UNIT 4 PRODUCT LINE DECISIONS

Objectives

After reading this unit you should be able to :

- explain the concept and logic behind product line
- discuss reasons for the proliferation of product lines
- enumerate the demerits of product line extensions
- describe the main factors influencing the decision process for product line
- analyse the changes in product lines of different companies

Structure

4.1 INTRODUCTION

In the last 'few years products have proliferated at an unprecedented rate in every category of consumer goods and services. There has been widespread line extensions of all types of consumer goods and services. This puts the focus of all the marketing executives on the product line, the length and breadth of consumers it is catering to and the future direction to be taken.

A group of products within a product class that are closely related because they perform a similar function, satisfy the same basic want, are sold to the same customer groups, are marketed through the same distribution channels, or fall within given price ranges, or share some other common characteristic. Example: Detergents, `nail polishes, soaps, life insurance etc. For example the product line of a detergent manufacturer will consist of all the different types of detergents he has to offer: the product line of Hindustan lever Ltd. consists of all its detergents including those in premium segment and as well as non premium segment catering to the mass market..

4.2 EVALUATION OF PRODUCT-LINE

Each product line consists of product items, which should be evaluated. The product-line manager should study the sales and profit contributions of each item in the product line as well as the way the items are positioned against competitor's items. Then the competitors analysis in the relevant product categories is also required to be done. This provides information needed for making several product-line decisions.

One major issue faced by product-line managers is that of optimal length of the product line. A product line is perceived to be efficient if no- extra profit can be garnered by either addition of one more item or deletion of one item from the product line.

Line stretching involves the question of whether a particular line should be extended downwards, upward, or both ways. Line filling raises the question of whether additional items should be added within the present range of the line. Line filling should not lead to cannibalization of the existing products. Line modernization raises the question of whether the line needs a new look and whether the new look should be installed piecemeal or all at once. Line featuring raises the question of which items to feature in promoting the line. Which item has to be put in the forefront of promotion to attract customers to that particular category. Line pruning raises the question of how to detect and remove weaker product items from the line. It is aimed at getting rid of the dead wood and making the product line more efficient..

Activity 1

Enlist the product line of detergents of top three detergent manufacturers in India and analyse the length and breadth of consumer segments they cater to.

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4.3 BASES FOR PRODUCT LINE EXTENSION

The following seven important factors make companies pursue line extensions as a significant element of their marketing strategies.

Customer Segmentation

Line extension is perceived by managers as a low-cost, low-risk way to meet the needs of various customer segments, and by using more sophisticated and lower-cost market research and direct-marketing techniques, they can identify and target finer segments more effectively than ever before. In addition, the depth of audience-profile information for television, radio, and print media has improved; managers can now translate complex segmentation schemes into efficient advertising plans.

Consumer Desires

There is widespread volatility in the consumer behaviour and brand loyalty has taken more or less a back seat in many different categories of consumer goods and services. More consumers than ever are switching, brands and trying products they've never used before. Line extensions try to satisfy the desire for "something different" by providing a wide variety of goods under a single brand umbrella. Such extensions, companies hope, would fulfill customers' desires while keeping them loyal to the brand franchise.

Moreover, according to studies conducted by the Point-of-Purchase Advertising Institute,USA, consumers now make around two-thirds of their purchase decisions about grocery and health and beauty products on impulse while they are in the store. Line extensions, if stocked by the retailer, can help a brand increase its share of shelf space$_s$ thus attracting consumer attention. When marketers coordinate the packaging and labeling across all items in a brand line, they can achieve an attention-getting billboard effect on the store shelf or display stand and thus leverage the brand's equity.

Pricing Breadth

Managers have found a novel way of increasing profitability through line extension. Managers often tout the superior quality of extensions and set higher prices for these offerings than for core items. In markets subject to slow volume growth, marketers can then increase unit profitability by trading current customers up to these "premium" products. In this way, even cannibalized sales are profitable - at least in the short run.

In a similar spirit, some line extensions are priced lower than the lead product. For example, American Express offers the Optima card for a lower annual fee than its standard card, and Marriotte introduced the hotel chain Courtyard by Marriotte to provide a lower-priced alternative to its standard hotels. Extensions give marketers the opportunity to offer a broader range of price points in-order to capture a wide audience.

Excess Capacity

Line extension helps in utilizing the excess capacity of the production facilities of the firm. In the 1980s, many manufacturing operations added faster production lines to improve efficiency and quality. The same organizations, however, did not necessarily retire existing production lines. The resulting excess capacity encourages the introduction of line extensions that require only minor adaptations of current products.

