CORE CURRICULUM

Marketing

READING

Framework for Marketing Strategy Formation

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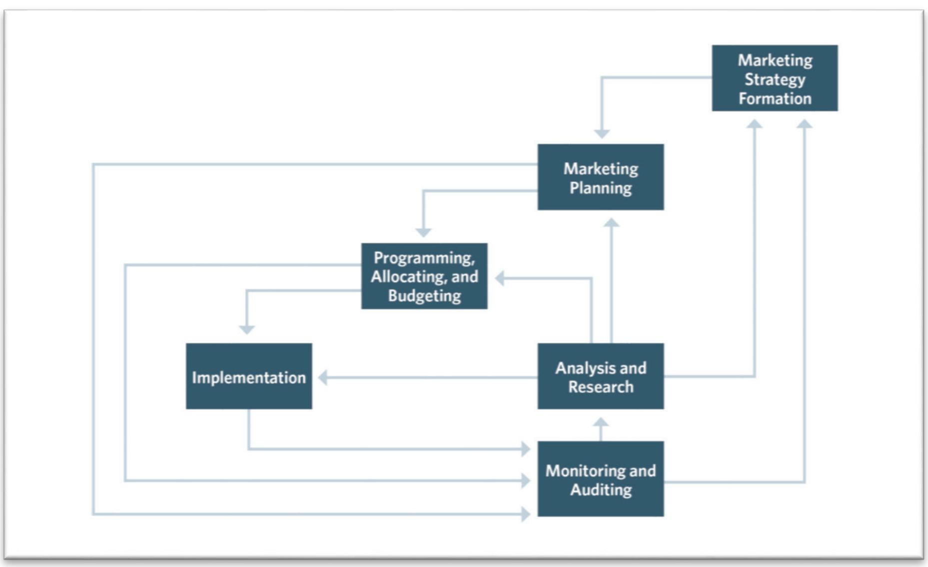
1 INTRODUCTION

In the early 1970s, Peter Drucker, the renowned management scholar, noted that "the purpose of business is to create a customer."[1] A decade later, Theodore Levitt, a Harvard Business School marketing professor, made an important addition in his book *The Marketing Imagination*: "The purpose of a business is to create *and keep* a customer" (emphasis added).[2] Levitt also noted that achieving those goals and, implicitly, the financial goals of the firm, requires "differentiating what you do and how you operate."[3] In a highly connected world where a social media platform can average more than two billion users a month,[4] it is useful in many product categories to add a third purpose: to make customers active ambassadors for your brand.

But how can one achieve the differentiation necessary to do that? Benson Shapiro, in "The Marketing Process,"[5] helps answer that question by showing the relationship among the six key elements of a customer-centered marketing proces (see Shapiro's flowchart in **Exhibit 1**).

EXHIBIT 1 Relationships Among the Six Parts of the Marketing Process



Shapiro defined the parts of the process as follows:

1. *Marketing strategy formation.* Set the overall long-term goals and basic approach to the marketplace. This typically involves making choices about specific customer groups to serve, customer wants to address, and the best way to create value for customers.
2. *Marketing planning.* Depending on the industry, the time horizon for planning can vary. In dynamic situations—for example, in a technology-driven industry—plans need to be reworked regularly. In other, more stable situations, the basics of a plan might extend over two or three years.
3. *Programming, allocating, and budgeting.* Set near-term objectives and detailed plans (typically once a year), including how resources will be allocated to the necessary activities.
4. *Implementation.* Execute the programs specified in step 3.
5. *Monitoring and auditing.* Evaluate results against goals and develop corrective action plans as needed.
6. *Analysis and research.* Gather necessary data from inside and outside the company to support the four action steps (steps 1 to 4). This data gathering should occur before executing each of the first four steps and should be ongoing, as depicted in Exhibit 1.

This reading focuses on the top portion of Shapiro's diagram, the *market strategy formation* stage, in which an organization articulates its overall goals—especially which kinds of customers it will seek to create and keep. We will also outline the basic approach for achieving those goals. A good way to think about a marketing strategy is, in Robert Davis's words, as the "blueprint by which the firm plans to compete."[6] In this reading we will set down a sound process for developing that blueprint.

Note that while a company is making the all-important choice about the customers it hopes to acquire, retain, and develop into brand ambassadors, potentially competing firms are making similar decisions—each attempting to achieve Levitt's "differentiation" among a specific customer set. For example, as fitness startup Peloton entered the market, it faced a variety of competitors offering different ways to help someone get in shape. Traditional home fitness equipment manufacturers such as NordicTrack continued to offer "new and improved" products like treadmills for home use. Fitness facilities like Planet Fitness offered access to equipment via an array of membership plans. Relative newcomers such as SoulCycle (founded in 2005) offered a new experience, founded on a vision of creating "an alternative to the fitness routines that felt like work." SoulCycle described its spin classes as "an inspirational, meditative fitness experience that's designed to benefit the body, mind and soul . . . The experience is tribal. It's primal. It's fun."[7]

Peloton identified potential shortcomings of these offerings for some customers. While there is admittedly nothing "tribal or primal" about running on a treadmill in the basement of your home, SoulCycle's engaging social experience still required getting to the studio—a significant cost to the time-pressured. Peloton thus sought to create what it called "the Peloton Difference," delivering "a world-class indoor cycling studio experience on your time, and in the comfort of your own home." To accomplish this, Peloton created a smart bike with a Wi-Fi–enabled monitor to deliver live classes from its Manhattan studios, along with tracking services that measured riders' speed, effort, miles, and other performance metrics. Initially, the bike was priced at $1,995 plus a $250 fee for delivery and setup by Peloton professionals. Access to live classes and the library of thousands of recorded classes on-demand was via subscription at $39 per month. In August 2018, with annual sales at $700 million and over 1 million members, a $550 million funding round valued the company at $4.15 billion. Peloton's 96% annual renewal rate showed its ability to retain customers. And its over 400,000 Facebook followers and the comments they posted showed its ability to create brand ambassadors as well. Later in this reading, we will elaborate on the Peloton story and the lessons it provides.

A key point is that winning the sustainable differentiation contest—and doing so in a way that yields revenues, covers costs, and contributes profits—is no simple task. Most new products, in fact, do not find a way to do so and often fail before they even get to market.[8] Organizations must recognize that they do not necessarily need to create a mass-market product loved by everyone. Peloton clearly understood that the bike's $2,000 price tag would eliminate some as potential customers. Focus is key. For example, electronics maker Vizio carved out a niche for itself in home entertainment (televisions and sound bars) by offering the "latest innovations at a significant savings."[9] On the other hand, the luxury electronics brand Bang & Olufsen directs its offerings to a price-in-sensitive group seeking maximum performance. Marketing strategy is about the process of selecting customers, deciding on the competitive point of differentiation to present to them, and developing a plan for reaching those customers.

In this reading, we set out a basic framework for thinking through the decisions to optimize an organization's chance for success. We begin with a description of the classic *5 Cs analysis* for developing a marketing strategy (customer, company, collaborators, competition, and context). We then discuss two sets of decisions every organization needs to make: the *aspiration decision* (what the company hopes to achieve in the market) and the *action plan decision* (commonly known as the *four Ps* of the marketing mix—product, promotion, place, and price). As an overview of marketing strategy, this reading does not provide extensive treatment of each area, but it does offer references throughout to appropriate sources of in-depth coverage.[10]

2 ESSENTIAL READING

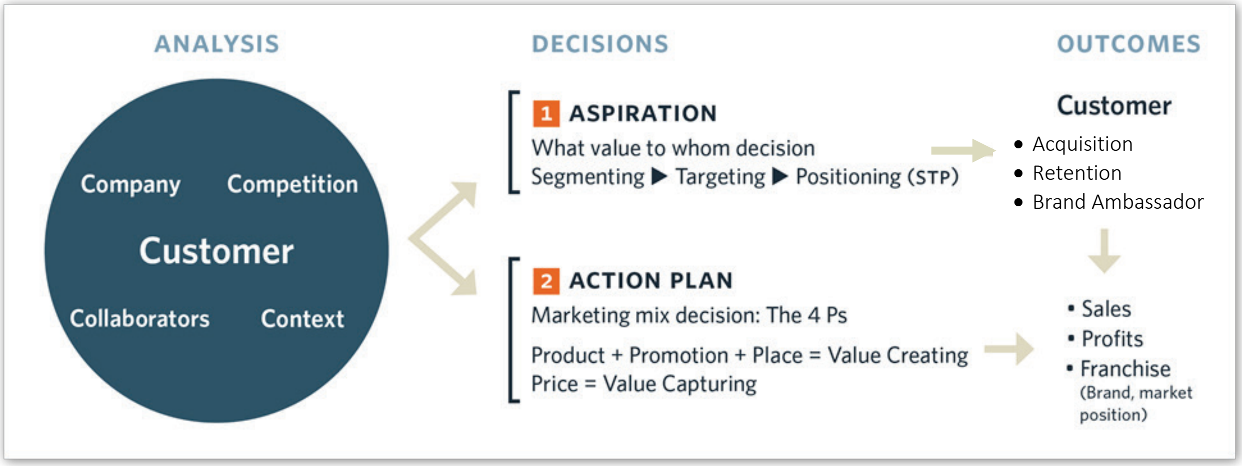
There is no one standard way to market a product or service effectively; indeed, organizations often adopt different strategies for their different offerings.[11] The approach must be tailored to the particular circumstances. Black and Decker's marketing approach to selling power tools to construction companies is quite different from marketing power tools to households for home use. Similarly, different firms within the same industry employ different approaches. Steinway devotes itself to "Making the World's Finest Pianos" (and nothing else) by strictly limiting the types of pianos it manufactures and the types of outlets through which it sells. Competitor Yamaha, on the other hand, offers everything from grand pianos and uprights to digital pianos and portable keyboards. The L'Oréal Paris line has a policy that its cosmetics can be found at a wide variety of retail partners in the United States, including department stores, grocery stores, drugstores, and mass merchants, while Mary Kay cosmetics can be purchased only from a certified Mary Kay beauty consultant (including online, telephone, and in-person orders).

