BOOK REVIEW

Beating the Commodity Trap – Richard A. D'Aveni

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It was in 1994 that Richard A. D'Aveni through his seminal work 'Hyper Competition' advanced the argument that competitive advantage of companies was becoming unsustainable because of globalization and disruptive technology. Sixteen years on, he finds himself sufficiently vindicated to weigh in with the thesis that many companies today are actually in the grip of a deadly form of competition. He calls it 'commodity trap' and invests it with the potential to disrupt whole industries and drive previously successful firms out of business.

Commodity trap, says the author, can be set by firms' competitors – they would, wouldn't they? – or by themselves. The former happens in any number of ways, manufacture in China, the Walmart effect and off-shoring and outsourcing to low cost countries. But the latter is the more common occurrence. For commodity traps are very much related to how managers act or do not act; the process of entrapment happens mostly when managers fail to innovate, create bad products or deny trends already in motion, says D'Aveni's new book. It proceeds to set out a new way for managers, whether brand managers, product designers or business planners, to recognize the threats to their companies' competitive positions and the opportunities to create new positions.

D'Aveni's broad argument can be summed up as follows: Much as product differentiation is the stuff of competitive strategy of businesses, it is not enough, or, more plausibly, differentiation is a game everyone is playing by offering much the same bells and whistles; to be successful companies must rather constantly identify the lurking commodity traps and find ways and means of reducing and eliminating them. A telling example he mentions is of Harley–Davidson which

missed the intimations of commoditization by fixing its gaze merely on the market share; while it successfully differentiated itself from the Japanese rivals since the late 1980s and announced record revenues in 2003, it faced new competition from its American rivals offering different benefits that also earned higher prices by appealing to changes in consumer base. Not to have done the crucial price-benefit analysis was the reason why Harley-Davidson was unable to spot the signs of the change and the creeping commoditization till 2006.

According to the author, there are three most common patterns in which the commodity trap ensnares companies: one is deterioration, where low-end firms compete with low-cost low-benefit offerings that attract the mass market, causing both prices and benefits of a focal company to go down. The second is proliferation, where companies develop new combinations of prices and unique benefits that attack part of an incumbent's market, leading to prices going up or down, while benefits go up and down in all directions, around a focal firm's products. And the third is escalation where companies offer more benefits for the same or lower price, squeezing everyone's margins. While the book provides a commodity trap checklist to determine whether a company is facing any of these traps, there are many variations on the three themes and a mapping of price versus product benefits would be needed to identify distinctive challenges faced by a company or industry at any time.

The Spanish retailer Zara whose business model has successfully threatened the mass, bridge and diffusion brands by offering better quality and style but at lower prices than other players in the fashion industry figures in the book as a trendsetter of the deterioration trap, presaging the emergence of many such companies in numerous other industries, from plastic goods to insurance companies. D'Aveni puts forward three strategies to confront this version of commodity trap: sidestepping the discounter (by moving upscale, moving away and moving on – the Italian silk industry against low-cost Chinese rivals, Starbucks against Folgers and end runs by Southwest airline's major rivals by focussing on international routes, are all examples); undermining (through reinvention of the value chain like H&M's redesigning of its store formats in order to do better than Zara and redefinition of

price as was done by GE to fight off its lower-priced rivals) and containing (by establishing positions around the low-end discounter as Target did to Walmart's market share with emphasis on design and style over price alone) or controlling ,(by moving customers to an upscale value proposition as Gillette did to its rivals at the price-sensitive low-end by bringing in products like the Sensor which raised the bar at the high end). Within the framework of this strategic approach, D'Aveni has some cautious advice to offer companies: If a company already has a valuable brand, sidestepping may stop deterioration temporarily, but the long-term brand equity may be in jeopardy. As GM realized to its cost in competition with Toyota, flight from confrontation may signal weakness to the competitor and lead it to pursue you more aggressively up the price-benefit line or in other markets.

The second commodity trap, proliferation, occurs when a multiplicity of price-benefit positions disrupt what were once a few broad positions and rivals use those new positions to appropriate market space from broadly positioned incumbents – Sears in retails industry and Holiday Inn in hotel industry have faced such threats. D'Aveni lists three primary ways in which companies seek to manage the threats of proliferation: by selecting the threats carefully in terms of positions or segments; by overwhelming the threats through concentration of resources either sequentially (Microsoft's typical offensive) or simultaneously, and thirdly, by outflanking commoditizing rivals with "creative proliferation of (their) own". The choice of the specific threat-management strategies to meet proliferation, says D'Aveni, depends on the complex balance between ambitions, resources and level of threats. His own advice is that companies must use their resources wisely by narrowing their fronts and conserving their resources and, when necessary, by building critical mass through acquisition and merger.

