T. Rudolph / B. B. Schlegelmilch
J. Franch / A. Bauer
J. N. Meise (Eds.)

Diversity in European Marketing

Text and Cases

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Thomas Rudolph • Bodo B. Schlegelmilch
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Editors
Thomas Rudolph
University of St. Gallen, Switzerland

András Bauer
Corvinus University, Budapest, Hungary

Bodo B. Schlegelmilch
WU Vienna University of Economics
and Business, Austria

Jan Niklas Meise
University of St. Gallen, Switzerland

Josep Franch
ESADE Business School Barcelona, Spain

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Preface

Europe has always been diverse, and it is becoming more so. One of the founding principles of the European Union is respect for its diversity. For marketers, this marks a challenge of marketing goods and services in Europe. This is hardly surprising when one considers that the EU is comprised of currently 27 member countries, over 500 million people, and over 20 different languages (not counting regional dialects). Five main religions are represented, and there are significant variations in the social, economic and political systems. Consequently, consumer differences exist within countries as much as between countries.

The idea for this book was inspired by a course developed jointly by some of the book's editors, members of the CEMS Marketing Faculty Group. CEMS, formerly known as the Community of European Management Schools, is a strategic alliance of 26 leading business schools and 64 corporate partners, which nowadays reaches beyond Europe. CEMS partner schools offer a joint degree, the CEMS Master in International Management. Students enrolled in this Master's program have a background in management or business administration. Partner schools develop specific courses for this program and some of the courses are jointly designed and delivered by partner schools.

Within the CEMS network, Faculty Groups are responsible for co-coordinating teaching and research initiatives. They play an important role in the CEMS network, as they provide coordination opportunities for joint development of courses, seminars and research, and thus broaden the perspectives of participating educators and researchers. Recent seminars focused on branding, market development, multicultural research, product design and innovation. The Marketing Faculty Group is one of the most active groups in the CEMS network and its history dates back almost 20 years. One of the group's previous endeavors was the collection and publishing of casebooks in 1994, 1997 and 2000[1]. These publications took the initiative to address up-to-date issues and offer short cases for educators who wanted to take a European perspective. These collections served their purpose well, however, marketing practices and Europe itself have undergone major changes since; the Internet has arrived and is in full power now, the European Union has expanded to 27 member countries, and the 2008 economic crises changed the behavior of customers and firms alike. So the challenge is obviously there to update and improve our knowledge of marketing.

A few members of the CEMS Marketing Faculty Group undertook the challenge of developing an advanced marketing course specifically for the CEMS Master in International Management. The course had to go beyond the basic marketing concepts already covered in

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[1] *Understanding Marketing: A European Casebook*, edited by Celia Phillips, Ad Pruyn and Marie-Paule Kestemont. John Wiley and Sons, Ltd. (2000)
Cases in Marketing, edited by Hanne Hartvig Larsen. Sage Publications (1997)
Marketing in Europe, edited by Jordi Montaña. Sage Publications (1994)

previous Bachelor's degree programs; it had to be based on active-learning methodologies, such as case studies or student projects, have a strong European focus, and illustrate the latest issues or challenges with which managers have to cope.

As a result, a course called 'Marketing Challenges in a Diverse European Market' was devised and successfully delivered at Corvinus University (Budapest, Hungary), ESADE Business School (Barcelona, Spain) and WU Vienna University of Economics and Business (Austria). The course syllabus included some of the topics featured in this book: marketing and sustainability; marketing and new technologies; aging population in Europe; coexistence of mature and emerging markets; growing migration and minorities in Europe; EU regulations; prevalence of small and medium-sized companies; private labels and retail development in Europe. The idea of putting cases and materials from the course into a book format soon followed and the idea of this book was born.

This book offers a non-traditional perspective to European marketing approached through cases and relevant received theory. The originality of the approach immediately led to interest from other colleagues, who proposed additional topics to be included, along with interest from publishers, who identified this book's potential beyond the original course. All members of the CEMS Marketing Faculty Group were invited to provide a chapter addressing a relevant marketing challenge in Europe, based on a case study, and followed by a specific student assignment. This book is written by expert academics of the best management schools in Europe representing a diversity in culture and approaches. The cases are based on the relevant trends of marketing in Europe that allow companies to understand, and effectively react to different markets to craft pan-European marketing strategies.

Besides managers involved in diverse marketing issues (such as product and brand managers, retail category managers, supply chain managers or communication and public relations experts), this book is highly relevant for Bachelor- and Master students wanting to pursue a European career in marketing and related domains. Furthermore, participants in executive education such as EMBA programs or dedicated seminars will find this book an inspiration and valuable source of knowledge how to deal with European diversity and resulting management issues.

The topics covered in this book are as diverse as its contributors and audience. It is structured in three main parts covering the diverse challenges marketers face in Europe. **Part 1** deals with diverse demographics and structural diversity. Issues such as migration and catering to ethnic minorities are discussed and illustrated in case studies of Deutsche Bank's subsidiary Bankamiz and the fast-food chain KFC in France. The second chapter adresses ageing consumers and provides the case of Bazile Telecom offering simple communcation solutions to such consumers. How to deal with changing and incongruent media regulations is outlined in the third chapter and illustrated by the case of the TV station VIASAT 3 in Hungary. The first part closes with a chapter on managing early and mature markets and a case on the banking industry, focusing on the UniCredit Group.

The cases of **Part 2** pertain to acknowledging and managing diversity in consumer behavior in Europe. First, the resurrection of old traditional brands and the increasing trend towards nostalgic branding in Europe are outlined following the example of the Czech cola brand Kofola. Next, chapter six addresses diversity in European retailing and outlines the history and challenges of the German hard-discounter Aldi in the United Kingdom. The importance of private label products in Europe is illustrated in chapter seven and illustrated by insights into the private label strategy of the Belgian supermarket chain Delhaize. The second part closes with a case on how the Norwegian food producer Toro empowers its consumers to become co-producers of their convenience food.

Part 3 of this book is concerned with the questions how to respond to the outlined diverse marketing environments and how to manage such diversity. It opens with a case on the role of regional headquarters and presents the case of the sporting goods producer Puma. Next, chapter ten turns to managing consumer's experiences and provides two short cases on design as a solution for transformation. Chapter eleven provides insights into European market entry strategies illustrated by the case of the Swedish international market leader in dairy farming equipment and automation DeLaval. The important issue of renewable energies is eventually addressed in chapter twelve providing a case of the Danish company Vestas Wind Systems.

We thank all authors for provding such insightful case studies and also need to recognize the support they have received from the respective companies covered in their cases. We also extend our sincere thanks to Jan Niklas Meise, who coordinated the project and thoroughly put the book together, to Gina Cook, who served as an editor to the manuscript, and to Gabler for bearing with us during the creation and completion of this book.

We believe that because of its diversity and unique heritage Europe is more than the sum of its parts and deserves distinct marketing attention. As part of the CEMS Marketing Faculty Group we will continue propagating this opinion and feel confident this book will help accordingly.

Thomas Rudolph, University of St.Gallen

Bodo Schlegelmilch, WU Vienna University of Economics and Business

Josep Franch, ESADE Business School (Barcelona, Spain)

András Bauer, Corvinus University of Budapest

Jan Niklas Meise, University of St.Gallen

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Part 1

Targeting Diverse Demographics and Managing Structural Diversity in Europe

1 Migration and Minorities in Europe

Josep Franch, Research Group on Brand and Consumption at ESADE, Barcelona, Spain

Verena Gruber, International Marketing Management, WU Vienna, Austria

Matthew Hawkins, Research Group on Brand and Consumption at ESADE, Barcelona, Spain

> **Cut-throat competition: Feeding Europe's Muslims is a growing business**
>
> Just before the beginning of Ramadan, the month-long Muslim fast which ends this weekend, an unusual advertisement appeared on French television. Panzani, a pasta-maker, was touting its Zakia line of halal ready-meals. In a secular nation it seemed like "a little revolution", as *Le Parisien*, a newspaper put it. The French can presumably take it in their stride. Trade in halal food is growing fast and is likely to continue to do so.
>
> Big food producers have long catered to Muslims, a market worth some $630 billion globally according to KasehDia, a consulting company that specializes in the trade. But only recently have big European shops followed suit.
>
> The main reason for growth is demographics. Although many European countries do not tally Muslims or any other religious group (estimates in France range from 4m to 7m) it is clear that Muslim populations have grown quickly as a result of immigration and higher birth rates.
>
> Although Muslims are disproportionately poor, they spend plenty of money on food. Islam is associated with a strong tradition of communal feasting. […] Nearly a third of the money goes on meat. That demand, which contrasts with a drop in meat eating among health-conscious Christians and godless folk, has helped transform the global livestock market.
>
> ***Press Clipping from The Economist, 17 September 2009***

Panzani's appreciation of Muslims' preferences and tastes in France illustrates the important task of accounting for the needs of different ethnic groups, which increasingly form a crucial customer segment. As the marketplace becomes ever more pluralistic, accommodating various minorities and cultural subgroups, marketers increasingly need to be aware of these differences in order to remain viable and competitive players.

One of the most crucial and paramount tasks for marketing managers in the global marketplace is the ability to adapt to consumers from different cultures. The interrelatedness of economies has accelerated interactions of cultures, markets and consumers and the globalized marketplace is characterized by multiple cultural spheres. Marketing managers re-

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ceiving an intimate knowledge of consumers' cultural customs and preferences possess an important competitive advantage (Penaloza 1995).

1.1 Background

Migration is not a new phenomenon. People have been moving to and from countries for hundreds of years. And, some countries traditionally receive, or host, immigrants from other countries while other countries typically provide immigrants. Migration is defined as "flows of people (workforce) between nations […] which leads to a long-term or permanent change of the habitual residence of participating persons" (Gabler 2011). It is a phenomenon that is triggered and influenced by a combination of economic, political and social factors. These factors can either stem from a migrant's country of origin (push factors) or from the country of destination (pull factors). The EU's economic prosperity and political stability are considered to be important pull factors for immigrants.

Over the past few years, many European countries have been receiving a considerable amount of immigrants; as a consequence, their populations have increased. The composition of the foreign population in Western Europe is a reflection of successive waves of post-war migration connected with labor shortages. Starting from the mid-1970s, it has also mirrored family reunions and formations, as well as the flight of refugees from war-torn areas both within and outside Europe (Geng 1997). Immigration in the EU has continuously increased over the past few years and in 2006, around 3.5 million people settled in the EU-27 (member states (MS) including Belgium, Bulgaria, Czech Republic, Denmark, Germany, Estonia, Ireland, Greece, Spain, France, Italy, Cyprus, Latvia, Lithuania, Luxembourg, Hungary, Malta, the Netherlands, Austria, Poland, Portugal, Romania, Slovenia, Slovakia, Finland, Sweden, and the United Kingdom), a rate nearly a quarter higher than in 2002. The largest numbers of foreign citizens, in absolute terms, can be found in Germany, Spain, the United Kingdom, France and Italy.

The development of new technologies has made it possible for companies today to target smaller-sized segments than in the past. Traditional marketing wisdom suggested that, amongst other characteristics, market segments should be homogeneous and responsive to the marketing effort but they should also be large enough to be profitable. Thanks to the Internet and new technologies, companies can target market segments that were not profitable in the past due to their relatively small size.

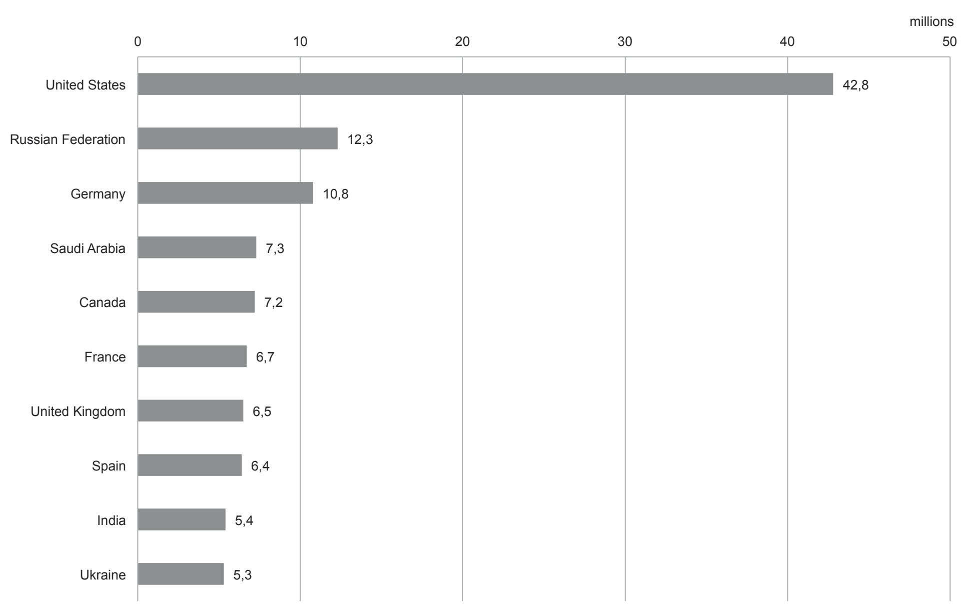
As migration trends continue to increase, marketers are presented with both threats to their position and exciting opportunities to take advantage of these newly created markets. This chapter begins by presenting key migration trend statistics. First global statistics are presented and then the focus narrows in on Europe. Next, the impacts migrants have on business, from a marketing perspective, are discussed. Two cases are presented at the end of the chapter: Deutsche Bank's response to a growing migrant community in their home country Germany and KFC's struggle to serve the Muslim market in France. The first case is particularly interesting in that financial services depend on trust with the community and

Deutsch Bank could not target the migrant community with cosmetic changes, like changing the language of brochures. Instead, a new brand and full marketing strategy devoted to addressing the specific needs of the migrant community were developed. The second one highlights the challenges of serving specific religious segments, which in the case of KFC in France is accompanied by heavy resistance among their core customers.

