COMPETITOR ANALYSIS

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COMPETITOR ANALYSIS

Competitive marketing strategies are strongest either when they position a firm's strengths against competitors' weaknesses or choose positions that pose no threat to competitors. As such, they require that the strategist be as knowledgeable about competitors' strengths and weaknesses as about customers' needs or the firm's own capabilities. This chapter is designed to assist the strategist understand how to gather and analyze information about competitors that is useful in the strategy development process. It discusses the objectives of competitor analysis and proceeds through the processes involved in identifying important competitors and information needs, gathering necessary information, and interpreting this information.

THE OBJECTIVES OF COMPETITOR ANALYSIS

The ultimate objective of competitor analysis is to know enough about a competitor to be able to think like that competitor so the firm's competitive strategy can be formulated to take into account the competitors' likely actions and responses. From a practical viewpoint, a strategist needs to be able to live in the competitors' strategic shoes. The strategist needs to be able to understand the situation as the competitors see it and to analyze it so as to know what actions the competitors would take to maximize their outcomes to be able to calculate the actual financial and personal outcomes of the competitor's strategic choices. They must be able to:

1. Estimate the nature and likely success of the potential strategy changes available to a competitor;

2. Predict each competitor's probably responses to important strategic moves on the part of the other competitors; and

3. Understand competitors' potential reactions to changes in key industry and environmental parameters.

What then should one expect from competitor analysis? Underneath all of the complexities and depth of competitor analysis are some simple and basic practical questions, of which the following are typical:

- Which competitors does our strategy pit us against?
- Which competitor is most vulnerable and how should we move on its customers?

- Is the competitor's announced move just a bluff? What's it gain if we accept it at face value?
- What kind of aggressive moves will the competitor accept? Which moves has it always countered?

IDENTIFYING COMPETITORS

Identifying competitors for analysis is not quite as obvious as it might seem. Two complementary approaches are possible. The first is *demand-side based*, comprised of firms satisfying the same set of customer needs. The second approach is *supply-side based*, identifying firms whose resource base, technology, operations, and the like, is similar to that of the focal firm. However, the firm must pay attention not only to today's immediate competitors but also to those that are just over the horizon (such as cellphones once were to cameras, social networking sites once were to web portals, or the internet once was to video rental stores). There are three domains for recognizing the sources and types of direct and less direct competitors to which the firm must also attend. These domains represent (1) the *areas of influence*, (2) the *contiguous area*, and (3) the *areas of interest.*[1]

- The *area of influence* is the territory, market, business, or industry in which the firm is directly competing with other firms to serve the same customer needs using the same resources. It is the arena in which Ford, Honda, Toyota, Kia, and General Motors compete with each other; where Nokia competes with Samsung and Motorola in cellphones. These are a firm's *direct competitors*.

- *Immediately contiguous areas* are those in which competition is close but indirect; comprising those firms that serve the same customer need but with different resources. Many food products fit into this category such as snack foods (potato chips versus pretzels versus peanuts), or packaging (glass versus plastic versus aluminum). They may serve the same need but through differing distribution channels (direct such as Avon versus retail such as Revlon). These are a firm's *indirect competitors.*

- *Areas of interest* are composed of firms that do not currently serve the same customer base but have the same resource base or, in broader terms, have *capability equivalence* – the ability to satisfy similar customer needs.[2] For

[1] William L. Sammon, Mark A. Kurland, and Robert Spitalnic, Business Competitor Intelligence: Methods for Collecting, Organizing, and Using Information. John Wiley and Sons, 1984; Mark Bergen and Margaret A. Peteraf,"Competitor Identification and Competitor Analysis: A Broad-Based Managerial Approach," *Managerial and Decision Economics* 23, (June-August 2002): 157-169; Bruce H. Clark and David B. Montgomery, "Managerial Identification of Competitors," *Journal of Marketing*, (July 1999), 67-83.
[2] Margaret A. Peteraf and Mark E. Bergen, "Scanning Dynamic Competitive Landscapes: A Market-Based and Resource-Based Framework," *Strategic Management Journal* 24, 2003, 1027-1041.

example, many firms possess the necessary capabilities to produce a wide range of digital electronic devices whether cell phones, PDAs, cameras, or "pad" computers. These comprise a firm's *potential competitors*.

We will first examine product/market level competition – serving the same needs to the same customer group. Next we will examine firm-level competition.

Identifying Competitors at the Product-Market Level

The most direct competitor competes for the exact same customers in exactly the same way as the subject firm. It sells the same product made by the same technology to the same customers via the same marketing channels. If the firm cannot win customer patronage versus such an identical competitor, then it is unlikely that it can do any better competing against its indirect or potential competitors. Why? If the firm's exact counterpart can win in direct competition, then that same competitor should also win more against the less direct competitors.

Companies, *per se*, do not compete with each other in the marketplace. Rather, their individual businesses compete with each other. The strategic marketing literature denotes a business as a division, product line, or other profit center with a company that produces and markets a well-defined set of related products and/or services, serves a clearly defined set of customers, and competes with a distinct set of competitors.[3]

A business is further defined in terms of a number of key dimensions, which reflect the ways and places in which it has chosen to compete. Primary among these are the *products* it offers and the *types of customers* to whom it chooses to sell.

The *products* a firm offers can be defined along three dimensions: *functions*, *technology*, and *materials*:

- *Customer function* is concerned with what need is being satisfied. This is the most natural way to think about a product. Electromechanical devices, for example, can frequently be designed to satisfy any size set of functions from very narrow to very wide. For example, some cooking appliances are single function (microwave ovens), others are dual function (combination convection-microwave ovens), while others are multifunction (combination convection-microwave-conventional ovens). Another example concerns over-the-counter medications which, although identical in ingredients, may be positioned or sold for the

[3] Roger A. Kerin, Vijay Mahajan, and P. Rajan Varadarajan, Contemporary Perspectives on Strategic Market Planning. Boston: Allyn & Bacon, 1990.

relief of colds or allergies or sinus symptoms. Others, such as Nyquil, are sold for even more specific usage applications (night-time cold relief).

