Factors to be considered for market segmentation

ASSIGN BUSTER

This section reviews the literature related to various key deliverables identified for this dissertation. The main deliverables of this projects are developing a growth strategy to expand in domestic as well as international market and identifying the potential location for a cross dock or a warehouse. This section is divided in six parts, first part gives idea about the grocery market, in second part key elements and approaches of strategic management are discussed, third part looks at factors to be considered for market segmentation and market attractiveness, in fourth section a survey conducted by Lawson Software on growth strategies adopted by distributors discussed , in fifth part export expansion strategies are reviewed and last part overviews warehouse/ depot location problem and approaches to identifying new depot.

2. 2 Grocery Market Overview

Grocery market can be divided in two main categories one is grocery retailing and other is grocery wholesaling. Eden farm is a wholesale distributor supplying frozen food and ice cream to wholesalers as well as convenience store, hence understanding structure of both the market segment is important.

2. 2. 1 Grocery Retailing

The UK grocery retail market is considered to be oligopolistic as there are so many players and competition is fierce to earn the market share and customer loyalty. The following diagram shows that the retail industry has grown consistently at 3 – 5% to the present value of £ 146. 3bn (IGD website, 2010).

D: Business Projectfrozen food – eden farmliterature reviewpaintmarket performance. JPG

The retail market is dominated by superstores, supermarkets and hypermarkets operated by big retailers such as Tesco, Asda, Sainsbury's and co ops, which enjoy more than 70% market share. Convenience retailing has c21% market share which is mainly dominated by symbol groups. The following diagram shows the overall structure of the retail market.

D: Business Projectfrozen food – eden farmliterature reviewpaintuk retail structure. JPG

2. 2. 2 Grocery Wholesaling

Wholesalers supply goods to small retailers who cannot directly reach to the manufactures. Wholesalers also support retailers by offering other services like store design and management, delivery and distribution services. Grocery wholesaling is mainly divided in two groups, first is cash and carry service where the retailer visits the large warehouse and picks the items he needs and the second is delivered wholesale where the retailer orders the items over phone or on the internet and receives the order at his store. The total wholesale business is c£18. 3bn (IGD website, 2010). The following chart shows the growth of cash & carries and delivered wholesale in last ten years.

D: Business Projectfrozen food – eden farmliterature reviewpaintcash and carry. JPG

A research conducted by Quinn and Sparks (2007) on evolution of grocery wholesaling and wholesalers since the 1930s in UK and Ireland observed that the research on grocery wholesaling is almost non-existent.

2. 3 Strategy- what is it?

Strategy word is used by many people day to day in different context and has become a catchall (Hambrick and Fredrickson, 2001). Carpenter and Sanders (2009) defines strategy in simple terms as " Strategy is the coordinated means by which an organization pursues its goals and objectives" (Carpenter and Sanders, 2009). This simple definition emphasizes on actions that are either taken or needs to be taken or planned to achieve the company objectives. Hambrick and Fredrickson (2001) supports above definition by mentioning that strategy should integrate internal and external orientation to achieve firm objectives. The following diagram clearly separates strategy from company mission and objectives.

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Strategy should address how the firm will achieve the set objective. For Eden Farm the objective is to achieve profitable sales increase by £20 million in next five years.

2. 3. 1 Strategic Analysis

Michel Porter (1996) argues that strategy is not about achieving operational effectiveness (OE). Porter defines operational effectiveness as doing identical activities in a superior way than the competitor. The reason he says that OE cannot be a strategy is that rivals can easily copy the operational

improvements and match the performance levels. He further mentions that operational effectiveness and strategy should go hand in hand to achieve the top performance which is the main goal of any firm. Doing benchmarking makes rivals look alike, so the heart of strategy lies in doing the activities in a way different than others. This highlights the importance of competitive advantage, which is defined by Carpenters and Saunders (2009) as “ A firm’s ability to create value in a way that its rivals cannot”. Porter (1980) suggested that competitive advantage can be achieved by firms by either positioning itself in an attractive industry or devising strategies which can make the existing industry more attractive. He suggested Five Forces framework to analyze the industry structure and identify the sources of competitive advantage among these forces and then positioning the firm to achieve an edge over rivals. Barney (1991) argues to achieve sustained competitive advantage firm should have resources and capabilities which are valuable, rare, inimitable, non substitutable and rare (VRINE), this school of thought is called resource based view (RBV). A third school of thought focuses dynamic conditions and argues that RBV has limitations in fast changing environment and competitive advantage is achieved by firms by continuously configuring its resources.