1.2 Global Overview

The World Bank reports that in 2010 there were some 215.8 million international migrants in the world, accounting for 3.2 percent of the total population (World Bank 2011). The United States has the most international migrants by far, but European countries have a significant amount of migrants as well (see **Exhibit 1.1**).

Exhibit 1.1 Countries with the largest number of international migrants, 2010

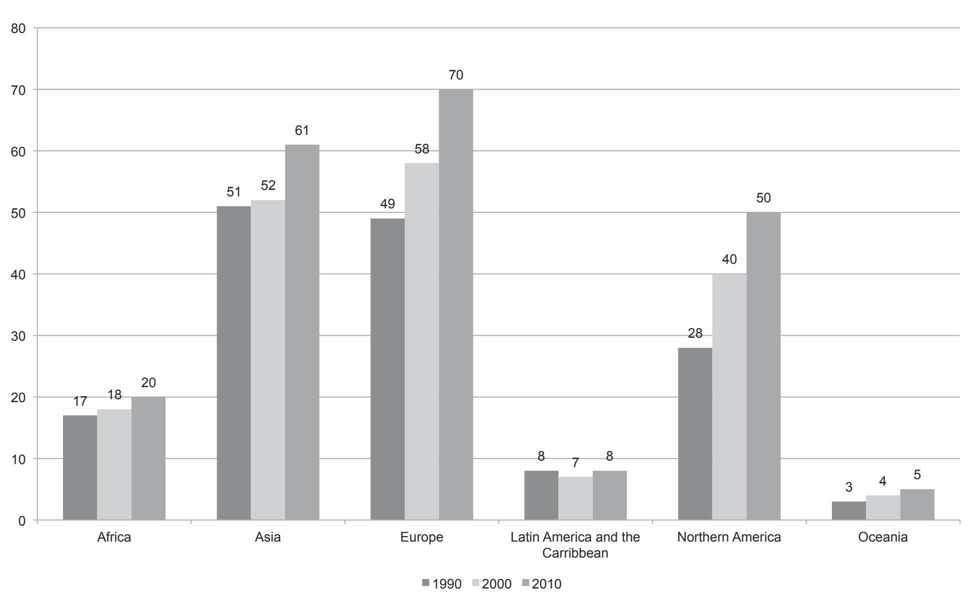


Source: United Nations (2009a)

Despite geographically smaller countries having higher population percentages of foreign-born inhabitants, Europe hosts roughly one-third of all international migrants. This is not entirely unexpected due to the relaxed mobility regulations for European Union citizens and the sustained economic progress of many European countries. Asia has the second largest share of international migrants, then North America and Africa. Notice the upward

international migrant trends in **Exhibit 1.2**, which presents the international migrant figures, by major area, for the last three decades.

Exhibit 1.2 Estimated number of international migrants, 1990-2010



Source: United Nations (2009b)

Table 1.1 presents a more detailed breakdown on the percentage of population composed of international migrants. Clearly the US has a higher percentage of international migrants than European countries but countries like Austria and France have fairly high percentages of foreign-born residents, considering their geographical size.

What is remarkable about migration figures is all future projections foresee an increase in international migrants. In only four years, the migration statistics rose from 191 million in 2005 to 215.8 million for 2010 (IOM 2010a; World Bank 2011). At this rate, 405 million international migrants are expected by 2050 (IOM 2010a). Therefore, it is quite easy to anticipate that the flow of international migrants can create challenges and opportunities for businesses.

Table 1.1 International migrants as a percentage of the population

Year	Europe	US	Austria	France	Germany	Sweden	UK
1990	6.9	9.1	10.3	10.4	7.5	9.1	6.5
1995	7.5	10.5	12.5	10.5	11.0	10.3	7.2
2000	7.9	12.1	12.5	10.6	12.2	11.2	8.1
2005	8.8	13.0	14.0	10.6	12.9	12.3	9.7
2010	9.5	13.5	15.6	10.7	13.1	14.1	10.4

Source: United Nations (2009b)

Migration statistics offer valuable insights for marketers into the composition of a country's consumer landscape. However, there is also a downside concerning this data: it never accurately reflects the truth as there are many migrants living and working illegally in a country. Even though in most data collection this factor is somehow incorporated via projections from illegal border crossings, police data or trafficking and smuggling data, such estimations are hardly suitable for accurate statistics. Furthermore, many countries do not even collect data on immigrants and emigrants. Altogether, these factors indicate that final numbers tend toward underestimation and immigrants to the European Union are even more numerous than reflected in the official statistics.

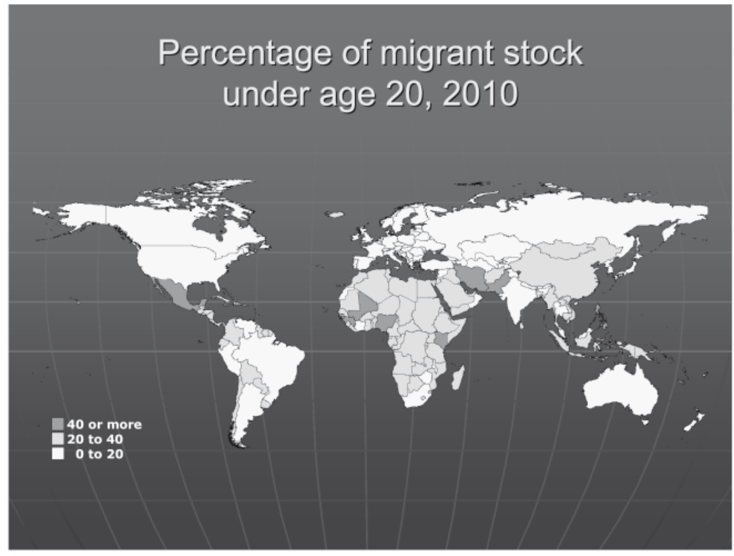
Economic Opportunity Trends

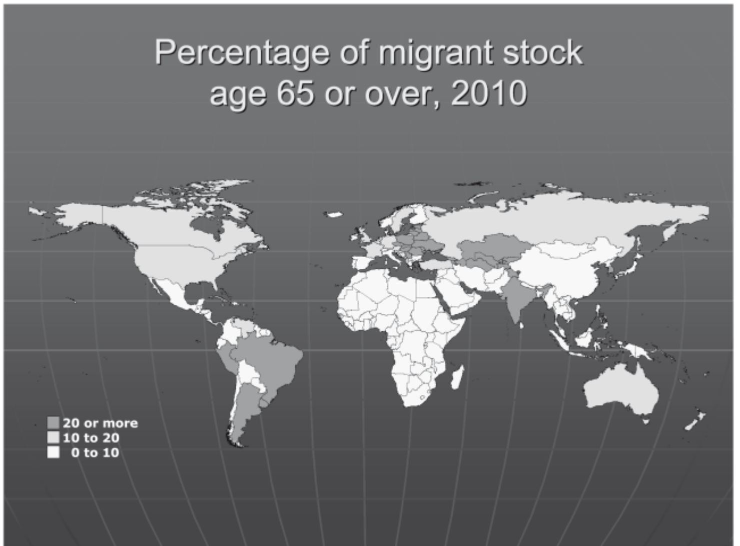
Migration occurs for numerous reasons; however, the primary migration driver is access to economic opportunities. Access to the labor market includes the educated, highly-skilled engineers and doctors as well as the low-skilled labor necessary to meet the growing demands of the world economy. For example, 4.2% of the world's physicians are international immigrants (World Bank 2011). Labor based migration will undoubtedly increase due to the fact that the labor stock of developed countries is expected to stay relatively flat at 600 million while the labor stock of developing countries is expected to increase from 2.4 billion in 2005 to 3 billion in 2020. As these youth enter the labor market, they will need to explore job opportunities farther from home (IOM 2010a). This could become a significant issue for sub-Saharan Africa where it is projected that by 2025, 60% of their population will be under the age of 30 (IOM 2010a). Economic opportunities are hard to obtain in a fiercely competitive labor market, potentially driving outward migration.

Age Trends

Exhibit 1.3 shows the migration trends based on age. Notice the percentage change for developed and developing countries based on age. As marketers, the challenge is to understand the needs of the selected target consumers and offer a product or service that has value to them. Migration based on the life-stage of the migrant is an important factor to consider when developing strategies to target migrants.

Exhibit 1.3 Percentage of migrant stock under age 20 & age 65 and over, 2010





Source: United Nations (2011)

While developing countries typically serve as a source of migrants for labor issues, developed countries are a large source of the retired migrants (IOM 2010a). Retired migrants are

expected to increase, especially from the European Union, where educated workers retire and want to spend their retirement pursuing personal interests. Targeting retired migrants requires different adjustments to the marketing mix compared to targeting younger, labor-based migrants.

Gender Trends

Of the total migrant population, 56.7% are females compared to a 48.4% global female population (World Bank 2011). In relation to labor-based migration, males tend to focus on manual, lower-skilled work while females tend to focus on domestic and education services.

Remittance Trends

As educated and capable workers leave their home countries to pursue economic opportunities in other countries, the human capital in their home country is diminished. Interestingly, remittance payments from migrants to relatives in their home country contribute significantly to the economic standing of smaller countries. Remittance occurs when migrants work in foreign countries and transfer portions of their earnings back to family members, relatives or friends in their home countries. Clearly, remittance payments make up a significant portion of some countries' GDP. The implication of remittance means this money has left the host country of the migrant. Therefore, just because a migrant is working and making money does not mean he or she is spending the money in the host country.

Global Highlights

This section has shown that migration is influenced by many factors and marketers need to understand the motivation for migrating to a new country in order to develop offerings and marketing messages that cater to the needs of the targeted migrant population. At the very least, incorporating light touches to the marketing mix that demonstrate respect for the migrants culture and promote comfort is advisable.

It should be noted that the global recession has led to a decline in migration (IOM 2010a). Much of this decrease is in response to reductions in labor demands. As the global economy gathers momentum, migration is expected to increase. However, global migration statistics are not to be confused with nation-state migration statistics since select countries will experience migration trends that are not representative of the global statistics. The following section moves into some of the migration and minority group statistics for Europe.

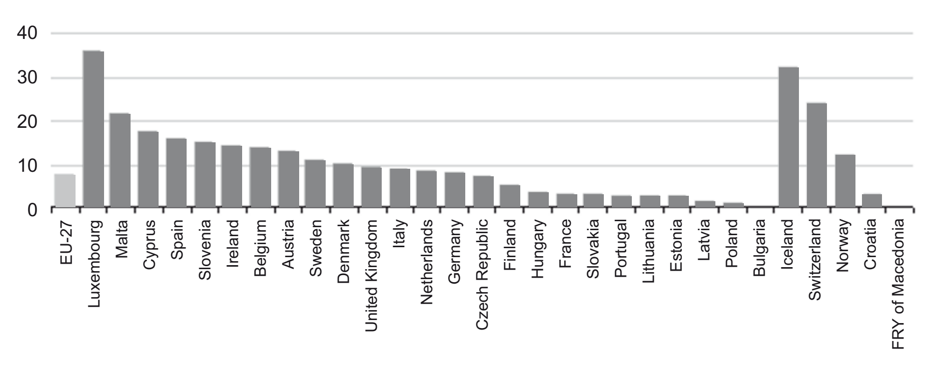
1.3 European Overview

Europe and Central Asia have roughly 6.8% of their population consisting of migrants, or 27.3 million individuals. The global average is 3.2% of the population being migrants (World Bank 2011). The decrease in travel restrictions within the European Union will only increase the number of foreign-born residents residing in EU countries. Migration accounts for a significant portion of the population growth for some European countries. While

France has experienced a natural population increase, roughly 90% of the population increase for Austria, the Czech Republic and southern European countries was due to migration (OECD 2010). With such high migrant inflow rates, these countries could experience significant cultural shifts in the coming years. Businesses will need to monitor the consumer market for changes that threaten their current position.