- *Technology* tells how the customer function(s) are being satisfied. For example, kitchen ranges may use two sources of thermal energy (gas or electric) or, alternatively, microwave energy to cook. X rays, computerized axial tomography (CAT scan machines), and NMR (nuclear magnetic resonance) are three different technologies used in medical diagnostic imaging.

- The *materials* used in the manufacture of the product may also differ, producing slight differences in products that are otherwise identical. Cabinets may be made of chipboard versus plywood; bottles of glass or of such plastics as PET, polypropylene, or polyethylene; and beverage cans of aluminum or steel.

The *customer group* being served is a key dimension. Automobile parts manufacturers, for example, may choose to serve either the original equipment manufacture (OEM) market or the automotive aftermarket, or both. One competitor may focus on serving urban markets while another serves rural markets. Wal-Mart's initial success came from its focus on serving small, rural markets that traditional discounters had thought too small and too poor to serve. In contrast, J.C. Penney has defined its customers as those households in the middle 80% of the U.S. income distribution. Lane Bryant stores cater to women in need of larger sizes. There are obviously many ways of defining a firm's targeted customer groups.

The product manager needs to understand the exact extent of competition among the products available on the market. At this level, competitors are best identified by customers – the demand side – rather than by supply characteristics.

Substitution-in-use. Current thinking about identifying the competitive structure for any given product is based on the idea of substitution-in-use. Three premises underlie the idea:

1. People seek the benefits that products provide rather than the products per se.

2. The needs to be satisfied and the benefits which are being sought are dictated by the usage situations or applications being contemplated.

3. Products and technologies are considered part of the set of substitutes if they are perceived to provide functions which satisfy the needs determined by intended usage.[4]

[4]George S. Day, "Strategic Market Analysis: Top-Down and Bottom-Up Approaches" (Cambridge, MA: Marketing Science Instjtute, Report No. 80-105, August 1980), p. 14.

Determining a product's direct competition, then, may provide an answer that says, "It depends." It depends on (l) the number of separate and different uses or applications for the products in the market; (2) the number of different usage situations which customers encounter; and (3) user characteristics, including the number of product types or brands that a customer would evoke and choose among.[5] Some markets are relatively simple because the offerings within them provide only a single function for one or a few uses. Travelers checks or bathroom tissue are two such products. Other examples include home pasta makers and irons, both of which perform a specific function across a small number of different usage situations. At the other extreme are complex markets in which each customer has many uses for the product and many alternatives to consider. Snack foods or dessert foods are such. Depending on the intended usage occasion or situation, each of those product categories has many different kinds of products in competition. In the snack category, potato chips, pretzels, and various kinds of nuts, among others, compete. In the dessert realm, cakes, pies, ice cream, cookies, brownies, among others, compete.

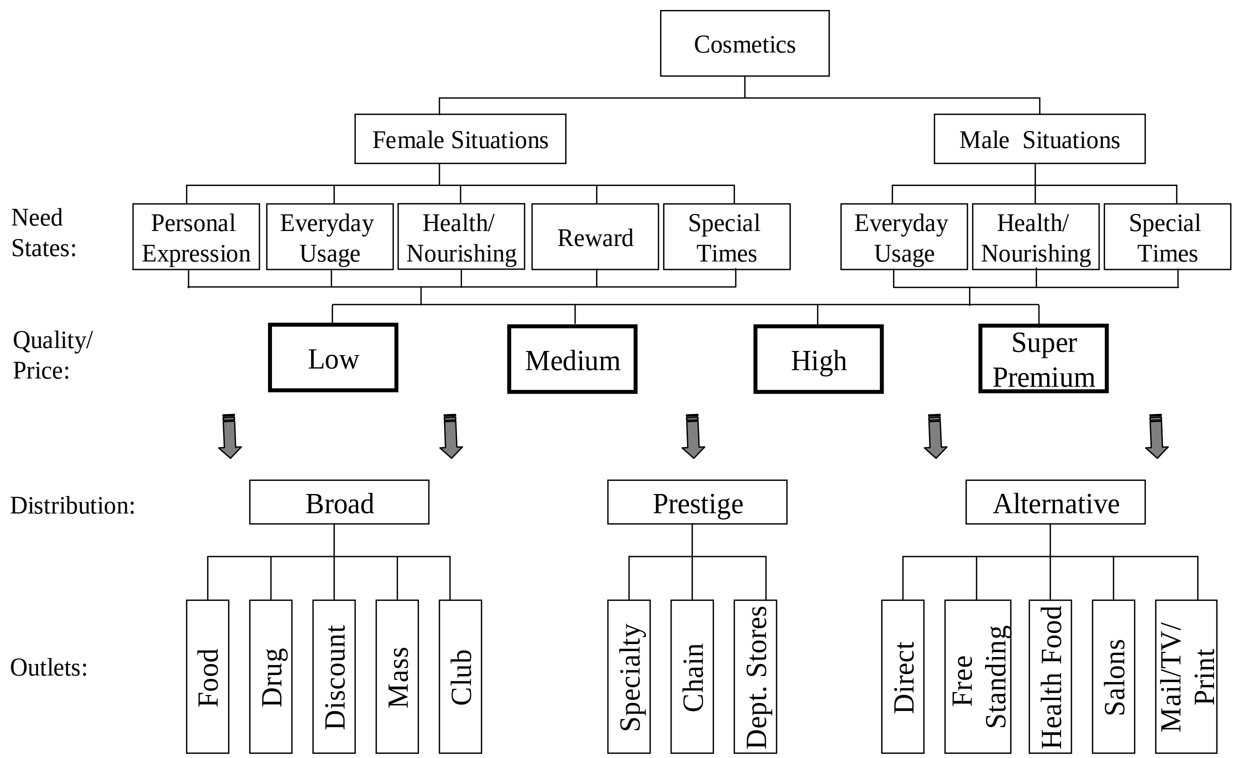
Consider the cosmetics market structure shown in Exhibit 1. Consumers have a number of different need states ranging from personal expression, everyday usage, health or nourishing, reward, or special times. Depending on both their own economics and the need state, they may seek different price points and distribution outlets for their purchase. For any given need state, then, the competitive set will vary depending on price points, distribution, and exact type of outlet chosen or encountered. Consider the cosmetics brand Aveda. Aveda distributes its cosmetics and personal care products through its own stores. While its products compete at a high level with those offered by such firms as Revlon or L’Oreal, the competition is not as direct as it is between brands whose products are next to each other on the drugstore shelf .

