FINDING NEW MARKETS

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JANUARY 17, 2006

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Introduction

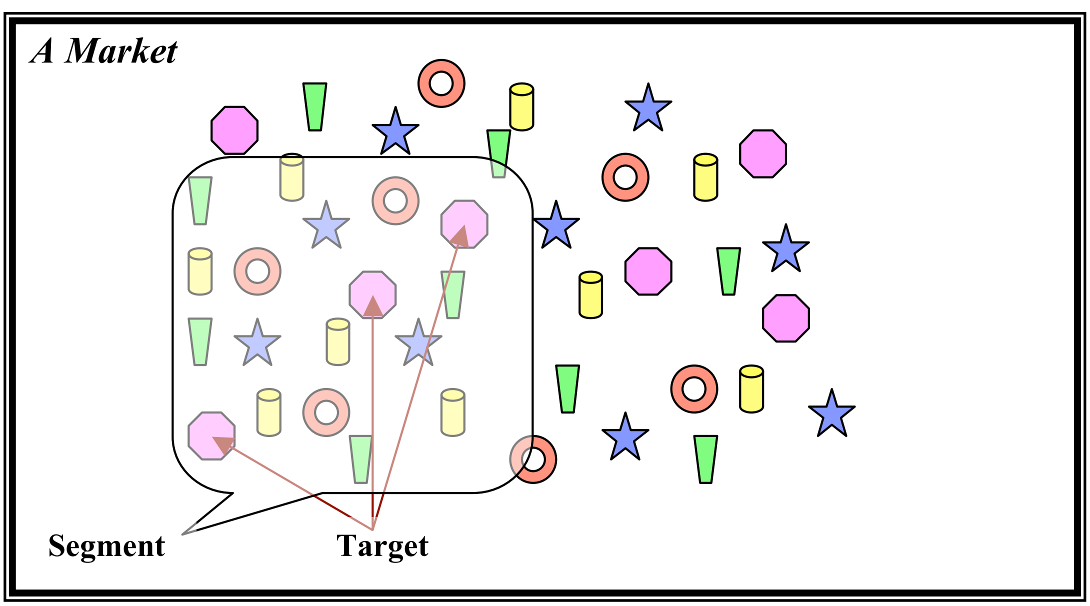
Our August newsletter report, *Fundamentals of Marketing*, introduced the reader to the overall discussion of how to manage markets, products, channels and marketing programs. It was kind of the "everything you ever wanted to know, but were afraid to ask," version of marketing, in twelve pages. There are two additional marketing processes for which organizations often seek more information - the process of finding new markets for existing products and the process of developing successful new products. This article introduces the reader to the basics of how to identify new markets. The new product development process will be addressed in a future newsletter article.

Background

Over the years it has been common to hear individuals use the terms "markets" and "products" interchangeably. Yet markets are groups of people while products are bundles of benefits, usually goods or services. Thus the process of finding new markets is solely about finding more or different people who might buy your product. From our previous article you may remember that a market is defined as people with:

- Needs to satisfy,
- Money and ability to spend,
- Willingness to spend

Also, we noted that a good market is one that is accessible, of sufficient size, unique in some way, and likely to respond to your marketing efforts. As a reminder, the image below demonstrates the market segmentation and targeting process.



What is the first step in finding new markets?

It comes as a surprise to many that there are a number of steps that must be taken internally prior to looking around externally for new customers. The basic approach we recommend is for a company to ask itself:

- What products do we make money on?
- What products would we make money on if we sold more of them?
- What products do we like to sell?
- Who is our favorite customer and why?
- What do we do well?
- What do our current customers think we do well, and which things are important to them?

Once you have answered these questions, you have a profile of the kind of new customer you would like to have and the products and product features you might offer them. Once this is known, you can begin the process of deciding where to look!

What Products do we make money on?
This seems obvious once you think about it, but it is also really common for businesses to NOT know which products are their most or least profitable. This ignorance usually results from the fact that many firms evaluate profits in total, rather than by individual product groupings. Total profit margins can seriously decrease when a company dominantly or even modestly expands in less profitable products. Without careful planning, organizations can accidentally "succeed" at selling more stuff they don't make money on in new markets, and end up competing solely on price. Alternately, expanding the most profitable product lines can have significantly positive impacts on total profit margins. In our September commentary "*What would a caveman tell today's wood industry*" we pointed out that even a small percentage of additional sales in very profitable products has a huge impact on total profitability. Careful internal analysis is required to understand not only which products make the most money, but also *why* they are the most profitable. Are they profitable because they are the cheapest to produce, because customers are willing to pay more for them, or perhaps because your company is uniquely qualified to make them?

