



Institute for Market-Oriented Management

Competence in Research & Management

Prof. Dr. Dr. h.c. mult. Christian Homburg, Prof. Dr. Sabine Kuester

IMU Research Insights

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Managing Business Activities in Lower-End Consumer Segments in Emerging Markets

Prof. Dr. Sabine Kuester
Sergej von Janda, M.Sc.
Dr. Monika Schuhmacher, MBA

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Relevance of topic

While traditional, developed markets become more and more saturated, emerging markets and their rising middle classes experience increasing importance as drivers of global growth. Managers need to be aware of and prepared for the distinct requirements of these high-potential target markets.

Investigated industries

Textiles/sportswear, automotive, health care, FMCG, renewable energies, agriculture, and telecommunications

Study characteristics

Aim: To identify the key success factors for multinational corporations that seek to do business with lower-end consumer segments in emerging markets

Methodology: Semi-structured expert interviews with managers with 2-20 years of emerging market experience

Key learnings and implications

- The 'lower' the target segment in the consumer pyramid, the higher the **need to adapt – respectively localize –** product, price and distribution strategy
- Universal need of adaptation of promotion activities across all consumer segments
- Emerging markets require a **decentralization** of marketing and R&D functions in combination with high degrees of **internal embeddedness** characterized by intensive intra-organizational information- and communication flow
- 'Acentric' organizational orientation leverage each market subsidiaries' resources
- Offerings characterized by favorable price-performance ratios, modular design, simplicity and high degrees of novelty or radicalness on the one hand unlock the great potential of lower-end consumer segments in emerging markets and on the other hand entail **opportunities for reverse innovation**

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- Topic Relevance and Research Question
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- Study Characteristics
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- Study Results
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- Managerial Implications
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- Contact and Further Information
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The saturation of many developed markets increases the importance of emerging markets as drivers of global growth

Current global developments

- Developed markets achieved an average of 1.1 % gross domestic product (GDP) growth in 2012 (UNCTAD 2012)
- In contrast, emerging markets as a whole grew by **5.0 %** (UNCTAD 2012)
- Emerging markets' share on global GDP is expected to grow from 36.0 % in 1980 to over 51.0 % in 2014 (UNCTAD 2012)

Shift of 'center of gravity' from developed to emerging markets

Emerging market developments

- Multinational corporations (MNCs) more customarily highlight emerging market **investments** (Arnold and Quelch 1998)
- Number of **innovations** coming from emerging markets grows rapidly (Petrick and Juntiwassarakij (2011))
- **Growing global competition** from 'Emerging Giants': Emerging market based MNCs
- Offering of local firms often very well tailored to emerging market consumer needs

'Emerging Giant' examples



- The global competitive landscape changes with Emerging Giants grasping at their 'share of the pie', challenging developed market based MNCs in local as well as global markets
- Shift of center of gravity calls for a **deliberate extension** of business activities into future growth markets

1. Socio-political environment

Challenges:

- **Reevaluation** of the competitive advantage
- **Integration** of business ventures into the local context of socio-political institutions (e.g. government, business groups, nongovernmental organizations, local community)

2. Resource shortages

Challenges:

- Particularly **effective** resource management
- **Innovation** of affordable, versatile and often disruptive products and services

3. Inadequate infrastructure

Challenges:

- **Adaptation** of the marketing mix to local conditions and usage of available marketing tools
- Lack of readily available market data results in increased need for own **market research**

Source: See Sheth (2011)

4. Market structure

Challenges:

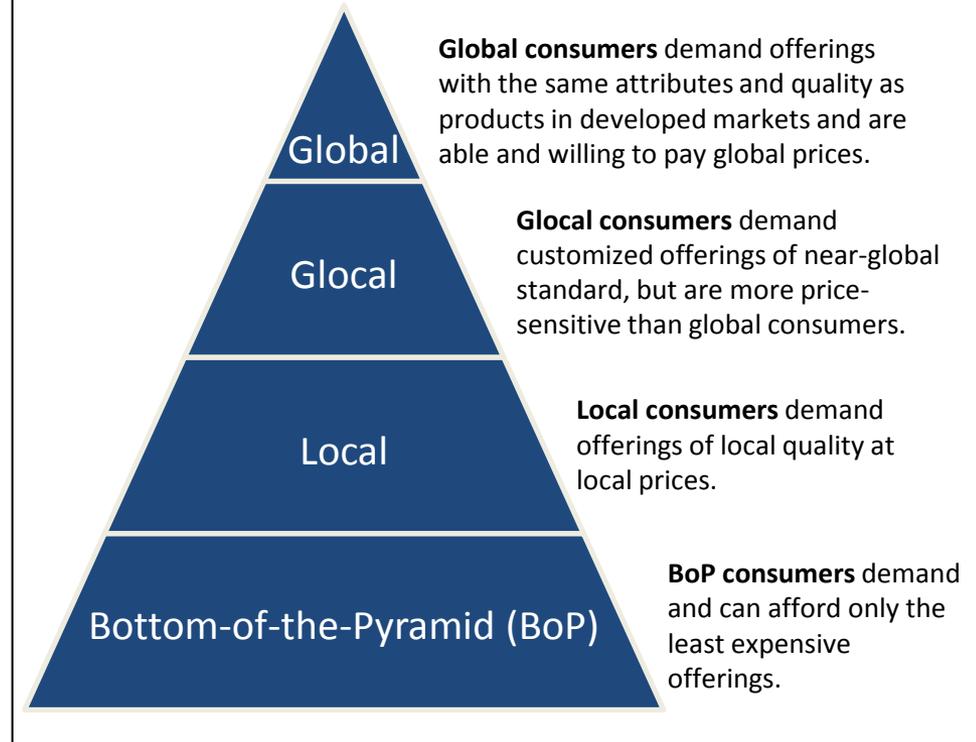
- Prevailing number of consumers are part of the **unfamiliar** lower-end consumer segments (Local and BoP)
- Need for offerings of considerable quality at **very low prices**

5. Competitive environment

Challenges:

- **Increasing competition** from local competitors with often very well tailored offerings for promising lower-end consumer segments
- Necessity to **adjust** the portfolio or even redesign the overall business model

Emerging market consumer pyramid



The **strategic challenges** arising from the expansion into emerging markets and lower-end consumer segments in particular comprise (1) the adjustment, extension or reinvention of the marketing mix, (2) the re-structuring of organizational functions, and (3) the realignment of global and local management strategies.

Sources: See Sheth (2011); Khanna and Palepu (2006)

To address these challenges, the main research question for deeper investigation was formulated

Research Question

What are the key success factors for MNCs that seek to do business with lower-end consumer segments in emerging markets?

How about status quo?

Current state of research

- Current research fails to **combine different research fields** (innovation management, marketing, organizational design) in order to present an all-embracing success factor model for emerging markets.
- **Contradictory propositions** for emerging market ventures exist with regard to the choice between an incremental and a radical innovation approach (see e.g. Iyer et al., 2006 and Ray and Ray, 2011) and **imprecise recommendations** with regard to the concrete design of offerings for lower-end consumer segments prevail.
- Present claims come exclusively from single case study examples.

This study aims at **filling the current gaps** in research to provide practitioners with guidance regarding how business activities in lower-end consumer segments in emerging markets should be designed and managed.

Research approach and methodology

- Qualitative research study applying an exploratory approach: **Semi-structured expert interviews**
- **Pretesting phase** to ensure adequate wording and question order
- Respondents were interviewed about factors related to (1) **marketing mix**, (2) **R&D process** and (3) **management and organization**, that foster or inhibit business success in emerging markets