Financial services offer a similar example. One study, for example, defined a product market to be "the set of products judged to be substitutes within those usage situations in which similar patterns of benefits are sought by groups of customers."[6] In the study, upscale customers were asked to judge the appropriateness of twenty-four different financial services across each of twelve different usage situations. One such usage situation was described thus: While you are out of town on a trip you have

[5]Day, "Strategic Market Analysis, "p. 20; see also Glen L. Urban, Philip L. Johnson, and John R. Hauser, "Testing Competitive Market Structures," Marketing Science, 3, no.2 (spring 1984), 83-112.

some unexpected problems with your car. The repair bill, at a small independent garage, is about $100 and must be paid immediately.

EXHIBIT 1: Cosmetics Market Structure



Using Purchase Behavior to Identify Competitors. No matter how much logical sense an analysis such as the foregoing makes, it is based on what customers say, not on what they do. Several researchers have developed techniques which are based on actual purchase data. Exhibit 2, for example, depicts the competitive structure of the toothpaste and bathroom tissue markets estimated on the basis of supermarket scanning data.[7] In this instance, the map positions products on the basis of their attributes on a per-dollar basis. As the map shows clearly, all toothpastes are not alike. Customers preferring taste over anti-cavity qualities are more likely to buy Close-Up or Aim than Crest. Furthermore, Close-Up and Aim are closer competitors than either is with Crest. The bathroom tissue market shows a similar

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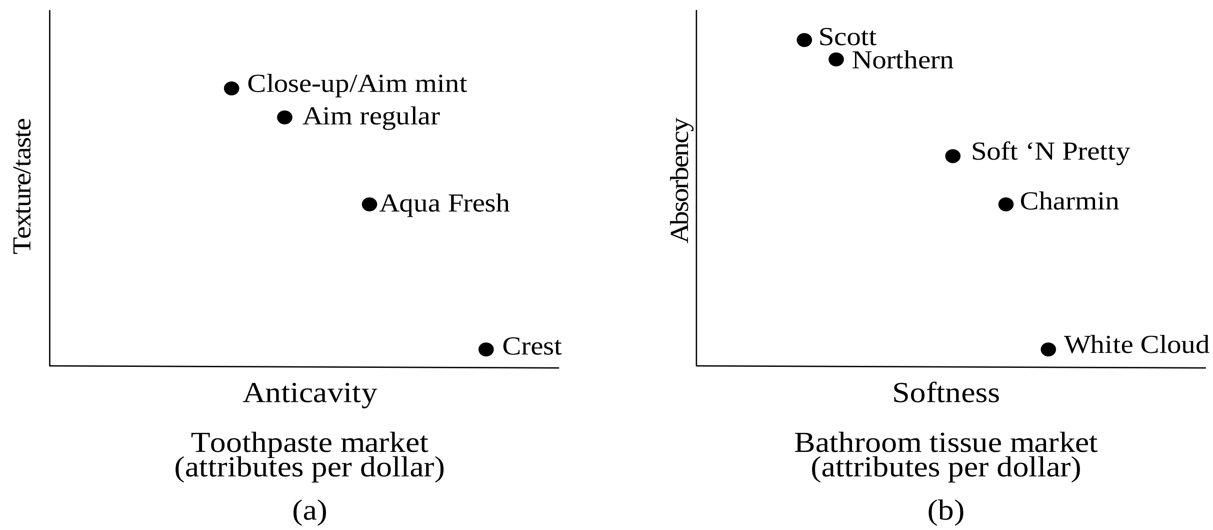
[6]Rajendra K. Srivastava, Mark I. Alpert, and Allan D. Shocker, "A Customer-Oriented Approach for Determining Market Structures," *Journal of Marketing*, 48, no.2 (spring 1984), p. 32.

[7]Steven M. Shugan, "Estimating Brand Positioning Maps Using Supermarket Scanning Data," *Journal of Marketing Research*, *XXIV* (February 1987), 1-18; see also Steven M. Shugan, "Brand Positioning Maps from Price/Share Data: The Case of Bathroom Tissue" (unpublished working paper, University of Chicago Graduate School of Business, July 1986, Revised) and Terry Elrod, "Choice Map: Inferring a Product-Market Map from Panel Data," *Marketing Science*, *7*, no. 1 (winter 1988), 21-39.

positioning along its two primary dimensions: absorbency and softness. To say that Scott and White Cloud compete is true and not true at the same time. One might better say that Scott and Northern are in closer competition than either is with White Cloud or Charmin.

EXHIBIT 2: Brand Positioning Maps



SOURCE: Adapted from Steven M. Shugan, "Estimating Brand Positioning Maps Using Supermarket Scanning Data," Journal of Marketing Research, XXIV (February 1987), p.8; and "Brand Positioning Maps from Price/Share Data: The Case of Bathroom Tissue" (unpublished working paper, University of Chicago Graduate School of Business, July 1986), p.21

Identifying Potential Competitors

Depending on the purposes of the competitive analysis, it may also be important to identify potential competitors. The process starts by identifying firms for whom the various barriers to entry to the industry are low or easily surmountable. These may include the following:

- *Technology*: Firms which possess the technologies necessary to operate in an industry represent one source of potential competitors. Analysis of patent activity frequently signals intentions well prior to actual entrance.

- *Market access*: In businesses where market access is a key factor for success, firms with that access frequently attempt to leverage it by acquiring additional product lines to be sold in that channel or to those customers.