What products would we make money on if we sold more of them?
A slight variation on the previous question brings into consideration the issue of volume. In general, it has been our experience that companies completely understand the concept that an increase in volume of sales can cause efficiencies in operating and provide purchasing power with vendors. The caveat here is to recognize that volume based activities have what are called *optimum sales-operational points*. That is, if you plot the volume of sales versus expenses it is generally not a straight line but rather one with waves (ups and downs). In some cases, this volume/sales graph actually appears as a frequency or sine wave. This results from the fact that volume based sales increase in profitability as sales increase, dependent on a given set of expenses. At some point though, you need to add a forklift, or more storage, or a service person. When these expenses are added the organization's net profitability often goes down at least

temporarily. Thus it is really valuable to know where your firm currently is on the profitability curve for each product. A company should also identify points where profits are optimized, where additional expenses are necessary, and, specifically where an increase in the volume of sales would really help the profits of a particular product line (e.g. to better utilize some special equipment or personnel).

What products do we like to sell?

Companies are often surprised by this question. A common response is "what has our liking it got to do with it? It's the customer's opinion that matters!" The answer is that, sure, the customer's opinion absolutely rules. However, the combination of finding products that your customer really likes to buy and that the firm really likes to sell can be a winning combination. For example, I've often thought that all Porsche salespeople ought to be teenage boys. They have memorized every detail about the cars and have boundless enthusiasm for them – even when they may have never even driven one. This kind of enthusiasm can result in higher profitability. The idea is to harness the energy that comes with personal interest and apply it to your business. Cirrus, one of the most successful small private airplane manufacturers today, and Google are great examples of this approach. These firms specifically hire people that love, not just like, their respective product lines in the belief that those who feel passion for the products they sell would translate to enthusiastic customers and company growth.

Google's seven key principles to make knowledge workers most effective.

- Hire by committee.
- Cater to their every need.
- Pack them in.
- Make coordination easy.
- Eat your own dog food.
- Encourage creativity.
- Strive to reach consensus.
- Don't be evil.
- Data drive decisions.
- Communicate effectively.

http://www.msnbc.msn.com/id/10296177/site/newsweek/

When trying to figure out what products you like to sell it is very valuable to ask all levels of the company. A top selling product favored by company executives may provide an ongoing headache for those on the production floor and a drain on company creativity and energy. It is important to get broad input and to clearly understand discrepancies in views of various products and product lines.

Who is our favorite customer and why?

If a company only asks staff one question about current practices, this is the most important one. It is critical to the success and growth of a company that they understand the customer they enjoy doing business with and why. *The response to this question tells you a tremendous amount about your own firm and the people in it.*

There are countless examples of companies that are struggling with an account and service is poor, quality is poor, damage is occurring, and when you ask company staff about their favorite accounts, the description is usually very different in style from the one they are having problems with. Now you might say, "that is because they are having problems." But alternately, the answer also is often, "that is why you are having problems." What you get sometimes is a mismatch in values. The person providing the product values it differently than the person purchasing the product. When an organization broadly defines whom they like to do business with they get a better picture of themselves. This self-awareness is critically important when trying to expand because this is the opportunity to take a core identity and create growth based on that. Lots of firms have grown organically over the years, basically taking whatever business came across their bows with little consideration of what they liked and disliked. It was dominantly about survival. But growth and finding new markets can be a different matter, and can positively affect the company in ways well beyond increased revenues.

In evaluating what you like about the customer it is important to be specific and comprehensive. Is it their buyer? Then why? Is it the fact they pay promptly? Do they buy stuff no one else seems to want, or do they pay extra to get exactly what they want? Is it the fact they buy weekly, or monthly, or give you an annual contract? The key is to identify exactly and completely everything you like about your favorite customer(s) and use that as your customer profile, or target, in the new market segment you expand into.

What do we believe we do well?