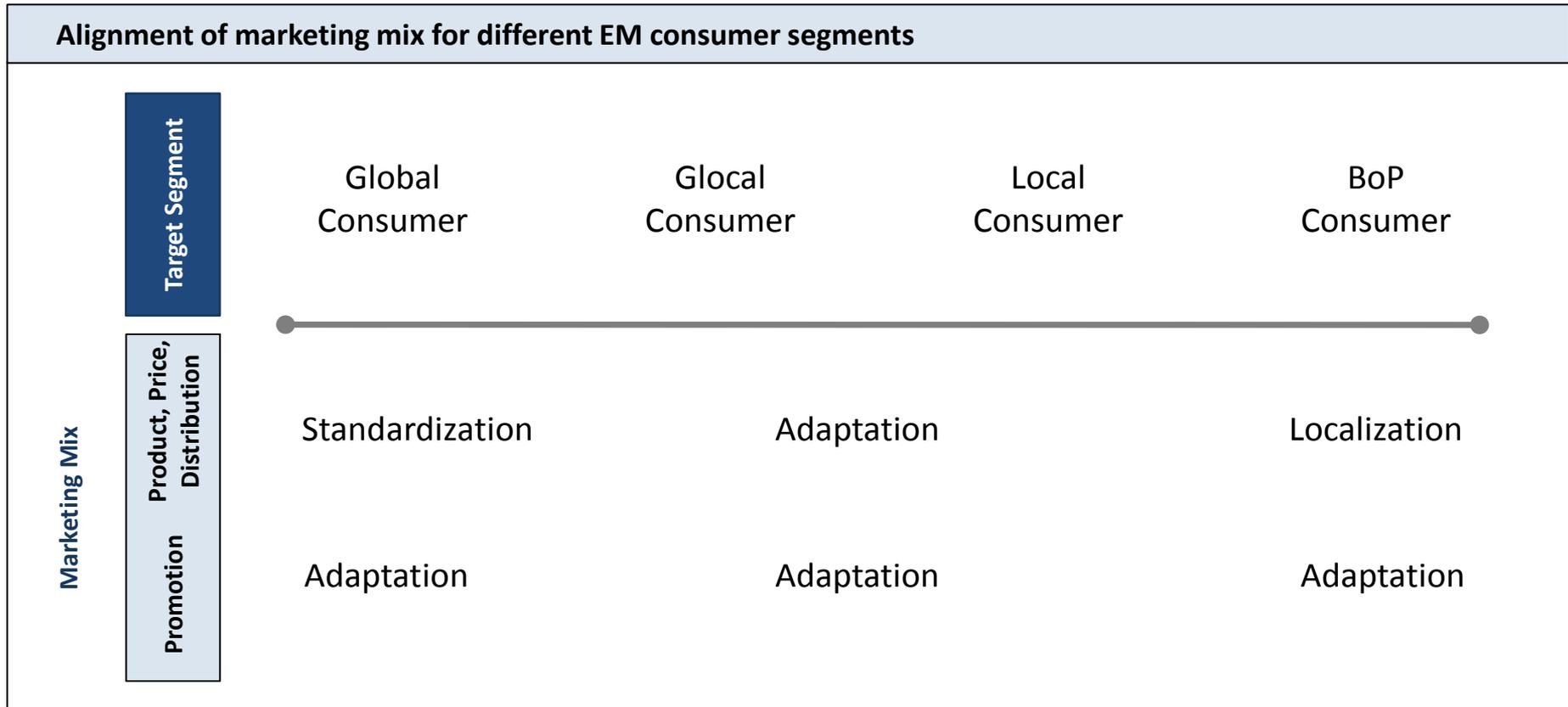
Sample

- **8 marketing and management experts** from multiple backgrounds (see table)
- **Mid-and senior level** management positions in MNCs
- **2-20 years** of experience in various markets (e.g. China, India, Sri Lanka, Indonesia, Vietnam, Uganda, South Africa, Europe, Russia, U.S.A, South and Central America)

The data collection resulted in ~ 600 minutes of digitally recorded audio data respectively 124 single-spaced DIN A4 pages of interview transcripts

Industry	Function
Sportswear	Global product category manager
Automotive	Head of marketing services and product planning
Health care	Internal consultant and management trainer
FMCG, health care	Head of product development
Renewable energies	Founder and CEO
FMCG	International marketing manager
Agriculture	Managing director
Telecommunications	Head of international marketing and sales

(1) Marketing mix related insights: Emerging markets require a radical rethinking when seeking to align the local marketing mix



- The ,lower‘ the target segment in the consumer pyramid, the higher the need to adapt – respectively localize (thus, design from scratch) – the marketing mix
- BoP consumers demand a **radical localization** of product, price, and distribution strategy
- Universal need of **adaptation of promotion activities** across all consumer segments in emerging markets