A given organization might also change its marketing approach over time. Samsung Electronics, for example, launched in 1969 with a low-cost strategy, and in 1990, the company's marketing head referred to Samsung as a "third-tier commodity brand with very little product differentiation."[12] Shortly thereafter, Samsung focused on developing manufacturing expertise to compete on the basis of the highest-quality products. By 2013, it was rated number eight in Interbrand's "Best Global Brands of 2013" tabulation—the highest-rated non-US company on the list. That same polling had rival Sony at number 46, showing the extent of Samsung's transformation from a low-cost player with a reputation lagging far behind Sony to a top-quality producer.[13] By 2018, Samsung had advanced to the number six spot in Interbrand's ranking.

Customer differences—in what they value in a product or service, how they want to buy, and how they trade off price versus benefits—mean that some customers more naturally fit the capabilities and aspirations of a given company. As companies seek to find and keep different kinds of customers, it logically follows that the market will be populated with products of varied specifications, promoted and distributed in a variety of ways, and priced at different levels. For more detail, see *Core Reading: Segmentation and Targeting* (HBP No. 8219).

While there is more than one way to go to market, we can articulate the best process for developing a marketing strategy for a particular circumstance. Such a framework is shown in **Exhibit 2**.

EXHIBIT 2 Schematic of Marketing Strategy Formation Process



2.1 Overview of Marketing Strategy Formation

In Exhibit 2, we see three interrelated elements in the marketing strategy formation process: analysis, decisions, and outcomes. The middle of the diagram depicts the two different sets of decisions an organization needs to make: the aspiration decision and the action plan decision.

The aspiration decision (which we can think about in terms of what value the product will represent to what kind of customer) specifies what the firm hopes to achieve in the market. This involves three steps: (1) ***segmenting*** the market to identify possible groups to serve, (2) selecting or ***targeting*** a specific group or groups to address, and (3) determining the desired ***positioning*** in the mind of the selected customers (that is, what should the potential customer be thinking about the product offering, relative to other options?). The steps in working out the aspiration decision are popularly known as STP (segmenting, targeting, and positioning).

Once the aspiration decision has been made, the firm can begin to work out its action plan, the four Ps of the marketing mix. (We use the term *mix* because the elements all need to work together to form a cohesive plan.) Three elements of the plan create value for the customers: the product offered, the communication to the customer about the product (promotion), and the mechanisms to distribute the product to the customer (place). The final element of the mix is the price charged for the product. This is primarily the firm's way to capture some of the value it has created, generating revenue to fund operations and provide for profit. The value created for the customer through the first three Ps is the upper bound on the price the company can charge and still attract a customer. Obviously, organizations aspire to create value, such that this upper bound on the price which can be charged is greater than the unit cost of producing the value.

As shown on the left side of Exhibit 2, an organization needs to analyze the market in order to make good aspiration and action plan decisions. Usually this requires an analysis of the five Cs (customer, company, collaborators, competition, and context). To indicate its primacy for marketing decision making, Exhibit 2 places the first C—customer—in the center of the circle under analysis.

A company's choice of actions in the middle of Exhibit 2 then has to be funded and implemented. For example, if part of the chosen marketing mix is promotion via a company-owned sales force, the company must develop and field such a sales force. The decisions in the middle column thus determine how successful the company will be at acquiring a customer, whether that customer is retained over time and at what rate of purchase, and whether the customer will have a positive influence on other members of the target market, e.g., by word-of-mouth and posted reviews. The decisions made also determine the costs of the product or service and the supporting marketing costs.

As Exhibit 2 illustrates, the actions of the firm create outcomes—not only short-term financial results but also a *franchise*, the platform for future marketing efforts, including brand reputation and customer loyalty. This is not a linear process. Rather, there is a back and forth between analysis and decisions. The need to choose between action alternatives determines the specific analysis the firm should undertake. For example, if a manufacturer decides to distribute its goods through retail channels, rather than just selling on its own website, it will need to drill down further in its analysis to decide between, say, Target and Walmart as channel partners, or to identify smaller, local firms.

We will keep the interactive process between analysis and decisions in mind while, in the sections that follow, we describe the other concepts shown in Exhibit 2. Thus, we begin with analysis and a brief discussion of the five Cs.

2.2 Analysis Underlying Marketing Strategy Formation

When developing a marketing strategy, a company should undertake a five Cs analysis, starting with the primary C of (1) customer behavior (see Exhibit 2), supported by analysis of the (2) company (e.g., what special skills, competencies, and assets does the organization bring to the task of creating and keeping customers?), (3) collaborators (e.g., which suppliers can partner with the firm in its effort to attract and keep customers, and how they can be enlisted and motivated to participate as desired), (4) competition (e.g., who else seeks to create and keep the same customers? What capabilities do firms bring and what are their aspirations? What is their blueprint for competing?), and (5) context (e.g., what cultural, technological, and legal factors limit what is possible?).

In the sections that follow, we will look at each of the five Cs in an actual company context—the example of Peloton, which we introduced at the beginning of this reading.

Customer Analysis[14]

In customer analysis, one tries to understand how potential customers make a purchase decision in a product category. First, who is involved in the decision—an individual or a group? In a business-to-consumer (B2C) situation such as Peloton, for example, the customer could be a couple living together; in a business-to-business (B2B) situation, it would be the group involved in any aspect of the buying decision, from gathering information about alternatives, to making the final purchase decision, to using the product. Once this *decision-making unit* (DMU) is specified, analysis turns to understanding the *decision-making process* (DMP). Formal market research, such as focus groups or surveys, are often useful at this stage. The key is to understand the buying criteria of the targeted segment to ensure the fit of the firm's offering to the target market's wants—in short, a *product/market fit*.

John Foley, Peloton's founder, developed the Peloton concept based on his own dissatisfaction with available exercise options. Before starting Peloton, Foley was a busy executive and "became addicted to high-energy indoor cycling classes"[15] such as those offered by SoulCycle. However, Foley found that, given the demands of work and family, getting to classes was a challenge, and that the most popular instructors and classes were often sold out. With his IT and business background, Foley knew technology could be brought to bear on this problem. Foley had also analyzed the rise of social media and understood the potential for creating an online community that could simulate the energy and support of an in-studio class. The company name was derived from a *peloton*—"the main group of riders in a race" that support one another.

To assess potential market size and customers willingness to pay $2,000 for a bike plus the $39 monthly subscription fee, Peloton researched current fitness spending levels and found "tens of millions of Americans who spend more on fitness than the cost of a Peloton bike when averaged over three years."[16]

The market size analysis supported Peloton's development of the full system—a "smart" bike, select and highly trained instructors, and software to deliver the content. Peloton's initial concept was targeted to a specific market: one that was affluent (could afford the initial $2,000 for the smart bike) and suburban (in areas where high-energy cycling classes were less available). As reported by Carolyn Tisch Blodgett, Peloton's senior vice resident and head of global brand marketing, "We had this idea of a very affluent rider, who many of our early adopters were. We realized through conversations with our community that there was a huge opportunity with people who thought $2,000 was a huge investment but were [buying] it over and over again because the product is so important to them." These conversations took place in the growing number of Peloton-owned and -operated showrooms and in regularly conducted surveys. An interview with Brad Olson, Peloton's senior vice president of member experience, indicated that "Peloton surveys patrons throughout their member journey" and "looks for trends across its email and social channels."[17] This research revealed, among other things, a "huge urban opportunity" in areas where SoulCycle and others actually served to "give Peloton a boost" rather than acting as a competitive barrier.[18]

As Peloton came to understand that its potential customer market extended beyond the affluent, price-insensitive segment, the company began to communicate that Peloton was really an economical alternative. It reframed the price of the bike by offering interest-free, "no money down" financing. In 2019, its website effectively restated the $2,262 bike purchase price as "$58 per month for 39 months with 0% APR financing."

Peloton's DMU was typically fairly simple: an individual or a couple living together. In a B2B situation, however, the DMU can be quite complex. When trying to ascertain the DMU, the marketer should ask: Who are the participants in the buying process, and what role does each play? In an influential article, Thomas Bonoma set out six major roles generally played across a broad set of buying situations:[19]

- *Initiators.* Initiators recognize the value of solving a particular issue, so they stimulate the search for a product.
- *Gatekeepers.* Gatekeepers act as problem or product experts and control information and access to other members of the DMU.

- *Deciders.* Deciders make the purchasing choice.
- *Influencers.* Although they do not make the final decision, influencers have input into it.
- *Purchasers.* Purchasers consummate the transaction.
- *Users.* Users consume the product.

In his work on capital equipment and service purchasing, Bonoma found an average of seven people typically fill these six roles.

After determining the DMU, a marketer must next understand the purchaser's decision-making process, which includes finding responses to questions such as, Will there be a search for information, and how will it be conducted? How do the DMU members interact? What criteria will be used in making the decision? What is the relative importance of each of those criteria? Can one criterion be traded off against another, or is there some minimum level that must be reached on each?

A variety of research methods can be used to answer these questions, ranging from quantitative surveys to qualitative methods such as focus group discussions or customer interviews. (For a survey of these methods, see *Core Reading: Marketing Intelligence* [HBP No. 8191]).

Company Analysis

The second C to consider in developing a marketing strategy is the company's strengths and weaknesses. Through customer analysis, Peloton attempted to design a product that fit the market; the next requirement was to ensure that the product and approach fit the company's existing skill set—or a skill set it could assemble.