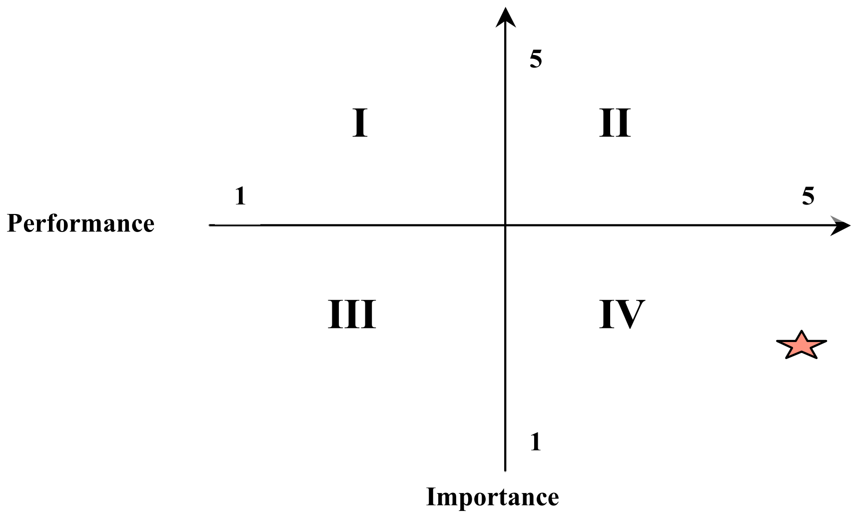
It is important to ask this question internally as well as of your customers. Internally the process is pretty straightforward. It is a very good idea to generate a list of your product's attributes and ask your employees to rank how well they think the company does in providing them to customers. With employees it is very valuable to allow the opportunity to respond beyond a simple ranking. For example, you could ask for comments, or "any exceptions" about the particular attribute. That way an employee could rank something like on-time shipping with a five and add a comment like "except for Sandra's locksmith shop, whose orders we always seem to ship late for some reason." The more information you can get from employees in this process the better.

What do our customers think we do well and how important is it to them?

One of the best tools for evaluating this question is called the Importance-Performance Grid. This marketing tool not only evaluates what you do well but also provides insight into how much your customer cares. There are many examples of companies expending energy on things that they do well, but that their customer doesn't fully appreciate for one reason or another. Rather than trying to convince a customer they ought to care, a firm's energy is better spent in figuring out what they may already care more about.

A fairly simple way to do an importance-performance analysis is to give each of your customers a sheet of paper with the same list of company attributes on both sides. Company attributes are things like guaranteed on time delivery, ninety-day credit terms, free shipping, fax machine available, and every part individually wrapped. It is ok to list up to twenty different attributes in a random order. Be sure to include all the ones you care about. Then, on one side of the paper you ask your customer to rank your company's performance on each attribute by putting a number from 1, poor performance, to 5, excellent performance, beside each attribute. Next, on the opposite side of the paper, you ask the customer to rank how important each attribute is to them, by putting a number from 1, unimportant, to 5, extremely important, beside each attribute.

You end up with a series of attributes for which you have information as to how well you perform and how much the customer cares for each. This is very valuable information for reviewing how well you are doing for an individual customer, and is valuable as well for identifying how the marketplace views your company in general. For purposes of finding new markets, you care mostly about the latter and about the response of your "favorite" customer.



To evaluate this further, it is worthwhile to plot the answers on a graph that looks like the one to the left, with Performance results plotted 1 to 5 from left to right and Importance values plotted from bottom to top, and with the intersection representing a value of 3 for performance and 3 for importance. As an example, if the attribute "free shipping" received a 5 for performance and a 2 for importance you'd plot a point that was 5 to the right (all the way) and 2 up from the bottom (or halfway between the very bottom and the intersection, or about where the star is.

Those attributes that fall into Quadrant II are the ones you should promote in new markets.

You can then plot the attributes for each customer, or average the responses of all customers for each attribute. Attributes that show up in quadrant I represent a problem: these are things that are important to customers but that your company doesn't do well. *Attributes in this quadrant require immediate attention and investment.* You need improvement quickly. If an attribute falls into quadrant II this means that the customers generally feel you do it well, and it is important to them that you do that. Keep up the good work and keep improving on the attributes in this quadrant. If the attributes ranking lands it in quadrant III, it means that you don't do this very well but customers in general don't care. So don't put much effort here. That doesn't mean that you should completely ignore these factors; it just means this is not a place to put your resources. Finally, if an attribute's ranking falls in quadrant IV, it means that you do a very good job at providing these attributes, but they aren't really important to your customers. Sometimes this means you should de-emphasis some of these attributes, particularly if they are places you have invested significant resources. Alternatively, an appropriate strategy is to simply not worry about these attributes and to not invest much time into maintaining them.

In summary, all the attributes that are in the top half of the grid are things you should put resources into. And for expansion purposes, those attributes that fall into quadrant II (which you do well and are important to the customers) are the ones you promote in new markets. These are the strengths that matter.