(1) Marketing mix related insights: Experts named numerous tools which can be used by managers to localize product and pricing strategies

1. Localized product strategy

Tool	Example
Extremely high efficiency/functionality	<u>Health care</u> : “Mass production Techniques” in surgery to improve resource efficiency and procedural routine
Disruptiveness/radicalness	<u>Water purification</u> : Extremely cost effective purifier using waste from rice cooking as filter
Human touch	<u>Financial Services</u> : Adding human intermediaries from the community, that provide additional services and support, increasing acceptance for the offering
Reusability	<u>Medical Dosing</u> : Designing medical devices against asthma for reuse
Scalability/Platform approach	<u>Software Platforms</u> : Easily adaptable design (to different requirements) and integration of up-scaling features to enhance future functionality, extend product lifecycles
Simplicity	<u>Agricultural Services</u> : Database for agricultural information, available through very native Android application

2. Localized pricing strategy

Tool	Example
Small packaging units	<u>Washing powder</u> : Sold in individually wrapped tablets instead of whole box
Radical innovation	<u>Water purifier</u> : Cost effectiveness through use of free components
Cross subsidy	<u>Health care</u> : Premium consumers cross-subsidize services for BoP consumers by paying for extra services (e.g. single bed room)
Reusability	<u>Medical Dosing</u> : Reusability of appliances
Infrastructure sharing	<u>Shared Telecom Tower Approach</u> : Shared use of networks and common infrastructure
Customer empowerment	<u>Telecommunications</u> : Allowing customers to participate in profits by empowering them to set up own entrepreneurial ventures (e.g. distributors of firms’ products and services)
Scalability/Platform approach	<u>Software Platforms</u> : Mass production and integration of up-scaling features to achieve scale effects and extend product lifecycles
Simplicity	<u>W-Lan Router</u> : Radical reduction of product features

- Localized offerings at very low prices ensure **affordability** for lower-end consumer segments
- Overlaps in the offering- and pricing-related tool sets for strategy localization entail great **synergy effects**

(1) Marketing mix related insights: Localized offerings should be supported by an adequately tailored distribution and promotion strategy

3. Localized distribution strategy

Atomized distribution model

- Targeting low-end consumer segments in geographically dispersed areas through the **integration** of local communities/ individual consumers into the distribution process
- **Highly dispersed** channel structures
- E.g. Coca-Cola's Village Women Program (beverages-selling out of private kitchens), Avon Women or Unilever Shakti Women



4. Adapted promotion strategy

- Adaptation of marketing communication in **all existing consumer segments** to account for distinct conditions and environments of emerging markets
- Usage of available tools/channels as well as **innovative promotion strategies** (e.g. encourage local community members to share product experiences and to provide product demonstrations)
- Focus on building **strong brand presence** to make use of potential first-mover related loyalty effects

EM specific marketing mix

The **adaptation** of marketing communication to local requirements, a **strong brand presence** and a distinct **localization** of offering, pricing and distribution are the underlying marketing mix related strategies, that enable firms to target the promising lower-end consumer segments in emerging markets

(2) R&D process related insights: The specific conditions in EMs require the installation of local, decentralized and open R&D processes

Design of the R&D process in emerging markets

- R&D process managed and led by **decentralized, autonomous** R&D and marketing functions
- **From-scratch marketing research** to get to know the unfamiliar lower-end consumer segments and their contexts in-depth
- Intensive **observation of consumers** and **open innovation**

Voices from the experts

“We talk a lot – we talk to strangers and we talk to everybody and we seek a lot of opinions. [...] We receive a lot of information and that is what we and our engineers and marketers need, working on our innovations. [...] you don’t need consultants – you can speak to anyone on the street about your problem and you will receive their opinion and consultancy for free.”

“[...], local market employees should be able to pursue their own ideas to some extent. At least there are some examples for the fact that you have to give employees some freedom to enable them to develop and pursue their own ideas. Subsidiaries thus should not just get their instructions by headquarters, but be something like an equal partner, having some freedom and knowing the local market very well.”