- *Reputation and image*: Brand extension strategies are based on the use of a firm's reputation in one product area to leverage its entry into another. Clairol used its reputation in hair coloring to enter into the hair dryer business.

- *Operating knowledge and skills*: Regional competitors in a business often expand geographically. Entenmann's Bakeries moved into Florida and Midwestern markets from their original Northeastern base, similar to the path taken by Thomas's English Muffins. Folger's coffee was originally a regional brand on the West Coast until purchased by Procter & Gamble which expanded its distribution nationwide.

Identifying Competitors at the Firm Level

The concept of interfirm rivalry extends beyond the product/market level. Competition can also occur as firms use related resources to bear on individual product/market level rivalry. The theory of multimarket competition describes those situations in which firms compete against each other in multiple markets.[8] For example, in 1989, America West entered the Houston, Texas market – Continental Airline's home base -- with low introductory fares.[9] Continental retaliated, not by lowering prices in Houston but by lowering prices in Phoenix, Arizona , America West's home base and then communicated its displeasure with America West's actions in Houston. As a result, America West rescinded its low prices in the Houston market and, subsequently, Continental ceased its low-price counterattack in Phoenix. Such behavior requires that the manager understand the broader firm-level competitive set capable of such competitive behavior. One approach is to identify the different *strategic groups* in an industry.

The strategic group approach to identifying competitors is based on the differences in firms' strategies for competing in an industry. As such, it is a more general concept than the business definition approach. Like the business definition approach, the concept is intuitively appealing and understandable. For example, a hypothetical industry may be composed of three strategic groups:

1. A set of large firms pursuing a strategy of low-cost production of a full line of standardized products through mass-market outlets;

2. Another set of firms whose strategy emphasizes high-quality, differentiated, and branded products sold through specialty shops; and

[8] Aneel Karni and Birger Wernerfelt, "Multiple Point Competition," *Strategic Management Journal*, 6 1985, 87-96 and Satish Jayachandran, Javier Gimeno, and P. Rajan Varadarajan, "The Theory of Multimarket Competition: A Synthesis and Implications for Marketing Strategy," *Journal of Marketing*, (July 1999), 49-66.
[9] Asra Nomani, "Airlines May be using a Price-Data Network to Lessen Competition," *The Wall Street Journal*, June 28, 1994, A1.

3. A group of smaller firms which have gained strategic advantage by specializing in serving either specific customer groups or producing a very narrow range of products.[10]

The strategic group concept is useful in identifying and analyzing firm-level competitors because members of a strategic group not only resemble each other but are also affected similarly by any given event or change in the environment. Given that they are playing the same game in the same way, it would indicate that their economics are similar. The commonality in their strategies means that they will likely respond in a similar manner to competitive threats or moves.

A further point should be noted about strategic groups. While all of the firms in an industry are in competition at a broad level, those in the same strategic group compete more closely among themselves than with those in other groups.[11] For example, Proctor & Gamble, Unilever, and Colgate-Palmolive in the household and personal care products markets are in closer competition with each other than they are with direct sellers of household and personal care products such as Amway or Avon. Further, the competition between and among groups is not equal – the various pairs of groups may compete more or less intensely. By observing the successes of the different strategic groups, one can better understand the potential for multimarket competition.

Competitive Blind Spots

Much competitive information is bounded by the assumptions that managers' have with respect to their industry and these assumptions may lead to *blind spots*. The effect of such blind spots may cause the strategist to not recognize the significance of events, interpret them inappropriately, or see them only slowly.[12] There are six serious blind spots in competitive analysis:[13]

1. *Misjudging Industry Boundaries*. Too often firms define their industry around their current products, customer groups, and geographies blinding themselves to adjacent competitors which subsequently enter their current space.

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[10]This hypothetical industry, in fact resembles the home appliance industry in the 1960s as described by Michael S. Hunt in his dissertation. Hunt coined the phrase "strategic groups" to explain the differences in profitability he observed within the industry. Michael S. Hunt, "Competition in the Major Home Appliance Industry, 1960-1970" (unpublished doctoral dissertation, Harvard University, 1972).

[11] The biological analogy predicts this. As Bruce Henderson(the founder of the Boston Consulting Group) noted, "The more similar competitors are to each other, the more severe their competition. This observation was made by Darwin in *The Origin of Species*." Bruce Henderson, "The Anatomy of Competition," *Journal of Marketing*, (Spring 1983), p. 8.

[12] Michael E. Porter, Competitive Strategy. New York: The Free Press, 1980, 59.

2. *Poor Identification of Competitors*. Strategists frequently focus on only the largest and most well-known companies to the exclusion of other viable competitors – those potential competitors noted earlier in this chapter.
3. *Overemphasis on Competitors' Visible Competence*. Competitor analysis often focuses on competitors' hard assets and technology skills and ignore equally potent capabilities such as logistics, product design, or human resources.
4. *Emphasis on Where, Not How to Compete*. Strategists too often assume that competitors' strategies will shift only incrementally to the exclusion of radical repositioning in how they could compete.
5. *Faulty Assumptions about Competitors*. Prisoners of assumptions about competitors – the overuse of stereotypes – cause strategists to misjudge competitors' competences and competitive advantages.
6. *Paralysis by Analysis*. Obsession with the task of data collection results in information overload to the detriment of analysis and insight.

