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Value-for-Money Strategies for Recessionary Times

by *Peter J. Williamson* and *Ming Zeng*

Lessons Western businesses must learn from emerging-market companies to succeed—at home and abroad.

No one needs convincing that the economic situation we're facing today is almost unprecedented. Yet much of the advice that executives have received is remarkably similar to what they heard during the recession in 2000. Particularly in Western enterprises, the preferred antidotes seem to be standard ones: Evaluate your risks, develop contingency plans, focus on your core, reduce costs, expect the unexpected, and so on. The unspoken objective appears to be to survive or, at most, to maintain market share.

Like many orthodoxies, however, this will not serve companies well today. The world has changed so much because of, among other reasons, deregulation, lowering of trade barriers, rapid technological advances, demographic shifts, and greater urbanization, that strategies that worked a decade ago are unlikely to do so anymore. Previously, downturns often favored incumbents, which possess economies of scale and customer relationships that allowed them to prevail over upstarts. What's different now is that companies from several emerging markets are poised to wrest market share from, or even take over, Western firms. What's more, recessions can alter industry dynamics. Studies conducted by both McKinsey & Company and Boston Consulting Group show that around a third of the companies in the first quartile of their industries tumbled from their perches during the 2000 slowdown. Only 10% of them had clawed back five years later, while 15% of today's market leaders vaulted to the top during that recession.

Smart companies perceive not just threats in a recession but also opportunities. Their goal is to grow so they can emerge stronger from the downturn. In fact, during the Great Depression of the 1930s, companies like General Electric, Kellogg, and Procter & Gamble outmaneuvered rivals to become leaders. They turned adversity into advantage in different ways, but a quick analysis reveals one common thread: During the Depression, these companies developed value-for-money strategies: They grew by delivering products and services that enabled hard-hit consumers to do more with the same resources and become more effective; to do the same with fewer resources, thereby improving their efficiency; or to do less with far fewer resources, which helped them economize.

Value for money has again become a strategic imperative—and not just because of the recession. Even before the slowdown began, there were signs that it ought to be a major consideration for companies. In developed countries, increases in household income over the past decade have favored the top 20% of earners, while the spending power of most families has stagnated or declined. Many people in the United States, for instance, have found it difficult to maintain their standard of living after paying for such necessities as their mortgage, transport, utilities, and health care without borrowing money. More recently, small salary increases and the steady drumbeat of job losses have turned many consumers into value shoppers, as they tighten their

belts.

Unsurprisingly, Wal-Mart has been gaining share from premium retailers, and apart from luxury cars, only sales of small or fuel-efficient vehicles have been growing over the past five years. In Western Europe, according to a recent Credit Suisse study, the market share of value-priced store brands rose by two percentage points in 2007 while that of premium labels fell by the same amount.

In developing countries, consumers are traditionally value conscious. Many have entered the consuming class recently and have limited disposable income. For instance, Credit Suisse projects that the number of Chinese households whose income exceeds their basic needs will rise from around 55 million in 2008 to 212 million by 2013. However, many of them will earn only a little over $5,000 a year. By 2020 in India, the market research firm Information Resources predicts, 5% of the population will be part of households that earn more than $4,000 per annum, but they, too, are unlikely to have much excess income. Meanwhile, upper- and middle-class consumers in both countries must stretch limited earnings to cope with rising aspirations and inflation. Business buyers in developing countries depend on low costs to gain competitive advantage, so they always look for value when purchasing equipment and services.

In both the developed and the developing world, therefore, delivering value for money has become critical. What capabilities must companies possess to thrive in this environment? Our research suggests that instead of refining cost-cutting techniques, companies should develop cost-innovation capabilities. They must learn to reengineer their cost structures in novel ways so they can offer customers dramatically more for less. That may not be good news for many U.S., European, and Japanese corporations, which have usually dealt with low-cost competitors by going upmarket and creating premium segments, both at home and abroad. Because smart emerging-market companies have built cost-innovation capabilities to unlock mass markets, that's no longer a viable strategy. Unless multinational companies learn from emerging rivals and, in some cases, from their own overseas operations, they are unlikely to weather the recession well —or stay competitive for very long.

Three Dimensions of Cost Innovation

Innovation is traditionally associated with developing new products and services or with adding more functionality and features to existing ones. In both cases, companies expect customers to pay a premium. The idea of innovating to develop offerings that provide greater, or almost the same, functionality but at a lower price is unconventional. Some executives may regard it as silly: Why invest in research to sell products for less than the prevailing price? However, smart companies in emerging markets have done just that to appeal to the great mass of value-conscious customers at home.

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