Carpenter and Sanders(2009) clubs these three perspectives together as shown in the diagram below and suggests that competitive advantage is not long lasting and firm needs to continuously look back and analyze how they achieved this position and predict competitive landscape in future to influence it.

D: Business Projectfrozen food – eden farmliterature reviewpaintcompetitive advantage. png

2. 3. 1. 1 External Analysis – Industry Analysis using Porter's Five Forces

External analysis forms a very important part on strategic analysis. The external environment can be divided into two groups as macro and micro environment. To analyze macro environment PESTEL tool is used which is acronym for Political, Economical, Socio cultural, Technological, Environmental and Legal analysis. This analysis is more useful when companies plan to expand internationally and enter into new countries. For Eden Farm being a distributor of frozen food, PESTEL analysis is not more appropriate as the firm does not foresee it establishing a base in other country and is focusing direct export only. (Carpenter and Sanders, pp 133-135, 2009)

Micro analysis focuses on analyzing industry structure using five forces model developed by Porter(1979). The model suggest that in any industry a strategic analysis should look at buyer and supplier power, competition among the players in the industry, analysis of threat posed by substitute products or services and understand the entry barriers for new entrants. Porter mentions that depending on the industry the power of each force varies, but it is the cumulative strength of these forces which drive the profitability of the particular industry.

The following diagram shows the Porter's five forces model.

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Above diagram shows in detail the factors contributing towards each market force, managers should give due attention to each point shown below to draw appropriate conclusion for developing the strategy. Porter argues if these forces are weak then companies can achieve very good performance and adds, it is the strongest force among these forces which decides the overall profit potential of the industry and managers needs to give due attention to this strong force while formulating the strategy. Carpenter and Sanders(2009) added complementors as the sixth force to the five forces model and argues that complementors are those factors which help to increase the sales of the firm and increase profits. When understanding the industry structure Porter (2008) emphasizes importance of defining the industry boundaries, defining boundaries too broadly loses the focus and managers become unable to see the real competition and defining industry boundaries narrowly misses the similarities in product groups or potential markets which are crucial for competitive advantage.

2. 3. 1. 2 Internal Analysis – A Resource Based View (RBV)

Jay Barney (1991) suggested that firms should focus on internal strengths to exploit the opportunities in the market and defuse the effect of external threats and mitigate the weaknesses. The diagram below splits the SWOT analysis in two parts, one is internal analysis which focuses on firm’s resources and the second is external analysis which classifies industry attractiveness.

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Barney (1991) argues that proponents of environmental model (Caves & Porter 1977, Porter 1980, 1985) have assumed that in an industry firms possess similar resources and heterogeneity in the industry is cannot stay for longer as resources are same, however supporters of resource based model (Penrose, 1958; Rumelt 1984; Wernerfelt, 1984, 1989) believes that firms do possess heterogeneous resources of strategic importance and that this difference of resources can last longer. Barney (1991, 1995) states that to achieve the sustained competitive advantage firms need to employ value creating strategies in a way that no other firm can reproduce it and mentions that it can be possible when a firm have resources which are heterogeneous and immobile. To be the source of competitive advantage resources needs to fulfill criteria of being valuable, rare, inimitable and non substitutability. Valuable resources are those which enable companies to develop strategies which improve efficiencies and effectiveness to reduce the cost, resulting into exploiting opportunities and defusing threats (Barney 1991, 1995; Collins and Montgomery, 1995). Barney mentions that firms having resources which fulfill four criteria's should be in a position to exploit them to achieve the sustained advantage. Wernerfelt (1984) highlights customer loyalty as a source of competitive advantage. Collins and Montgomery (1995) mention that inimitability of the firm resources can be because the firm has unique physical location, a strong brand image or casual ambiguity about the source of such advantage.