Escalation, the third commodity trap in D'Aveni's scheme, is where customers get more and more for their money and companies lose their margins – and the dilemma is that no company involved can be the first to blink. In the story of artificial sweeteners D'Avenis finds a copy book illustration of the process at work, with players trying to break out of the cycle before they reach the rock bottom at the low price-high benefit position. On the other hand, the story of Primo, a Fortune 500

US company as related in the book, shows that by leading the way to lower-price and higher-benefit positions through investment in R&D and by outpacing rivals and controlling their movement, a company can hold its own against the rivals. Likewise, Hewlett-Packard found its way out of the escalation trap by choosing to gain the scale and the new technologies it needed to compete through acquisition of Compaq, while IBM, for its part, followed a different approach, selling its PC business to Lenovo, the low cost manufacturer par excellence and deciding to concentrate more on its differentiated IT services and products. D'Aveni shows how Dell which had appeared unstoppable as a low cost high benefit producer of computers today finds itself facing commoditization of its desktops by proliferating products attacking from above through HP, below through Lenovo and from the sides through laptops of diverse manufacturers.

According to the author, the most effective way to escape from the escalation trap is for the threatened company to re-seize the momentum with a 'momentous move'. For that to happen, shifts in consumer needs with change of work and life patterns have to be divined and corresponding changes in primary benefits re-defined. This has occurred in insurance, as evidenced by the success of Geico with its emphasis on branding and new distribution channels that are more customer friendly. Other examples are Allstate and auto insurer Progressive with their sophisticated pricing models. In all these organizational execution is crucial. Other ways to escape the escalation traps are trying to slow or even reverse the momentum towards lower-price and higher-benefit positions. The third approach is to use the momentum to drive and control escalation, forcing others 'to race to keep up', as ITT did by lowering prices, improving performance and expanding the market for its military night-vision goggles. Apple has similarly harnessed the momentum of escalation in launching successive generations of iPods, reducing price and increasing the primary benefits, thereby deterring a host of entrants that might have tried to initiate the iPod. All these examples notwithstanding, however, the author warns that the battles are never won permanently; no matter which momentum strategy you select, escalation will return owing to "changes in technology, disruptive competitors and entrants, or shifting customer needs".

D'Aveni proceeds to consider how companies could find their best competitive position in the context of commodity traps. His research on repositioning of the restaurants in the New York city hotels of a US hotel firm had shown him that hard analysis plus the willingness to adapt to the findings was the way to approaching commodity traps and to anticipate the way the market was moving in terms of the relative importance of different benefits like locations, cuisines or experiences. So, by looking at different benefits in more detail and understanding how they are changing over time, it is possible to gain deeper insights into the opportunities that may exist to defeat commodity traps when using various strategies like containing and sidestepping. Such analysis can help identity the right value proposition by benchmarking prices and benefits against competitors within the same segment and help set R&D priorities so that product development is focused on what customers are willing to pay for, not now but in the future. That is to say, the strategy followed by Apple in respect of iPod – extending the lifespan of a prestige product by timing the introduction of new features. In particular, companies have to create the customer benefits desired in different segments or markets they wish to enter as part of an overall containment or outflanking strategy and sequence the benefits being produced by R&D sp as to enable efforts to avoid, undermine or overwhelm rivals driving commoditization in the market.

D'Aveni points out the paradox of new products and services being the source of tremendous growth for companies, while failure rates for newly launched products are as high as 50 percent or more. He quotes two analysts, Ogawa and Piller, to the effect that traditional marketing approaches such as focus groups and even quantitative research have serious limitations in that these tools are based on customers' stated intentions rather than actual purchasing behaviour. And even the best managers do not do a very good job of finding distinctive positions on the price-benefit map by offering benefits that customers are willing to pay for, rather than imitating and moving to crowded positions. Visualizing price-benefit positioning is a serious challenge, says the author, adding that displaying your price-benefit position in a convincing and accurate way can be a powerful tool to develop better products and price-benefit positioning strategies that justify premium prices and encourage increased purchases by customers. The same products will

products will be positioned very differently when plotted on a graph of price versus one attribute or other – the results can be used to reposition a company's product line to fit the desired or correct customer segment, as the case may be.

D'Aveni's conclusion is that "by using the price-benefit analysis" (which he describes in detail in the appendix) and "good managerial judgement to anticipate the different commodity traps and opportunities created by them, executives can stay one step ahead". But he adds, in rather a startling throwaway line, "In the end, it is up to you. Anticipate the trap. Escape the trap. Turn the trap to your advantage. Or get trapped. It's your choice".

Reading this book, with its urgent eloquence on the pestilential nature of commoditization, I was reminded of the incisive pronouncement of Clayton Christensen of Harvard Business School that perfecting of technology by a well-managed company catering to its best customers leaves it vulnerable to disruption by a cheaper, scrappier alternative that is good enough for everyone else. In pointing out the universal nature of commoditization and in offering insights into business strategies needed to grapple with it, the book addresses lucidly what is indeed a governing concern of strategy and marketing at the present time. The case it makes for bringing rigour into the understanding of price-benefit relationships is persuasive, especially when the author calls for old-fashioned managerial intuition and up-to-date experience into the equation. For another, the various industry examples mentioned in the book add great value to its content.

Business strategy and marketing are areas criss-crossed by well-trodden paths. So the scope for innovative approaches as such is limited. D'Aveni's book largely follows the usual pattern of putting together ideas and approaches figuring in the copious literature that exists. Not to speak of the exegeses on a standard work like International Marketing by Hans Muhlbacher and associates or Strategic Management by Burgelman and associates would be seen to contain or anticipate much of D'Aveni's basic argument. That is par for the course, given the saying that marketing could be taught in a day but needs a life time to learn.

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