IDENTIFYING COMPETITOR INFORMATION NEEDS

The goal of competitor analysis is to be able to predict a competitor's probable future actions, especially those made in response to the actions of the focal business. This requires information that is both quantitative and factual (what the competitor is doing and can do) as well as that which is qualitative and intentional (what the competitor is likely to do). There are four key knowledge areas:

1. The competitor's *marketplace strategy* in terms of *scope, posture*, and *goals;*[14]

2. The sources of *competitive advantage* that give its marketplace strategy potency including resources and capabilities, organization, mind-set, and its place in the industry eco-system;

3. The interpretation of the *signals* being sent by the competitor both by its actions and communications; and

4. A *competitive response profile* which analyzes the competitor's possible future moves.

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[13] Shaker A. Zahra and Sherry S. Chaples, "Blind Spots in Competitive Analysis," *Academy of Management Executive*, 7, no.2, (1993), 7-28; E. J. Zajac and M. H. Bazerman, "Blind Spots in Industry and Competitor Analysis: Implications of Interfirm (Mis)perception for Strategic Decisions, *Academy of Management Review*, 16:1, 1991, 37-56.
[14] Liam Fahey, *Competitors: Outwitting, Outmaneuvering, and Outperforming***.** New York: John Wiley & Sons, 1999.

The Competitor's Marketplace Strategy

The competitor's marketplace strategy defines the way the competitor is currently competing in the marketplace. [15] It defines the strategic choices the competitor has made about *where*, *how*, and *why* it seeks to attract, win, and retain customers. A competitor's marketplace strategy has three elements:

1. *Scope* – the product-customer segments the organization is in or wants to be in;
2. *Posture* – how it competes or wants to compete in those marketplace segments;
3. *Goals* – its purpose in being in those segments.

Scope defines the products offered to the market and the customers that purchase them. It needs to incorporate both "static" and "dynamic" analyses. A static analysis defines where the competitor is and what it is doing at the present time; dynamic analysis refers to the moves the competitor has or is making over time in its choice of products or customers or both. Customer segments may be identified by needs or the demographics tied to those need states.

Posture defines how a competitor plays in the marketplace to win customers; most importantly it is about how it differentiates itself from competitors in the eyes of customers. As with scope, it needs be both static and dynamic. Exhibit 3 lists eight of the more common means of defining how the competitor competes, such as product line width, product features, and the like. Successful competitors generally employ a number of interrelated modes to compete. Seldom is the reliance on one dominant mode (say low price, for example) a successful strategy.

Goals address the *why* of the scope and posture strategies that a competitor uses. Goals are the *end* whereas scope and posture are the *means* to that end. While it is easy to say that the goal is to generate profit, that is an end result several steps beyond the scope and posture actions being taken. Goals may be at the highest level of the business's intent and vision, such as Apple's intention to integrate voice, data, and video. It may be at a lower level focusing on the short to medium term such as penetrating each major channel of distribution or the attainment of a specific gross margin objective. Or it may be even more short term as achieving market share goals, cost efficiencies, or cash flow targets. Unless the goals have been publicly announced as a signal to the marketplace or to competitors, the analysis often

[15] This section is based on Liam Fahey, pp. 108 – 118.

must infer the competitor's goals from the flow of observable actions it has taken. At the heart of such an analysis is the question: "Why is the competitor taking the observed action?"

EXHIBIT 3 Identifying How a Competitor Competes

Modes of Competition	*Possible Dimensions*	*Sample Indicators*
Product line width	Breadth of product lines Breadth of types within lines	Product lines and items
Features	Physical aspects of individual products Packaging Terms and conditions	Shape Style Color Design
Functionality	Performance Reliability Durability Ease of use Taste Shelf life	Speed Breakdowns Customer perceptions
Service	Maintenance Installation Help line Training Technical assistance Repair Response time	Contracts Service announcements and programs Customer reports Speed of competitor's responses
Availability	Distribution channels Amount Delivery	Individual channels
Image and reputation	Image of the company Image of products Reputation for rapid response time Reputation for best value	Content of advertising Actions and words of customers Third-party reports
Selling and relationships	Customer coverage Detailing of products Relationships with distributors Relationships with end users	Actions of sales force Frequency of calls Judgments of channels Customer's comments
Price	List prices Discount prices Price-performance Price-value	Actual prices Channel/Customer assessments

SOURCE: Liam Fahey, *Competitors: Outwitting, Out Maneuvering, and Out Performing.* John Wiley & Sons, Inc. 1999 at p.11.

The Competitor's Source(s) of Competitive Advantage

Beneath a competitor's marketplace strategy lie the organization and the functional operations and processes that make the strategy possible. If the competitor is rational, then its marketplace strategy will have been built around those functions and activities where it is competitively advantaged versus competitors.[16] The ability to assess the economics of a competitor is key to competitive analysis. Incorporating knowledge about the competitor's advantages is key to understanding its strengths and weaknesses and its likely moves in the marketplace.

Inputs are a key source of advantage in many industries. Since very few businesses are completely vertically integrated, but simply add value to purchased inputs through its operations, assessing a competitor's costs of its raw materials is an important analysis. Identifying a competitor's suppliers and estimating such things as transportation costs is the first step. In businesses for which labor is a large part of its cost structure, that is the second step. Labor contracts are one source of such information as are the various wage surveys available. The third element of inputs is the firm's weighted average cost of capital (WACC). A firm with a lower WACC can invest at a lower hurdle rate – the rate of return an investment must earn to gain corporate approval – and expand faster than one with a higher WACC. Equity analysts and many financial data services calculate the WACCs of firms.

Technology is the second focus, especially in industries that are still evolving. Assessing competitors' current operations and product technology is one step. Assessing the direction of its technology investments is the second. Many firms announce the present and future state of their technology to signal to competitors their competitive advantages. In other instances, following a competitor's published patents and scientific publications can give the analyst good indications of its direction. Estimating the number of R&D personnel is another common technique. As a generalization, a competitor that put more resources against a given technology will create better technology faster than competitors giving it better products and operations.

Operations is the third focus. Many aspects of a competitor's operations can be accessed simply by buying its products and examining or reverse engineering them. Quality, fit and finish, durability, and the like can give the analyst insight into aspects of its operations. In service businesses, it is not difficult to benchmark one's own operations versus competitors' to understand how customers experience those operations. Comparing the Cost of Goods Sold line of competitors' operating statements is another route.

Products are the primary locus of marketplace strategy. There are many ways to assessing advantage of competitors' products. The important aspect is to assess the products as customers see them. Customer surveys are a key and frequently used tool in this analysis. While many of the technical performance features are easy to measure, understanding the sources of customer value indicate what aspects of the products to analyze.