Exhibit 1.4 depicts the concentration of foreign-born population per 1,000 inhabitants in European countries while **Table 1.2** lists the European countries with the largest quantity and percentage of foreign-born residents.

Exhibit 1.4 Number of Foreign-Born Population per 1,000 Inhabitants



Data for the number of inhabitants refers to 1 January 2009; Greece and Romania, not available

Source: Eurostat (2008a)

Table 1.2 Stock of Foreign-Born Residents

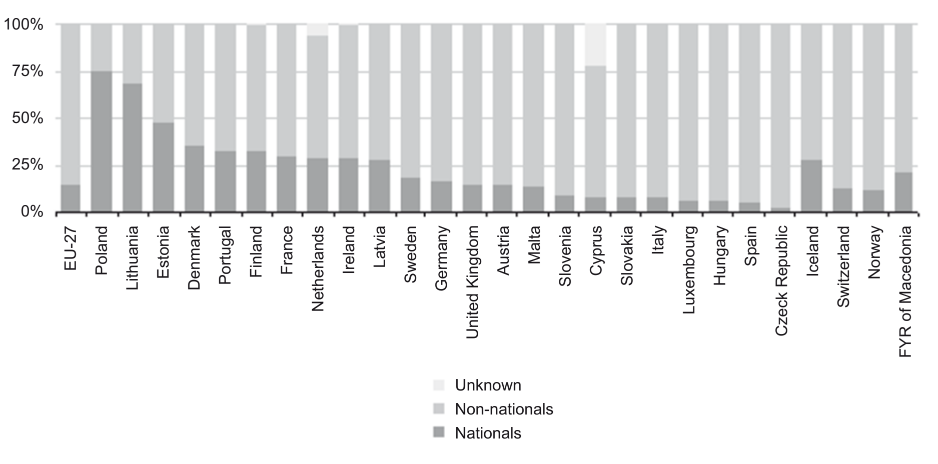
Countries with the Largest Number of Foreign Born Residents	Countries with the Largest Percentage of Foreign Born Relative to Population
Germany	Luxembourg
France	Liechtenstein
United Kingdom	Switzerland
Spain	Ireland
Italy	Cyprus

Source: IOM (2010b)

Overall, EU-27 has received between 1.5-2 million migrants each year since 2000. This migration accounts for nearly 80-90% of the total population growth for the EU (IOM 2010b). However, many of the EU migrants come for seasonal or temporary labor situations, with roughly 600,000 migrants being classified as such (IOM 2010b). The transitory nature of some segments of migrants further challenges marketers when developing a sustained commitment to target these consumers.

While international migrants were born in different countries, it does not mean they do not have host country nationality or pre-existing ties with the host country. **Exhibit 1.5** shows that in 2008 the percentage of migrants who were nationals of the country they arrived in varies. This occurs when at least one of the parents was a national from the home country, but moved to another country. Poland, for example, saw 75% of their migrants having Polish nationality. This fact highlights the challenges in targeting migrants; just because someone is a migrant does not mean this individual lacks attachments to the host country.

Exhibit 1.5 Percentage of migrants who are nationals or non-nationals



Source: Eurostat (2010)

Outflows

Of the EU-27 countries, Italy and Spain have experienced the largest net inflow of migrants since 2000 (IOM 2010b). On the other hand, countries such as Bulgaria, Poland, Romania, Turkey and the Ukraine are the largest suppliers of migrants (IOM 2010b). Firms located in high migrant outflow countries face some serious challenges. Market saturation, increased foreign competition from globalization, and a shrinking consumer base all need to be addressed.

Rationales for Migration

The relative freedom in mobility for European Union citizens within the EU resulted in roughly 44% of the migration within Europe being from EU citizens in 2008. Central and Northern EU countries, like Austria, Denmark, Norway and Switzerland had over 50% of their migration inflows stemming from EU citizens (OECD 2010). In 2008, Mediterranean countries (Italy, Portugal, and Spain) and the United Kingdom had between 20%-30% of their immigrants arriving with work-related permits (OECD 2010). This is in contrast to Japan, Korea and the United States who see family migration as the primary rationale for migration (OECD 2010).

International students typically target schools located in France, Germany and the United Kingdom. However, Italy, Ireland, Spain and the Netherlands have experienced increases in international students over the last few years. Researchers have just begun exploring the impacts international students, who do not leave the country after graduation, have on the host country's society. It is estimated that between 15% and 35% of international students stay in the host country after graduation (OECD 2010).

Because the European Union is one of the world's leading economies, countries are actively pursuing acceptance into the EU. Accordingly, these countries want to enter the EU to see their economic situation improve. Thus, it is projected that as countries enter the EU they will see their migration trends move from outflow countries to inflow countries (IOM 2010b). This is because labor driven migrants tend to target countries with promising economic opportunities.

Residency Permits

It would be a mistake to think that many of these migrants are transitory or will return to their home countries after a few years. A total of 90% of new EU citizens in 2008 were previously citizens of non-EU countries. Moroccans, for example, accounted for 9% (64,000 in total) of the new citizenships granted in the entire EU. France, Italy and Spain granted the majority of these citizenships. Similarly, migrants of Turkish origins accounted for 7% (50,000 in total) of new EU member nation citizenships granted. Germany and France accounted for the majority of these new citizenships (Eurostat 2010). Businesses that target migrants can help them feel welcomed and adjust to their new homes and if these migrant communities have a high rate of becoming citizens, developing a long-term relationship with the communities could result in increased revenue and improved financial stability of the firm.

Communication Concerns

European countries, as most developed countries, tend to be more selective in their officially accepted migrants. The selection criteria usually favor skilled labor. France has one of the most stringent migrant acceptance policies in the EU, since they focus on the entire family's ability to integrate into French society. As migration policies become more restrictive, the ability to speak the host country's language will become more common, for example United

Kingdom has already formalized English language knowledge as part of their Points-Based System for admission into the country (IOM 2010b). Perhaps, in the future the need to communicate to international migrants in their home country language will decrease; however, offering promotional material and access to customer service representatives in an alternate language can help build the emotional bond between the customer and firm that is necessary in today's competitive marketplace.

Spain presents an interesting example; in 2007, roughly 75% of its immigrants had Spanish as their mother tongue (Instituto Nacional de Estadística 2010). Therefore, language is not always a barrier when targeting a migrant or minority population, but subtle cultural differences in vocabulary do exist. It should be noted that Morocco supplies the highest number of migrants to Spain but because of the cumulative amount of Latin American migrants Spanish speakers account for the majority of migrants (Instituto Nacional de Estadística 2010).

Table 1.3 Number of international migrants by sex in select EU countries

	Men	Women	Total
Germany	3,938,086	3,893,873	7,831,959
Italy	920,805	1,100,129	2,020,934
United Kingdom	2,102,505	2,400,961	4,503,466
France	2,772,523	2,827,675	5,600,198
Spain	963,060	951,860	1,914,920
Netherlands	689,883	730,057	1,419,940
Portugal	287,813	298,119	585,932
Belgium	489,916	529,386	1,019,302
Austria	442,254	481,438	923,692
Sweden	453,640	480,190	933,830
Switzerland	694,458	759,727	1,454,185
Denmark	155,079	164,222	319,301
Finland	55,710	56,720	112,430
Norway	149,495	156,428	305,923
Luxembourg	64,124	65,637	129,761

Source: OECD (2011)

Gender Differences

Economically driven male migrants typically find jobs in construction, manufacturing and finance. Since these industries were impacted the most during the economic downturn, male migrants suffered more than driven female migrants, who typically work in domestic related jobs. **Table 1.3** shows that except for in Germany and Spain, females account for more than 50% of the migrants, and in the United Kingdom nearly three hundred thousand more females have migrated there than males. The United Nations reports that females have composed between 52% and 53% of all European migrants for the last two decades (see **Table 1.4**).

Table 1.4 Female migrants as a percentage of all international migrants

Year	1990	1995	2000	2005	2010
Europe	52.7%	52.4%	52.8%	52.5%	52.3%

Source: United Nations (2009b)

European Highlights

Europe is becoming an increasingly popular destination for non-European migrants, and for citizens of EU member countries mobility among other EU member countries is relatively open. Further, migration impacts the demographics and size of a firm's target market in both the home and host country of the migrant. For the host country, over time a migration corridor can develop, providing an adequate concentration level warranting attention and the development of an ethnic marketing strategy.

1.4 Acculturation Process and Ethnic Marketing

The first two sections of this chapter described migration trends. Migration is both changing the consumer and the corporate landscape. We will first have a closer look at the consumer perspective.

1.4.1 The Consumer Perspective

Migration is a phenomenon that strongly influences the consumer landscape. Not only are the needs and demands of distinct subgroups very different, but immigrants also change preferences of the national non-immigrant consumers by introducing them to new food (just think of a kebab, which is a popular snack among many consumers outside Turkey; or Panzani's decision to offer products adapted to Muslims' needs), clothes, music and so forth. Immigrants do not just embrace the host culture, they help to change it. Intercultural contact is very dynamic and implies changes and influences simultaneously in both direc-

tions. This alignment of national and minority domains affects and alters the character of a country and its inhabitants. For the migrating persons, it constitutes an internal conflict as they face the dilemma of balancing their in-group attachment and desire to feel comfortable in the new environment with the attachment to their home country and culture (Grinstein and Nisan 2009).

Our own culture shapes our consumption behavior and activities – we actively seek out specific products and services to satisfy our individual needs (Grinstein and Nisan 2009). Consumption especially is very much influenced by cultural peculiarities: it affects the products and services consumed as well as the stores and marketplaces visited (Penaloza and Gilly 1999). People often use consumption as a means to express themselves, their identity and values. For minorities, this proposition entails even more profound implications: they use specific products not only to demonstrate their personal identity and values but also the ones from their ethnic group, the goals as minorities and position in relation to the majority group (Grinstein and Nisan 2009).

The way the host culture "welcomes" immigrants and the degree to which they are accepted by the majority influences their acculturation process and whether they consider the new environment as either hostile or friendly and adopting (Penaloza 1994). Accordingly, consumers can react in a multitude of ways.

Acculturation

When a person moves to a new culture there are four main modes of acculturation: assimilation, integration, rejection, and deculturation. Acculturation is the process a person undergoes while adjusting and managing themselves in a new culture and context (Berry and Sam 1980). It is important to remember that acculturation occurs at both the individual and group level.

Assimilation

Assimilation occurs when the person living in a new culture abandons or forgoes their home country's culture in order to completely accept and immerse themselves in the new host country's culture (Berry and Sam 1980). The rationales for assimilation are different for each person but the motivations for moving to the new culture help influence the desire to assimilate to the new culture.

Oftentimes the majority group intentionally or unintentionally pressures the minority group to assimilate to the majority group's culture and values in order to reduce perceived negative implications from being in the minority. Understanding how a migrant or minority group perceives themselves within the host country's social system helps determine the degree in which a marketing mix needs to be adjusted when targeting the minority group.

Integration

Integration occurs when an individual, or group, makes a conscious effort to show an interest in maintaining their original culture but is still willing to accept and interact within their new culture (Berry and Sam 1980). Overtime, interculturation can occur in groups who

integrate parts of the new culture into their home country culture. Interculturation addresses the creation of new cultures as a result of the melting of two or more cultures. You can see the emergence of new cultures from second-generation immigrants who form new traditions based, in part, on traditions from both cultures.

It is important to recognize that individuals can give the impression of assimilation while they have only integrated into the new culture. This is especially common regarding religious components of culture. Thus, individuals will appear as if they have accepted the host country's culture but their values and beliefs are still closely aligned with their home country religious practices and social customs.

Firms targeting European citizens who move to another European country should give particular attention to the distinction between assimilation and integration. While conducting an interview with a high-level manager at a world leading chemical company, the interviewee – who had lived as an expatriate in exotic countries like Thailand and Taiwan – stated to one of the authors that:

"…I always claim that the most difficult culture shock for me was the first time I came into Switzerland from the UK, because the cultural differences are not so visible, and you don't realize that you are going against some of the cultures – people or houses look the same, the shops are basically the same, but the underlying culture is quite powerful – but if you go to live in Bangkok, it is so visible what the differences are, and you quickly learn the major things on what to do and not to do…"

Besides illustrating how deep and subtle cultural differences can be, this quote highlights how easy it is to incorrectly assume people believe and act the same just because aesthetic features overlap. Research into consumption rituals can help marketers discover if similar objects have different meanings or roles in society between cultures.

Rejection

Rejection, sometimes called separation, occurs when an individual or group withdrawals from or avoids the host country's culture in an effort to preserve their own. Oftentimes these individuals will try to avoid interactions with the host country nationals entirely (Berry and Sam 1980). As a marketer, targeting individuals rejecting the host country's culture will require a more thorough marketing mix examination to ensure the minority group's deep cultural preferences and values are addressed.

