charge premium price when the simple stuff goes wrong.

Second building block is product design and features

The second building block is the product’s inner workings; this includes the product design and the product features. From a marketing and sales perspective, these inner workings are often described in comparison to competitor’s products and/or to earlier versions of the same product. Products that offer a favorable comparison in one or more of the “Big 3” – better, faster, cheaper – strike a responsive chord with customers who rate them as superior to other similar products. However, the product differences must be real and sustainable. For example, optional side airbags are only a competitive advantage when your car make and model can substantiate enhanced safety in objective crash tests.

Product Leaders really excel at designing products and the inner workings of their products lead the pack (hence the term Product Leader). This can be a daunting task and a company that intends to win through Product Leadership needs to be prepared to devote significant resources to ensure that product features are fresh, flexible and creative and they capture the interest of the company’s target markets.

Distribution Giants often choose price (the “cheaper” component of the Big 3) as their most important product feature. Commerce Bank, a growing regional in the Northeast is a good example of the power of distribution. This bank’s products include the fairly typical lineup of loans and deposits. But Commerce really flexes its muscle by price-cutting and by offering “totally free checking” and branches open seven days per week. The Distribution Giant lets the Product Leader bear the costs for distribution and for warming up the market for a given product. The Distribution Giant is content to be on the back end of the curve of product innovation; its goal is to be a

“fast follower” that repackages a high demand product in a low price wrapper and then markets it everywhere to everyone.

Product Leaders and Customer Lovers favor products that include a heavy emphasis on the third building block, a point-of-view as a key product feature. However, each of these winning strategies uses products with a point-of-view very differently. Product Leaders imbed a very obvious point-of-view in a totally new and radically different product. For example, home pregnancy tests and other self-administered health care diagnostics come imbedded with a point-of-view that says to the customer, “You’re smart enough to administer this test and interpret the results without running to the doctor for this routine health diagnostic”. This plays to the “better” component of the Big 3.

The Customer Lover takes a slightly different approach by imbuing an ordinary product with a point-of-view, which is often delivered with kid gloves and customer tailored advice as to product selection and usage. Discretionary money management built on a best-in-class model of outside and in-house top money managers is one example of a product which illustrates the Customer Lovers’ point-of-view. Here the client is buying the advice, pre-screening, expertise and market outlook of the chief investment officer and paying a premium price for this product.

Figure 4 shows examples of bank products built using one or more of the three product building blocks.

Linking products with customer needs

One common mistake that companies make is to assume that cramming more features into a product will widen the prospective target market and result in more sales and higher customer satisfaction. The logic seems to be that if

Figure 4 Product building blocks: retail banking

Performs As Advertised	Superior Inner Workings	Point-of-View
Basic Checking	Totally Free Checking	Sweep Checking
Line of Credit	Overdraft Line of Credit	Margin Line of Credit
Conforming Mortgage	Custom Mortgage	Reverse Mortgage
Credit Card	Debit Card	Pre-Paid Cash Card
CD	Fixed Annuity	Wrap Investments
Financial Newsletter	Financial Planning	Family Office
Term Life	Variable Universal Life	Long-Term Care

there are lots of offerings in each product category and lots of features in each product, there will be a product that fits each customer's needs perfectly. Marketers seem to be taking this approach to show a wide selection assuming the customer will self-select products to meet his/her needs.

Witness the number and types of laundry detergent; the proliferation of pre-wash treatments, soaps, rinses and other additives have made the home laundry room look like a chemistry lab. Truth be told, clean, hassle free washing is the essence of most customers' needs. But the product offerings in this category suggest that nothing could be further from the truth.

To really meet customer needs, the team must first understand those needs in ways that are actionable from a product development, product management and marketing standpoint. In a perfect world, each prospect would be asked about his or her needs and the dialog around those needs would continue over the life of the relationship. For those companies that chose to win as Customer Lovers, there is an opportunity to do this by making significant investments in top-notch people and systems to focus exclusively on the customer. For the Product Leaders and Distribution Giants, the economic models of their respective strategies preclude this high touch approach and these companies must substitute technology and market intelligence for first-hand knowledge about each client.

Whether the company is relying on experienced staff, technology and market intelligence or a combination of these tools, the product development team's anecdotal understanding of the individual customer must be translated to larger target populations. To achieve the right balance between the customer's needs and the shareholder's needs, product development will need to apply just the right product building blocks – nothing more and nothing less. Knowing which product building blocks to apply to which customer segment and how to link the products to the company's winning business strategy is the essence of building great products.