2. 3. 1. 3 Dynamic Environment Analysis

Despite its popularity resource based view (RBV) has been criticized by some authors because it does not explain how firms achieve relevant resources for dynamic markets. Mosakowski and Mckelvey (1997), Priem and Butler (2000) and Williamson (1990) argues that RBV is unclear and tautological and fails to explain the mechanism by which resources contributes towards achieving competitive advantage. Teece and Pisano (1994) coined a new terminology of dynamic capabilities; the word ‘ dynamic’ refers to the ability to reconfiguring competencies in this fast paced continuously changing world and the term “ capability focuses on strategic management’s role in adapting, integrating and reconfiguring skills, resources and functional competences to fulfill requirements of a changing world” (Teece and Pisano, 1994) . Eisenhardt and Martin (2000) observed that dynamic capabilities exhibit three main characteristics; firstly dynamic capabilities include certain value creating strategic processes which can be influenced to create new strategies to win in the dynamic market. Second observation is that dynamic capabilities are the best practices in an industry supported by extensive empirical resources hence they are homogeneous in nature which is opposite of the RBV’s assumptions. Third observation is that dynamic capabilities demonstrates different patterns in different market conditions, they are complicated and analytical in stable market conditions because the knowledge is established and detail analysis is required for getting new insights and in dynamic market conditions they are simple processes relying on quick execution as the knowledge is limited about specific situations and experiments needs to be done on a more frequent basis to keep the firm ahead of the competition. Eisenhardt and Martin (2000) states that dynamic

capabilities are necessary to continuously reconfigure resources and the competitive advantage is achieved by newly configured resources. Dynamic capabilities are means to achieve the competitive advantage; they are not competitive advantage in themselves. A firm's ability alliance, developing new products and strategic decision making are some of the examples of dynamic capabilities (Eisenhardt and Martin, 2000).

2. 3. 2 Strategy Formulation using Strategy Diamond

Hambrick and Fredrickson (2001) states that there are various tools available to analyze internal and external environment but there is no guidance what the output of these analysis should be and how to formulate a strategy. Strategy should highlight how the company will achieve its goals by integrating internal and external analysis. A strategy diamond model is proposed by Hambrick and Fredrickson (2001) to help formulate a coherent strategy which contains five elements namely arena, vehicles, differentiators, staging and economic logic. The diamond is shown below.

D: Business Projectfrozen food – eden farmliterature reviewpaintDiamond. png

Arenas is the first element of the strategy diamond which demands strategist to answer fundamental question about what are the areas the business will be focusing its attention and the amount of efforts put in these areas. Managers need to clearly define which products, channels, market segments and geographic location will be targeted. Vehicles are the means to enter the arenas chosen. Deciding appropriate vehicles is of strategic importance. A firm can decide to develop organically, may decide to form a joint venture or

may acquire the business of existing player in the targeted arena. A firm can use one or combination of these different vehicles to penetrate arenas. Each vehicle has its positive and negative implications depending upon the market dynamics and manager should give due considerations to these implications. After deciding arenas and vehicles strategist should answer the question as how the company will win the customers in targeted markets. Knowing why customers chose the firm over its competitors can help strategist to identify differentiators. Differentiators can be company image, its ability to customize products, price and location advantage, quality and reliability of the service provided. Hambrick and Fredrickson (2001) state that to achieve a competitive advantage a firm does not need to have very special in one of the above mentioned dimension but having a combination of these dimensions which are mutually reinforcing can give the firm a strong position in the market. Creating differentiators is very important task top management should because without them a firm may lose its market position soon. Staging is the forth stage towards forming a good strategy and asks mangers to sequence the actions decided in the first three elements. Staging process depends on many factors such as resources required carrying out the task, sometimes business need to respond quickly to grab opportunities available, in such situations urgency in taking actions is critical, achieving credibility is very important for attracting resources and stakeholders and lastly wining early in the strategy implementation phase is important. All the above mentioned factors needs to be given due consideration. Finally managers should look at the economic logic before finalizing any strategy; the business should be able to achieve profit above its cost of capital. Hambrick and Fredrickson (2001) states that, “ the most