Short-Term Gain

Besides sales promotions, line extensions represent the most effective and least imaginative way to increase sales quickly and inexpensively. The development time and costs of line extensions are far more predictable than they are for new brands, and less cross-functional integration is required.

In fact, few brand managers are willing to invest the time or assume the career risk to introduce new brands to market. They are well aware of the following: major brands have staying power (almost all of the 20 brands that lead in consumer awareness were on that list 20 years ago); the cost of a successful new launch is now estimated at $30 million, versus $5 million for a line extension; new branded products have a poor success rate (only one in five commercialized new products lasts longer than one year on the market); and consumer goods technologies have matured and are widely accessible. Line extensions offer quick rewards with minimal risk.

Senior executives often set objectives for the percentages of future sales to come from products recently introduced. At the same time, under pressure from stock exchanges for quarterly earnings increases, they do not invest enough in the long-term research and development needed to create genuinely new products. Such actions necessarily encourage line extensions.

Competitive Intensity

Mindful of the link between market share and profitability, managers often see extensions as a short-term competitive device that increases a brand's control over limited retail shelf space and, its overall demand for the category for new branded or private-label competitors and to drain the limited resources of third and fourth place brands. Close-up and Colgate toothpastes, for example, both available in more than 15 types and package sizes, have increased their market shares in the last decade at the expense of smaller brands that have not been able to keep pace with their new offerings.

Trade Pressure

The proliferation of different retail channels for consumer products, from club stores to hypermarkets, pressures manufacturers to offer broad and varied product lines. While retailers object to the proliferation of marginally differentiated and "me-too" line extensions, trade accounts themselves contribute to stock-keeping unit (SKU) proliferation by demanding either special package sizes to fit their particular marketing strategies (for example, bulk packages or multipacks for low-price club stores) or customized, derivative models that impede comparison shopping by consumers. Black & Decker, for example, offers 19 types of irons, in part to enable competing retailers to stock different items from the line.

4.4 THE DISADVANTAGES OF LINE EXTENSION

Given this backdrop, it's easy to visualise why so many managers have been swept into line-extension mania. But, as more managefs are discovering, the problems and risks associated with extension proliferation are formidable.

Weaker Line Logic

Manager often extend a line without removing any existing items. As a result, the line may expand, to the point of over segmentation, and the strategic role of each item becomes muddled. Salespeople should be able to explain the commercial logic for each item. If they cannot, retailers turn to their own data - the information collected by checkout scanners - to help them decide which items to stock. Invariably, fewer retailers stock an entire line. As a result, manufacturers lose control of the presentation of their lines at the point of sale, and the chance that a consumer's preferred size or flavor will be out of stock increases.

A disorganized product line can also confuse consumers, motivating those less interested in the category to seek out a simple, all-purpose product, such as All Temperature Cheer in the Laundry detergent category.

Lower Brand Loyalty

Some marketers mistakenly believe that loyalty is an attitude instead of understanding that loyalty is the behaviour of purchasing the same product repeatedly. In the past 50 years, many of the oldest and strongest brands have had two and three generations of customers buying and using products in the same way. When a company extends its line, it risks disrupting the patterns and habits that underlie brand loyalty and reopening the entire purchase decision.

Although line extensions can help a single brand satisfy a consumer's diverse needs, they can also motivate customers to seek variety and. hence, indirectly encourage brand switching. In the short run, line extensions may increase the market share of the overall brand franchise. But if cannibalization and a shift in marketing support decrease the share held by the lead product, the long-term health of the franchise will be weakened. This is particularly true when line extensions diffuse rather than reinforce a brand's image in the eyes of long-standing consumers without attracting new customers.

Underexploited Idea

By bringing important new products to market as line extensions, many companies leave money on the table. Some product ideas are big enough to warrant a new brand. The line extensions serves the career goals of a manager on an existing brand better than a new brand does, but long-term profits are often sacrificed in favour of short-term risk management.

Stagnant Category Demand

Line extensions rarely expand total category demand People do not eat or drink more, wash their hair more, or brush their teeth more frequently simply because they have more products from. which to choose. In fact, a review of several product categories show no positive correlation between category growth and line extensions. If anything, there is an inverse correlation as marketers try in vain to reinvigorate declining categories and protect their shelf space through insignificant line extensions.

