“Hypercompetition, customer-value competition, and the new role of market research”

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Hypercompetition, customer-value competition, and the new role of market research

Abstract

Based on findings from a large-scale research project, this article discusses customer-value competition and presents approaches to tackling the increasingly competitive environment. The study entailed an in-depth analysis of questionnaires completed by over 300 senior executives in Germany, Austria and Switzerland. Its origins lie in Richard D’Aveni’s concept ‘hypercompetition’. Against this background of rapid innovation, higher quality demands and considerable pressure on prices, the researchers focused on examining companies with regard to three central questions: What are the top executives’ assessments of the current and future market and competitive situation? What do they consider to be the key challenges with regard to successfully confronting the market dynamics of the future? How successful are the companies studied at facing these challenges today and which strategic thought patterns guide them in this task? The answers to these questions provide an excellent framework with which companies can develop business strategies that will see them out of the global economic crisis and into the future.

Keywords: hypercompetition, customer value, market research, innovation.

Introduction

Richard D’Aveni’s concept of hypercompetition argues that globalization, deregulation and privatization will dramatically change competitive dynamics. Technologies and offerings are so new that standards and rules are in flux; competitive advantages are compensated for by competitors increasingly quickly and, thus, cannot be sustained (D’Aveni, 1994; D’Aveni, 1995). A price-quality competition develops which leads to companies’ constantly having to innovate and increase quality, often whilst under pressure to reduce prices at the same time. Furthermore, the more intense the competition, the more transparent the markets and the lower the switching barriers for customers, the more important it is to persuade customers of the value of a product or service – that is, of the customer value (Bailom et al., 2007).

The value attributed to a product or service by the customer is the result of two factors, perceived quality and the price (Gale, 1994). This relationship is illustrated graphically in figure 1.

Here, one can see the zones of different customer value. The straight line represents equilibrium, where the price-quality ratio is in balance (i.e. the customer is getting exactly what he or she pays for). To the right of the straight line, a product or service offers high quality at a relatively low price; contrarily, to the left of the line the price is too high in relation to quality. If a company wishes to win market share (Company A in Fig. 1), it can achieve this by improving quality or reducing prices. The competitor positioned immediately next to it (Company B) will be forced to follow suit, triggering a chain reaction in the entire market. As a result, the equilibrium line shifts to the right. As the graph indicates, a company must now accept a lower price point for the same level of quality, or maintain the original price point but give the customer a higher quality product – either way, profitability is at risk and customers’ bargaining power is amplified.

The intensified competition and increasing difficulty to turn any substantial profits have many companies moving in a downward spiral. Over-capacity, fewer opportunities for differentiation with lasting effect, and growing market transparency have all contributed to this phenomenon. Customers have turned into well-informed, merciless buyers, and senior executives are feeling the effects.

Hypercompetition and other market dynamics discussed heretofore are patterns that have existed for quite some time, in almost every market. However, the sheer speed at which these trends are moving is the source of unparalleled and overwhelming pressure – to merely keep up with the velocity of change is the real challenge companies face today.

To make matters worse, the pressure on businesses has multiplied as a result of the current economic crisis. It is easy for senior executives to forget about the future of the company in order to focus their

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efforts on surviving from one day to the next. Consequently, it is imperative to discuss which strategic challenges decision-makers consider crucial to overcome in order to stay afloat in this competitive dynamic and survive in the long term.

1. Customer Value Competition in a Hypercompetitive Market

The study discussed in this article is based on an analysis of the responses to a questionnaire sent to executives in a cross-sectional study in Austria, Germany and Switzerland. 371 usable responses were obtained, covering a wide variety of industries (61.1% services, 25% manufacturing, 7.4% healthcare, 7% retailers) and company sizes (41.6% < 100 employees, 27.8% 100-100 employees, 30.6% > 1.000 employees).

Of those interviewed, 27 percent said that over the past three years, prices remain unchanged but consumers’ expected level of quality has increased; worse still, over 30 percent of the companies have had to accept price decreases for their products or services despite higher quality (see Figure 2).

For individual suppliers this means that continuously improving customer value will become a prerequisite for succeeding in this competitive environment. According to the study, only a mere 14 percent of companies have managed to innovate and demand higher prices. But this begs the question, Are these companies also financially successful? As it turns out, over 56 percent of them were more profitable than the industry average, almost 40 percent were averagely profitable, and only the few remaining ranked lower. Thus, such companies not only performed better with regard to quality improvements and price increases, but they were also considerably more profitable. Henceforth, these exceptional companies will be termed “innovators” and the rest “optimizers”. So what strategic differences separate the innovators from the optimizers?