“You get the idea to innovate such a product by observing the customer how he is using an existing product. [...] you see a vendor selling blood samples that should be refrigerated and he carries them in a box of ice on a bicycle. You say: Wait a minute, this man is selling these things on a bike. [...] If he carries blood in an icebox and with the hot weather here, if the ice melts, the blood becomes useless. So you think: Maybe if I can offer this man a little refrigerated van to carry blood samples, I think I can save far more lives. So in the end you come up with a small, refrigerated van that can take blood samples to small hospitals in areas that are difficult to access otherwise.”

(3) Management and organization related insights: An acentric organization structure helps MNCs to win both on a local and a global level

Organization design

Acentric organization structure

- Local decentralized marketing and R&D functions with high degrees of autonomy (**Local Growth Teams**)
- High degrees of **internal embeddedness** (ongoing collaboration and exchange of information, knowledge, personnel and technologies among sister subsidiaries or between headquarters and subsidiaries)
- High degrees of **external embeddedness** (the manner and extent of relationships with local business partners, competitors, institutions, communities, non-governmental organizations and consumers)

How
to get
there

Managers should...

- ...install local business units with high degrees of decision making authority
- ...install local teams to build on local expertise and relationships and initiate/incentivize broad, intensive relationship building with local partners
- ...build high internal awareness for emerging market business units
- ...enable intra-organizational exchange through platform and channel building (e.g. idea platforms or instant messaging)
- ...emphasize personal interaction and initiate/support the establishment of frequent periodical meetings
- ... decrease travel restrictions where possible

Through an acentricly organized network structure, MNCs can make use of the full potential of their widespread subsidiary network, source knowledge and technology from all around the world and **leverage emerging market subsidiaries as incubators** for innovations, which can be taken global over time (reverse innovation)

(3) Management and organization related insights: Two additional building blocks help MNCs to win both on a local and a global level

Strategic orientation

- **Long-term commitment** towards individual emerging market projects and venture as a whole by both local and head quarter based management

Organization culture

- **Democratic** leadership style
- **Flat hierarchies**
- Overall culture to foster close interaction between leaders and employees as well as open discussion and **communication flow**
- Strong focus on value system to create common identity

The three explored management and organization related **building blocks** (1) acentric organization design, (2) long-term strategic orientation and (3) democratic and open organization culture **create an environment** in which the R&D process can yield effective results with regard to the **adequate tailoring** of the marketing mix for emerging market consumers

The findings from this study result in five major managerial implications to be considered in detail

Implication 1

MNCs' **product, pricing and distribution** strategies in emerging markets should be heavily **localized** to account for these markets' distinct requirements and to meet the specific needs of lower-end consumer segments.

Implication 2

Localizing their firm's strategy, managers should **make use of tools** such as simplicity, reusability, scalability, customer empowerment, radical innovation, and atomized distribution to ensure affordability and availability of offerings.

Implication 3

An **adapted marketing communication** is a necessary precondition in all consumer segments in emerging markets to account for differences in preferences as well as the lack of marketing infrastructure.

Implication 4

The **R&D process** in EMs should be led by **decentralized, autonomous** R&D and marketing functions that carry out from-scratch marketing research characterized by intensive consumer observation and open innovation.

Implication 5

Managers must seek to create an organizational structure and environment, that enables intensive and ongoing **intra-organizational collaboration and exchange** of information, knowledge, personnel, and technologies.

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If you are interested in further information or have any questions, please contact us at:

Institute for Market-Oriented Management
University of Mannheim
L5, 1
68131 Mannheim / Germany
Phone: 0621 / 181-2388
E-Mail: marketing3@bwl.uni-mannheim.de

or visit our website at: www.imu-mannheim.de.

The Authors:

Prof. Dr. Sabine Kuester holds the chair of Marketing III at the University of Mannheim. She is also Director of the Institute of Market-Oriented Management and Academic Director of the Mannheim MBA Program at the Mannheim Business School.

Sergej von Janda, M.Sc. is a doctoral student at the Chair of Marketing III.

Dr. Monika Schuhmacher, MBA is assistant professor at the chair of Marketing III and member of the advisory board of study affairs at the University of Mannheim.