Poorer Trade Relations

On average, the number of consumer-packaged-goods SKUs grew 16% each year from 1985 to 1992, in' USA, while retail shelf space expanded by only 1.5% each year. Retailers cannot provide more shelf space to a category simply because there are more products within it. They have responded to the flood by rationing their shelf space, stocking slow-moving items only when promoted by their manufacturers, and charging manufacturers slotting fees to obtain shelf space for new items and failure fees for items that do not meet target sales within two or three months. As a manufacturer's credibility has declined, retailers have allocated more shelf space to their own private label products. , Competition among manufacturers for the limited slots still available escalates overall promotion expenditures and shifts margin to the increasingly powerful retailers.

More Competitor Opportunities

Share gains from line extensions are typically short-lived. New products can be matched quickly by competitors. What's more, line-extension proliferation reduced the retailer's average turnover rate and profit per SKU. This can expose market leaders to brands that do not attempt to match all the leaders' line extensions but instead offer product lines concentrated on the most popular line extensions. As a result, on a per - SKU basis, 'lesser known brands, as compared to market leaders, can deliver a higher direct product profit to the retailer than brands with -larger shares and more SKUs.

Increased Costs

Companies expect and plan for a number of costs associated with a line extension, such as market research, product and packaging development, and the product launch. The brand group may also expect certain increases in administrative costs; planning the promotion calendar takes more time when an extension is added to the line, as does deciding, on the advertising allocations between the core brand and its extensions. But managers may not foresee the following pitfalls:

- Fragmentation of the overall marketing effort and dilution of the brand image
- Increased production complexity resulting from shorter production runs and more frequent line changeovers. (These are somewhat mitigated by the ability to customize products toward the end of an otherwise standardized production process with flexible manufacturing systems.)
- More errors in forecasting demand and increased logistics complexity, resulting in increased remnants and larger buffer inventories to avoid stockouts.
- Increased supplier costs due to rush orders and the inability to buy the most economic quantities of raw materials.
- Distraction of the research and development group from new product development.

The unit costs for multi-item lines can be 25% to 45% higher than the theoretical cost of producing only the most popular item in the line. (See the Chart "The Cost of Variety.") The inability of most line extensions to increase demand in a category makes it hard for companies to recover the extra costs through increases in volume. And even if a line extension can command a higher unit price, the expanded gross margin is usually insufficient to recover such dramatic incremental unit costs.

The costs of line-extension proliferation remain hidden for several reasons. First, traditional cost-accounting systems allocate overheads to items in proportion to their sales. These systems, which are common even among companies pursuing a low-cost-producer strategy, overburden the high sellers and undercharge the slow movers. A detailed cost-allocation study of one line found that only 15% of the items accounted for all the brand's profits. That means that 85% of the items in the line offered little or no return to justify their full costs.

Second, during the 1980s, marketers were able to raise prices to cushion the cost of line extensions. A review of 12 packaged-goods companies shows that price increases in excess of raw-material-cost increases contributed 10.4 additional percentage points to gross margins between 1980 and 1990, but 8.6 points were absorbed by increased selling, general and administrative (SG&A) costs. Now that low inflation and the recent recession have restricted marketers' ability to raise prices, margins will be more clearly squeezed by new line extensions.

Third, line extensions are usually added one at a time. As a result, managers rarely consider the costs of complexity, even though adding several individual extensions may change the cost structure of the entire line.

Once a company's senior managers take the time to examine the downside of aggressive line extension, rationalizing the product line becomes a fairly straightforward process.

Activity 2

Take two leading Colour television manufacturers in India and analyse the changes in their product line over the last five years and its affect on the total market share of the company.

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4.5 FACTORS INFLUENCING PRODUCT LINE DECISIONS

An analysis of a product's potential to achieve a desired level of return on the company's investment is an essential component of the marketing planning process. An analysis of this type not only assesses financial opportunities but also provides ideas about bow to compete better given structural characteristics of the category.

