Strategic responses to market changes

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Abstract This paper sets out to answer a simple question: How might companies in medical markets create better marketing strategies? It is an overview of the author's PhD Research at Cranfield University under the supervision of Professor Malcolm McDonald, one of the world's leading authorities in the field of marketing strategy. Reflecting the author's industry background, this research concerns itself only with medical markets such as Pharmaceuticals, Medical Devices and Diagnostics and reflects primary research in approximately 60 companies in the medical products sector.

INTRODUCTION

Strategy is the sustained pattern of resource allocation by which companies align themselves effectively to their external environment. Hence, a useful place to start is to consider the macro-environmental context in which industry finds itself. This is a period of unparalleled change, driven by factors such as genomics, information technology, demographics, health economics and globalisation. Each of these factors individually would call for a considered response from the industry, but taken together they represent a fundamental change in the market environment. This implies a concomitant fundamental response by the industry. Traditional incremental changes to the way we do business risk is akin to rearranging the deckchairs on the Titanic. The thrust of this paper is that such a fundamental response ought to include a review of how business processes work and in particular, the process by which resources are allocated.

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In order to consider how businesses work, it is useful to remember that most businesses actually involve only four fundamental processes:

- The product development process, by which new value propositions are conceived and turned into something deliverable.
- The supply chain process, by which the businesses procure, manufacture and supply those value propositions.
- The customer relationship management process, by which customer relationships are built and maintained.
- The strategy making process, from where the limited resources, between internal processes and external customer groups, are allocated.

Of these four, the last, strategy making is the most fundamental for two reasons. First, all of the other three processes depend on it; if resources are not allocated appropriately, a business cannot invent, make or sell adequately. Secondly, strategy making is the only one of the four business processes that cannot be sub-contracted or out-sourced in some way. It is the basis of all sustainable competitive advantage. In the fundamentally changed market environment for medical marketers, they must choose to be excellent at strategy making or simply hope that their competitors do not become so.

The first step in choosing to become excellent at strategy making is to agree what excellence looks like. Traditionally, the quality of an organisation's strategy has been judged in terms of its commercial results, yet mountains of research show that this is a poor indicator for two reasons. First, it is a long lag indicator. It typically takes 2–3 years for a strategy to show results, good or bad. By the time a weak strategy shows poor results, the harm is done. Secondly, it is a non-specific indicator. Good performance may result from good strategy, or from weak competitors or fortunate timing. Bad performance can arise from bad strategy or from good strategy combined with bad luck. For both these reasons, current financial performance is a poor measure of current strategy quality. If the strategy making process is to be improved, there is a need an objective, context-independent, measure of strategy quality.

Fortunately, decades of research have produced a strong consensus about what a good marketing strategy looks like. It is beyond the scope of this paper to detail the characteristics of a strong strategy, but the most important may be summarised as:

- Good strategies define one or more target markets each of which is homogeneous in terms of the benefits it seeks. Weak strategies define targets as product groups or sectors, such as clinical specialities. Usually, for instance, the stent market or the cardiology market is heterogeneous in terms of its needs and behaviour.
- Good strategies differ from those of the competition. Weak strategies involve attacking basically the same people with essentially the same proposition. Strong strategies are based on segmentation, targeting and position, which are significantly different from the other major players, thus avoiding head on competition.
- Good strategies minimise risk by avoiding unnecessary diversification in markets or products. Weaker strategies are characterised by multiple targets, small sector shares and commensurately higher levels of business risk that are not justified by higher return. This ignores the truths uncovered by Ansoff in 1965.
- Good strategies leverage distinctive competencies against market opportunities and minimise relative weaknesses in the face of threats. Weak strategies often arise from a weak, incomplete or subjective appreciation of relative strengths and weaknesses.
- Good strategies recognise the implications of macro-environmental changes. Weak strategies are built around today's market conditions or allow for only individual changes in the political, economic, social, legal or technological situation. Strong strategies calculate the implications of each change and, crucially, allow for the combined implications of them all.

Using these and other diagnostic tests of marketing strategy, the Cranfield Research has objectively evaluated the strategy quality in a large number of medical companies, across different sectors, of different sizes and of different market positions. This evaluation clearly shows that many medical companies have sub-optimal strategies and survive only because of the relative incompetence of their competitors.