Deculturation

Deculturation, or marginalization, occurs when individuals withdraw from the host country's culture because they find themselves unable, for personal and societal reasons, to maintain their cultural origins (Berry and Sam 1980). At the individual level, this mode of acculturation can be psychologically and mentally challenging.

1.4.2 The Corporate Perspective

What makes ethnic marketing challenging to companies is developing a strategy to cater to the needs of the segment while respecting their culture. Ethnic marketing, or ethnomarketing, can be defined as marketing to homogeneous ethnic groups under the great cultural diversity that characterizes current cultures (Páramo 2005). According to Geng (2001, p. 23), "ethnic marketing is referred to as the deliberate effort by marketers to reach a group of consumers presumably due to their unique ethnic characteristics." In order to make this deliberate effort successful, marketers need to consider various facets: Are there specific needs among minority groups that need to be catered to? How will a company have to change to serve this market segment? Will it require reconfiguring products or services? At what cost? What are the risks?

Furthermore, before deciding on a specific strategy, the following points should be taken into account:

Anticipation of stakeholder reactions:

- What is the likely reaction of the ethnic target to your offer? How will the target group respond to the offer in the stores?
- How will the existing customer base react to amendments? Should the existing customer base be informed and educated about the new offerings?
- How will the political environment and the community react?

Companies should try to calculate both potential additional revenues and sales due to ethnic targeting, as well as possible negative repercussions among the existing customer base. In case a particular company is the first one to implement such a strategy: how likely is the adoption of a similar strategy from its competitors?

Segmenting in Ethnic Marketing

Migrants have different cultures, preferences and consumption practices but how should a marketer decide if the ethnic segment is worth targeting? The following section presents a few issues that should be considered when evaluating whether or not to adjust the marketing mix to a migrant or minority group.

Clear Profile: One of the biggest challenges with ethnic marketing is clearly identifying the group and developing marketing messages and offerings that address its needs. Additionally, migrants from the same country could approach acculturation differently; a portion of the migrant community could be assimilating while the other portion is rejecting the host country's culture. Therefore, developing a clear, actionable profile of the minority group is quite challenging, if possible at all.

Concentration: Ethnic marketing rests on the foundations of market segmenting, specifically the market segment has to be big enough to support investment. Targeting a migrant group presents an additional challenge in that the concentration might not be long-term.

Economically driven migrants, for example, might return to their home country as the country's or their own economic standing increases. Thus, concentration of minority groups can fluctuate which in return changes the projected return on investment.

Access: Similar to concentration, the selected market needs to be accessible. The firm needs to reach the ethnic group with effective advertising, perhaps in a different language. Further, the firm needs to have the distribution network in place to get the products on the shelves of the stores the ethnic group frequents. The distribution network also includes distributors, sales representatives and advertising professionals who have or can develop contacts within the minority group. For example, Cumin, an advertising agency whose primary objective is to help firms target Turkish migrants in Germany, was selected by Deutsche Bank when they created Bankamiz to target Turks in Germany.

Demographics: The demographics of an ethnic group, especially composed of international migrants, can be quite challenging and dynamic. This is because the age, sex and education of the migrant group can change as the group establishes itself in the community.

1.5 Challenges Facing Marketers

Marketers face many challenges when addressing minority groups. Targeting an ethnic or migrant group relies on the fundamental market segmenting strategies while having the added challenge of acculturation, possible transitory nature of a migrant community, and group and individual identity issues. However, the number of international migrants is projected to continue increasing which presents a series of threats to European manufacturers. Therefore, developing an effective marketing mix can address these threats and produce additional revenue generating opportunities. This section provides an overview of some of these challenges or opportunities.

New migrant consumers: New consumers are typically great for firms. However, these new consumers have different tastes and preferences, not to mention potential languages, beliefs, and customs. Developing a marketing mix that attracts these new consumers without losing current consumers is challenging, especially if consumers or the press think the firm is exploiting the minority group.

European expansion: European firms are presented with an interesting marketing challenge in that: as the European Union continues to grow population mobility will become less restricted. Consumers will continue to move within the European Union even without the inflow of non-EU migrants. The increased mobility provided to the citizens of future EU countries could result in demographic changes for all EU member countries.

Changing demographics: Migration has a two-way effect on demographics. First, the country that receives, or hosts, the migrant will see its age or gender statistics change. Similarly, the home country of the migrant will see a reduction in the demographic statistics. This reduction is particularly challenging for the home country since the migration outflow is concentrated in one country whereas the migrants could go to a few different countries.

Romania is a good example since Romanians tend to migrate to Italy and Spain, enabling these countries to share the population growth; however, Romania loses all those citizens regardless of the migration destination.

Employee training: Front-line employees interact with consumers on a daily basis. Interacting with foreign consumers can be challenging for employees, especially if there is a language barrier. Employees could need training to improve their understanding of the minority group's culture and preferences. Companies that sell products or services that require negotiations are particularly good candidates for cultural training.

Legislative issues: Governments have the responsibility for managing their borders and addressing the needs of citizens and migrants. Occasionally legislative changes in migration related legislation can impact business issues. The most obvious business issues impacted by migration are related to employment issues. Firms are often attracted to the low cost labor provided by migrants but host country nationals can feel threatened resulting in legislative debates surrounding migration restrictions and quotas (IOM 2010a). During the global recession, many developed countries debated or implemented migrant worker restrictions, most particularly by reducing the quota of migrants to be accepted. Monitoring migration related legislation could be especially important for firms that engage in employee training programs, which cycle employees through different international divisions.

Information sources: Migrant preferences also extend to sources of information. Many migrants want to maintain a connection with their home country resulting in them reading newspapers, magazines and Internet pages from their home country. The probably of obtaining information from outside the host country increases if the migrant does not understand the host country's language.

In Europe, migrants can easily move to neighboring countries. This enables foreigners to watch television and listen to radio stations from their home country with relative ease, not to mention satellite and Internet television. Therefore, even if an ethnic group can be segmented and identified, reaching them with advertising could be difficult.

Idea diffusion: Migrants also bring new ideas and innovations to their host country. Conversely, when the migrant returns to their home country they help diffuse ideas and technology to their home country (World Bank 2008). A correlation has been found between outward investment from corporations based in the United States with the quantity, or concentration, of migrants living in the United States from the country receiving the outward investment (World Bank 2008). Therefore, developing close links with migrant communities can facilitate future growth into the migrants' home countries.

The products, styles and the different ways migrants use existing products can be a good source of innovation. Observation and field based marketing research strategies are well-suited to identify new uses for existing products. Also, researching the products migrants bring with them can stimulate innovation and help identify potential products to import or brands to acquire.

Marketing research: Research methods that place the researcher in the field are good options to develop an understanding of the minority or ethnic group. Traditional survey methods might need to be adjusted for few reasons. Access to minority groups could be difficult if they do not have landline phones or permanent addresses. Language barriers could also be an issue. Additionally, the culture might not be accustomed to traditional survey response procedures or, conversely, a firm's typical research methods might not be appropriately designed for the migrant group. Migrants that are not used to challenging opinions, such as some Asian cultures, or openly sharing their opinions could lead to incorrect assumptions about the community.

Branding Strategies: When ethnic marketing requires more than a simple adjustment to the marketing mix, such as using a model from the minority group or different languages, four main branding strategies can be used.

1. Brand extension: Introducing a new product developed for the minority group under an existing brand.
2. Create a sub-brand: Using an existing brand in the product category but adding a sub-brand to indicate that the product was developed for the minority group.
3. New Brand: Introducing a new brand to the market that is specifically developed and targeted towards the minority group.
4. Acquire an existing brand: Purchasing a brand that is already being used by the targeted ethnic group. Acquiring a brand presents additional challenges at the corporate level but it also comes with an existing distribution network and human capital with knowledge on the ethnic group.

Ethnic Marketing Highlights

This chapter began by showing that international migration is projected to increase for the coming years. Further, within the European Union there is a significant amount of population movement among countries. Migration obviously impacts the size of a country's population but also the demographics, such as age and sex ratios. Further, as migrants settle and form minority groups, they exert pressure on the host country's culture adjusting consumer preferences.

Marketers faced with increasing saturated markets and competition due to globalization migrant and minority groups can be attractive sources of additional revenue. Further, the advancements in technology now make targeting smaller but concentrated minority groups more profitable. However, developing an effective marketing mix that addresses the needs of the minority group is challenging. This is assuming that the minority group can be clearly identified and the firm has access to the group both in the terms of advertising channels and product placement.

1.6 Case Study: Bankamiz

Josep Franch and Matthew Hawkins, Research Group on Brand and Consumption at ESADE, Barcelona, Spain

1.6.1 Targeting Immigrants in Financial Services and the Banking Industry

Establishing trust is a basic requirement in any customer relationship; however, trust is a fundamental issue in financial services. Moreover, developing trust with consumers from another culture presents additional challenges. For this reason, many financial institutions are concerned with how to best target immigrants and foreign populations in their home countries. Accordingly, EFMA (European Financial Management & Marketing Association) has organized numerous conferences on how to target migrant markets.

Further, at a recent presentation, Roland Berger Strategy Consultants (2011) identified the increasing diversity of society as one of the trends in the European retail banking. Immigration was specifically recognized as part of this increasing diversity, arguing that financial institutions need to adapt their financial services and provide customized advisory services to meet the needs of consumers from different cultures. The presentation concluded by stating: "The challenge remains in the complexity of segmentation and branding strategies."

Spain's Banco Santander, Italy's Agencia Tu of Unicredit, and Germany's Bankamiz, a division of Deutsche Bank, are just a few examples of how some financial institutions are targeting immigrants with specific marketing strategies.

Banco Santander, Spain's largest bank, acquired Latinoenvios, a remittance company, after identifying that more than 10% of the Spanish population was composed of immigrants who had the need of transferring money back to their home countries every month. Further, most of these potential customers were from outside the EU. Latinoenvios services were integrated into Santander's approximately 3,000 bank branches. To fully capture this market, money remittance services were provided free-of-charge to all Santander customers who had their salaries directly deposited to the bank and the service was made easily available through ATMs 24 hours a day, 365 days a year.

Money remittance is very popular amongst the Latin-American immigrants in Spain, which account for account roughly 45% of all immigrants in Spain. But Spain also has immigrants from other countries; therefore Banco Santander has developed other partnerships. For example, Santander has partnered with Morocco's Attijariwaffa Bank since Moroccans are one of the main and growing nationalities migrating to Spain.

After estimating that there are more than four million foreigners working and living in Italy, the Italian bank UniCredit launched the concept Agenzia Tu (literally "your agency")

to target these foreigners. Agencia Tu hires people who can attend to foreign customers in different languages so they feel more comfortable. Furthermore, specific products have been developed for foreign nationals working and living in Italy, with information available in different languages. Even opening hours have been adapted to be more convenient to foreign nationals.

1.6.2 Bankamiz: A new division of Deutsche Bank for Turkish immigrants

Deutsche Bank discovered that their customer based had roughly 230,000 Turkish immigrants living in Germany. Besides the fact that Turks are the second largest foreign nationality represented in Germany, there were many other important reasons to consider Turkish customers as an attractive target group for Deutsche Bank to be addressed by a specific marketing strategy. The Turkish migrant population in Germany was concentrated in specific areas or regional clusters. This is highlighted by the fact that Deutsche Bank estimated that the majority of Turkish customers could be reached with only 100 branches. Conversely, to reach a similar number of Russian immigrants, more than 600 branches would be needed. The purchasing power of the Turkish migrants was estimated to be more than €16 billion. The majority of Turks living in Germany planned on staying in Germany for the immediate future. They felt integrated in the country, were looking for a future in Germany, and wanted better living standards not only for them but also for their families.

Saving was important behavior for Turkish people. For example, more than 50% of the Turks in Germany saved a respectable amount of money each month, with an average saving rate per household around €440 (Erdem and Schmidt 2008). Additionally, some research studies were showing that the degree of integration of Turkish migrants in Germany was positively related to their total saving amounts and that the higher the level of integration the more likely it is for them to have savings in a German bank rather than in a Turkish bank (Ulku 2008).

Financials were typically discussed within the family (Pohl 2008) and first, second and third generation of Turks in Germany shared the same values and emotions (Kaya 2009). But, despite the high level of integration, research showed that the Turkish culture and language prevailed and that Turks in Germany typically felt more comfortable with their own culture. They had developed their own way of living, their own cultural identity, as a subculture melting elements from the Turkish and the German cultures. But it is estimated that approximately 30% of all Turks living in Germany only buy Turkish newspapers and around 40% watch Turkish TV exclusively. However, the good news was that there are a lot of media available in Turkish. Newspapers like Hürriyet, Sabah or Milliyet are widely distributed in Germany, and TV channels in Turkish like TV avrupa, Show TV or Euroshow are available. Regardless of the media habits of the Turkish community, Deutsche Bank estimated that the costs of acquiring new Turkish-German customers was generally lower than the cost of acquiring traditional German customers.