successful strategies have a central economic logic that serves as the fulcrum for profit creation”. Hambrick and Fredrickson (2001) emphasis that together with strategic analysis and addressing the five elements of the strategic diamond a firm can develop a sound strategy for achieving the competitive advantage.

2. 4. Market segmentation and attractiveness

Segmenting the market to identify the needs of the customer groups and accessing attractiveness is very important to develop a growth plan. Kotler (1993, p. 263) defines “ Market segmentation is the act of dividing a market into distinct groups of buyers who might require separate products and/or marketing mix”. Smith (1956) suggests that segmentation help companies to align product offering to different customer needs. Dibb (1995) suggested a matrix to help firms to identify which market segments to target, the matrix is called Segment Evaluation Matrix (SEM) which consist three step approach as defining segments, targeting and positioning. In the first stage, defining segments, many authors (Haley, 1968; McDonald and Goldman, 1979; Johnson and Flodhammer, 1980; Brow, Shivashankar and Brucker, 1989) have suggested a need for appropriate base. Segmentation of customers should be done considering homogeneous needs of the group by a suitable base. Targeting involves focusing resources on identified segments; this is achieved by considering market conditions, competition, availability of firm’s resources and customer needs. Positioning is the final stage which asks to develop marketing plans keeping 4P’s (product, price, promotion and place) in mind to attract the targeted customers.

Porter (1996) proposes three types of positioning choices for a firm, first is variety- based positioning which focuses on products or services offered by the firm rather than segmenting customers, this is suitable for firms able to produce products or services using distinguishing sets of activities. Second type is need- based positioning which require grouping customers on the basis of needs. This is particularly suitable when each identified group has differing needs like different products, service level and supported needed. Third type is access – based positioning which focuses on different modes to reach customers having similar needs like other customers.

Geographic location or customer scales are two examples which require different set of activities to reach the customers. Wind and Cardoza (1974) observed that many companies formulate segments based on intuition, Doyle et. al (1986) supports above finding by stating that key decision makers misunderstand importance of segmentation process. Kotler (1991) offers guidelines for segmentation by stating that they should be measurable, substantial, accessible and accountable. Halvacek and Reddy (1986) have developed a three step market segmentation model consisting of identification, qualification and attractiveness which is the basis for Dibb’s (1995) Segment Evaluation Matrix (SEM). Hlavacek and Reddy (1986) suggests guidelines for segment qualification which highlights segmentation based on common needs and measurable characteristics, identifying the competition, similar distribution channel for each segment and defined communication channel for each segment. Study conducted by Abratt (1993) identified segment attractiveness criteria as

“ Ability to reach buyers in market

Competitive position in market

Size of market

Compatibility of market with objectives/ resources; and

Expected market growth” (Dibb, 1995)

Dibb (1999) categories segment attractiveness in four major categories as market factors, economic and technical factors, competitive factors and environmental factors which are as shown below in the diagram.

segment attractivness 1

Dibb (1995) suggests that for developing a marketing strategy analysis can be done on the basis of different markets, segments in the same market which can give lot of insights. Market segmentation encourage firms to do competitor and customer resulting into more focused approach in terms of offering products or services and improved responsiveness. As suggested by Dibb (1995) a matrix can be used to summarize the findings of the analysis as shown in the diagram.

segment attractivness

The matrix approach gives a holistic view of the portfolio of all segments and helps companies prioritize actions and develop strategy accordingly for each segment.