Generally, assessing product/company fit requires an understanding of the firm's finances, research and development (R&D) capability, manufacturing capability, and other assets. A highly influential concept, developed by Prahalad and Hamel, is a company's *core competency.* Two key elements of core competency are to (1) make a significant contribution to the creation of perceived customer value in products and (2) be difficult for competitors to imitate.[20]

Peloton's success came from having a clear vision of what kind of company it wanted to be. Carolyn Tisch Blodgett commented, "We didn't set out to be a stationary bike company. We set out to revolutionize the fitness industry through technology."[21] The skills required to be a successful revolutionizer were quite different from those required to be a stationary bike company. After all, a traditional stationary bike company would not need a head of music, one of the key positions on the Peloton leadership team.

The vision of the "Peloton Difference" delivering a "world-class indoor cycling studio experience on your time, and in the comfort of your own home" required augmenting the typical smart bike with great content in the form of instructors, who are able to deliver a SoulCycle–like experience remotely, with accompanying music, and who could generate a loyal following. Peloton knew that the market education job required was quite substantial. Stories of expensive fitness equipment soon abandoned by purchasers were plentiful. Given the education task at hand, Peloton chose to manage sales in-house rather than distribute the smart bike through an intermediary. To provide for appropriate demo opportunities, by 2019 the company set up over 60 US showrooms in more than 25 states, along with locations in the UK and Canada.[22]

Collaborator Analysis

The C of collaborators involves analyzing the set of external assets that may be accessed to complement those of the company. At the start, Peloton's company analysis would have identified some significant holes to fill. The company had a good idea, yes, but it still needed money for R&D and the capacity to manufacture at large scale.

With respect to money, one of Peloton's collaborators was the website Kickstarter. In June 2013, Peloton announced a campaign offering future delivery of a bike for a pledge of $1,500 or more. More than 170 backers gave their support at the "bike" level, and the overall campaign raised $307,332 from 297 backers against a goal of $250,000.[23] The company also attracted backing from well-known venture capital firms.

Still, Peloton enlisted as its collaborators "two core manufacturing partners," one for the bike and the other for the tablet computer.[24] The bike partner was described as "one of the best indoor cycle manufacturers in the world" having produced "nearly one million indoor cycles over the past two decades."[25]

Having upstream collaborators in manufacturing allowed Peloton to concentrate on (1) development of instructors, music, and content and (2) market education.

Competitive Analysis

Winning the customer acquisition game requires creating more value (benefits minus costs) for customers than any other options known to them. Thus, a firm must identify who its competitors are now and who they are likely to be in the future.[26] Peloton's founders were quite familiar with competitors through their experience as consumers.

Peloton also demonstrated best practice in this area by defining the competition in an appropriately broad way: In addition to pinpointing companies that were competitors, it also identified one significant competitor as *not engaging in regular fitness activity*. Peloton has reported that eight of 10 people buying a Peloton bike were not in the market for fitness equipment. Peloton's goal was not so much to claim to have a better stationary bikes or studios, but rather "to create an experience that makes people 'want to work out.'"[27]

Competitive analysis requires assessing others' offerings, the market they address, how they address it, and how all that will evolve over time. As with company analysis, any realistic assessment of the competition must begin with a fundamental understanding of its strengths and weaknesses. Marketers can gain this information in a number of ways, including analyzing competitors' statements about themselves (for example, 10-K filings for publicly traded companies) and interviewing potential customers about their perceptions of competitors' offerings. Marketers can also observe a competitor's marketing actions, including the product it has on the market and, when possible, reverse-engineer or "tear down" a product to understand its features and likely cost.

Context Analysis

A good marketing strategy takes very little for granted. The context shapes what is possible, and the context is always changing. This point is vividly illustrated by the disruption that technology—and, specifically, the internet—has brought to existing business practices. For Peloton, this context analysis identified cultural trends related to social media interactions and vibrant online communities.

Like technology itself, a context such as culture can shift quickly and bring surprises unless it is carefully monitored. Many fortunes are made by anticipating cultural trends (consider the success of McDonald's and Nike). Products and services acquire meaning from their place in a culture, and they acquire economic value from that meaning. Thus, value is vulnerable to shifts in the culture. The systematic analysis of cultural trends (popularized as *coolhunting* in consumer ethnography) is increasingly an integral part of marketing strategy formation.

Similarly, politics, regulation, law, and social norms are not fixed features of the marketing landscape; rather, they are dynamic factors to consider and monitor for signs of disruption. Markets such as banking, television, and pharmaceuticals operate in particularly unstable settings. It is dangerous to design marketing strategies for such environments without a carefully developed point of view on the regulatory context.

Each of the five Cs we have just examined is critical, but in marketing, none is more important than the C of customers—understanding their preferences and perceptions, and how they make decisions. Devising an effective marketing program requires deep analysis to support decision making on a host of interrelated issues. With this preliminary understanding of key analysis types, we will now explore in depth the specific marketing decisions to be made.

2.3 The Aspiration Decision: Segmenting, Targeting, and Positioning

As we've said, the aspiration decision specifies what the firm hopes to achieve in the market. This decision involves three steps: *segmenting* the market, *targeting* a specific customer group or groups to address, and determining the desired product or service *positioning* in the mind of the selected customers (commonly abbreviated as STP).[28]

Examples abound of firms consciously positioning products and services to target a particular set—or segment—of customers. In fact, many companies renounce some potential customers so they can focus exclusively on a select customer group whose wants their product is particularly well suited to serve. The Coca-Cola Company described its Coke Zero as being "created with young adults in mind."[29] (Later, this product was renamed Coke Zero Sugar, since research showed that few customers understood it contained no sugar and had zero calories.) In the financial services market, Chase designed its new Sapphire Reserve credit card specifically for millennials, a group it had not attracted well to date.[30] For many years, IKEA stated that it would want you as a customer "if you can do simple things like pick up your purchases and assemble them at home."[31] "Bugs" Burger Bug Killers unconditionally guarantees pest elimination, not just pest control, and therefore accepts only customers willing to follow its strict cleanup regimen—and to pay premium prices.[32] In contrast, Spirit Airlines addresses the price-sensitive customer directly, stating, "Spirit gives you more go for less money . . . our low ticket prices are designed to save you an average of 30% . . ."[33] Marriott designed its Courtyard hotels for business travelers and its Residence Inns for those on an extended stay. Zipcar's car-sharing service, first operating in Boston, sought to solve the transportation and parking problems of urban dwellers and college students, who were generally neglected by car-rental companies with their "no one under 25" rules. Outotec of Finland offers its gold- and copper-mine design and construction services for the most challenging set of circumstances, because those circumstances play to the firm's distinctive engineering skills.[34]

Looking at customer segments and how the purchase process varies across them allows organizations to fine-tune the marketing mix to meet the particular needs of chosen customers. Indeed, segmenting customers has become a key aspect of marketing today. In the words of Theodore Levitt, "If you're not thinking segments, you're not thinking."[35]

An organization's target market selection decision is critical because customers ultimately set their own purchase criteria and thus dictate the rules by which the marketing game will be played. Thus the target market selection should consider the firm's corporate goals and the fit of the segment with these goals; it should also consider the firm's comparative strengths and weaknesses vis-à-vis competition, given the target market's purchase criteria.

As the examples listed earlier suggest, and as **Exhibit 3** shows, markets can be segmented in a variety of ways. Note also that segments can be defined by simultaneous use of more than one variable; for example, Zipcar combines demographic (age under 25), geographic location (urban), and psychographic (environmentally concerned) variables to define its ideal customer.

EXHIBIT 3 Common Segmentation Variables

Variable Type	Example	Segment Defined
Demographic	Coke Zero	Age (young)
	Chase Sapphire	Age (Millennial)
	Zipcar	Age (under 25)
	Marriott Courtyard	Business traveler
Geographic	Zipcar	City dwellers and college students
Psychographic/lifestyle	Zipcar	Environmentally concerned
	IKEA	Value-oriented
Benefit sought	"Bugs" Burger Bug Killers	Pest elimination (not control)
	Spirit Airlines	Low price
	Outotec	High performance
Usage	Marriott Residence	Long stay

The most widely used segmentation bases are demographic (e.g., age, income, gender, occupation), geographic (e.g., nation, region of country, urban versus rural), and lifestyle (e.g., hedonistic versus value-oriented). An alternative type of segmentation variable is the customer's behavior or relationship to a product: for example, the customer's user status (nonuser versus user), usage rate (light, medium, or heavy user), and loyalty status (none, moderate, strong, or totally loyal). With the increasingly widespread use of customer loyalty cards, usage-related customer segments can now be readily identified and targeted. Digital marketing firm Catalina Marketing has gone from tracking 200 million unique loyalty card identifiers to maintaining two-year purchase histories for over 650 million shoppers.[36]

In the segmentation and target market selection process, a company has to play out various scenarios. Consider the positioning part of the aspiration decision: If we pursue this segment, how would we approach it and what would we want segment members to see in us? Positioning answers these questions. The answers should be formalized in a positioning statement. A positioning statement can take many forms, but effective statements specify the following essential elements:

1. The target customer, as defined by the segmentation variables
2. The wants of that customer
3. The product type and category, as seen by the customer
4. The key benefit to be provided to the target customer

For example, Tybout and Sternthal recount the following positioning statement for Zipcar:

> To urban dwelling, educated, techno-savvy consumers who worry about the environment that future generations will inherit, Zipcar is the car sharing service that lets you save money and reduce your carbon footprint, making you feel you have made a smart, responsible choice that demonstrates your commitment to protecting the environment.[37]

The Ross School of Business at the University of Michigan developed this positioning statement for its MBA program:

> For prospective students seeking leadership capability development, Ross is the best MBA program because of the opportunity sensing skills and teamwork capabilities developed through extensive action-learning experiences, complementing classroom learning.[38]

The positioning statement is intended to get the whole organization aligned regarding the aspiration decision. External statements derive from the positioning statement. Both Zipcar and Ross had taglines related to, but shorter than, their positioning statements: Zipcar proclaimed “Wheels When You Want Them” and Ross touted itself as “Leading in Thought and Action.”

