



Strategic Direction

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Shubhabrata Basu

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Product market strategies and innovation types: finding the fit!

Shubhabrata Basu

Shubhabrata Basu is based at Strategic Management, Indian Institute of Management, Indore, India.

Firms, especially multidivisional, multinational corporations, are said to sit on a stockpile of innovations, waiting for the opportune moment to launch them. New innovative products and services are perceived as the key to sustainable competitive advantage. However, firms that launch such products do not always enjoy the benefits of being a first mover. For example, Nokia with their 7650 smart phone, IBM with their Personal Computer, and a whole range of corporations, lost out to second movers such as Samsung and Compaq. Scale advantage of the second movers cannot adequately explain this phenomenon – IBM, for example, was far bigger than its nimble competitors. Similarly, disruptive innovations cannot properly address this – Nokia and IBM's competitors were traditional players. Firms appear to be caught in the horns of dilemma. If they innovate (thus incurring R&D expenses), there is no guarantee of success; if they don't, their positions would surely be disrupted. Is there a way to overcome this problem? Possibly yes; but that requires understanding the product-market framework and finding an innovation to fit into it.

Ansoff's matrix revisited

Ansoff's (1957) product-mission (market) matrix represents the co-evolution of a product with that of the market and the strategies to be adopted thereof. This, along with an action framework is presented in Table I.

The table reveals that product development and diversification strategies require the firm to commit its resources and capabilities on what new content(s) need to be supplied within the product. Consequently they are capital intensive and proactive endeavors to popularize the products in the market. On adoption, they lead to path dependence or exit barriers for the firm. Penetration and market development strategies, on the other hand, deal with how efficiently can the content, be supplied to the existing or new market, in the presence of competitive threats. Consequently, they are reactive strategies that focus on cost savings by harnessing scale and scope advantages. With the above characteristics of product-market strategies, a matching innovation framework needs to be considered.

The Henderson-Clark framework of innovation

The Henderson-Clark (Henderson and Clark, 1990) framework had categorized innovation into four broad types based on the following criteria:

- technological novelty at the component or functional level within the innovation; and
- novelty of the linkages that integrate the components, giving a market acceptable form to the product/service.

Table I Product market strategies and action framework

<i>Product-market characteristics</i>	<i>Adopted strategies</i>	<i>Action framework</i>
Existing product × existing market	Market penetration	(i) Increased volume sales per existing users (ii) Advertisements, loyalty schemes, sales promotions, personal selling to existing customers (iii) Increase volume sales by acquiring new users (iv) Market consolidation, mergers and acquisitions (v) Competitive pricing, discounting
New product × existing market	Product development	(i) Enhanced R&D efforts and innovation (ii) Developing insights into customer's needs (iii) First movers in a product category (iv) Increase the overall efficiency of the users
Existing product × new market	Market development	(i) Modify existing product to have new usage for new set of customers (ii) Highlighting new dimensions/packaging of products (iii) New geographical expansion – exports (iv) New distribution channel (v) Market segmentation – new pricing policies
New product × new market	Diversification	(i) New product in new markets (ii) New technology, new skills (iii) New merchandizing, new facilities (iv) New financial investments, new financing models (v) High risk-high rewards

Based on the above criteria, the four types of innovation proposed were:

1. incremental innovation having minor improvements in function and form;
2. modular innovation with significant improvements/alterations in function due to change in technology – but no change in form;
3. architectural innovation with minor change in technological function but significant alteration of linkages and hence form; and
4. radical Innovation where both the form and function have undergone major changes.

Modular and radical innovations are capital intensive due to their focus on improving function. To improve function, significant R&D expenses for technological improvements have to be undertaken. In contrast, architectural innovation focuses on forms and hence on alternative superior process of integration. Incremental innovations provide minor improvements in both.