The challenge for Deutsche Bank was how to generate a sense of proximity and build trust amongst Turkish customers. Deutsche Bank decided to create a new division to target Turkish customers in Germany. The brand name chosen was Bankamiz, which literally means in Turkish "our bank" or "the bank of us". And one of the first images to be developed to promote this new brand, which has since become the brand's icon, was a cup of tea. Deutsche Bank selected tea since it is part of the Turkish culture. Tea, as a product, is appreciated and often consumed by the Turks; and tea is also a symbol of friendship and hospitality. Accordingly, one of the main images became a glass of tea with the Deutsche Bank logo on the side; together with some sugar cubes (see **Exhibit 1.6**).

Exhibit 1.6 Bankamiz – Welcome to your bank, the one that speaks your language

Source: Bankamiz

Not only is this image shown in the majority of pictures, posters and promotional materials such as brochures, but Bankamiz also serves tea and typical Turkish pastries in all the branches in order to create a familiar atmosphere and a "feel of home" feeling for the Turkish customers. Bankamiz was born with the idea of generating trust by making Deutsche Bank accessible for Turkish customers and generating the feeling that Bankamiz really understands the Turkish immigrant needs, by providing services not just for today but also for their future needs. In order to generate trust and understanding, Bankamiz staffed people fluent in Turkish to attend to the customers in their own language, with the aim of better understanding the customer needs and to be able to provide better financial advice. More than half of the ATMs operated by Deutsche Bank in Germany also have menus available in Turkish. Bankamiz started in 2006, in only 13 of Deutsche Bank branches and with 22 Turkish speaking staff. Overtime time, Bankamiz progressively increased to 59 branches and 120 Turkish speaking staff in 2010. As a result, Deutsche Bank attracted 75,000 new customers.

A product portfolio tailored to Turkish customers

Bankamiz offers a product portfolio designed to address the specific needs of Turkish customers. Product offerings have been tailored to help customers identify and relate with the products. The following are a few examples of specific products developed for the Turkish-German customer.

- Bankamiz Account ("Bankamiz Konto"). This bank account is presented to Turkish customers as an account for daily operations. It offers a basic account and a premium account for a higher fee. In both cases, five free of charge money transfers a year are offered to the customers. Customer service by phone is provided in Turkish and German, 24 hours a day 365 days a year. Customers have access to 7,000 ATMs in Germany and 35,000 ATMs abroad through partner banks in 32 countries. In case of an emergency, customers have access to €1,500 in cash in 120 countries, including Turkey. There is a 50% discount for customers with more than one account and a 50% discount for family members. Bankamiz customers can also choose Turkish motifs to be printed on their credit cards associated with this account, including the famous Turkish eye-shaped protective talisman called Nazar Boncuğu or Nazarlink, a picture of the Turkish national football team or some important Turkish monuments or Turkish landmarks.
- Bankamiz Private Credit (Bankamiz PrivatKredit). This is a credit line for an amount between €5,000 and €50,000 and a term between 12 and 72 months for buying furniture or a car, going on holidays or organizing a wedding. Customers should be German residents and with an age above 18. Credits are probably not that different from Deutsche Bank credits, but they are targeted for different moments or situations in the life of a customer, such as couples that are getting married, for students and those people continuing education, with a focus on typical Turkish values. Money can be received the same day, there is a 6-month period free of interest payments and debt repayments, and one monthly quota per year can be adjourned. Additional insurances cover the quotas in case the customer becomes unemployed. The brochure has a picture of a car key with a Nazar Boncuğu (traditional Turkish eye-shaped protective talisman) key ring and a message that says "Directly to the destiny of your wishes" (see **Exhibit 1.7**).
- Bankamiz Fixed Interest Savings (Bankamiz FestinzinsSparen). This is a savings account with a fixed interest rate for amounts from €2,500 onwards. Terms are selected by customers between six months and eight years. The longer the term selected the higher the interest rate, but money withdrawals should be noticed by customers three months in advance. The brochure shows a picture of two wedding rings with the words in Turkish "hope" and "desire" engraved and a message that reads "Save for the most beautiful goal of your life" (see **Exhibit 1.7**).

Exhibit 1.7 Brochures of different Bankamiz products

Source: Bankamiz

- Bankamiz Home Loan Savings (Bankamiz Bausparen). This savings account is intended for a period of time between 7 and 10 years at an attractive interest rate. After saving for at least seven years, a customer can use the savings for acquiring a house, or other things like a car or to pay the expenses of a wedding. In case the customer wants to acquire a house, a mortgage with a low interest rate is available and government subsidies can also be applied. The brochure presents a picture of the door to a house open, with a key in a lock and a key ring with the Nazar Boncuğu (traditional Turkish eye-shaped protective talisman) and a message that says "Welcome to your own home."
- Bankamiz Retirement Funds (Bankamiz Zukunftsvorsorge). This retirement fund shows a picture of a typical Turkish tablecloth and a cup of Turkish mocha coffee and a message that reads "See the future clearly with our consultants" (see **Exhibit 1.7**). The brochure explains to the Turkish customers that several years ago their parents arrived in Germany with the intention of going back to Turkey after saving some money, but nowadays many of them are pensioners who are enjoying their retirement in Germany. Unfortunately, in the near future, state pension funds will not be high enough to maintain current living standards. Therefore, this account allows customers between the

ages of 60 to 67 years to withdraw a maximum of 30% of the funds. In the event of a decease, disablement or unemployment, the funds are maintained or transferred to family members.

An advertising campaign designed by experts on intercultural marketing

The advertising campaign for Bankamiz was designed by Cumin, an agency founded in 2002, with branches in Berlin and Istanbul, who are experts on intercultural marketing. Deutsche Bank commissioned Cumin in 2007 with the design and development of the Bankamiz campaign. The main challenge for the agency was to generate trust amongst the target group members.

Accordingly, Cumin developed a TV ad featuring a Turkish family unit in Germany some two or three decades ago. The ad showed the father visiting a Deutsche Bank branch with his young daughter who translated what the bank staff was explaining, as he did not seem very fluent in German. A few years later, the same family was celebrating the graduation of the daughter and moving into a new house. At the end of the TV ad, the daughter is shown working at the Bankamiz division of Deutsche Bank and attending customers. This ad was showing what could be the story of a Turkish family migrating to Germany in the late 60s or early 70s looking for job opportunities and how the second generation managed to get university education and progressively they became integrated into German society. This ad was so effective that a version was adapted to be used in cinemas as well. A series of print ads, promotional leaflets and a direct marketing campaign were also produced in both German and Turkish.

After a six-week advertising campaign in different media (TV, radio, newspapers) and additional promotions, Cumin reported that Bankamiz had achieved a brand awareness close to 70% amongst the target group and had an increasing the level of trust. The Bankamiz web page (www.bankamiz.de) is available in Turkish and German. The first message one can see on the Bankamiz web page is the following: “Life is easier if there is a bank you can trust, who speaks your language and understands you. A bank with services and products specifically tailored to your individual situation. This is now possible with Bankamiz”. This further demonstrates the importance of trust for financial institutions.

Personalized credit cards with Turkish motifs

Deutsche Bank was the first bank offering customers the opportunity to print on a credit card a motif chosen by the customers. A very popular motif is the Turkish national football team. This allowed customers to “Always carry the 11 heroes with you” – this motif was particularly popular during the 2008 UEFA European Football Championship. Customers can also select other Turkish motifs, like the Turkish eye-shaped protective talisman called Nazar Boncuğu or Nazarlink. Customers can choose from monuments like Maiden’s Tower (Kiz Kulesi), the Grand Imperial Mosque (Ortaköy Mosque) by the Bosphorus, or the Blue Mosque (Sultanahmet Camii) or some Turkish landmarks like Hierapolis (Pamukkale), a UNESCO World Heritage Site to print on their credit cards. Alternatively, customers can also print a family photo on the credit card.

Bankamiz's promotional campaigns appealing to Turkish customers

All the promotional campaigns designed by Bankamiz are also focused on the Turkish culture. Turkish values and icons are consistently used in Bankamiz's marketing campaigns and promotional materials.

A very effective campaign during the 2008 UEFA European Football Championship was a starter's kit for new accounts that included the Turkish national team football jersey as a present. Customers opening an account also received in the past a €75 discount for LIG-TV, a pay-per-view TV channel of the Turkish soccer league. Discounts vouchers for specific shops for an amount between €25 and €50 have also been given during certain Turkish national holidays.

Other typical gifts include a key ring with the traditional Turkish eye-shaped protective talisman ("Nazar Boncuğu"), a piggy-bank with a very popular Turkish cartoon character for kids, called "Nasrettin Hoca", or reduced fees with a mobile operator called E-plus.

Member-get-member promotions include football jerseys from the top Turkish football clubs – like Galatasaray, Fenerbahçe, Beşiktaş or Trabzonspor, the biography of Mustafa Kamal Attatürk – the founder and first president of modern Turkey, a "Tavla" – the Turkish version of backgammon, Semaver – a famous Turkish brand – tea wear products, and many other gifts.

In different Turkish traditional holidays or celebrations, like Ramadan or the Turkish Sacrifice Holiday – also known as the Feast of Sacrifice ("Kurban Bayram") – greeting cards are sent to all customers. On Ramadan, some selected customers are invited to dinner when the sun sets. Bankamiz also actively supports different Turkish traditional events such as Children's Day ("Çocuk Bayrami"), the Day of the Republic ("Cumhuriyet Bayrami") or the day Attatürk is commemorated, which is also the Youth and Sports Day ("Gençlik ve Spor Bayramı").

Career opportunities at Bankamiz

Bankamiz tries to staff people not only fluent in Turkish but who are also well aware of the Turkish culture. Employment opportunities are offered to people with financial or banking education, who are customer- and service-oriented, fluent in Turkish and integrated with the Turkish community.

Student Assignments

1. Describe the marketing mix of Bankamiz. How is it different or similar to the marketing mix of Deutsche Bank?
2. Develop a segment profile of Bankamiz's customers as a minority group. What are the challenges of targeting this segment? What would you do to overcome these challenges?
3. What are the largest minorities in your home country? Are there similar experiences of banks or financial services targeting immigrants in your country? Prepare a short description of similarities and differences with Bankamiz.
4. What are the main take-aways from the Bankamiz case? Can we apply these take-aways to other products or industries?
5. Looking at your home country, find experiences of targeting immigrants from other markets or industries.
    a. Identify a product or service that is a combination of your home country and another country's culture.
    b. Develop a marketing strategy for a new product or service that includes components from a migrant community's home country culture.
    c. Identify a minority group in your home country and develop a marketing strategy to reach these potential consumers.
6. Select a candidate to the European Union and discuss how their entrance would affect the broader European market.

1.7 Case Study: KFC in France

Verena Gruber, International Marketing Management, WU Vienna, Austria

The global foodservice sector is a very dynamic one, characterized by continuous expansion, product innovations and fierce competition. YUM! Brands, with its portfolio of five brands, leads the global foodservice market in terms of outlets but ranks second behind McDonald's in value terms (Euromonitor 2011). Four of the company's restaurant brands – KFC, Pizza Hut, Taco Bell and Long John Silver's – are the global leaders of the chicken, pizza, Mexican–style food categories and quick–service seafood categories (Restaurant News 2011). Within the foodservice market, fast food chains are strongly represented and constituted the growth leaders in 2009, as consumer perceived fast food chains offering good value. The company operates franchises in over 110 countries and employs about 350,000 people (Datamonitor 2011). YUM! Brands Inc. is ranked #216 on the Fortune 500 List, generating revenues of more than $11 billion in 2010.

According to Business Week and Interbrand, YUM! Brands is one of only five companies in the world to have two of the top global brands with KFC (64th brand in their top 100 global brands ranking in 2009) and Pizza Hut (79th position). Kentucky Fried Chicken operates in 108 countries with more than 5,000 units in the US and more than 11,000 outside the US. BusinessWeek-Interbrand valued KFC at $5,722 million in 2008.

Table 1.5 Top chained foodservice brands 2009

Brand	Sales, 2009 (US$ bn)	% Value Share, 2009
McDonald's	71.7	13.1
KFC	17.8	3.3
Burger King	14.2	2.6
Subway	13.5	2.5
Starbucks	13.5	2.5
7-Eleven	12.5	2.3
Wendy's	9.4	1.7
Pizza Hut	9.3	1.7
Taco Bell	6.9	1.3

Source: Euromonitor 2011

1.7.1 KFC – Company Development

Kentucky Fried Chicken, based In Louisville, Kentucky is the world's most popular chicken restaurant chain. In 1930, Colonel Harland Sander opened his first restaurant in Kentucky and named the dining area "Sanders Court & Café".