This begs the obvious question of why are bad strategies made? The research failed to uncover a single marketing director with the deliberate intention of making weak marketing strategy. Instead, the findings are that weak strategy arises from failed strategy making processes, and that strategy making processes typically fail in one of three ways. This is significant, because it allows companies to predict and pre-empt failure in their own strategy making process. The three ways in which strategy making processes fail are:

- They fail to cope with market complexity. For instance, they do not grasp the intricacy of market segmentation, channel structure or competitive forces.
- They fail to cope with the turbulence of the market. For instance, the process is unsuccessful at keeping up with significant changes in customer needs or the macro-environment.
- They clash with the organisational culture. For instance, new habits or systems required to support the strategy making process fail to displace culturally entrenched behaviour.

It is one thing to understand what a good strategy looks like and how strategy making processes fail, and another thing entirely to prevent those process failures in order to create strong strategy. The first step is to understand how companies really make strategy, as opposed to how the text books tell them to, because the two are not the same. In reality, companies make strategy via a hybrid process that is a mixture of three sub-processes:

- Rational planning processes; the formal, often quantitative procedures that make use of analyses and the text book management tools.
- Incremental processes; the combination of experiment, politics and make-it-up-as-you-go-along that often implicitly underlies explicit formal processes.
- Command processes; the centralised, sometimes autocratic manner in which a management team or external head office imposes strategy on sub-ordinate teams.

The Cranfield research found evidence of all three sub-processes in all companies. No companies used a pure process of any type. Companies differed, however, in the ratio of the three sub-processes used. Each company employs a unique blend of the three sub-processes to create its own distinctive strategy making process.

The discovery that each company has its own characteristic strategy making process naturally raises the question of which process is the best. Sadly but predictably, the answer is 'it depends'. No single hybrid of strategy making process was optimal in all cases. Comparing companies with strong strategies to those with weaker strategies, it was clear that the best strategy process (that is, the most appropriate hybrid process) depended on both market conditions and the organisational culture.

In terms of market conditions, two dimensions of the market are critical; market complexity and market turbulence. The research found that in markets that were simple and stable, almost any hybrid strategy making process would create good strategies. Few markets now meet these criteria, however. As markets become more complex, with more segments, competitors or channels, it was found that the strategy process needed to change if it was to create strong strategies. In complex markets strategy processes that were predominantly planning, supported by some command and incrementalism, were needed. In simple, turbulent, markets, heavily command processes worked well, but these failed as the market became more complex. Most challenging of all, complex and turbulent markets required a sophisticated balanced mixture of all three processes.

These market factors partly explain why making strong strategies is so hard in practice. They also explain why simple text book planning often fails. They hint at a sensible approach; understand the level of complexity and turbulence of the specific market and create an appropriate strategy process hybrid. The research found, however, that this is only half the story. Even when the process matched the market conditions, organisational culture was able to sabotage strategy making. To develop good strategy, the strategy making process has to match both the market conditions and the underlying organisational culture. Anyone who has attempted process change in an organisation will point to culture as the primary barrier to change. Predictably, many companies attempt to solve this by trying to change the culture, ignoring masses of research about what culture is and how it works.

Organisational culture is rooted in the core assumptions held by the company about the best way to do business. These core assumptions translate into commonly held values and thence in cultural artefacts, such as systems, structures and habits. It is the artefacts that interfere with strategy making, but the solution lies in the assumptions. Those who attempt culture change often fail to understand its depth and complexity. As a result, two mistakes are made. First, the inertia of the existing organisational culture is often under-estimated. Peter Drucker described culture as 'persistent and pervasive', and lots of research supports this. For example, a large supermarket chain which spent a lot of money and management effort in attempting to create a more customer-oriented culture. Their work was reported in an excellent piece of work by Lloyd Harris and his colleagues at Cardiff University. They interviewed both senior managers and workers at the checkouts. Whilst senior managers claimed widespread cultural change, their sub-ordinates told a different story. To quote: 'Yes, we say things like "have you got your loyalty card" and so on because if we don't we are invited into the boss's office for a chat'. The researchers concluded that what was occurring was not cultural change but, in their words 'resigned behavioural compliance'.

The second problem with culture change is that it risks throwing the baby out with the bathwater. If an organisation has been successful for some time, this implies that its culture has, to some degree at least, been successful in aligning the company to its market. If not, the company and the culture would not have survived. There may be elements of the culture that are not now appropriate to the market and to the strategy making process, but that is not the same as suggesting that the entire culture is at fault. Hence, attempts at wholesale cultural change risks destroying good assumptions, values and artefacts as well as those that need to be changed. The result may be reduced efficiency of internal transactions and unpredictable negative results in many parts of the organisation.