The various factors influencing the product line decisions of a corporation are:

Category Size

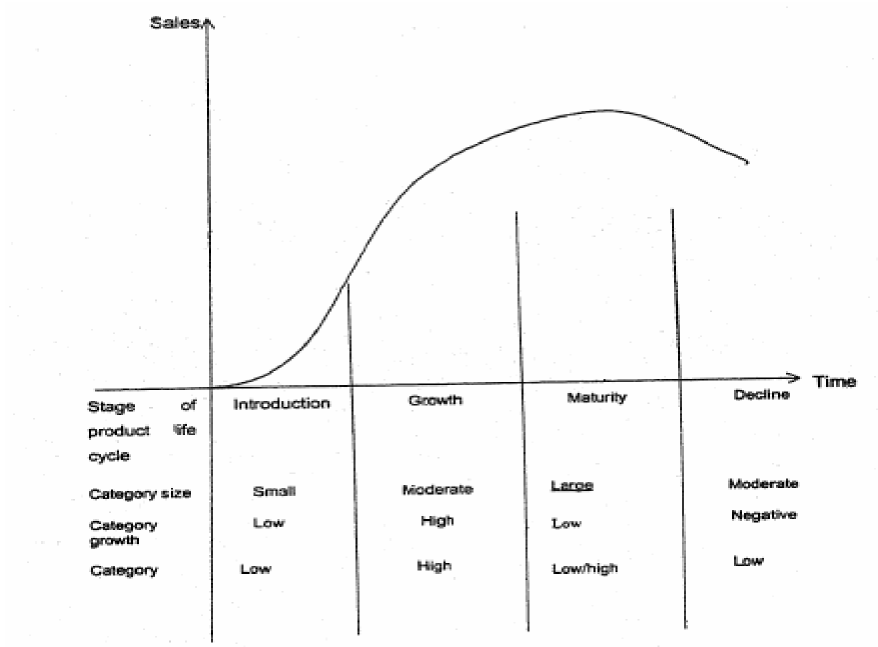
Category size is an important piece of data about any market. It is clearly an important determinant of the likelihood that a product will generate revenues to support a given investment. In general, larger markets are better than smaller ones. Besides having more market potential, large categories usually offer more opportunities for segmentation than small ones. Large markets, however, tend to draw competitors with considerable resources, thus making them unattractive for small firms.

Market Growth

Market growth is a key market factor advocated by various planning models. Not only is current growth important, but growth projections over the horizon of the plan are also critical. Fast-growing categories are almost universally desired due to their abilities to support high margins and sustain profits in future years. However, like large categories, fast-growing ones also attract competitors.

Product Life Cycle

Category size and category growth are often portrayed simultaneously in the form of the product life cycle. Usually presumed to be S shaped, this curve breaks down product sales into four segments: introduction, growth, maturity, and decline. The introduction



Category Attractiveness over the Product Life Cycle

and growth phase are the early phases of the life cycle when sales are growing rapidly, maturity represents a leveling off in sales, and the decline phase represents the end of the life cycle.

In the introductory phase, both the growth rate and the size of the market are low, thus making it unattractive for most prospective participants, who would rather wait on the sidelines for a period of time. When market growth and sales start to take off, the market becomes more attractive. In the maturity phase, the assessment is unclear; while the growth rate is low, the. market size could be at its peak. Finally, the decline phase usually is so unattractive that most competitors flee the category.

Sales Cyclicity

Many categories experience substantial inter year variation in demand. Highly capital-intensive business such as automobiles, steel and machine tools, are often tied to general business conditions and therefore suffer through peaks and valleys of sales.

Seasonality

Seasonality - intra year cycles in sales - is generally not viewed positively. Seasonal business tends to generate price wars because there may be few other opportunities to make substantial sales. However, most products are seasonal to some extent. Some, are very seasonal.

Profits

While profits vary across products or brands in a category, large inter industy differences also exist.

These differences in profitability across industries are actually based on a variety of underlying factors. Differences can be due to factors of production (e.g., labour versus capital intensity, raw materials), manufacturing technology, and competitive rivalry. Product categories that are chronically low in profitability are less attractive than those that offer higher returns.

A second aspect of profitability is that it varies over time. Variance in profitability is often used as a measure of industry risk. Product managers must make a risk-return trade-off, evaluating the expected returns against the variability in those returns.

Attractiveness of Market Variables

	Attractiveness	
	High	**Low**
Market size	+	-
Market growth	+	-
Sales cyclicity	-	+
Sales seasonality	-	+
Profit level	+	-
Profit variability	-	+

4.6 CATEGORY FACTORS INFLUENCING PRODUCT LINE. DECISIONS

Although the aggregate factors just described are important indicators of the attractiveness of a product category, they do not provide information about underlying structural factors in ' assessing the structure of industries: such as

- The threat of new entrants.
- The bargaining power of suppliers.

- The amount of intracategory rivalry.
- The threat of substitute products or services.