2. 5 Growth Strategies for Wholesale Distribution

Ansoff (1957) suggested a tool to help companies decide their product and market growth strategies. The matrix suggests four growth strategies as shown in the diagram below.

D: Business Projectfrozen food – eden farmliterature reviewpaintAnsoff. JPG

For existing products Ansoff (1957) suggest market penetration and market development strategies. For new products product development and diversification strategy is suggested.

Lawson software in 2007 conducted a survey of 1274 wholesale distributors operating in three regions North America, Europe and Australia and New Zealand to find out what strategies and tactics wholesale distributors in these regions will adopt to achieve targeted growth and find out similarities and differences in the strategic choices in different regions. The participants were picked from different industries such as industrial spare parts, consumer goods, building material and food service. 70% of the participant view existing customers as the main source of growth. Following diagram shows results for three regions.

D: Business Projectfrozen food – eden farmliterature reviewpaintlawson 1 current customers. png

2. 5. 1 Selling more to existing customers

In Europe executives of food service distribution think that 41 % of the sales from current customer will come from selling existing products more, 46% sales would result from selling new products and offering fee based value

adding services will improve 12% sales. The following diagram shows results from different industries in Europe and North America. Europe is more optimistic about charging customers for offering value adding services.

D: Business Projectfrozen food – eden farmliterature reviewpaintcurrent customers. png

2. 5. 2. Adding New Customers

The survey found that majority of the distributors are focusing on current geographic locations to identify new customers, 78% foodservice distributors are focusing on new customers in the current geographic locations, only 22% sales expected from customers in new geographic locations .

D: Business Projectfrozen food – eden farmliterature reviewpaintNEW CUSTOMERS. png

Targeting new customers in current geographic areas is challenging because they already have preferred suppliers and to win these customers distributors need to offer better service and performance. A good sales management is needed to avoid winning new customers with low gross margins than current customers.

2. 5. 3. Organic or Growth by Acquisition

The survey tried to find growth strategies adopted by distributors. More than sixty percent respondent considers organic growth as the means to improve current operations. Sixteen percent in Europe consider acquisition as a growth strategy. The diagram below shows results of the three regions.

D: Business Projectfrozen food – eden farmliterature reviewpaintgrowth strategy. png

All the above findings suggest that wholesale distributors are focusing market penetration and market development strategies as explained by Ansoff's growthmatrix.

2. 6 Export Market Expansion Strategies

When small and medium sized firms want to go in international market , exporting is the most popular route adopted to enter, penetrate and develop foreign market because it is less risky and impact on domestic operational resources are limited (Katsikea et. al., 2005).

Firm's willingness and propensity and its actual capacity are the two main factors which determine a firm's decision to initiate and maintain exporting determination. According to Cavusgil and Zou (1994) when a firm decides to engage in export activity the most critical decision they need to take is about market expansion strategy. The strategy includes identification, analyzing and selecting export markets and deciding number of markets to target. Lages and Montgomery (2004) conducted a survey of 400 export managers and found that export performance of a firm depends on firm commitment and the way strategy is formed. Designing an export strategy for a firm has attracted many researchers, contributing conceptually and empirically. Ayal and Zif (1979) and Lee and Yang (1990) suggested that export market expansion is considered as a firms strategic decision to expand export business by allocating firm's marketing resources to identified markets.

According to Katsikeas and Leonidou (1996) exporting literature has identified two main marketing strategies as market concentration and market spreading. Katsikeas and Leonidou (1996) defines “ market concentration as the firm’s strategic focus on and allocation of export operations in certain carefully selected export markets” and “ market spreading as exporting to as many markets as possible with no particular focus on specific export markets”. The main difference between these two strategies lies in the speed of expansion in export markets.