Colonel Sanders is still an important figure for both the company and its consumers. He represents the American origins and is an essential part of the brand. In 1952, Pete Harman in Salt Lake City became the first franchisee for KFC. This was the beginning of a world-wide chain. Today, more than 12 million daily customers are served in one of KFC's 15,000 restaurants in 109 countries.

Exhibit 1.8 Central figure Colonel Sanders and Development of KFC Logo

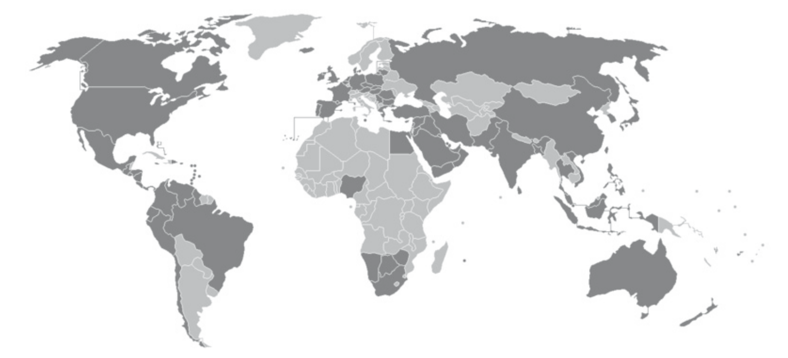
Source: Kentucky Fried Chicken (2011a); Logolook (2011)

KFC is positioned as a family dining brand as it is offering a large selection of total meal solutions. KFC restaurants offer fried and non-fried chicken-on-the-bone products under the names Original Recipe, Extra Tasty Crispy and Kentucky Grilled Chicken. Other principal items on the restaurant's menu include chicken sandwiches, KFC Famous Bowls, Colonel's Crispy Strips, chicken wings, Popcorn chicken and Chunky Chicken Pot Pies. The outlets also offer a variety of side items such as biscuits, mashed potatoes, corn and potato wedges as well as desserts (Datamonitor 2011). As a consequence, KFC restaurants are not only competing against fast food operators but also against full-service restaurants, which cater to the whole family.

KFC is actively involved in community programs and promotes education, diversity and animal welfare in a number of positive ways. Diversity is an especially important topic for both KFC and YUM! Brands: "For us, diversity is not a target - it's a way of life and a way of doing business. This adds perspective and depth to everything we do. We've also found

that a diverse team makes for better problem solvers, services all our customers more effectively, and creates a richer culture for all of us to enjoy. In our company-owned operations in the U.S. for example, about 30 percent of our associates are Caucasian and the remaining 70 percent are Hispanic, African American and/or Asian. Minorities and women made up 64 percent of our external management hires and 41 percent of internal management hires (promotions) in 2007" (YUM! Brands 2011).

Exhibit 1.9 KFC worldwide



Source: Wikipedia 2011

Concerning the ownership structure of the chain, KFC has passed many stages. In 1971, Heublein Inc. acquired KFC Corporation, which was later on acquired by R.J. Reynolds Industries, Inc. (now RJR Nabisco, Inc.). For a few years, KFC was a subsidiary of Reynolds until being bought by PepsiCo, Inc. in 1986. A decade later, in 1997, PepsiCo announced the spin-off of its quick service restaurants, namely KFC, Taco Bell and Pizza Hut, into Tricon Global Restaurants, Inc., which changed its name 2002 to YUM! Brands, Inc. Nowadays KFC is still part of the world's largest restaurant company and continues to serve high quality and innovative products to its customers (Kentucky Fried Chicken 2011a). In the US, the market is stagnating: sales declined by 8% in 2010 due to the YUM! Brands continued refranchising activities in the market and KFC's poor performance and 8% same-store sales decline. Overall for the whole year 2010, Euromonitor predicted a sales growth of just over 4% to US$ 11.3 billion (Euromonitor 2011).

There are several factors YUM! Brands has to consider for its strategic development:

- KFC, the core brand of YUM! Brands, is performing poorly in the US market; new product introductions failed to sustain momentum but also core products fail to yield expected sales due to a lack of marketing support.
- France is a vitally important market, especially for KFC as chicken fast food is predicted

to continuously increase from 2009 to 2014. As YUM! Brands has invested heavily in France, it will be the main beneficiary of this projected US $500 million sales increase.

- YUM! Brands has been very committed to increasingly offer healthier food options among its chains, especially at KFC restaurants. However, this preference of healthy food options over core fried chicken products has already entailed negative consequences as core customers have been alienated.

1.7.2 KFC expansion and KFC France

What started in 1952 with the first franchise in Salt Lake City led to over 190 KFC franchisees and 400 franchise units in the U.S. and Canada in 1960 and over 600 franchised outlets and a first oversee unit in England four years later. KFC initially got off to a meek start in France. Its former parent PepsiCo opened just seven locations in 1992 before abandoning the effort to expand elsewhere. Nowadays, KFC’s presence in France is of particular importance, as the Wall Street Journal (May 5th 2010) noted:

Yum executives see KFC's France business as an anchor for what could be a broader expansion in continental Europe. KFC's European footprint is under 800 restaurants, lagging behind burger chain McDonald’s Corp., with about 5,600. KFC plans to have 300 stores in France by 2015, and sees a possible tenfold increase over time. "One day I'd like to have over 1,000 stores here, though we're going to take it 100 by 100" at a time, Ivan Schofield, general manager of KFC France, said in an interview. "It's their most important market in Europe," […] restaurant analyst Steve West said. "Obviously, China's the most important market, but there's a lot of growth opportunity for Yum in France” (Wall Street Journal 2010).

Fast-food competition remains less intense in France, where McDonald's and local operator Quick dominate the market. In addition to relatively tame competition, France has another major appeal: It is one of the largest dining-out markets in Europe. Many French consumers still frequent locally owned, corner restaurants, but fast food has made headway as diners cut their lunchtime down to 30 minutes or so, Mr. Schofield said. France's fast-food customers also tend to prefer full meals with desserts, rather than just sandwiches, which bring the average sale to between €6 and €8 (about $8 to $10.50) at KFC. As a result, KFCs in France make more money than anywhere else in the world. Stores on average reach sales of $4 million a year, about three times that of the average KFC elsewhere in the world (Wall Street Journal 2010).

The French market is of crucial importance for YUM! Brands and KFC as well as other fast food companies and constitutes an important strategic basis for Western Europe. Consider the following statement by David C. Novak, the Chairman and Chief Executive Officer at YUM! Brands (YUM! Brands 2009): “Meanwhile, we are off and running, widening our competitive advantage, getting stronger and more diversified every year. What excites me most is that there’s no doubt our calculated investments in high potential markets are definitely paying off. Five years ago we were just starting to make headway in France. Today,

France has the highest average unit volume in the world and now the rest of Continental Europe has a proven model to follow”.

The French market is a primary target market for YUM! Brands as the country is considered to be underpenetrated and offering a strong potential for outlet expansion despite local competitors such as Quick. This chain, however, has made some attempts in the last few years to strengthen its customer base by focusing on the lucrative group of Muslim consumers:

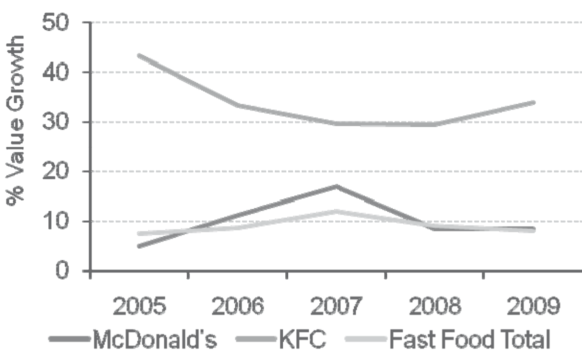
“The Quick chain of 358 restaurants around France said it would boost its halal-only outlets to 22 on Wednesday after the trial in eight areas with a strong Muslim population also saw a doubling of customers and a rise in the amounts they spent. The growing halal market is now twice as large as that for organic food in France, whose five million Muslims make up Europe’s largest Islamic minority. Quick came in for criticism earlier this year when its trial, which sold only halal beef and replaced bacon with smoked turkey, hit national headlines. Agriculture Minister Bruno Le Maire said ethnic marketing like this was against French values” (Reuters 2011).

KFC’s presence in the French market has continuously increased from just 19 outlets in 2002 to 115 outlets by November 2010. Due to this dynamic growth, KFC has outperformed McDonald’s as well as the total fast food market. YUM! Brands plans on aggressively continuing this expansion strategy and reaching 200 outlets by 2013. However, McDonald’s also considers France to be the most attractive market in Western Europe and will therefore maintain competition at a high level.

KFC competes with a strong and innovative product menu, including both healthier and more customized offerings. The aggressive outlet expansion together with a continued menu innovation should smooth KFC’s way to keep up momentum in this highly attractive growth market.

The situation in France is not only very promising in financial terms but also highly demanding when it comes to marketing. The population’s composition is very diversified and the country accommodates a number of ethnic subgroups, stemming from former French colonies and DOM-TOM (Département d’outre-mer - Territoire d’outre-mer). It is paramount from migration statistics that the inflow from these countries is a continuous one and will further change the French landscape.

Exhibit 1.10 Fast food in France: value growth of KFC vs. McDonald's vs. total market 2005-2009

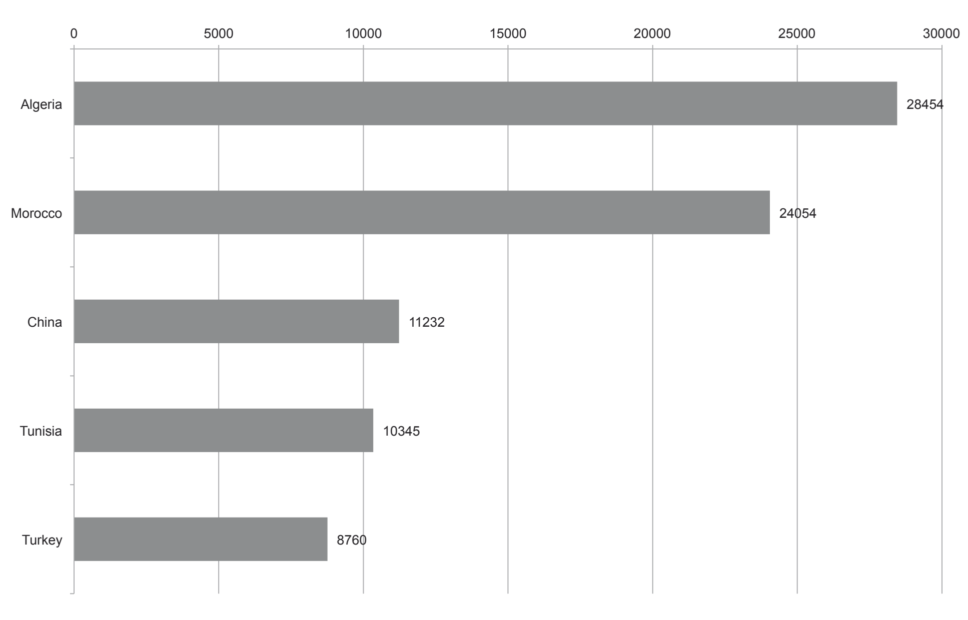


Source: Euromonitor 2011

Exhibit 1.11 KFC in France

Source: Kentucky Fried Chicken (2011b)

Exhibit 1.12 Most numerous immigrants to France, 2006



Source: Eurostat (2008b)

There is, however, a common characteristic among these subgroups: most of their members follow the Muslim religion, which is why we will have a closer look into this religious orientation.

1.7.3 Muslim Religion

Muslims follow a belief system that is based upon five pillars (Islam Guide 2011):

- Shahada: a testimony of faith which is the basic creed of Islam,
- Salat: a prayer which is performed five times daily,
- Zakat: which means supporting the needy,
- Sawm: fasting which occurs from dawn until sundown during the month of Ramadan,
- Hajj: a pilgrimage to Mecca once in a lifetime for those who are able.

Strictly observant Muslims further follow the sharia, a framework extending religious beliefs into the private, social and political life. The religion also prohibits its members to engage in haram activities (or haraam, the Arabic word for forbidden), which include for instance drinking alcohol or consuming proscribed food products such as pork. Additionally the followers of the Islamic religion are not allowed to eat already dead animals, birds of

prey, land animals without ears, blood or animals improperly slaughtered. The last rule implies that animal slaughter must be done in such a way that results in a quick and humane death and reduces the animal's suffering. To be even more specific, an animal's jugular veins and carotid arteries must be cut with a sharp knife in order to produce a maximum blood flow (Islam Guide 2011). All this is done in the name of Allah. The Sharia law applied to food products further specifies that they must not contain additives that are not "clean" or untainted during processing, packaging, storage, transportation or transaction. Other food products which contain ingredients such as gelatin, enzymes, emulsifiers, and flavors are questionable (mashbooh), because the origin of these ingredients is not known (IFANCA 2011). If these premises are fulfilled, the food product is considered to be Halal or permitted according to Islamic law (Islam Guide 2011).