Years ago marketing analysts did an importance-performance analysis for a hotel in a rural area. Hotel management was very excited about the new fax machine available for client use, new pictures on the walls in the rooms, and the swimming pool they had just put in. The importance-performance analysis of visitors over a period of a month indicated that, although they thought the hotel did those things really well, those attributes weren't very important. Instead they indicated that "a comfortable bed, clean linen, and hot shower" were all extremely important, and the hotel didn't perform very well (less than a 2) on hot shower. In fact one visitor even commented, "You should have invested your money in new hot water heaters rather than a pool." So the importance-performance grid can provide very valuable, and sometimes rather blunt, information.

Internal Summary

Once you have done an internal analysis, you have a clear view of what defines the "ideal" customer –one you like to do business with and who buys products you make money on. You also know which products you want to grow in general, which ones would benefit from a little specific growth attention, your company's strengths and weaknesses, and those attributes of your company that are both important to the marketplace and that you do very well. This is a lot of good information.

If you do not have an existing "ideal" customer, then you should define one. This definition should have all of the characteristics of market segmentation so that your sales force knows what they are looking for. And don't forget to include the attribute rankings in this process. For example, a description of your ideal customer might look like the example below. The key is the recognition that finding a new customer is significantly easier if you know what you are looking for. Then it is just a matter of where to look.

Our ideal customer:

- *Is located within 500 miles of our facility (geographic),*
- *Is in a community of 50,000 that is growing at a rate of 5 percent or more (demographic), Has purchasing agents that like to fish (psychographic), and who buy at least half truckload quantities per month of our product (behavior),*
- *Appreciates the attributes we emphasize (e.g. fast delivery and service),*
- *Buys products that are profitable for us,*
- *Pays our invoices promptly, and*
- *Respects our employees and our business.*

Next steps

To a certain extent, the definition of your ideal customer will help to define where you expand to next. If there are potential additional ideal customers in your existing territory, then that may be the best place to focus your efforts. And never negate a potential new customer just because they appear loyal to your competition. To a certain extent, your competitor's best and most loyal customer is your ideal target. Efforts need not have an objecting of getting all the business, but simply to gain a small share of what could later become significant business activity.

Segmentation

Segmentation is the process of dividing the overall market into manageable chunks. Most companies start by doing this geographically. However, there are often very good reasons for staying within an existing region. When an organization decides to expand within an existing geographical region it is called "increasing the market penetration." The most common rationale for marketing more intensively within an existing region is that this provides an opportunity to utilize existing infrastructure more fully or to at least limit the amount of additional infrastructure necessary to achieve market growth. In some cases the type of product being sold (e.g. snowshoes) may effectively limit the potential sales region.

There are a number of ways to increase market penetration, the most common of which is to simply hire more salespeople and send them out to sell stuff. However, it may be that the best thing you can do is to more effectively use the present sales force. For example, subdividing an existing sales territory into smaller segments sometimes makes sense. In this case most of the components of the marketing mix (promotional pieces, pricing methods, and delivery methods) effectively stay about the same. Subdividing territories is fairly simple, allows the manager to use existing sales pros to manage the new sub-territories, and the segmentation process can also keep top sales staff "motivated." My brother-in-law was the top sales person in a large electrical firm. Over a thirty-year period his territory was regularly segmented (i.e. reduced) until, over time it went from being all of New England to just four or five key accounts. During all that change he remained the top sales person in the company as he kept focusing his highly skilled efforts on a narrower and narrower region or customer base. This is an example of achieving market penetration by stimulating the competitive nature of skilled sales staff.

An alternate method of increasing market penetration is to divide an existing market by some other means, such as demographic, psychographic, or behavior characteristics. As one option, an organization might have sales people that specialize in certain size accounts throughout the region (e.g. very large or very small ones) because of some common unique behaviors within that group (e.g. they buy full truckloads of your product). Alternately you might have sales people that specialize in certain product applications, e.g. industrial versus retail. And it is very common to have overlap in these approaches, i.e. the market is divided into territories, but specialists call on certain types of clients across territories to aid the territory representative.