The 3Cs: credibility, collaboration, contribution

In essence, what a customer needs from a product or service falls into a continuum from the most basic needs to the most complex:

- *Credibility.* The customer needs the product to deliver basic functionality reliably. Pricing should be competitive and the customer should be able to access the product and customer service through a variety of no hassle delivery channels.
- *Collaboration.* This next step on the continuum is manifested by the customer's need for a product with

imbedded and optional features, one that adapts to different users or different uses. The customer is willing to do some shopping and product selection but is willing to accept direction, as long as prices and delivery options are competitive.

- *Contribution.* This customer is the pinnacle of demanding in terms of custom tailored solutions to what the customer sees as unique and very important needs. The person/technology providing the custom tailoring better be smart, know the product inside out and be worthy of winning the customer's loyalty. When these conditions are met over and over again, the customer willingly pays for the experience.

Taking the example of a company whose winning strategy is as a Customer Lover, our research suggests that, on average, about 50 percent of the target market will be looking for the basic product array, but wrapped with advice, flexibility, creativity and premier service. The most important action for the company and its products is to establish and maintain Credibility with the target segment. Products should be routine, with all the important basic features but absent fancy or complex add-ons. Building more complex features into the basic product line would go well beyond what the Credibility customer needs or wants and would be willing to pay for.

CEOs and sales execs should remember that most new customer relationships start out at this credibility level. With care and attention, ± 20 percent or so of these customers should evolve and grow into larger more profitable (and more demanding) relationships. It is up to the sales and service managers to keep in touch with their front line client handlers, who must be trained to deliver advice, expertise, and product know how and, at the same time, to evaluate the customer's potential. This front line staff should be incented to identify high potential customers with more complex needs who can move up to the next level on the continuum.

Moving along the continuum, our experience suggests that the company should target about 40 percent of its customers and prospects to fall within the category of clients looking for contribution from the product, the sales process and the after-sales service. For this contribution segment, new products should be introduced that will be perceived by the business customer as "better" or "faster", but not "cheaper", given the Customer Lover strategy and the added product features and benefits.

For those customers seeking contribution, the relationship manager, customer service team and technology must appear to be seamless such that the customer is understood, valued and appreciated, no matter what the access point. Contact with this customer segment is proactive (as opposed to reactive with the credibility customer) and the most important

“product” now becomes advice and counsel about how to make the customer’s business grow and prosper. If the Customer Lover can move about 10-20 percent of its customer base to the collaboration level and does so profitably, most likely the company would be considered as a high performer *vis-à-vis* peers.

Product Leaders, Distribution Giants and Innovation Superstars will have different segmentation strategies consistent with their winning strategies and the percentage of customers at each level of the needs continuum will also be different. Figure 5 shows the target percentage of customers at each level of the needs continuum for each of the winning strategy models.

Conclusion

Building great products can be a reality for any company that takes the time and effort to create and execute the linkages between: winning strategy; the role of products and services; the product building blocks; and, linkages to customer needs. Our research and work with clients suggests that lack of alignment of these factors is the number one cause for the poor performance of many new products.

Company executives should review their strategy annually and clearly articulate how the company intends to win in the market place. Importantly, executing the winning strategy means adhering to the business model, product and customer imperatives and financial realities that align with each winning strategy model. Losing focus on the chosen strategy or

Figure 5 Customer needs continuum goals

Winning Strategy	← Needs Continuum Targets (%) →		
	Credibility	Contribution	Collaboration
Product Leaders	50-55	35-40	5-15
Distribution Giants	65-75	25-35	NA
Innovation Superstars	±40	55-60	0-5
Customer Lovers	45-50	35-40	10-20

interspersing, say, the product priorities from one winning strategy with the customer imperatives from another is a recipe for lackluster earnings and poor stock performance.

The linkage between product development, target marketing and customer needs segmentation must be a constant effort. Aligning the company’s strategy with specific targets for customer acquisition and retention for each level of the needs continuum drives the product development team to consciously match the product building blocks – performance, inner workings and point-of-view – with the appropriate customer needs segment from the 3Cs needs continuum. This alignment optimizes customer satisfaction and boosts profitability through winning products. ■