Threat of New Entrants

If the threat of new entrants into the product category is high, the attractiveness of the category is diminished. Except for the early stages of market development, when new entrants can help a market to expand, new entrants bring additional capacity and resources that usually heighten the competitiveness of the market and diminish profit margins. Even at early stages of market growth, the enthusiasm with which new entrants are greeted is tempered by who the competitors are.

the barriers to entry erected by the existing competition are key to the likelihood that new competitors will enter the market. This sounds anticompetitive and illegal, but it is only definitely anticompetitive; making it difficult for new competition to enter the market. Some of the potential barriers to entry are -

Economies of Scale

Product Differentiation

Capital Requirements

Switching Costs

Distribution

Bargaining Power of Buyers

The following diagram is useful for discussing the power of both buyers and suppliers: Suppliers -> Category of Concern -> Buyers

Buyers are any people or institutions that receive finished goon or services from the organizations in the category being analyzed. Buyers can be distributors manufacturers, original equipment manufacturers (OEMs), or end customers. Suppliers are any institutions that supply the category of concern with factors of production such as labor, capital. raw materials, and machinery.

High buyer bargaining power is negatively related to industry attractiveness. In such circumstances, buyers can force down prices and play competitors off against one another for benefits such as service. Some conditions that occur when buyer bargaining power is high include the following:

1). When the product bought is a large percentage of the buyer's costs.
2). When the product bought is undifferentiated.
3). When the buyers earn low profits.
4). When the buyer threatens to backward integrate.
5). When the buyer has full information.
6). When substitutes exist for the seller's product or service.

Again, the product manager's concern is to decrease buyer power. This is accomplished, for example, by increasing product differentiation (e.g., making your services such as technical assistance or manufacturing-related consulting, and building in switching costs. Thus, the implications of this analysis of buyer power are as critical as is the overall concept of buyer power.

Bargaining Power of Suppliers

High suppliers power is clearly not an attractive situation because it allows suppliers to dicate price and other terms, such as delivery dates, to the buying category. Some conditions that prevail when supplier bargaining power is high are:

1) When suppliers are highly concentrated, that is, dominated by a few firms.

2) When there is no substitute for the product supplied. ,

3) When the supplier has differentiated its product or built in switching costs.

4) When supply is limited.

Current Category Rivalry

Product categories characterized by intense competition among the major participants are not as attractive as those in which the rivalry is more sedate. A high degree of rivalry can result in escalated marketing expenditures, price wars, employee raids, and related activities. Such actions can exceed what is considered `normal' market competition and can result in decreased welfare for both consumers and competition..

Some of the major characteristics of categories exhibiting intensive rivalries are:

- Many competitors
- Slow growth
- High fixed costs
- Lack of product differentiation
- Personal rivalries

Pressure from Substitutes

Categories making products or delivering services for which there are a large number of substitutes are less attractive than those that deliver a relatively proprietary product, one that uniquely fills a customer need or solves a problem. Since almost all categories suffer from the availability of substitutes, this may not, be a determinant of an unattractive product category. However, some of the highest rates of return are earned in categories in which the range of substitutes is small.

Category Capacity

Chronic overcapacity is not a positive sign for long-term profitability. When a category is operating at capacity, its costs stay low and its bargaining power with buyers is normally high. Thus, a key indicator of the health of a category is whether there is a consistent tendency toward operating at or under capacity.

Attractiveness of Category Factors

Attractiveness	**High Attractiveness**	**Low Attractiveness**
Threat of new entrants	+	-
Power of buyers	+	-
Power of suppliers	-	+
Rivalry	-	+
Pressure from substitutes	+	-
Unused capacity situations	-	+

Activity 3

If you are a car manufacturer aiming at the Indian market. What are the conditions that will influence your product line decision. Enlist all the factors and decide about the length of your product line.

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4.7 SUMMARY

There are lots of external and internal factors affecting the product line decision of a particular product line manager. The decision about the product line ultimately is a function of the company's short term and long term, objectives and the external and internal factors as mentioned earlier. This should be the only criteria for reaching at a product line decision aimed at improving the overall profitability of the firm.

4.8 SELF ASSESS ENS' QUESTIONS

Product Line Decisions. are crucial and vital in a corporation. Discuss the factors influencing the product line decisions.

Comment on the demerits associated with line extensions.

4.9 FURTHER READINGS

Kotler, Phillip, 2002 *Marketing Management,* Prentice Hall of India Pvt. Ltd., New Delhi.
Rainanuj Majumdar, 1998 Product Management, Vikas Publications-New Delhi.