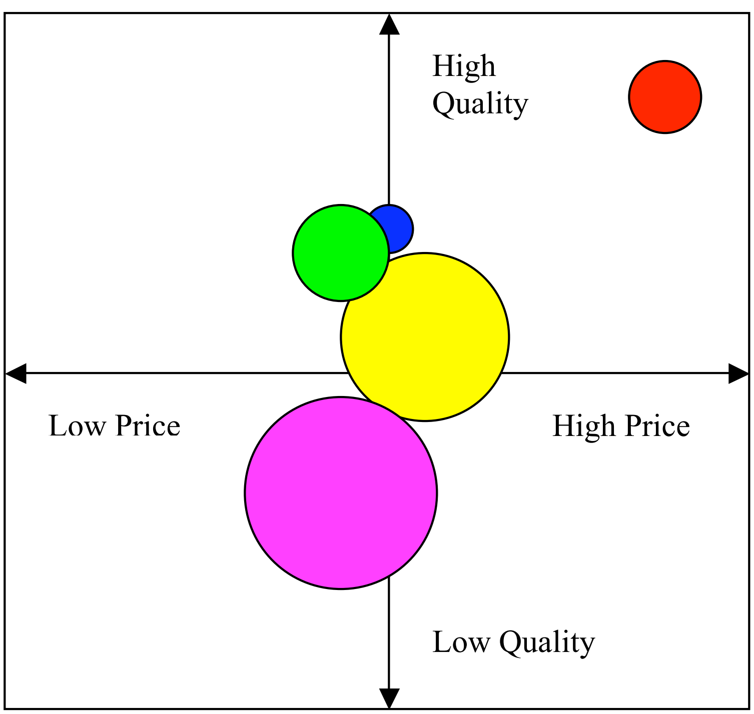
Finally, it is important to think outside the box when trying to identify new markets within a geographic region. It is, for example, important to be open to customers that require the same company attributes regardless of which of the traditional segment they fall into, e.g. a commercial construction client may be more similar to an industrial business than to a residential construction client.

It is often a good idea to first look at increasing market penetration before expanding geographically.

If geographical expansion is determined to be the best option for market growth, the next question is where and how. Often, a growing organization simply identifies a likely neighboring region with similar characteristics, duplicates their marketing programs from the initial region and voila they've expanded. To a certain extent it is that simple. But it is important to recognize the actual skills are that you are applying to the existing region and to recognize that straying beyond those skills can be difficult.

Finding your "position"

Traditionally, positioning of a product or company is defined as "creating an image in the eye of the customer." This is one of the most important concepts in marketing, and all sales, marketing, and operational efforts must be linked to a common image to be effective. Marketing brochures with pictures of mahogany desks and leather chairs may conflict with a goal of being viewed as the lowest cost provider. Conversely, brochures with employees working at stacked milk-crates for desks may conflict with trying to create an image of high quality and professionalism. Consistency is the key here, and most people understand this concept intellectually if not intuitively, so we won't spend much time on this aspect of positioning. However, there is a strategic component to positioning as well, particularly when an organization is seeking new markets.



To the left is a figure that shows various companies and their relative position in a specific market based on perceptions of product price and quality. The size of the circles reflects the relative size of the various organizations.

A figure such as this can be used to both identify opportunities in the market or concerns about your company's current position. For example, if this figure represented a new market a company was trying to enter, it would appear that there is an opportunity for a high quality, above average priced approach, as there appears to be room between the small company that is high quality and high priced (red circle) and the large medium quality, moderately priced company (yellow circle).

Alternately, it can be seen that two companies (green and blue) are already trying to compete with yellow by providing a slightly better product at a slightly cheaper average price. It can also be seen that the largest company competing in this market is viewed as having the lowest quality at a very slight price discount. This large company has done a good job of maximizing their price, given the competition.

Analyses such as this can be done by company, or even for a specific product line. Needed is access or a reasonable estimate of the competition's market share and reliable information (preferably customer-based) regarding product price and quality.

Conclusion

The most common mistake companies make in trying to expand is to try to do too many new things at once. They often try to take a new product to a new customer in a new region while trying to develop new skills. It should not be a surprise that failure is more likely than not.

It is important to limit the number of new things you attempt at once. In this discussion *we have assumed that the only thing changed was the customer*. This is the best way to apply existing skill sets and abilities for growth, successfully. The reader might ask, what if we have totally permeated our accessible markets with our existing products? Ah, then you need new products – which is a totally, and dramatically, different discussion and the subject of a future Dovetail report!

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This report was prepared by

DOVETAIL PARTNERS, INC.

Dovetail Partners is a 501(c)(3) nonprofit organization that collaborates to develop unique concepts, systems, programs, and models to foster sustainable forestry and catalyze responsible trade and consumption.

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This Dovetail Report is made possible through the generous support of the Rockefeller Brothers Fund, Surdna Foundation, and the McKnight Foundation.

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