The majority of senior executives interviewed were of the opinion that the future success of a company ultimately depends on the extent to which it can achieve the following (see Figure 3):

- modify and reduce cost structures so as to outweigh the substantial challenges presented by price competition;
- strengthen the commitment of its employees and thereby exploit their true potential in order to make the firm flexible, innovative and powerful at the international level;
- continue to increase customer orientation in spite of enormous pressure on prices; and
- successfully introduce innovations to the market on an ongoing basis.

![Fig. 2. Changes in quality and price (3 years’ period)](image1)

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![Fig. 3. Key priorities of top performers](image2)

Analyzing these corporate objectives provides deeper insight into the strategic thought patterns of decision-makers, since it revealed that over 80 percent of the companies – the optimizers – seek survival via improving existing processes. In doing so, senior executives allow themselves to be heavily influenced by the paradigm of cost-reduction. Thus, making business processes even more efficient by means of IT and the like, exploiting the potential of employees to realize further cost savings, and developing products with as little investment as possible are strategies of primary importance to the optimizers. This group puts considerably less emphasis on strategically realigning the company through radical process changes and successfully introducing innovations. In fact, very few optimizers believe it is even possible to further differentiate themselves from the competition through new, unique products and services or extraordinarily streamlined business processes.

On the contrary, the remaining 14 percent, the innovators, put their faith in the development of “radical”, market-changing innovations in products and processes. They are fundamentally driven by differentiation, pure and simple. And, while cost-optimization is still a consideration for the innovators, it is not, however, the driving force behind their business strategy.

Thus the question becomes, How successful is each group in doing what they set out to do? The results
of the study illustrate that, when compared internationally, most of the optimizers have not succeeded in improving their cost structures with lasting effect. This is quite remarkable given that 75 percent of all managers interviewed indicated that they had implemented cost-reduction programs in the last few years. These programs focused primarily on the more common courses of action, such as overhead-value analysis and process-cost analysis based on the value-chain concept.

Still, the optimizers made little progress in the very area where they place the most importance. The cost situation of the optimizer group has developed as follows:

- only 34 percent of companies managed to achieve a sustained reduction in relative costs;
- thirty percent of the companies indicated that they had held costs at roughly the same level;
- costs had continued to rise at 26 percent of the companies.

These findings demonstrate that operational excellence and cost-optimization continue to be key issues, even when they are at the very core of a company’s strategy. At the same time, however, it is clear that, when viewed overall, measures whose scope is limited to optimizing processes and costs are not nearly sufficient to ensure success in today’s competitive environment. In fact, at almost 65 percent of companies interviewed, the cost-reduction programs they carried out have resulted in no improvement or only short-term improvements in their competitive position.

There is no question that exploiting the potential of employees also plays a key role in helping companies cope with the challenges they face, as illustrated by the high strategic significance the senior executives interviewed placed on employee commitment. According to their perspective, employee commitment has a decisive influence on the success of both innovations and cost-reduction programs. Eighty percent of the decision-makers see employees’ commitment to company objectives as the central success factor in achieving sustained cost-reduction. Interestingly, however, senior executives in the group of optimizers work on the assumption that, on average, approximately 60 percent of employees are fully committed to the company; in the case of the innovators, the figure is over 70 percent.

In this context, the findings show that the optimizer companies are seemingly still failing to implement concepts which increase employee commitment over the long term, despite decision-makers’ awareness of this problem. A major reason for this could be that in many cases employees cannot identify with their employer company, either in terms of what it does (products/services) or on an emotional level (relationships with colleagues/managers). Often, employees seem to have lost sight of the purpose or vision of their company and what it does, and therefore tend to lose their “inner motivation” along with it. Accordingly, they lack the sense of fulfillment that comes with making worthy contributions. Furthermore, these employees do not experience any personal development within the context of the working environment, which creates circumstances hardly conducive to enhancing motivation and commitment. Senior executives must create some element of intrinsic value for their employees; if this is not achieved, companies have little chance to retain highly qualified, committed employees who will work to their utmost potential and benefit the firm in the best way possible.

In the last few years, the majority of optimizer firms have restructured their customer orientation strategy, and some have made large investments in doing so. Yet, in numerous cases, this has only led to modest successes in the area. Despite their efforts, many of the companies could not raise customer loyalty or the number of new customers. Because such a large number of companies fail to systematically strengthen customer and market orientation in their organizations, it is no wonder that 50 percent of senior executives pinpoint improving this focal area as a key strategic challenge their companies face.

Particularly in the last few years, managers have had to learn from unfortunate experience that the much-praised customer-relationship management (CRM) systems have made the way a company attends to customers neither more effective nor more efficient. The study shows that most of these companies neglected to develop innovative strategies for CRM and market development. Knowledge of the criteria which drive customers’ purchasing decisions is a central, basic prerequisite for developing successful customer-relationship strategies. However, research findings suggest that many optimizers lack the essential information about purchase decision-making criteria because they did not use adequate methods in their customer analysis. Often, customers’ true problems are not accurately identified and transferred into product-service bundles that deliver value. Furthermore, deficiencies exist in the permanent performance measurement systems on which companies usually base strategic decisions regarding CRM and market development.