Access, Segments, and Customers are the final steps in understanding a competitor's sources of competitive advantage. Analyzing the type, number, and quality of channel members serving a competitor, and its coverage in different channels of distribution are key to assessing a competitor's advantage. For example, Anheuser-Busch, which sells almost 50 % of the beer in the United States, has been able to attract the highest quality distributors. In fact, some 60 to 70% of those distributors carry only Anheuser-Busch products. Other brewers, therefore, are not able to attract the same quality or must settle for distributors that also sell competing beers. Knowledge of competitors' penetration of the various segments is also important. Competitors who have a large share of growing customer segments are advantaged. Similarly, the customers a firm chooses sells to can be a source of competitive advantage or disadvantage. One supplier to the slow growing personal care market, for example, chose to target as its customers the small number of firms that were growing in the otherwise stagnant market, thereby growing while its competitors lost volume. In the early 2000s, Mitsubishi targeted the youth market in the United States with fast, small and sporty cars. Unfortunately, their customers' credit was poor and too many defaulted on the car loans.

Assessing and Interpreting Competitive Signals and Actions

Competitor analysis is more than a static activity. It requires more than the creation of a comprehensive report detailing the apparent strategies of the key industry competitors. It often means having only an hour or two to interpret the meaning of a competitor's 10% across-the-board price cut and to formulate a response. It often means being able to predict the reaction of competitors to your announcement of a

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[16] George S. Day and Prakash Nedungadi, "Managerial Representations of Competitive Advantage," *Journal of Marketing*

major joint venture with the technology leader from an adjacent industry, or to your preannouncement of a major new product.[17] It means being able to understand what the leading competitor's chief executive means when quoted as saying of his company, "We must absolutely be as competitive as we possibly can." Is the message intended to rally the troops or to warn competitors?

Interpreting Competitive Signals. Exhibit 4 presents a representative picture of the domain of competitive signaling. Interpreting a competitor's message requires that one simultaneously consider the *form* of the message, its probable *function*, the *forum* or medium in which it is communicated, and the probable *veracity* of the message.

Message Form. Prior announcements are perhaps the most often used form of competitive signaling because of their absolute versatility and ambiguity. One can announce with complete truthfulness the intention to expand capacity at some future point in time and change one's mind at some point thereafter. Prior announcements admit to the largest range of purposes and forums.

Announcements of accomplished fact or results, on the other hand, admit to a smaller range of application perhaps, but gain in the willingness of the receiver to believe that what has been announced has actually happened. Of course, this belief does not necessarily extend to swallowing whole the exact numbers, market shares, and so forth that are offered in the announcement.

Public discussions of the state of the industry or competition within it rival prior announcements in their frequency and breadth of purpose. Speeches made at industry conferences, especially those attended exclusively by top-level executives, are carefully crafted to convey messages to participants and just as carefully dissected by rivals. Some, of course, need little interpretation. In an article in the Wall Street Journal, a portfolio manager with large holdings of Alcatel-Lucent stock was quoted saying:

> "the debilitating price wars between Alcatel-Lucent and its rivals could be "stabilizing," citing statements by Ericsson's (an Alcatel-Lucent competitor) management that the firm wouldn't push to gain market share in wireless equipment by cutting prices as it had early last year."[18]

(April 1994), 31-44.
[17]Jehoshua Eliasberg and Thomas S. Robertson, "New Product Preannouncing Behavior," *Journal of Marketing Research*, (August 1988), 282-92.

[18] Wall Street Journal, "Alcatel-Lucent Deal, Revisited," February 7, 2007, p.C2.

EXHIBIT 4: The Domain of Competitive Signaling

FORM	PURPOSE (UNDERLYING OSTENSIBLE)	VERACITY	FORUM OR MEDIUM	MESSAGE CONTENT
• Prior announcement • Announcement after the fact • Public discussion of industry • Discussion of own moves	• Preemption • Communicate strategic advantages • Threat of contingent action • Express pleasure or displeasure • Test of competitors' sentiments • Minimize provocative potential of own action • Avoid simultaneous actions • Inform financial community • Gain internal support	• True/untrue • Bluff • Misleading • Over/understated	• Broad, prestigious industry audience • Financial analysts meeting • Interview in major industry/business publication • Press release • Letter to customers or suppliers • Private communication with competitor	• Firm's goals • Internal situation of firm • Firm's intention • Expectations of competitor behavior • Rules of game/nature of dilemma

Discussing one's own move in terms of its intent or rationale happens with less frequency than prior announcements but possibly with greater impact. The apparent openness with which a competitor discusses the rationale underlying a given strategic move adds the luster of truth to the message, especially if it is shared in whispered tones with key customers or suppliers, Few public relations campaigns can spread news through an industry faster than sharing a strategy "in confidence, of course," with a customer whose greatest benefit is served by keeping competition for his or her business at a high pitch.

Message Function. The range of functions served by signaling is wide, and any given message may fulfil1 several simultaneously. Attempts to preempt competitors are certainly a leading function. During periods of shortages, industry publications are replete with competitors trying to preempt others from adding capacity by announcing their own capacity additions first. Announcing the future availability of major product developments to postpone customer purchase of competitors' products is another form of preemption. To the extent that it can be achieved, preemptive announcements are also used as the occasion to communicate strategic advantage to discourage less advantaged competitors from cluttering up the playing field.

Some messages are intended to minimize competitive provocation by explaining the rationale behind projected actions which could otherwise be interpreted as aggressively competitive. Consider, as an example, the announcement for lowering CD prices by the Universal Music Group in 2003:

> "We're going to reinvigorate the record business in North America. Our new pricing policy will allow us to take the initiative in making music the best entertainment value and most compelling option for consumers. UMG is responsible for almost 30 percent of album sales in the U.S. so we are uniquely positioned to try this new strategy. . . . We strongly believe that when prices are dramatically reduced on so many titles, we will drive consumers back to stores and significantly bolster music sales."[19]

Some external signals are given to gain internal support. Announcements in the public press by a company's president or chairman of its new drive to provide the highest level of quality are frequently more credible to employees than many internal communications programs. A variation is the external announcement that is made to cutoff further internal discussion of a given strategy or specific action. Along the same line, some announcements are made primarily to communicate indirectly with the financial community. Signals such as these may indeed carry little of import for competitors.