In practice therefore, changing organisational culture is very difficult and sometimes counter-productive. For most middle-managers, it is not an option and good examples almost always involve CEO involvement, long-term commitment and high costs. To make marketing strategy making processes work better, something more practical than wholesale cultural change is needed. Research into successful management of culture suggests that a more effective approach is to gently nudge the natural evolution of the culture by the intelligent use of symbolism by senior managers.

At this point, it is useful to attempt a summary of what has been covered so far. What the research tell us is that many, if not most companies in our industry make relatively weak strategies when judged by an external objective test. They do that not because they are bad managers, but because they just do not have a very good process for doing it. Interestingly, lots of companies are willing to admit that their weaknesses at other management processes, such as logistics or product development or cost control, but they are loathe to admit to being bad at making strategies.

The research gives strong guidance as to how to improve the process to better fit the market. This involves changing the hybrid mixture of strategy processes by enabling or disabling planning, command or incremental sub-processes. Even with a market-suitable strategy making process, however, there remains the issue of cultural hindrance of strategy making and the difficulty of changing persistent and pervasive cultures. All of this suggests why making strategy well is such a rare ability and why, when achieved, it leads to sustainable competitive advantage. What makes strategy making difficult, is the requirement to match strategy process to both the market and the culture at the same time. This difficulty makes it rare and hard to copy essential characteristics of organisational strengths.

So, how can strategy making in medical markets be improved? The research clearly shows that simply changing the process or the culture is not the answer. Instead, the answer lies in a difficult balancing act, which involves optimising both process and culture to the market environment at the same time. In academic parlance, strategy quality is a function of two things, macro-congruence and micro-congruence; where macro congruence is the fit between the external market environment and the strategy making process hybrid and micro-congruence is the fit between that process and the organisational culture. Note, however, that it is not sufficient to achieve either macro-congruence or micro-congruence. Good strategy only occurs when both are achieved. Two examples from the 60 studied so far illustrate this point.

First, a big medical device company operating in a complex stable market. This company has attempted a process change from a heavily command process with a small amount of incrementalism to a more formal planning system. This is an appropriate step, reflecting the fact that their market is more complex than it used to be. Their new process has failed however, to create strong strategy because it is culturally hindered. New systems and structures, necessary to the planning process, are left under-used and dysfunctional, because they clash with the existing, command and incremental oriented, culture. Examples include reporting systems not used and failure to devolve autonomy for research budgets. Ironically, this company has spent a lot of money and management time developing their new planning process, but failed to understand the cultural hindrances. Wholesale change was not necessary, but the key cultural interactions were left unconsidered and unchanged. As a result, their strategy remains weak, undifferentiated from their competitors and with poor targeting.

By contrast, the second example is a 'Big Pharma' company also in a complex but stable market. This company was attempting a similar change towards a more planning oriented strategy making process. The crucial difference, however, was that this company carefully and deliberately considered the cultural implications and set up a parallel cultural change programme. Not overall cultural change, but targeted to those areas and assumptions that were most important in the strategy making process. The outward manifestations of this cultural change programme were very evident and it was clearly well resourced and supported by the top management team. As well as obvious internal marketing efforts, the internal changes included fundamental changes to recruitment, retention and training policies. When the strategy of this company is closely examined against the objective criteria discussed earlier, the quality of the marketing strategy was evident. Clearly defined homogeneous target segments, unique sets of activities in the value proposition, all clearly designed to leverage their well understood strengths and minimise their weaknesses.

To summarise, the combination of macro-environmental changes facing our industry is unparalleled in its history. Medical companies, such as pharmaceuticals, devices, equipment and diagnostics will need to become much more effective than the past. Traditionally, attempts to become more effective have been incremental and focussed on the three traditional stages of the value chain; product development, supply chain or customer relationship management. This will be necessary, but not sufficient to meet the challenge of the future. In addition, medical marketers will need to improve their core process of strategy making. The research shows that medical marketers have not yet mastered these skills. That is not surprising because the barriers to entry to our industry such as technical difficulty, the regulatory regularity environment, the capital and scale issues, have all shielded us from some of the pressures that some other industries have faced. The medical industry has a lot of challenges other industries do not have, but it has been shielded and has not had to get great at strategy making yet.

To become excellent at strategy making, it is necessary to optimise macro- and micro-congruence. To do that, it is necessary to understand hybrid strategy processes, market complexity and turbulence and organisational culture. This is very difficult, but that is not why you should not do it, that is why you should do it. It is the difficulty that makes the difference. It is the difficulty that leads to sustained competitive advantage.