The study shows that, at present, only a few managers in the optimizer group are prepared or willing to make larger-than-average investments in the innovative strength of their company. The innovation management practices of these senior executives are focused primarily on improving existing products, building relationships with new customers, and developing new markets.
Nonetheless, almost 70 percent of the decision-makers believe that very few companies succeed in differentiating themselves from competitors through product innovation.

Hence, in many industries, gearing the innovation process toward the improvement of existing products leads to homogenization, and companies’ room to maneuver becomes smaller and smaller. Senior executives and employees often spend more time grappling with the competition situation than with the question of how they could create real added value for consumers and other business partners by means of innovations. As a result, true innovations frequently fail to materialize or to meet market requirements and customer needs.

Now, let us take a closer look at the innovators. The analysis of this group essentially leads to the following conclusions: Unlike the optimizer group, the innovators have been remarkably successful at radically changing the industry. In several instances they actually managed to achieve higher prices in the market by introducing new, unique products or to carve out clear advantages for themselves in terms of value creation and competitive advantage through radically changed business models.

Fundamentally, the cause of such accomplishments is that the innovators actively want to change the market. They place particular emphasis on making sure they understand the market and their customers’ expectations, as they want to develop tomorrow’s solutions for existing and potential customers. Moreover, they are considerably more successful than the optimizers at exploiting the potential of their employees. Perhaps the most impressive finding is that these companies not only possess advantages in terms of product innovation and employee commitment, but they have also dramatically improved their cost structure over the recent years. This is due, on the one hand, to the fact that they are far more radical when it comes to critically assessing and changing existing processes and do not merely optimize them; on the other hand, they already start thinking about how the processes behind new products and service can be made more efficient at the development stage, thereby securing a favorable cost position for themselves in the process. The innovators will enjoy a sustainable and profitable future because of their killer combination of skills – that is, they can successfully bring new and innovative products to market and effectively reduce their cost structures.

2. The new role of market research

The innovators also have a masterful understanding of the new role of market research. Peter Lorange (Lorange, 2005) calls on marketing departments to accept the challenge of really identifying new market opportunities before they become obvious, and this is exactly what the innovator group has been able to do. In doing so, these companies have actively shaped the market as opposed to running behind it. To achieve this, the marketing department in particular must be led by visionary thinking and not allow itself to be guided by a copycat mentality. There are many aspects of this marketing approach that are of key importance.

First, it is vital that companies orientate themselves toward customers’ real problems and latent needs. The difficulty of convincing customers of the value of new solutions and developments is shown in studies which prove that less than 10 percent of all new or further developments actually win customers’ favor (Christensen et al., 2005). Frequently, the seemingly ingenious ideas that firms develop or communicate simply do not correspond to the real needs of the market. These results are likely to occur because companies primarily orientate themselves toward the desires and needs that customers articulate in market research. However, oftentimes these statements merely reflect what is already generally known. Thus, it is not possible to derive successful developments from such results. Instead, the process must involve recognizing unconscious needs and relevant problems.

When conducting market research, it is essential to interview the right groups of customers – the trendsetters and early adopters. The basic premise of classic quantitative market research is that the group interviewed must be a representative sample of the population. This is comprehensible, since only then can the results of the sample be carried over to the population. However, when it comes to innovations, this creates a problem. Not all customers are equally innovative; some react more quickly to an innovation, while others need a long time until they are prepared to buy the novel product. In his book Diffusion of Innovations, E.M. Rogers (Rogers, 1962) discusses a curve resembling a Gaussian distribution that reflects customers’ propensity to innovate. The trendsetters (approximately 2.5 percent) are adventurous and prepared to take risks. Early adopters accept new ideas early but are more cautious; they are also frequently the opinion leaders. One can observe this distribution for almost any innovation. Take, for example, the carving ski, mobile telephone or the snowboard – not all consumers reacted to these innovations with the same speed. In fact, some need years before they take an interest in a particular product. Consequently, quantitative, representative market research studies cannot really help in the innovation process. Rather, if one tries to interview a representative cross-section of customers about desires or tries to test the potential of an innovation on them, the results will likely be misleading.
Discussion platforms within the company are also a crucial element to innovative marketing and product development (Bailom et al., 2007). They allow the firm to process and exploit the input gathered on a cross-functional level. There is no doubt that generating the “right” information from the markets is central to innovative success, but it is just as imperative to interpret this information in terms of the company’s circumstances and market position as a whole and to derive effective decisions from it. This interpretation should not take place in isolation in marketing departments. Instead, marketing teams must take advantage of the knowledge and experience of various individuals from different functional areas. Usually, only open and critical dialogue about the gathered information will open up the chance to obtain company-specific ideas for innovative leaps. This simultaneously removes the tendencies for silo thinking, thereby creating a sense of a common goal or mission across all functional areas. It is important to note, however, that a prerequisite for these discussion platforms is that top decision-makers themselves participate and engage in the process. This allows the discussions to gain vital strategic importance for the group and gives rise to fundamental decisions about the company’s positioning in the market.