A meaningful target market selection typically provides focus by deliberately excluding some customers from the market served. For example, in its early days, Dell consciously renounced first-time buyers of a personal computer because such buyers lacked the sophistication required to custom design a machine on the web.[39] The Ross School of Business consciously renounced MBA candidates not interested in developing teamwork skills through action learning. The previous positioning of the school was so general, focusing on the non-differentiating attributes of being collaborative and innovative, that no one was excluded. The new, narrower positioning caused a short-run decline in applications as the school actively sought to discourage applications from those not sold on action learning. But that strategy was validated when the percentage of accepted MBA students who enrolled increased dramatically because of the superior fit of the service to the selected target.[40]

Anderson, Narus, and van Rossum argue persuasively that a positioning statement or consumer value proposition (in their terminology) should have a "resonating focus" concentrating on "the one or two points of difference that deliver, and whose improvement will continue to deliver, the greatest value to target customers."[41]

The goal is to define a target market that can be reached by the firm efficiently, whose members value the firm's comparative advantage, and who are willing and able to pay for it. Kotler articulated the fundamental importance of making the aspiration decision: "The advantage of solving the *positioning problem* is that it enables the company to solve the *marketing mix problem*. The marketing mix—product, price, place, and promotion—is essentially the working out of the tactical details of the positioning strategy."[42] This marketing mix is the focus of the next section.

2.4 The Action Plan: The Marketing Mix Decision

Once an organization has made the aspiration decision, it can address the marketing mix decision (the action plan). Neil Borden of Harvard Business School originated the term *marketing mix* to describe the set of activities composing a firm's marketing program.[43] He noted the ways in which a firm blends mix elements into a program and that competing firms can have dramatically different mixes at work. Borden originally specified 12 distinct mix elements, ranging from product planning to display. Over time, an aggregation of these elements has become popular. As shown in Exhibit 3, the four Ps terminology of product, price, promotion (communications strategy), and place (channels of distribution) is often used to set out the marketing mix in a memorable way. As suggested by Borden's use of the term *mix,* it is important that the various elements blend well.

Benson Shapiro has identified "three degrees of interaction" in the marketing mix:[44] *consistency* of mix elements—the minimum standard, implying a generally good fit, *integration*—existence of positive, harmonious interaction, and *leverage*—where each element is used to its best advantage to support the value creation or capture of the overall mix. In the sections that follow, we examine some of the major issues involved in setting the four Ps.

Product Decisions

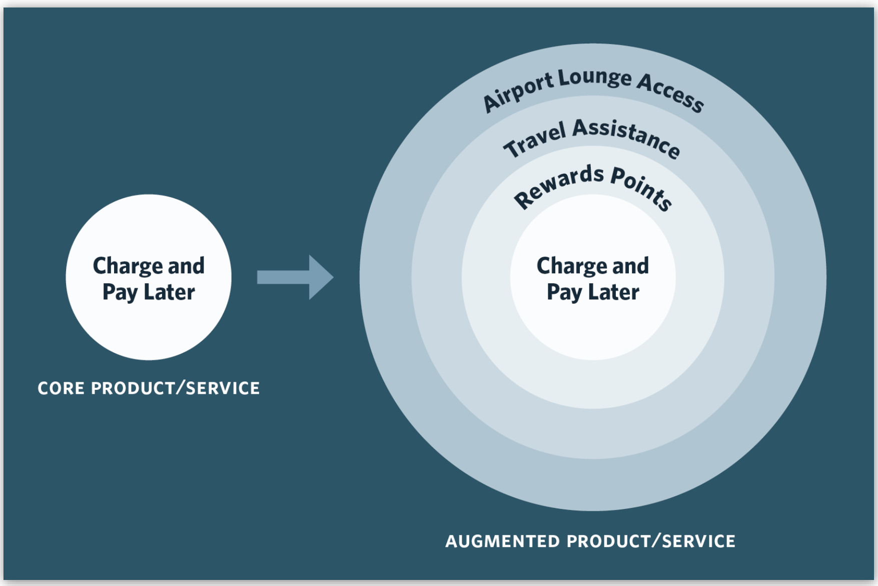
The product or service offered is the centerpiece of the marketing mix. The *product offering* is best conceptualized as the complete set of ways (rather than just a single core feature) that a firm delivers value to its chosen customers. For more detail, see *Core Reading: Product Policy* (HBP No. 8208).

For example, a conventional home thermostat, costing about $25, senses the room temperature and automatically turns on the heat when the room temperature falls below a specified level (or turns on the air conditioning if the temperature rises above a specified level). Programmable versions, costing slightly more, permit the desired temperature setting to vary by time of day and day of the week.

Even though the relatively low-tech thermostats work fine for many customers, the desires of some customers are best met by the Nest, the "Learning Thermostat," first introduced in 2011. The company was acquired by Google in 2014 for $3.2 billion. Although its core function of turning the heat on and off is the same as that of a $25 thermostat, Nest provides added benefits as reflected in its $249 list price (as of July 2019): First, it is designed to be simple to install. Second, it is easy to use. The customer doesn't have to program anything—just adjust the temperature as desired; Nest learns the desired temperature by the time of day, or the day of the week, and automatically programs itself to accommodate those desires. Third, if a customer is deviating from a usual pattern, such as heading home early from work, Nest can be controlled from a smartphone. Fourth, if a customer is not at home, Nest senses that and adjusts the temperature to conserve energy. Fifth, Nest reminds the customer to change the air filter. Sixth, the customer doesn't have to calculate the savings gained, Nest sends a monthly energy report. Seventh, it lights up when a person walks into the room. Eighth, it will call you if the furnace acts up and house temperature drops. Ninth, Nest's design and appearance have been highly praised in product reviews. In short, the Nest product is far more than just a device to turn the heat and air-conditioning on and off; rather, it is a complete bundle of benefits that can be offered to, and appreciated by, a particular segment of customers.

The logic here applies to services as well as products. For example, in 1958, American Express launched its charge card directed to business customers. It provided the basic function of charging purchases to a card. Over time, Amex added Gold and Platinum cards. These new offerings were not distinct from the original Amex card because of improvements on core credit card functionality; however, they were augmented with other benefits such as membership rewards points, concierge services, and, for Platinum holders, access to select airport lounges (see **Exhibit 4**).

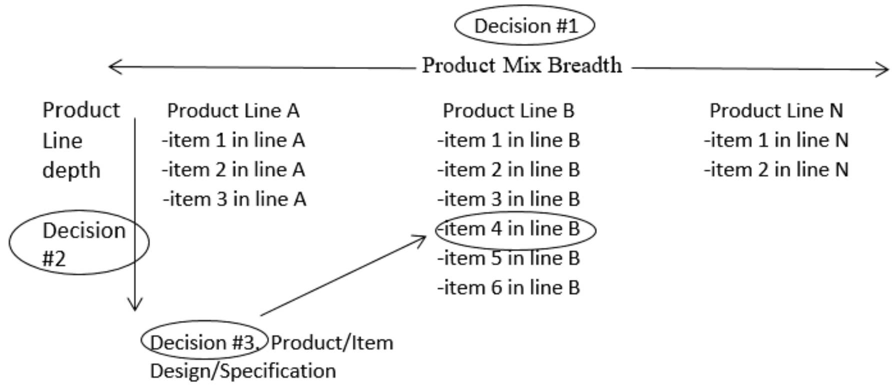
EXHIBIT 4 Range of Credit Card Benefits for American Express Customers



As these examples illustrate, the core function of a product is not what makes the sale in most situations. That is why, when defining a product or service, marketers need to think of the full set of ways in which value can be created for customers—be it by brand name, company reputation, core functionality, ease of installation, ease of use, post-sale assistance, or warranty. This broad conception of a product is the key to seeing possible valuable points of differentiation from competitors. In fact, Theodore Levitt advocated the adoption of a total product view, considering the product as the full set of ways in which an offering can solve a customer's problem.[45]

This mentality of broadly defining a product needs to be brought to all the firm's product decisions. **Exhibit 5** shows the three major product decisions that a firm faces.

EXHIBIT 5 Product Policy Decisions



Product Breadth

First, *product line breadth* refers to the variety and number of product lines offered (see Exhibit 5). Some firms have a narrow focus with few product lines. For example, since its founding in 1916, BMW has focused just on automobiles, and its "100-year plan" is the same, that is, to be "the leader in automotive engineering, without abandoning what got us here to begin with."[46] On the other hand, Mercedes-Benz makes buses and trucks along with its car line; the three different product lines are linked through technology. Contrast this with luxury goods conglomerate LVHM, which has chosen a strategy of very dissimilar use cases and enabling technology, but all products are linked by a similar designation of "luxury." LVMH operates in six business sectors with 75 different brands (or "houses," in LVMH terminology). The following are business sectors and example brands:

- Wine and Spirits: Dom Pérignon, Hennessy, Cloudy Bay Wine
- Leather and Fashion Goods: Louis Vuitton, Fendi, Christian Dior
- Perfumes and Cosmetics: Guerlain, Acqua di Parma, Fresh
- Watches and Jewelry: Tag Heuer, Bulgari, Hublot
- Selective Retailing: Le Bon Marché, DFS, Sephora
- Other Activities: Royal Van Lent (yachts), Jardin d'Acclimatation (amusement park), Belmond (luxury travel)

Product Depth and Line Organization

The second key decision shown in Exhibit 5 is *product line depth*: How deep should a given product line be? How many offerings of a given type will there be? What will the relationship among them be? A "good, better, best" strategy is common. In product lines with this architecture, most consumers see the higher-priced item in the line to be of higher quality. Consider the Regular, Plus, and Super gasolines of differing octane levels available at most gas stations, or subscriptions for products such as Docusign's "e-signature" system, which offers three levels:

- Personal: $10/month. Limited to five document sends per month.
- Standard: $25/month. Unlimited number of document sends.
- Business Pro: $40/month. Adds collect payments features, advanced fields, signer attachments, and bulk send.