The question whether a product is haram or halal is not always clear and unambiguous. Especially cases of cross-contamination are of great concern as well as the question of whether automated facilities are allowed in the slaughtering process (calling out the name of Allah via tape versus a person speaking the required words). As a consequence, countries and certifying bodies also diverge in their opinions regarding appropriate halal standards which impose difficulties for companies operating internationally.

What is more, there is no single unified authority in Islam which means that the interpretation of ambiguous cases is the responsibility of the certifying bodies, which are quite different concerning their certification standards. Halal certifications can be issued by one of over 100 halal certification agencies worldwide, whereby each of the organizations holds their own set of standards and guidelines concerning the certification. Whereas there is one major agency in the US, the Islamic Food and Nutrition Council of America (IFANCA), the situation in Europe is more difficult. There are numerous bodies offering Halal certifications and companies need to take care that the certifying body is the official agency of the specific country they are operating in.

1.7.4 The Muslim Consumer

According to a recent Business Issue paper of the AT Kearny consulting company specifically addressing the opportunities of the Muslim market, the demand for sharia-compliant products and services reaches a $2 trillion mark annually and is increasing rapidly (A.T. Kearney 2007). Western countries and governments increasingly accommodate Islamic peculiarities, such as Britain planning to sell treasury bonds compatible with Islamic rules against interest payments. The paper also stresses the importance of the Muslim market that western businesses cannot afford to ignore. Advertising executives are aware of the huge potential of this group and assume that ignoring them would be like missing the Hispanic market in the 1990s (NY Times 2007). According to projections for 2010 to 2030 of the Pew Research Center's Forum on Religion and Public Life, the world's Muslim population will increase about 35%, therefore growing at about twice the rate of the non-Muslim population. For Europe alone, the analysis projects a growth by nearly one-third, rising from 6% (44.1 million) of the region's inhabitants to 8% (68.2 million). There are on average

more people leaving Muslim-majority countries than migrating to them, target countries being more-developed ones such as Europe, North America, New Zealand and Australia.

Table 1.6 Number of Muslims in selected European countries

Countries	Estimated Muslim Population 2010	Estimated Percentage of Population that is Muslim 2010	Projected Muslim Population 2030	Projected Percentage of Population that is Muslim 2030
Austria	475,000	5.7%	799,000	9.3%
Belgium	638,000	6.0	1,149,000	10.2
Denmark	226,000	4.1	317,000	5.6
Finland	42,000	0.8	105,000	1.9
France	4,704,000	7.5	6,860,000	10.3
Germany	4,119,000	5.0	5,545,000	7.1
Greece	527,000	4.7	772,000	6.9
Ireland	43,000	0.9	125,000	2.2
Italy	1,583,000	2.6	3,199,000	5.4
Luxembourg	11,000	2.3	14,000	2.3
Netherlands	914,000	5.5	1,365,000	7.8
Norway	144,000	3.0	359,000	6.5
Portugal	65,000	0.6	65,000	0.6
Spain	1,021,000	2.3	1,859,000	3.7
Sweden	451,000	4.9	993,000	9.9
Switzerland	433,000	5.7	663,000	8.1
UK	2,869,000	4.6	5,567,000	8.2
Total	18,267,000	4.5	29,759,000	7.1

Source: Pew Forum (2011)

Due to continuous migration, the highest increases are likely to occur in Western and Northern Europe, for instance in Belgium from 6% today to 10.2% or in France from 7.5% to 10.3% (Pew Forum 2011). The population of Muslims in Europe has grown from 4.1% or 29.6 million in 1990 to 6.0% or 44.1 million in 2010 and is therefore increasing at a faster pace than the non-Muslim population.

Reuters (2011) assumes that the Halal food market is worth $560 billion. According to A.T. Kearney (2007), it is worth $30 billion to the top five food retailers worldwide and another $15 billion to the top 10 food processing companies. McDonald’s has been a pioneer in addressing Muslim consumers’ needs, especially in Asia. McDonald’s Singapore saw an influx of eight million patrons a year after obtaining a Halal certification (Lada et al. 2009).

Despite being inclined towards Western assortments, Muslim consumers are increasingly opting for products and services that reassert their identity as Muslims and respect their principles. They consciously choose Islamic brands, Halal certified food and financial services compliant with the Qur’an. Around 70% of the worldwide Muslim population adheres to Halal products and services and the vast majority of them (about 75%) indicate their willingness to stick to these standards even after having migrated to another country (Lada et al. 2009).

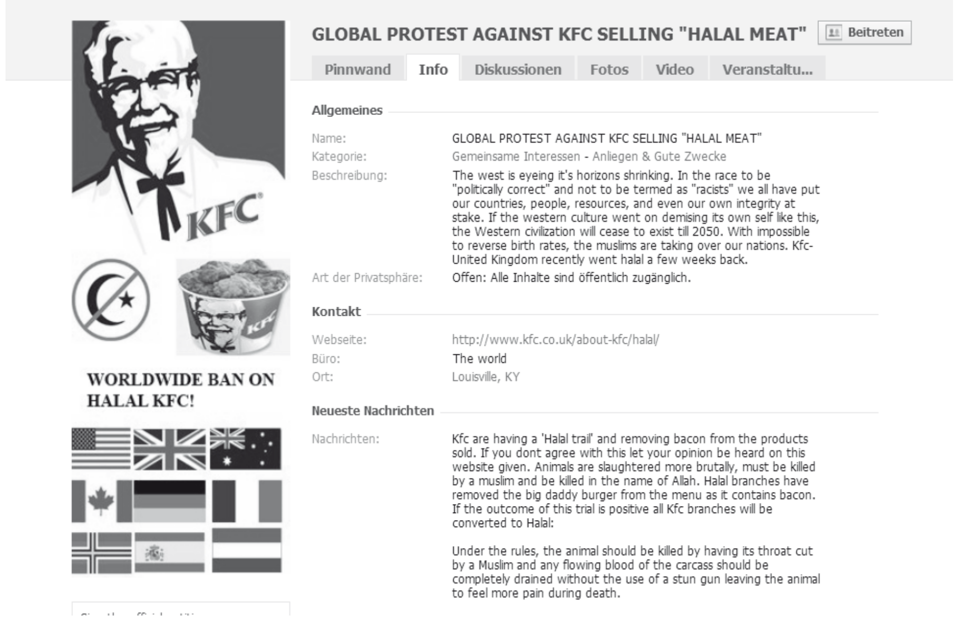
In summary, marketing managers should be aware of the following factors: the Muslim population is increasing rapidly as is its purchasing power. There also appears to be growing devotion to Islamic principles and prescriptions among its members.

Student Assignments

Yum! Brands and KFC have several key strategic objectives they want to pursue: First the company has to strengthen its performance in both domestic and international markets to generate a high return on invested capital and strong shareholder payout. Another goal refers to an aggressive global expansion, continuing the pace of 2009 with four new outlets opening each day.

YUM! Brands needs to find the right balance and offer a strong range of diversified choices without neglecting its core product range – as it otherwise risks alienating core KFC customers. This applies to both healthier food (which implies the risk of losing the Original [fried] Recipe loyal customers) as well as Halal food. Consider the following illustration:

Exhibit 1.13 Outcry of KFC customers



Source: Facebook (2011)

This Facebook group has several thousand members and clearly demonstrates the resistance among core customers to KFC's attempt to address the needs of Muslim consumers. The outcry is enormous even though there is only a single product, the Big Daddy, of more than forty items on KFC's menus that will not be served in Halal stores.

Where do you want to go with the KFC brand?

You are responsible for the strategic development of KCF France and need to decide upon the next steps of the brand's positioning. Of course you are aware of the strategic relevance of your country and the implications of your decisions for the rest of Europe.

Come up with a plan outlining KFC's strategy in France and its implications for other European countries. When developing your plan, consider the following questions:

1. What implications does the composition of immigrants to France and the European Union in general have for your marketing plan?
2. What needs do KFC restaurants fulfill? How are they perceived by minorities?
3. How do you feel about different stakeholders (majority vs. minority consumers, communities, politicians)? Are they of the same importance to your company or do you prioritize among them? How would you react to their wishes and cater their needs?
4. Are you going to communicate KFC's plan to the public? If yes, how do you want to accomplish this?
5. To what extent is the French market a role model for other European countries and KFC outlets? Would you suggest a similar strategy for other nations?

Possible further questions for discussion:

1. What is your general attitude towards the integration efforts of immigrants? When in a new cultural environment, should immigrants assume an adaptive behavior, as in the old saying "When in Rome, do as the Romans do" or should they stick to their heritage?
2. What consequence does this have for your targeting?

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2 Fighting social isolation through a user-friendly mobile phone: Bazile Telecom

Raphaëlle Lambert-Pandraud, Marketing Professor, ESCP Europe, Paris

Yves Morel, CEO and founder of Bazile Telecom

> **'A simplified high-tech phone to comfort Seniors: A single button mobile phone**
>
> Mrs. Telecom is back unexpectedly. A small firm, Bazile Telecom, is selling a single button mobile phone! By pressing it, users get in touch with a Tele Operator who puts them through to the number of their choice. The phone sells for €60, plus a monthly (and tax deductible) €15 subscription to make the service available. This fee does not include communications; the subscriber keeps the Mobile Operator of his choice. Bazile Telecom started in the south of France in 2008 and has since expanded to the rest of the country.'
>
> ***Joël Morio, 29 March 2009, Le Monde***

2.1 Introduction

Today, industrialized countries face the long-term aging of their population. The over-65s may account for 20% of the European population by 2020, and the over-75s comprise the fastest growing age group.

In contrast, new product innovation mainly targets consumers below the age of 50. One striking example comes from high tech markets: mobile phones were introduced at the end of the 1990s; they are now being progressively replaced by smart phones. In the second half of 2009, mobile phone sales declined by 6%, whereas sales of smart phones jumped by 27% (Calignon 2009), accounting for around 15% (Euromonitor GMID) of the mobile phone market.

These new communication devices are not very successful among the elderly, a target of growing economic importance. For example, in France, only 48% of the over-70s use a mobile phone compared to 78% of the population aged 12 and over (Bigot and Croutte 2010). In contrast, the over-60s own 60% of the assets (Secodip 2004) and account for 45% of the fragrances and 28% of the facial care markets (Secodip 2006).

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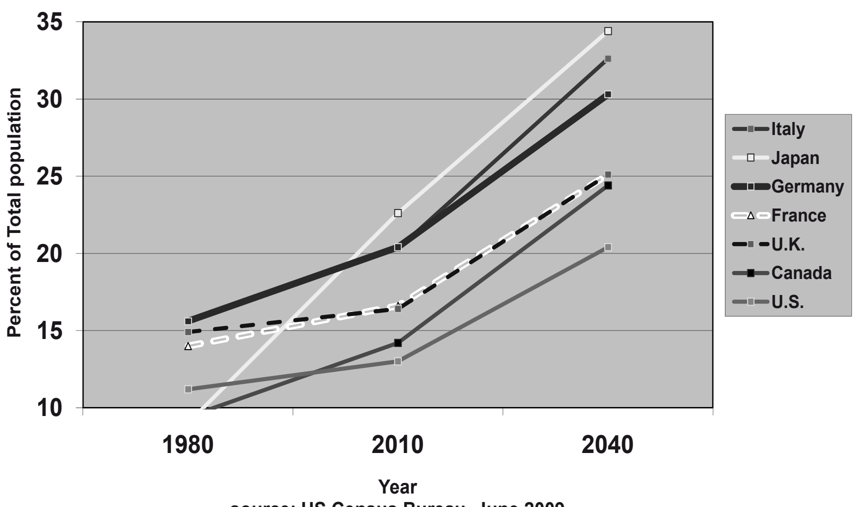
Exhibit 2.1 A Global Aging Population



Source: Kinsella and He (2009)

However, observers notice that the market for user-friendly devices in high tech products is taking off in the USA, northern Europe, Japan, South Korea and France. These products aim to facilitate elderly people's access to electronic devices and numeric services. They ease browsing, for example with simplified computers (Ordissimo), touch screen monitors (E-sidor and Ordimemo), and mail and picture printers (Hewlett-Packard). They offset visual impairment through enlarging screens or fonts (e.g. Mobile Magnifier sold at around €127), or offset auditory impairment by slowing down the flow of words or reducing background noise (RakuRaku Phone Basic). Bazile Telecom is a new mobile phone and service designed to make mobile phones easy and useful for older consumers. We first review the important results relative to ageing consumers and then present the Bazile Telecom mobile phone and service.