Message Content. The actual content type of the message is important. One researcher has studied the various messages allowed in experimental studies of negotiation, cooperation, and competition built around the various forms of the prisoner's dilemma and was able to discern different types of content.[20] Communication about the firm's *goals* has the potential to remove the dilemma in a situation in which the motivations are not clear. For example, if both are cooperatively disposed and both are aware of that, the obvious choice is to cooperate. Signals which communicate *information* about the internal situation of the firm, its health, success, and feelings about its outcomes and situation give others that knowledge necessary to infer its payoff matrix.

Signals about a firm's *intentions* give competitors information about how best to plan their own actions; this is especially so if the statement reveals commitment as well. Such knowledge is clearly important if

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[19] Ethan Smith, "Universal Slashes CD Prices to Revive Music Industry," Wall Street Journal, September 4, 2003, pp. B1, B8.

[20] Marian Chapman Bourke, "Signalling and Screening: Tactics in Negotiations Across Organizations" in Blair Sheppard, Max Bazerman, and Roy Lewicki, eds., *Research on Negotiations in Organizations* (Greenwich, CT: JAI Press, 1988).

the goal is to chart nonintersecting strategies. Communications or signals which state *expectations of the competitor's behavior* maybe helpful in situations in which competition or cooperation are the choices and it is not clear to others how they should act.

It has been said that discussing the rules of the game and nature of the dilemma is particularly relevant in competitive inter-firm situations because this message content contains more information than any of the others. Not only are statements about the nature of the game the most innocuous, but a cooperative equilibrium typically requires that competitors share a common view of how the game is played. Ultimately, of course, all competitors must limit their competitive behavior, and public discussions about how the buyer is the only winner in price wars are one way of signaling the need to cool the competitive state. David Steiner, the then Chief Executive Office of industry-leading Waste Management, made the following statements during a conference call with investors:

> "If you are going to continue to raise prices as an industry you've got to have all the industry players acting consistently. We're going to continue to raise price. We would certainly hope that the industry follows along with us."[21]

Forum or Medium. Where and how a message is delivered is of key importance in its interpretation. Messages delivered before prestigious industry audiences or to a formal meeting with financial analysts are taken to contain higher truth content than those delivered in other forums. This is simply because both groups have good memories and require relationships based on personal trust.

Interviews in industry and business publications, on the other hand, are taken for what they are---the attempt by the competitor to deliver a carefully crafted message to a specific audience. The reality of the situation is that no executive has to consent to be interviewed and that consent is only given when there is some purpose to be served. Press releases are in a similar category. Letters to customers, on the other hand, carry a lot of weight.

Veracity. Truth in strategic communication is a relative concept. While a communication may indeed be just what it is and says, the strategist is better off asking how it would benefit the sender if it were to be accepted as true by the receiver. Some signals are bluffs which will not be implemented if the bluff is successful in deterring competitive action but probably would not have been implemented anyway. Too many bluffs, however, and all parties suspend belief and the firm has lost a valuable tool through overuse. More often, the content of communications contains some aspects that are misleading or simply over or understated. These aspects require the analyst to cross-check all numbers and to analyze every statement for possible alternative interpretations. Sometimes ambiguity is intentional to allow one to read a possible worst-case scenario into an otherwise innocuous message. Some signals carry as much contradictory and hidden meaning as the gambits and contrivances one finds in the best of the Cold War spy novels.

Interpreting Competitive Actions. Interpreting a competitor's actions follows a similar analysis, beginning with the overriding question: "Why is the action being taken?" In seeking to answer that question, the first step is to characterize the type of action. A *frontal* attack is where the competitor directly attacks with an identical or similar product. In the 1990s, Unilever directly attacked P&G's Joy brand dishwashing liquid with an identical product under the brand name Sunlight. Both were yellow, lemon scented products in identical bottles promising shiny dishes. A *flanking* attack, on the other hand, is when the competitor enters an adjacent product-customer segment rather than going head-to-head. In the 1980s, for example, Bic entered the men's shaving business with a disposable razor rather than the traditional razors offered by Gillette. *Pricing* actions are of a number of types. They may simply be *meeting* the competition, *undercutting* the competition, a *cross parry* in order to retaliate, or a widely announced *increase*. Alternatively, a pricing action may be a "non-action" – that is not following a price leader's announced price increases. Northwest Airlines (now Delta) frequently acted as a spoiler by not following competitors' price increases in the early 2000s, causing them to be rescinded.

The nature of the action is the next step. The analyst needs to ask the following questions:

- What was the action relative to the potential actions that could have been taken? Was it more or less severe?
- How was the action taken? Was it announced? Quietly implemented?
- How did it match or differ from the competitor's past actions and strategies? Does it suggest a continuation of past policies or does it mark a change in its strategy or mode of action?
- Does the action follow accepted industry practice? Is the competitor seeking to lead the industry into a new competitive territory?

[21] Lan Brat, "Garbage Haulers Raise Prices: Truce Allows Waste Management, Allied, and Republic to Push Higher." Wall Street Journal, September 18, 2008, page B1.

- Does the competitor expect other firms to follow it?
- Is the move aggressive or does it suggest a more "cooperative" way of competing?

It should be noted that competitive actions can be outside of the marketplace. Legal actions are a case in point. Lawsuits over trademarks and brands are frequent and can tie up a firm's executive and managers for long periods of time. Private antitrust suits are another form of competitive action. In both instances, a deep pocketed competitor can cause great harm to smaller, less wealthy firms.