An alternative line organization is directed at appealing to different segments. For example, Chevrolet offers a number of vehicle lines, including cars, electric vehicles, trucks, crossovers and SUVs, and performance vehicles. Within its car line, Chevrolet offered five models directed to different segments of the market (see **Exhibit 6**). A city dweller may view the Spark as a superior car to the Impala because of a desire for a small vehicle that can contend with busy city streets.

EXHIBIT 6 Chevrolet Car Models, 2019

Model	Price (Starting at)	Positioning
Spark	$13,220	"Small wonder"
Sonic	$15,420	"Small car, big thrills"
Cruz	$17,995	"Sporty compact"
Malibu	$22,090	Midsize
Impala	$28,020	Full size

Source: Chevrolet, https://www.chevrolet.com/, accessed August 24, 2019.

In contrast to distinguishing products by price or quality, another line structure differentiates items not by price or quality, but instead by offering multiple items at the same price to appeal to different tastes (e.g., clothing in various colors, Gatorade of different flavors).

Evolving Product Lines

A firm's product offering obviously changes over time when new lines are added, when new items are added to an existing line, or when existing items are modified.

Modifications introducing "new and improved" features to existing items are quite common, and model changes may come at regular intervals (e.g., the auto industry's model years) or as technology developments warrant updates or new releases. For example, in November 2013, seven years after the introduction of PlayStation 3, Sony released PlayStation 4 with "deeply integrated social capabilities."

Adding an item to a product line alongside existing items can represent a *trade up* or *trade down.* For example, Tanqueray traded up its London Dry Gin, adding Tanqueray No. Ten, described as "born in the elegant 10th still" with "small batches and fresh fruit." No. Ten came at a 25% price premium over the original. Trading down is reducing the functionality or performance of a product (and its cost) to be able to hit a lower price point in the market. For example, Delta Airlines traded down its seat offerings, adding a Basic Economy fare that is lower and more restrictive than its Main Cabin fare. As positioned by Delta, "Basic Economy provides a value for solo travelers and light packers who don't anticipate changes to their travel plans." In contrast to Main Cabin seats, Basic Economy seat assignments could not be selected at purchase and were assigned after check in; no ticket changes or upgrades were allowed; and access to overhead bin space for carry-ons was restricted, since Basic Economy ticketholders are last to board.[47]

Product Testing

Based on extensive study of new product launches, Robert G. Cooper has identified key success drivers. While Cooper admits some of these markers of success may be fairly obvious, his experience shows that some firms simply neglect them.[48] The key success factor is to have the output of the product design process be "a differentiated product that delivers unique benefits and a compelling value proposition. . . . " That outcome is advanced by "building in the voice of the customer" and by "spiral development," wherein a company first develops a concept and then a prototype, which is put in front of the customer for feedback, and then revised based on the customer's feedback.

Testing with customers can be done in a number of ways, including surveys, taste tests, simulated test markets (in which mock stores are set up and customers are recruited to shop in the mock store environment), and actual test markets for consumer goods and beta tests for industrial goods.[49] In a beta test, potential later adopters of a technology are recruited to use and evaluate a product as an input to design refinements and the go/no-go decision. Testing is appropriate not only for the product itself, but also for the supporting elements of the marketing mix, such as the communication strategy and price.

Promotion Decisions

The next element of the marketing mix is promotion—how organizations communicate with potential customers about product positioning. Initially, the goal may be to create product awareness, then knowledge about the product's features, then a level of interest in purchasing to the point of making a trial purchase as the product value is communicated. After the customer has tried the product, promotion has a reinforcing role in, as Levitt specified in his definition of marketing, *keeping* the customer.

The emergence of the digital age of marketing has fundamentally changed the nature of this communication with the customer. Previously, the organization controlled the communication about its brand to a large extent. Now, however, customers more actively seek information about a brand (particularly online) and contribute to the conversation about the brand via ratings and postings on social media. Procter & Gamble is known for focusing on the "First Moment of Truth," as the customer stands before the display in a grocery store, and the "Second Moment of Truth," as the customer uses the product at home. Google has since coined the term "Zero Moment of Truth" (ZMOT), advocating for better understanding of customers as they begin their information search. Google research showed that consumer technology product shoppers used 14.8 information sources on average in making a purchase decision.[50]

Customer reviews are increasingly part of the purchase decision. In its early days, Amazon did anticipate customer reviews becoming an important part of e-commerce; however, it may have been hard to foresee that in July 2019, one could find on Amazon:

- 5,000 reviews for a $500 Toshiba 55-inch TV
- 4,000 reviews for $20 jar of Olay Regenerist Sculpting Cream
- 1,500 reviews for a $10 Light My Way Nightlight
- 350 reviews for a $5 bag of assorted-size Amazon rubber bands

Facebook's over two billion monthly active users often share product information, and many customers and reviewers also enjoy the video capability of YouTube, where viewers can find "unboxing" videos, reviews, and how-to videos of many products in use. For example, the YouTube channel Ryan ToysReview has over 20 million subscribers, and by 2018 eight-year-old Ryan and his family had generated $20 million in advertising on their YouTube channel.[51] In addition, Hardee's hired Ryan as an influencer to market its kids' meals with four toys designed by Ryan. A Hardee's executive explained the move as "Our customers are digital-first."[52] In the connected digital world, the power of consumers becoming brand ambassadors (paid in some cases, like Ryan or celebrity endorsers, and unpaid in others) is increasingly important.

Because of the variety of steps in the process of creating customers, keeping them, and developing them into brand ambassadors, an integrated communications plan is key to an effective marketing strategy. Such an effort brings together a variety of media, perhaps combining personal selling efforts with nonpersonal ones, such as advertising, sales promotion, and public relations. Let's look now at some of the tasks and tools required in promoting a product or service.

Tasks

A useful mnemonic for the tasks in planning a communications strategy is the *6 Ms* model:

Objective
1. *Market.* To whom is the communication to be addressed?
2. *Mission.* What is the objective of the communication?

Tactics
3. *Message.* What are the specific points to be communicated?
4. *Media.* Which vehicles will be used to convey the message?
5. *Money.* How much will be spent in the effort?

Results
6. *Measurement.* How will impact be assessed after the campaign?

By formalizing a positioning statement, an organization will be able to answer the market and mission questions and provide a foundation for answering the message question. The specific message should consider both the aspiration embodied in the positioning statement and the customer's current state of mind.

With respect to the fourth of the 6 Ms, media, a communications program sometimes comprises a wide variety of elements. For example, Sephora (part of LVMH), a retailer of specialty beauty products that has grown to over 2,500 stores worldwide in 2018,[53] expanding dramatically from 270 stores in 2010. At this earlier point in the company's growth, Sephora had formulated its integrated traditional marketing and digital media efforts into a communications plan that included many elements, as shown in **Exhibit 7**.

EXHIBIT 7 Sephora Communications Plan

1. Striking store window displays
2. A Sephora website home page "look" consistent with the store window
3. Advertising with specific keywords with Google AdWords to direct online web searches to the Sephora site
4. Print advertisements in leading magazines
5. A loyalty program called "Beauty Insider" in which enrolled customers received
   - E-mails once or twice a week
   - Direct Mail
   - A 32-page print catalog
   - Free gifts/samples
6. A "Very Important Beauty Insider" program for high-spending customers, featuring free gifts and invitations to special store events
7. Highly trained salespeople in stores, referred to as cast members, and attired in Sephora black, white, and red. This personal selling effort was responsible for embodying the Sephora message and providing advice to customers.
8. Facebook advertising
9. YouTube videos (typically directed to product application demonstrations)
10. Mobile applications

Source: Adapted and reprinted from "Sephora Direct: Investing in Social Media, Video and Mobile," HBS No. 511-137 by Elie Ofek and Alison Berkley Wagonfeld.

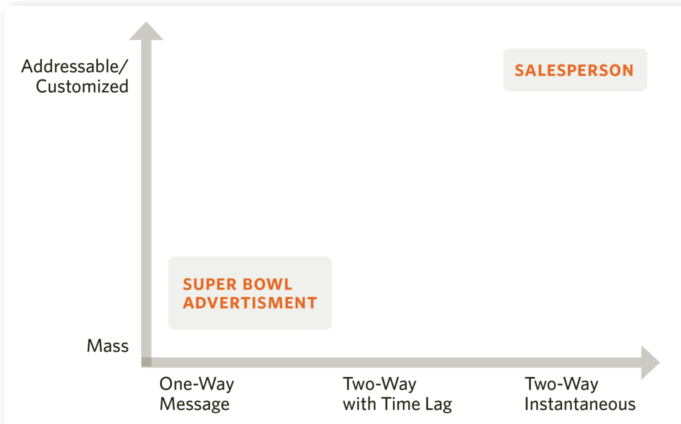
Tools

Exhibit 8 shows two dimensions along which it is useful to contrast communication vehicles: one-way versus two-way, and mass versus addressable/customized.