For example, consider the use of ceiling fan in the tropics. It has a rotor, a set of three blades, a perpendicular shaft that connects it to the ceiling and the resistance type regulators for speed control:

- an incremental innovation implies changing the color schemes, different sizes for different market segments, etc.;
- modular innovation implies replacing the resistance type regulator with diode/rectifier type regulator that saves energy consumption or replacing three blades with four blades for superior air circulation;
- architectural innovation implies changing the relative positions (hence configuration/form) between the rotor and the shaft from being perpendicular to parallel. The new form leads to new usages like table fans or exhaust fans (for industrial usage) that enable entry into new business domains; and
- radical innovation will be an air conditioner with different set of component technology and linkages. An air-conditioner has new functions (circulation and cooling) and a different form.

Finding the fit

Given the characteristics of innovation and product market strategies, a fit can be deduced. This is provided in Table II.

A penetration strategy is usually suitable for a competitive and price sensitive market with lower unit margin. Here maintaining a semblance of distinction amongst competing offerings is important. Hence incremental innovation is suitable. An incremental innovation delays the commoditization effect in terms of brand identity and margins. Examples are Microsoft Office versions 1997 to 2003, Microsoft Vista operating system to Windows 7 etc.

A product development strategy uses different variants of same or similar products for the same market. This involves a focus on component level technology, leading to modifying the functions and enhancing efficiencies. The visibly recognizable features are not altered. Consequently a modular innovation is suitable for this type of strategy where the relatively inefficient components are replaced or new modules added, leading to aggregate performance improvements. A sedan (3-box), a hatchback (2-box), a SUV/MUV or a limousine (an extended 3-box), are examples in the passenger automobile market. Similarly, Windows Vista was a modular innovation *vis-à-vis* Windows XP.

A market development strategy uses the same basic product, but adopts them for different markets by reconfiguring the components. This is similar to architectural innovation where the form, therefore the application gets altered due to change in the linkages leading to new market entry. The basic Boeing 737 can be internally refurbished as a military transport aircraft. Windows 7 has been architecturally reconfigured to Windows 8 for smart phones. Three molecules of Acetylene gas ($3C_2H_2$) (used in construction industry) can undergo architectural reconfiguration to Benzene (C_6H_6) used in polymer/plastic industries.

A diversification strategy requires a big bang entry into a new market with new product/service having new forms and functions. Consequently a radical innovation is the likely candidate. However, radical innovations are capital intensive and should be introduced in markets that can bear the development cost. Examples are mobile phones over fixed-line telephones, MS-DOS over proprietary operating systems, e-mails over snail mails.

Conclusion

The fit framework proposed above is a preamble that should guide top management on where to innovate, when to innovate and what to innovate. Innovating, just to imitate similar activities of a competitor or as a hedge against future uncertainties, has often left firms worse off. Innovation is a time consuming and costly affair that comes at the cost of the shareholders. As such, the above fit framework will prove to be useful, first to identify the market (existing or potential), next to choose the appropriate timeline and finally, to opt for an appropriate innovation that will maximize shareholder wealth.

Keywords:

Fit,
Innovation type,
Product market strategies

Table II Product market strategies and innovation type – a fit framework

<i>Product-market strategy</i>	<i>Innovation type</i>	<i>Activities and benefits</i>
Market penetration strategy	Incremental innovation	Adding incremental values to existing set of activities to get expected profits
Product development strategy	Modular innovation	Adding or replacing new activities (new components) to get more than expected profits
Market development strategies	Architectural innovation	Changing sequence of activities (reconfiguring components) to get more than expected profits
Diversification strategies	Radical innovation	Completely redesigning activities – may or may not get more than expected profits

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Further reading

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About the author

Shubhabrata Basu is an Associate Professor in Strategic Management Area at the Indian Institute of Management Indore. He is a Fellow (PhD) in Management from IIM Ahmedabad and a Chartered Civil Engineer before pursuing an academic career. Shubhabrata Basu can be contacted at: sbasu@iimahd.ernet.in

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