The Competitor's Response Profile

The likelihood of competitive reactions depends on:

1. The characteristics of the firm taking the action. For example, its size and reputation for competitiveness.
2. The characteristics of the action. It could be a new market entry or price change.
3. The characteristics of the rival. Its size, performance, or desired reputation.
4. Environmental characteristics such as market turbulence, growth.[22]

Given some insight into these four factors, the firm or analyst can take some more concrete steps as shown in Exhibit 5 which portrays a helpful framework for analyzing present and potential competitor moves and responses. The combination of this analysis of competitors' goals and assumptions together with competitors' current strategies and capabilities allow one to estimate their response profiles. A response profile tells one what kinds of actions a competitor is likely to take, if any, in response to the firm's own actions. Again, what this means is that you have to be able to think like your competitor.

It may sound simplistic, but one of the most powerful determinants of a competitor's future actions is the set of economic outcomes that would result from each different competitive response. To the extent, then, that one can calculate the financial results that would flow from different actions, one should be able to predict competitors' actions.

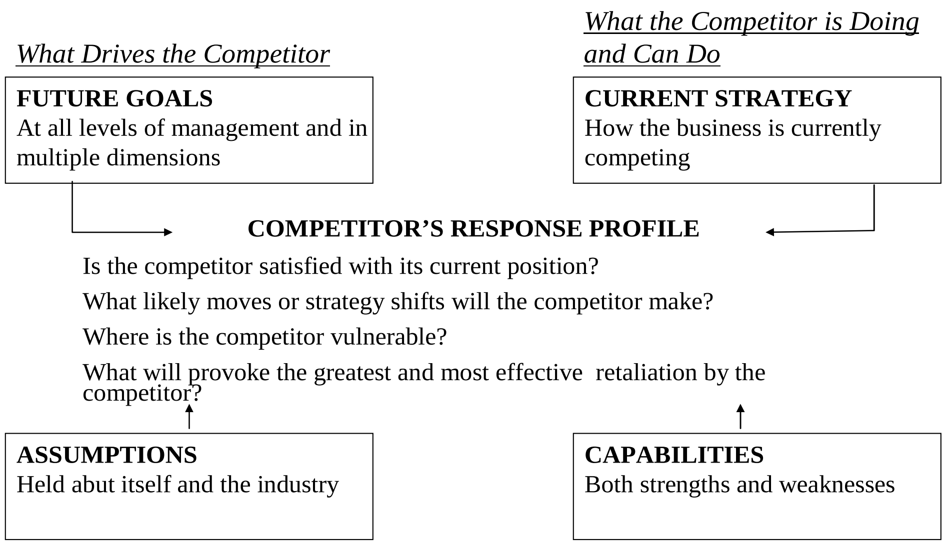
[22] David B. Montgomery, Marian Chapman Moore, and Joel E. Urbany, "Reasoning About Competitive Reactions: Evidence from Executives," *Marketing Science* (Winter 2005) 138-149;

One approach is to estimate the competitor's *reactiveness* to a competitive move on a particular product in a given geographical (or other defined market) market and the *relative clout* it has with which to respond to competitive move.[23] *Reactiveness* is simply the competitor's incentive to counter competitive moves. It can be measured by estimating the contribution (revenues, profits, etc.) that the product delivers in that market and that it delivers to the business unit of which it is a part adjusted for the strategic importance of the product and market to the competitor. Take, for example, a move against P&G's Tide laundry detergent product in the United States. With its leading market share it contributes both book profits and strong cash flow to the division of which it is a part and to the corporation as a whole. As the anchor product of the detergent aisle in supermarkets it is of strategic importance in maintaining the support of the channel. One can say with reasonable certainty that P&G would exhibit high reactiveness to any competitive move against Tide. *Relative Clout* asks which of the competitors is in a better position to make a strategic move in that specific product/market arena. It is the ability to fight or to fight back. As with reactiveness, relative clout can be estimated from the competitors' relative sizes, cash positions, distribution coverage, and the relative number of salespeople.

Theoretically, the issue goes beyond reactiveness and clout. It is more complex. Economists use the term conjectural variation to refer to what is known about the likelihood and the intensity of competitors' responses. Specifically, a conjectural variation is what is believed about the relationship between a firm's own behavior and the corresponding return-maximizing action that will be taken by the competitor.[24] The interesting aspect is that estimating a competitor's actions requires the recognition that the competitor's decision involves more than simply choosing the action that yields it the highest relative financial result from among the set of actions available to it. This is because those financial results themselves are simultaneously affected by the competitor's own conjectures concerning the acting firm's response profile to its response.

[23] Ian C. MacMillan, Alexander B. van Putten, and Rita Gunther McGrath, "Global Gamesmanship." *Harvard Business Review* Vol. 81, May 2003, pp 62-71.
[24] Raphael Amit, Ian Domowitz, and Chaim Fershtman, "Thinking One Step Ahead: The Use of Conjectures in Competitor Analysis," *Strategic Management Journal*, 9, (1988), 431-442.

EXHIBIT 5: Analyzing a Competitor's Response Profile



SOURCE: Michael Porter, *Competitive Advantage*, (New York: The Free Press, 1980, p. 49.

In more practical terms for the strategist, this means working two moves ahead—estimating whether the competitor would see its action choices as leading to more or less effective countermoves. Game theory provides one framework for analyzing the situation. The main point, however, is to attempt to calculate the relative financial implications of the competitor's possible responses. A second approach suggests that one analyze the past effectiveness of the competitor's marketing mix elements. As theory would suggest, a competitor's response to, say, the market entry of a new product will be to adopt the approach that has shown the greatest response elasticity in the past. [25]

SUMMARY

Competitive marketing strategy requires that the strategist position the firm's offerings such that they minimize direct competition either by choosing vulnerable competitors or by pitting strength against weakness. The goal of competitor analysis is to provide the strategist with the means needed to achieve that result.

[25] Kevin P. Coyne and John Horn, "Predicting Your Competitor's Reaction," Harvard Business Review, April 2009, pp. 90-97.