One-way versus two-way communication. The horizontal axis (dimension) in Exhibit 8 depicts the distinction between situations in which there is only outbound (one-way) communication and those in which there is two-way communication (an interaction between the initiator and receiver of the initial message). Television ads are typical one-way communications to a mass audience. When Pepsi ran its "More Than OK" ad featuring Steve Carell and Cardi B during the Super Bowl in 2019 (with ad rates running $5 million for a 30-second spot), it sent the same message out over the airwaves to the approximately 100 million viewers tuned to the US television network CBS.

At the other end of the spectrum is the two-way dialogue. For example, during the same Super Bowl, Audi used a 60-second spot during to announce the pending availability of its electric car, the e-tron SUV. That ad may induce a viewer to visit an Audi dealership where a salesperson is likely to engage that person and deliver a message. The prospect would then respond, and an exchange of some duration would ensue in which the salesperson tailors or customizes his or her reply to the prospect's comments. If the salesperson's message is persuasive enough, the prospect's ultimate response may well be to test-drive and then buy or lease the Audi. Thus, the communication begins as a one-way, instantaneous one, but it evolves into a two-way communication.

EXHIBIT 8 Characteristics of Communication Options



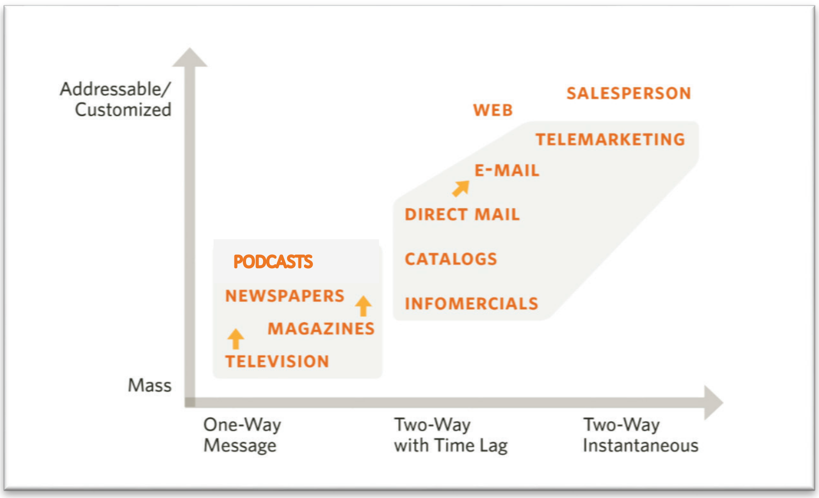
Source: Adapted from a set of dimensions originally suggested by Professor John Deighton, Harvard Business School.

As shown in the middle of the horizontal axis of Exhibit 8, other two-way interactions may occur with a time lag. For example, a direct mail piece may prompt a reply by the receiver, although that reply may await the receiver's attention or next trip to the post office.

Mass versus addressable or customized communication. The vertical axis (dimension) of Exhibit 8 describes the extent to which the message can be varied to meet the particular communication needs of the person receiving it. The Audi ad airing during the Super Bowl was not customized; it was delivered via a mass medium to everyone watching in precisely the same way at the same time. But the car salesperson can and should customize their message to the specific communication needs of the message recipient. A primary advantage and justification for the typically high cost of personal selling is this ability to adjust the message to the situation. For example, the Audi salesperson might augment discussion of the car's electric features with talk about its safety features to the family with four children, the car's cargo capacity to the young couple with ski weekends on their minds, and low initial payment leases to the first-time car buyer with no equity in a trade-in vehicle.

Exhibit 9 depicts some of the other important *communication vehicles* available. The positions of each of these messaging options are generally suggestions rather than absolutes for all situations.

EXHIBIT 9 Positions of Major Communication Vehicles



Source: Adapted from a set of dimensions originally suggested by Professor John Deighton, Harvard Business School.

The proliferation of cable TV channels has increased the addressability/customizability options for television, as represented by the upward arrow in Exhibit 9. Obviously, everyone watching the same national broadcast sees the same advertisement. But there are now many specialized channels that have specialized audiences. An ad can be customized to the kind of audience typically viewing a certain TV show (or reading a particular magazine, or viewing a particular website), thus matching the message to the audience.

Podcast advertising (such as Casper's ads for its mattresses on the "How Stuff Works" podcast) doubled in utilization from 2017 to 2019.[54] An advantage of this medium is that the message is typically embedded in the program content and delivered by the host, and thus more difficult to block out.

Promotions. In addition to advertising messages, two types of promotions commonly form part of the communications mix. *Customer promotions* may include free samples, continuity programs, and coupons. *Trade promotions* include incentives to retailers, such as free goods or discounted prices if the product is provided in end-of-aisle displays.

Free samples are especially useful in getting customers to try a product. They can be distributed in the mail or through online offers, passed out at points of purchase, or made available upon request from a potential buyer. For example, in 2019, Spotify, the leading music streaming company, offered one month of the its premium service for free, followed by $9.99 per month subscription rate thereafter. While samples typically prompt an initial use, a *continuity program* rewards customers for continuing the relationship; an example is an airline's frequent flyer program.

How promotion dollars are allocated across media vehicles varies greatly depending on the market situation. A fundamental decision is whether to focus on a push strategy or a pull strategy. In a *push strategy*, marketers focus on inducing intermediaries, such as a retailer, to play a major role in creating demand for the product. For example, high-end suit manufacturers such as Ermenegildo Zegna and Canali may spend a small amount in advertising and communicate to men via magazines, but given the key role retailers like Saks Fifth Avenue play in selling the brand, the manufacturers' key concern would be how to incent retailers to "push" their brand at the point of sale. In a *pull strategy,* for example, Levi's attempts to create a strong customer preference for its jeans, the retailer's role is merely to make the product conveniently available.

As the number of feasible communication vehicles has increased (e.g., event sponsorship, telemarketing, product websites, postings on someone else's website, social media, and infomercials), the job of specifying the right communications mix has grown more complex. At the same time, the situation presents the possibility of gaining competitive advantage if a company can successfully leverage these vehicles.

Publicis Groupe's Zenith agency collects and forecasts data on total marketing spending by type. **Exhibit 10** shows its results for 2019. Total spending on media and marketing services in the United States was estimated at $457.1 billion, with the breakdown on media ($209.8 billion) and marketing services ($247.2 billion).

EXHIBIT 10 Total Spending on Media and Marketing Services

Total Forecasted Spending on Media and Marketing Services

$457.1 billion

Media: $209.8 billion
(46% of total spend)

Spending Breakdown
Internet: 19%
TV: 15%
Radio: 4%
Newspaper: 3%
Magazine: 3%
Outdoor & cinema: 2%

Marketing Services: $247.2 billion
(54% of total spend)

Spending Breakdown
Sales promotion: 19%
Telemarketing: 13%
Direct mail: 10%
Event sponsorship: 9%
Directories: 2%
Public relations: 1%

Source: Adapted from "Ad Age Marketing Fact Pack 2019," December 8, 2018, http://adage.com/d/resources/resources/whitepaper/marketing-fact-pack-2019, accessedAugust 1, 2019.

The largest anticipated year-to-year changes in spending by category were increases on media spending on the internet (+11.5%) and event sponsorships (+7.0%). Zenith also estimated the most significant decreases to be in magazines and newspapers, each down by approximately eight percent. [55]

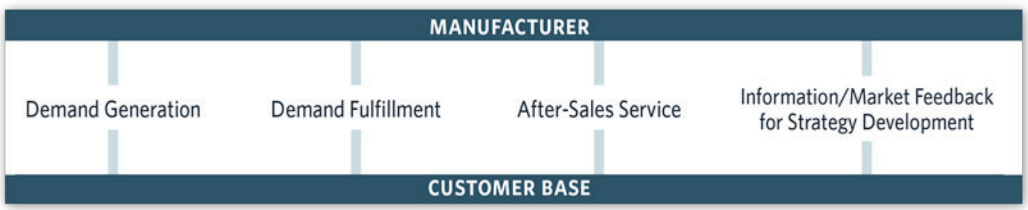
The fifth of the 6 Ms, money, is best addressed with an objective-and-task approach: first, setting your mission and market objectives and then defining the best set of tasks to accomplish them. Some iteration between objectives and spending is usually needed to ensure the plan's economic viability. Spending levels vary widely. Some firms spend well over $1 billion per year in advertising; for example, in 2017, in the United States, Procter & Gamble spent $4.4 billion, Amazon $3.4 billion, General Motors $3.2 billion, American Express $2.4 billion, Walmart $2.3 billion, Walt Disney $1.78 billion, and Capital One $1.59 billion.[56] These absolute numbers are obviously large, but viewing them as a percentage of sales puts them in perspective. For example, P&G's $4.4 billion ad spending represents about 15% of its sales in the United States.[57]

The final of the 6 Ms, measurement of results, should be done against the set objective of the communication plan. For example, if the goal is simply to raise product awareness, then the metrics should measure the increase in the level of product awareness. Behavioral measures, such as whether customers agree to try the product or buy it again, could also be appropriate.

Place Decisions

Place, the third P, refers to *distribution channels*, or where and how an organization decides to go to market. For more detail, see *Core Reading: Developing and Managing Channels of Distribution* (HBP No. 8149). As shown in **Exhibit 11**, a firm typically has to link (directly or through a partner) with its chosen customers to achieve four major tasks: (1) generate demand for a product or service, (2) fulfill that demand by getting the product to the customer, (3) provide after-sales service, and (4) gather and transmit feedback from the customers to the manufacturer.

EXHIBIT 11 Market Channel Tasks



Depending on customer requirements and their own strategies, different organizations place or distribute their products in fundamentally different ways. These choices determine the specific roles of players, their importance in the overall business, and their power to claim a share of the profits generated. For example:

- Gap Inc. describes itself as "an omni-channel retailer, with sales to customers both in stores and online, through company-operated stores and franchise stores…"[58] In 2018, it had 3,194 company-operated stores and 472 franchised stores. It outsources manufacturing, purchasing from 700 suppliers, but manages all aspects of brand development.