Ayal and Zif (1979) argues that in long term both strategies end up serving almost same number of export markets. Studies conducted by many authors (e. g. BETRO Trust Committee, 1976; Tessler, 1977, Fenwick and Amine, 1979) between 1975 and 1985 suggest market concentration strategy should be adopted because by focusing small number of markets a firm can achieve high market share resulting in long term profitability. Studies conducted by Hammermesh et. al (1978), Hirsch and Lev (1973) and Lee and Yang (1990) support market spreading strategy as it can exploit limited market share in many markets while reducing market related risk and gain higher profits . A contingency approach has been suggested by authors like Ayal and Zif (1979), Fenwick and Amine (1979) and Piercy (1982) which says that export strategy depends on company products, targeted markets and factors specific to the firm. Following table shows clear difference in two strategies as suggested by Katsikeas et. al. (2005).

D: Business Projectfrozen food – eden farmliterature reviewpaintconcentration vs spreading. png

Katsikeas and Leonidou (1996) identified certain characteristics of the exporting organization such as experience of exporting help management to minimize the perceived uncertainty associated with overseas market and operation. Marketing efforts and policy variables which include developing market entry and customer selection criteria (Samiee and Walters 1990; Bourandas and Halikias 1991), visiting customers frequently, conducting research of export market, play crucial role in shaping behavior of the firm.

A meta-analysis carried by Leonidou et. al. (2002) to identify marketing strategy elements of export performance found that market concentration strategy has a strong positive relation with export performance. The study further observed that export market performance is positively related to market segmentation, product quality, pricing strategy and advertising.

However, Katsikeas et. al. (2005) conducted a research on 1000 British small and medium size exporting manufacturers and concluded that market spreading strategy results in long term profitability and the firm achieves valuable knowledge and skills to deal with different markets and develops a very strong sales team.

Leonidou (2003) suggests that export business should be considered as overseas customer relationship management which is a process of establishing, developing and sustaining relations in export markets and this process should be monitored for its effective implementation.

2. 7 Determining Distribution Location

One of the most important strategic decisions is to identify the location of depot for supplying the products to customer on time every time. When

entering into new geographic location a company needs to design its complete distribution network. Companies need to improve efficiency of their logistic operations to optimize the flow of goods supplied to customers. When deciding location of distribution system a company need to give due attention to the cost of distribution system and offering a very good service to customers (Perl and Daskin, 1985). These decisions depend on number, size and location of the depot and deciding customers to be served from each depot. In distribution centre (DC) location problem two cost needs attention, one is warehousing cost and the other is distribution cost and the companies always want to find optimum balance between these two to keep costs low. Warehouse cost are divided into fixed and variable cost whereas trunking and delivery cost form transportation costs. Generally in distribution delivery cost is higher and hence lot of research is carried to develop tools to reduce these costs. In supply chain the problem related to DC are more closely related to vehicle routing problem (VRP), Location routing problem (LRP) and warehouse location routing problem (WLRP). The diagram below shows three components of delivery operation namely stem distance, variable running distance and stop time.

D: Business Projectfrozen food – eden farmliterature reviewpaintrouting componet. png

The stem distance is the total distance between depot and first customer plus the distance between last customer and the depot. The stem distance is depends on the depot location. The variable running distance depends on the number of customers being served and determines the cost of delivery. Both stem and variable running distance depends on vehicle routing.

Perl and Daskin (1985) define “ warehouse location routing problem as the problem of solving DC location and vehicle routing problem”. When solving the problem one needs to give attention to various constraints like warehouse and vehicle capacity, route lengths and durations and satisfying all customer requirements. The problem is solved by finding a optimal route to deliver the goods to customers at minimum delivery cost. Each customer is allocated to only one depot. Burns et. al. (1985) considers customer density, demand, value of items, inventory carrying cost and transportation cost per mile to solve the problem. They suggest designing optimal delivery regions to reduce the cost of delivery and then locate the depot. Bednar and Strogmeier (1979) , Nambiar et. al.(1981) and Barreto et. al.(2007) suggest to cluster customers together according to vehicle capacity and maximum distance constraint. Then locate the depot at a location from where all clusters can be served.