In addition, top decision-makers must themselves be market (research) experts. Understanding the market is not solely the job of the marketing department. In order for executives and top managers to assume their central role in the discussion platforms, they must possess an extensive command of market logic and of customers’ problems. This is the only way they will be able to effectively evaluate the discussions at hand and push the process forward in a solution-oriented way, especially during phases of conflict which continually arise between functions. Thus, top decision-makers must invest a considerable amount of time in direct contact with customers, distribution partners, and other market players.

Innovative success requires top decision-makers to drive forward the propensity to experiment and take risks. This is the only way that companies will be able to actually test their ideas in the market and learn important lessons from them; in other words, as someone once said, it is better to “make mistakes more often in order to learn more quickly”. The key to this is the willingness to systematically learn and to view mistakes that arise as a necessary part of this process. If employees are afraid of any kind of failure, however, they will continually hide behind endless data analyses and never move the market. Nestlé’s experience with the yogurt product LC1 illustrates this approach. Nestlé initially launched LC1 in France as a new yogurt, focusing its marketing message on a new, central product attribute – “helps the body to protect itself”. However, customers did not want a “medical” product. Rather, they wanted a healthy product that tasted great. The “failure” in France made it necessary for the core feature of the product – being good for the health – to be marketed differently. Nestlé’s top management allowed the same team that had made the “mistake” to learn from it. Because of the initial marketing failure, the company was able to successfully launch LC1 in Germany and other international markets on the basis of what it had learned in France.

Finally, it is of utmost importance to understand the innovators’ behavior in the context of the current economic crisis, or in any such market failure for that matter. At present the rules of the market are in complete upheaval, and most companies are merely trying to survive from one day to the next. In such circumstances, it is easy for senior executives to throw out all strategies that focus on the long-term and replace them with short-term survival tactics. The innovators, however, always take the future into consideration. Top managers of these companies
realize that surpassing the competitor and being a winner after the crisis require more than riding out the storm. Instead, they find ways to continue to innovate no matter how difficult it may be. They know that innovation is the key to moving successfully into the future, and thus make it a priority in all their strategic decision-making. Furthermore, economic crises and quickly changing markets open up countless new opportunities and present a perfect time to seize them. While the optimizers focus on their daily struggles and leave the ‘future in the future’, they miss these opportunities and leave them for the innovators to exploit. In their recent article, David Rhodes and Daniel Stelter (Rhodes and Stelter, 2009) offer advice on maintaining innovation strategies even during poor economic times:

*Investments made today in areas such as product development and information or production technology will, in many cases, bear fruit only after the recession is past. Waiting to move forward with such investments [however] may compromise your ability to capitalize on opportunities when the economy rebounds.*

Thus, it is of dire importance for companies to keep the long-term health and competitiveness of the company in mind at all times. The key is to make the right decisions today that bring success tomorrow.

**Conclusion**

If one follows Joseph Schumpeter’s conclusions, a prerequisite for the emergence of value is essentially “creative destruction” (Schumpeter, 1987). This concept describes the endless cycle of innovation which results in established goods, services, or organizations being replaced by new models. While this insight is not entirely new, the growing awareness that, in many industries and companies, changing systems is more critical and effective than merely improving them arguably is. The results of the study, however, show that far more companies are placing emphasis on maintaining existing processes than on creatively developing new ones. This is what sets the innovators, the top companies, apart from the rest. As most companies strive for continuous improvement and still concentrate heavily on process and cost optimization, increasing efficiency becomes the highest goal. But, in choosing this goal, companies generally have to accept price reductions even though they must continually increase the quality of their products and services. Furthermore, these are, for the most part, purely defensive measures. Numerous empirical studies show that there is hardly any correlation between measures such as downsizing and outsourcing and sustained corporate success (Kieser, 2002) – historically, there are few examples of companies which became great through shrinking.

As has always been the case with entrepreneurial activities, visionary thinking, the courage to make radical innovations, as well as systematic customer and market orientation are necessary for building sustained competitive advantage. Moreover, the potential of employees can be fully realized by creating an environment in which they can further develop their skills whilst feeling committed and enthusiastic with regard to the company’s goals and their own personal goals. The innovators have mastered all of these abilities and do not lose sight of them in the face of economic crises. They always have the future in mind and therefore continue to reap the rewards of enduring success.

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