- Avon Products generated approximately $5.7 billion in revenue in 2017 by selling through more than 6 million sales representatives worldwide.[59] Selling mostly cosmetics and fragrances, these representatives are independent agents, not employees of Avon, who work part-time buying product from Avon and then selling to customers directly via customized online stores or at in-person gatherings. Avon assists in the demand-generation task by training sales representatives and producing a sales brochure every two to four weeks. Sales representatives receive products from Avon and deliver them to the customer, collecting payment for their own accounts.

- Warby Parker began a "direct to consumer" eyewear business model with only an e-commerce sales strategy initially, featuring "free shipping and free returns, always." It has since added about 100 of its own stores.

- In the United States, in 2018, BMW went to market through partners, with 345 BMW passenger car and sport activity vehicle dealers, 152 BMW motorcycle dealers, 126 MINI dealers, and 36 Rolls-Royce dealers. The dealers and BMW share responsibility for demand generation. BMW designs and implements national advertising. Dealers provide product display and the opportunity for customers to test drive. Dealers fulfill demand by delivering vehicles to customers and providing local after-sales service.

- In 2018, SAP, a German enterprise software company, served a wide variety of customers—more than 437,000 in 180 countries—both directly and through a variety of collaborators, generating €25 billion in revenues. While most business development was driven by its own direct sales organization, it also had 18,000 partners, including original equipment manufacturers, value-added resellers, and distributors.[60]

- Distribution channel assignments can change over time. For example, in 1998, when Starbucks began to market its coffee beans and ground coffee in supermarkets and mass merchants, it entered into a joint venture with Kraft, which assumed the marketing of Starbucks in these stores. After 12 years, citing a desire to better integrate its "at home" and "away from home" target markets, Starbucks terminated its venture with Kraft and undertook the marketing task itself.[a]

Today it is common for companies to reach different customers through different routes. For example, some customers want the convenience of e-commerce, while others wish to "touch and feel" the product before purchase. Thus, Amazon sells its Amazon Echo products on its website, as well as at retailers such as Best Buy, which offers the Echo at its 1,187 large-format and 51 small-format stores, and online at bestbuy.com.[61] Best Buy had customer access that even Amazon could not economically generate for itself. Some customers combine use of both distribution channels: educating themselves at a retail store and then seeking a lower price online.

Note that the economic consequences of a company's choice of place—its distribution channels or partners—can be quite significant. For example, in its fiscal year 2019, Best Buy retained about 23% of the revenues it generated in selling the products of firms ranging from Amazon and Apple to Xerox document scanners, as well as its own private label sales.[62]

When setting go-to-market policy, companies must consider two major areas. The first is the choice of *channel design*. Will the manufacturer pursue a direct or do-it-yourself (DIY) strategy, undertaking all necessary functions? Or will channel partners be involved? If partners are to be involved, what go-to-market

[a] In an example of how difficult it can be to change a channel relationship, Kraft disputed its termination and eventually won a $2.7 billion arbitration award from Starbucks.

role will each one play? The second aspect is *channel management,* which addresses questions such as, What policies and procedures are needed to guide the functions performed by the various actors in the channel? A key issue here is where the channel power will reside. A retailer could simply provide convenient, local availability of a product (e.g., shaving cream at a drugstore). In that case, it would claim only a small percentage of revenues. Alternatively, a retailer could be highly influential in brand choice and thus claim a higher percentage.

A key goal of channel design is to minimize conflicts between partners in a distribution system. Parties' interests can seldom be perfectly aligned; for example, while they all might wish to generate a large "profit pie," each would like a bigger piece for itself. A downstream channel partner, such as Best Buy, may well carry a broad assortment of competitive products to draw customers to the store. That retailer, while wanting to make a sale, may be somewhat indifferent to the specific brand bought, or it might even be pushing its own private-label products, as the larger grocery chains do. For more detail, see *Core Reading: Developing and Managing Channels of Distribution* (HBP No. 8149).

Pricing Decisions

The three elements of the marketing mix discussed to this point—product, promotion, and place—represent an outlay of money from the firm. Effective execution of these activities creates, communicates, and delivers value to potential customers. Price (the final of the four Ps of the marketing mix) has the role of tapping into that value to create revenues for the firm and thus to cover costs and generate a profit.[63]

Getting pricing right is critical because of the highly leveraged effect it has on the bottom line. Consider what it would mean to be able to improve price realization (the revenue obtained from selling a given bundle of goods) by 1%. For example, Siemens, the German technology company, generated €83 billion in sales in 2018, generating €6.1 billion in net income.[64] A 1% improvement in "price realization" would yield an additional €0.83 in net income improving it by 14%. Looking at the *Fortune* 500 firms as a whole, a 1% price realization improvement produces about a 12% bottom-line improvement.

A complete pricing program has many components. The first is the pricing mechanism itself. Auctions, in which the price is determined by potential buyers' expression of their willingness to pay, used to be restricted to a fairly small set of products, such as thoroughbred horses, fine artwork, and distressed real estate. However, information technology advances have made auctions much more widespread. An eBay seller, for example, has to decide between using an auction mechanism and setting a buy-it-now price. Google Ads pricing is set via a cost-per-click-based auction, in which a potential advertiser specifies the maximum cost per click it is willing to pay. Google then serves up advertisements considering these bids and the relevance to the customer's search. For more details, see *Core Reading: Digital Marketing* (HBP No. 8224).

Still, the most common pricing mechanism is the posted price, where the supplier of the good states a price. In some cases, it is a take-it-or-leave-it proposition, for example, $6.00 for the *Sunday New York Times* at the newsstand, $750 for the Ferragamo Pellas shoes at Zappos, or $228 for a nonstop JetBlue flight from West Palm Beach, Florida, to Boston at 7 a.m. on an upcoming Sunday morning. Other times, the posted price is the starting place for a negotiation. Posted prices can also be fairly stable (such as the price for the *New York Times*), or they can be dynamic (JetBlue, for example, varies the price for a given flight over time, based on observed bookings).

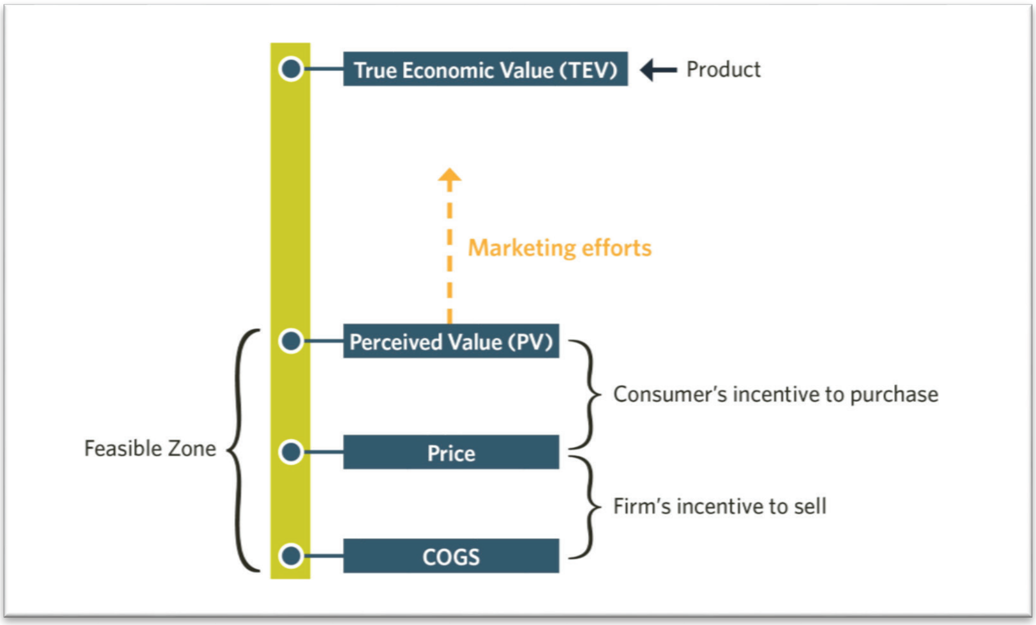
While the price itself is most central, the terms and conditions are also critical. For example, many firms offer quantity discounts where the price varies with the number of units purchased—either in the given order or accumulated over a time period.

The three points to consider for an effective pricing program are (1) the value of the product to the customer (rather than the firm's cost of goods being the major pricing determinant), (2) opportunities to vary price across customers according to the value they individually place on the item, and (3) customers' price sensitivity. We look at each of these next.

The Value-Based Approach

Exhibit 12 summarizes the important inputs to the pricing decision. The key element in the exhibit is the *perceived value* (PV) that the customer places on the item. This establishes an upper bound on what the customer is willing to pay. It is a function of the firm's offering and the price and features of competitors' offerings that are known to the customer.

EXHIBIT 12 Key Inputs to the Pricing Decision



As shown at the bottom of Exhibit 12, the firm's cost (cost of goods sold [COGS]) is generally a lower bound to the price. Sometimes, however, a firm may sell below cost to spur some trials and adoptions, with the belief that this will increase the perceived value and lead to greater pricing flexibility in the future.

Assessing perceived value (PV) can be done in a number of ways. A common and useful approach is to break down the value into its two components, as shown in **Exhibit 13**.

EXHIBIT 13 Calculating True Economic Value

The calculation of *true economic value* (TEV) must take place relative to the next-best alternative as seen by the customer. This is because a sale will be generated only if the product's value outweighs price when compared with all competing products or services. Competing products may be very similar to one another (e.g., golf balls from Bridgestone, Calloway, or Titleist), or they may be quite different, as in the competing services for a Delta Shuttle flight from New York to Boston. Such services could include the very similar service from American Airlines, but also Amtrak's Acela train service, regular train service, a luxury bus coach, a low-cost bus, and a car rental. Particularly in industrial and manufacturing situations, where the buyer's cost structure can be more closely estimated, this economic value equation can be very helpful.

An alternative to this way of assessing perceived value is to conduct market research on potential customers' willingness to pay, using straightforward questioning or more advanced techniques.

Price Customization[65]

Some products are sold under a *uniform pricing policy*, meaning the price is the same at all times for all customers. However, many firms have seen the benefit of customizing the price to better capture the value created which varies across customers.

For example, The Walt Disney Company has a variety of customized pricing models for its amusement parks, covering a wide variety of customer profiles. One insight is that Florida residents may view a trip to Walt Disney World in Orlando, Florida, differently than a family traveling from afar for a "once in a lifetime" experience. Perhaps Florida residents would be more price sensitive and increase the frequency of resort visits if the price were lower. Thus, for those able to document Florida residency, Disney offers a three-day pass at a 30% discount from the regular price.[66]

With four different theme parks at Disney World (Magic Kingdom, Epcot, Disney's Hollywood Studios, and Disney's Animal Kingdom), Disney also varies the price of park access per day based on the total number of days purchased on a given ticket. A one-day ticket for admission on July 25, 2019, cost $109; a four-day ticket offered only a modest $3 per day discount being priced at $424.40; however a six-day pass was priced at only $444.45, offering two additional days at an incremental cost of only $20.[67]

Finally, Disney offers not just a single item in its product line, but a product line with a trade-up option. The basic ticket restricts the holder to only one park per day. For an additional $60, one could add a "Park Hopper Option," granting admission to multiple parks on a given day.[68] Thus, Disney is an example of three types of price customization, generally practiced:

1. *Pricing based on buyer characteristics.* The key here is to find an observable characteristic of buyers that sorts the buying population

into groups based on higher and lower willingness to pay. A common tactic here is age, where older customers are deemed less able to pay and are offered a senior-citizen discount. Children also frequently receive kids' discounts. Pricing can also be valued by institution type, so that corporate accounts or educational institutions might be charged at different rates.

2. *Pricing based on transaction characteristics*. Tickets that are booked in advance for an event are often priced lower than "day of sale" tickets. Quantity and volume discounts are common, e.g., a retailer taking 15% off the price for a case purchase of wine.

3. *Pricing based on product line variations.* The *product line sort* is a strategy where a variety of products are offered and price-sensitive customers select the "base" model, while performance-sensitive customers with a higher willingness to pay select the "upgraded" model. This is common in the automobile industry. For example, Audi offers its base sedan in two models: the Audi A3 and the S3. The A3 has a manufacturer's suggested retail price starting at $33,000. It has a two-liter, four-cylinder engine with 184 horsepower at 5,200 RPMs. The Audi S3 is a sport model starting at $44,500, offering 288 horsepower at 6,200 RPM's and design features to "provide athletic appeal" and its "S model quad exhaust outlets put the finishing touch on its performance aesthetic."[69]

Price customization can be a powerful tool. Consider the simple hypothetical example shown in **Exhibit 14.** A video game producer is bringing out a new version (4.0) of a popular game. The producer first tests out a uniform pricing model, charging new and current users the same price. The market research captures the customers' "willingness to pay" (see the first column in Exhibit 14). In these results, 10% of the population is willing to pay $100, an additional 20% is willing to pay $95, an additional 20% will pay $70, and so on. Assuming a marginal cost of the game is zero, the contribution-maximizing price under a uniform policy would be $70, with 50% of the market buying at that price.

EXHIBIT 14 Willingness to Pay for Video Game Version 4.0: Uniform versus Custom Pricing

Uniform Pricing Model

Customer Willingness to Pay

All Customers
$100
$95
$95
$70
$70
$50
$40
$40
$20
$10

Optimal price = **$70**
Quantity sold = **5**
Total contribution = $350

Custom Pricing Model

Customer Willingness to Pay

New Buyers	***Upgraders***
$100	**$70**
$95	**$40**
$95	**$40**
$70	$20
$50	$10

New Buyers	Upgraders
Optimal price = **$95**	Optimal price = **$40**
Quantity sold = **3**	Quantity sold = **3**
Contribution = **$285**	Contribution = **$120**

Total contribution = $405

Now, suppose the firm was able to sort the potential buyers into two groups: new buyers and upgraders (those currently playing version 3 of the game). New buyers do not have the option of just continuing to play version 3, so as a whole, their willingness to pay was somewhat higher, as shown in Exhibit 14, where the 10 values on the left-hand side are now sorted by "new buyers" and "upgraders." With the opportunity to charge different prices to these two groups, the optimal customized price policy would now be $95 for new customers and $40 for upgraders. This would yield a contribution of $405, a 15% improvement over the best uniform price.

Price Sensitivity

A third factor in setting prices is determining just how price-sensitive a customer is in a given circumstance. One way to do this is with market research, but a business can also use the guidelines that follow to make handy predictions about the price sensitivity of its customers. A customer's price sensitivity increases (and a business's pricing latitude decreases) in the following circumstances:

1. When the end user, rather than a third party, bears the cost. For example, until recently, pharmaceutical manufacturers have had greater pricing latitude because neither the prescriber nor the patient bore most of the costs.

2 When the cost of the item represents a substantial percentage of a customer's total expenditure.

3 When the buyer is not the end user but rather sells their end product in a competitive market. It is worth noting that price pressure from further down a distribution channel ripples back through the chain. For example, one steel producer was able to obtain better margins by selling a component to buyers who produced specialty items, rather than to those who sold to commodity markets; the latter was much more price sensitive.

4 When buyers are able to judge quality without using price as an indicator. However, in some product categories, such as perfume, where judging quality is subjective, price sometimes has little impact on determinations of quality because customers often use price as an indicator of quality.

5 When customers can easily shop around and assess the relative performance and price of alternative products. Today, advances in information technology have enabled customers to increase their awareness of prices and their access to alternative options through comparison-shopping engines such as Google Shopping or PriceGrabber.

6 When there is no urgency to make a decision and thus the customer can take the time to locate and assess alternatives.

7 When buyers can switch from one supplier to another without incurring additional costs. In January 2014, T-Mobile, which confronted *buyer stickiness* due to termination fees from other cell phone service providers, offered to pay up to $350 per line for termination fees when a customer switched from other cell phone service providers.[70]

Finally, regarding the competitive situation, a company's pricing latitude decreases to the degree that (1) there is limited difference between the performance of its product and others in the category, and (2) a long-term relationship with the company and its reputation are not important, so the customer's focus is on minimizing the cost of this particular transaction. For more on the value of brand and the impact of brand loyalty on pricing, see *Core Reading: Brands and Brand Equity* (HBP No. 8140).

In addition to these customer issues, effective pricing considers competitors' potential reactions. As shown earlier in Exhibit 12, the true economic value that a customer ascribes to a firm's offering is a function of the competitor's price.

Thus, considered pricing actions need to take into account competitive reactions.

2.5 Conclusion

At the beginning of the reading, we set out three purposes of marketing:

1. Acquiring customers
2. Retaining customers
3. Incenting customers to be your brand ambassador in this connected digital world

Different marketing actions may be required for each of these purposes. For example, Levitt presents the customer-retention challenge in this way:

> The fact of buying changes the buyer. He expects the seller to remember the purchase as having been a favor bestowed on him by the buyer, not as something earned by the seller. Hence, it is wrong to assume that to have gained an account gives you an advantage by virtue of having gotten "a foot in the door." The opposite is increasingly the case. . . . The natural tendency of relationships, whether in marriage or in business, is entropy—the erosion or deterioration of sensitivity and attentiveness. . . . A healthy relationship requires a conscious and constant fight against the forces of entropy.[71]

Thus, the same marketing actions that *create* a customer might not necessarily help to *keep* that customer.

Some firms have distinguished themselves in their superior ability to retain loyal customers. The Walt Disney Company has fostered relationships to create loyalty so well that it has offered a course for other companies entitled "The Disney Approach to Brand Loyalty." Many companies now use a "net promoter score," tracking the percent of customers rating the company at the top end of the range, believing these customers will promote the brand to others.

Acquiring customers, retaining them, and enlisting them as brand ambassadors require a cohesive marketing plan based on proven analytical approaches for decision making. In this overview of the marketing process, we have set out a comprehensive framework for understanding the major marketing issues and the process by which to successfully address them in a marketing strategy.

3 KEY TERMS

buyer stickiness Resistance of customers to switching easily between one supplier of a good or service to another.

churn This is a measure of customer attrition. The churn rate is 100% minus the customer retention percentage rate, which typically measures customers who discontinue a service or subscription within a specified time period.

coolhunting Observing and predicting the emergence of and changes in cultural trends, visible in clothing fashions, popular music, urban lifestyles, uses of technology, etc.

distribution channels The network of individuals and organizations involved in the process of moving a product or service from the producer to the end user.

positioning (1) Defining a value proposition for the target segments. (2) Differentiating a product or service (or its brand) from others in the perception of customers.

product line Group of products manufactured by a firm that are closely related in use and in production and marketing requirements.

pull strategy A pull strategy involves motivating customers to seek out your brand in an active process via tactics such as advertising, customer relationship management (CRM), and sales promotions.

push strategy A push strategy involves ensuring the customer is aware of your brand at the point of purchase via tactics such as direct selling to customers in showrooms, packaging designs, or point-of-sale displays.

segmentation A marketing planning process that involves dividing a broad target market into subsets or groups of customers who have common needs or characteristics.

targeting Selecting the potential customer segments to whom a company wishes to sell products or services, after an analysis of each segment's attractiveness.

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