2.2 Ageing consumers in Europe

In Europe, the over-65s represented 17% of the population in 2008, compared with 12% in 1970. This age group is expected to number more than 100 million in 2020 (i.e. 20% of the European population). The fastest growing segment is that of persons aged 75 and over: in Europe, the over-80s represented 21.8 million people in 2008, and will grow to 29 million by 2020; this represents 33% growth, compared to 3.7% growth for the whole population of the European Union (Eurostat 2008). In France, the over-75s now number six million and will number 7.5 million by 2025. Women account for 60% of this age group, half of whom live alone. The very elderly (over 85) will also increase in number from two million in 2010 to 2.5 million in 2025 (Insee 2001, 2008).

The daily life of the elderly: public policy implications

In France, around 10% of those aged 75 and over live in specialized homes. Seventy-five percent of them are women, and 84% are dependent (Prévot 2007). Living in a retirement home (Etablissement d'Hébergement pour Personnes Agées et Dépendantes) costs the family between €1,500 and €4,000 per month. It also represents a public expense, since, with the exception of private institutions, retirement homes are partly financed by the French departments (Conseil Général) and by the departmental office of social affairs (DASS, Direction des Affaires Sanitaires et Sociales). However, if the family feels some relief in placing their older parent in an institution, the older persons themselves face real stress when they move out of their familiar environment. Such a move is considered as a classic stressor, creating anxiety and depression. Residents often perceive themselves as less dynamic (Michel et al 2009).

For economic reasons and due to personal preferences, most older persons still live at home, and avoid the stressful move to a retirement home. But isolation comes with age, as older persons are less inclined to go out, and feel less connected with their environment. According to the Chief Surgeon at Sainte Perrine Hospital's Geriatrics Department in Paris (Henrard, personal communication), biologically based slowdown occurs in daily social life at the advanced age of 80 years and older.

Gerontologists distinguish the young-old, that is, persons aged 65 to 74, from the old-old, the 75 years old and above (Schaie 1996). A majority of persons in the 60 to 74 year age group report having no problems walking and say they shop 'often' or 'every day'. In contrast, more than half of those aged 80 years or older report problems walking and shop only 'occasionally' or 'never'. Among those aged 60 to 74 years, more than 80% 'go everywhere', whereas only 34% of those aged 80 years and over do so (David and Starzec 1996).

Older persons tend to lose their balance more frequently in an unfamiliar or complex environment, for example on a bus, on the metro, on staircases. Twenty-five percent of respondents aged 75 to 84 and 33% of those aged 85 and above reported a fall in the last twelve months (Hornborock, Stevens and Wingfield in Bee & Boyd 2008). Gerontologists say it is not infrequent to find older patients who suffer accidents at home and are unable to contact

their neighbors or family although the doctors organize a gerontological coordination to look after their older patients (private conversation with Dr Florence Villard, gerontologist at the Institute Franco-Britannique, Memory consultation, Levallois-Perret).

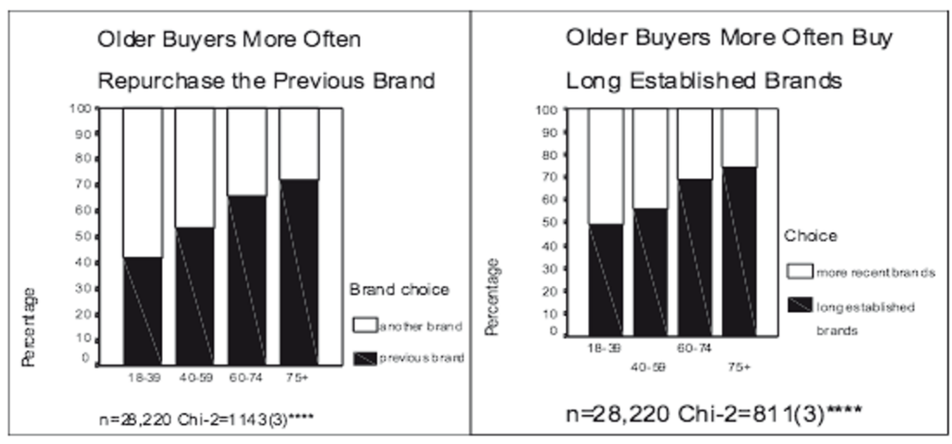
The daily consequences of growing old

Ageing implies motor, sensory and cognitive decrements, making it more difficult to live securely at home and go outdoors. Motor aging implies much slower reaction times, up to 50% slower for complex tasks, and 'poorer ability to handle very small objects' (Yoon and Cole 2008, p. 8). This makes it difficult for older persons to navigate quickly enough in complex mobile phone software. Sensory ageing includes auditory and visual decrements starting at 40. Half of adults aged 65 and over have cataracts. "In most cases, better illumination, higher contrasts, and reduced glare will help older consumers." Older adults have problems detecting low frequency sounds and discriminating between the background noise and the main message (Yoon and Cole p. 7).

Cognitive aging has an influence on daily decision-making. With impaired working memory, older persons experience more difficulty in retrieving pieces of information and their sources consciously (e.g. remembering an ad for a car manufacturer, when it was seen, and where it appeared). Older people may avoid cognitive efforts, such as a comparison of alternative choices and tend to rely on store loyalty or advice-seeking heuristic (Sorce 1995). In addition, age is negatively correlated with fluid intelligence, required for new problems and situations. But crystallized intelligence based on past experience and learning remains intact (Salthouse 1991, Chasseigne, Mullet and Stewart 1997). Cognitive decline may explain older buyers' tendency to consider familiar options, such as their current brand or long-established national brands in new car purchases, particularly for persons 75 years and older (see **Exhibit 2.2**).

Regarding social aging, the Carstensen Socio-Emotional Selectivity theory states that when the temporal horizon is perceived as limited, older persons give priority to long-known contacts such as family, old friends and other long-known acquaintances over new informative ones (Carstensen, Isaacowitz, and Charles 1999; Isaacowitz, Charles, and Carstensen 2000). When asked to choose between potential social partners who represented three degrees of familiarity (a member of their immediate family, a recent acquaintance and the author of a book they had read), 65% of older subjects chose the most familiar social partner versus only 35% of younger subjects (Fredrickson and Carstensen 1990). As a result, "Older people not only interact with fewer people, they interact primarily with people who are well-known to them" (Field and Minkler 1988, in Carstensen, Isaacowitz and Charles 1999, p. 169).

Exhibit 2.2 Older Buyers focus more on familiar brands



Source: Lambert-Pandraud, Laurent and Lapersonne (2005)

Older consumers are among the most vulnerable targets of scams. The US Federal Trade Commission (1999–2001) reports that a disproportionate number of consumer fraud victims, some 80% or more, are 65 or older. Interviews with officials in the French ministry in charge of consumer protection (personal communication, April 2004) provided numerous examples of this phenomenon of abuse of the elderly. For example, there have been many incidences of older adults purchasing expensive but unnecessary goods and services, such as a complete electric installation when replacing a fuse would have been sufficient. Cognitive decline, reduced information seeking, a tendency to avoid making decisions by oneself, and delegating decisions to people posing as experts are some tentative explanations for vulnerability to deceptive marketing practices (Yoon et al. 2005).

Ageing and New Products adoption

Relevant consumer behavior studies mostly attempt to find a relationship between age and the adoption of new product categories and do not offer any consensus. Rogers (2003, p. 288) concludes that "earlier adopters are no different from later adopters in age. About half of the many diffusion studies on this subject show no relationship, a few found that earlier adopters are younger, and some indicate they are older." These variations may be due to differences in the products under study. Similarly, Hauser, Tellis and Griffin (2006, p. 689) conclude that "while some studies have shown that innovators are better educated, wealthier, more mobile, and younger, other studies have failed to validate these findings." Still other studies identify a negative relationship between age and innovativeness; Tellis, Yin and Bell (2009, p. 12) claim that innovativeness measured by "reluctance is best explained by age and income, closely followed by mobility, education and gender." Indeed, Botwinick

(1978) finds that younger subjects are much more likely than older subjects to make a choice that could entail a change in their daily life situations and take risks in general, whereas older respondents tend to be more cautious.

The low rates of high tech equipment of the elderly

Indeed, among older consumers, in particular persons aged 70 and over, there is a significantly lower rate of owning high tech products, particularly mobile phones. In France, among young elderlies (60–69), there is a lower rate of owning mobile phones (75%) than for the 12 and over population (83%). The difference is much bigger considering the over-70s, only 48% of whom have a mobile phone, but encouragingly this grew by more than 6% in 2010. In addition to age, low education and income explain low ownership rates of high tech. For example, only 62% of persons having no diploma and 69% of those earning less than €900 per month have a mobile phone. The number of applications used in mobile phones declines with age: in 2010, only 38% of persons aged 60 to 69 and 19% of the 70 and over age group used text messaging, against 98% of those under 24.

Table 2.1 Lower rates of new technologies' adoption in older adults

Usage of population aged…	12 and over	60 to 69	70 and over
Mobile Phone	83%	75%	48%
Computer	76%	61%	28%
Internet	71%	57%	24%
Text Messaging	73%	38%	19%

Source: Credoc (2010)

Summary

Older consumers, particularly the over-75s, have become more economically important in Western and industrialized economies. Despite the quick pace of innovation mostly targeting young consumers, the high tech industry is now realizing the importance of designing new products that are adapted to the elderly. However, older consumers tend to be reluctant to adopt new high tech products, and they are under-equipped in mobile phones and the Internet. The majority of the elderly prefer to stay in their homes instead of moving to a retirement home, which indicates the growing relevance of communication aids. Bazile Telecom is a new simplified mobile phone designed to help older consumers contact their relatives at home and outdoors.

2.3 Bazile Telecom: A start-up in user-friendly mobile phone and service

Bazile Telecom was founded in 2005 by Yves Morel, Jean-François Peyre and Jean-Luc Grand-Clément near Aix en Provence. The first prototypes, a platform 'monbazile.fr' and a call center were created. Sales of the handset and subscription to the service started in late 2008. In 2009, Bazile Telecom became an Orange MVNO dedicated to older users. An MVNO has an agreement with a Network Operator, such as Orange, SFR or Bouygues, to use their mobile phone network. There are 25 MVNOs in France, the most famous being Virgin Mobile. As such, Bazile service won the 'Grand Âge Trophy', which was granted on 29 April 2009 during a symposium gathering of 1,000 health professionals. The start-up had 15 employees and around 1,000 customers in mid-2009.

The service

Bazile Telecom is a mobile phone equipped with a single large button. As with any phone, the user can make and receive phone calls through a classic mobile phone number. However, this mostly simple handset is completed with a service designed for older and (or) impaired users. When pressing the button, the phone reaches a phone operator, who in turn puts the subscriber in contact with the person of their choice. This person may be included in a pre-recorded list of contacts. The subscriber may also dictate a phone number, or request a search in the phone book. Phone operators are available 24/7 and are reachable from any place. Subscribers can also receive and send text messages as with a classic mobile phone.

Urgent calls are put through by depressing the button for five seconds. In such a case, a Bazile phone operator contacts the older person's relative or helper (e.g. a neighbor or a friend) and an emergency service for immediate assistance. By pressing the button twice, the phone vocally indicates its state of battery charge and the quality of signal reception. Bazile users are gently reminded to recharge the battery, a gesture which is not automatic in older users. In sum, Bazile's one button handset offers a reliable and easily accessible service. However, non-users may find this ultimate simplicity somewhat stigmatizing. As a lady of 95 years of age once replied to a telemarketing offer of the one button handset, 'I'm not that old!'

In addition to its core service, Bazile has several other attributes. The mobile phone is fully vocalized, i.e. it voices each command; for example 'I will call your phone operator.' when the user presses the button, or 'emergency call' when the user depresses it for five seconds, and 'good bye' when the user switches the phone off. The handset weighs 75g and therefore can be worn as a necklace device. When the phone is left on a table or used as a necklace, the 'smart free hands' mode automatically activates the loudspeaker. When the phone is used as a regular phone, the normal mode is reset. The average duration between the call center's 'Hello' and reaching the contact is 29 seconds. In total, it takes 35 seconds to reach a registered contact.

Exhibit 2.3 One Button Cell Phone and 24h Service

Source: Bazile Telecom (2010)

In July 2009, Bazile Telecom became an Orange MVNO. Since 2010, the Bazile service can be implemented in a SIM card introduced in Doro mobile phones. Therefore, Bazile services can be purchased through three different offers:

1. The 'Bazile Prestige' pack includes the one-button handset priced at €59.90, a 12-month subscription to the 24/7 access to phone operators, and a set communication time per month, e.g. 20 minutes (€20 per month plus 60 cents for each additional minute) or 60 minutes (€35 per month plus 45 cents for each additional minute).
2. 'Bazile classique' only includes the service and not the Bazile one button handset. Subscribers buy a 12-month access to the phone operators and communication time (see prices just above), but they use another mobile phone, such as Doro (see the coming paragraph on competition).
3. A third package includes the Bazile one-button handset (priced at €59.90) and a 12-month subscription to the phone operator service only (€25 for 120 minutes per month). In this case, the subscribers will supply the Bazile Telecom handset with their own SIM cards and will be billed for their communications separately by another Mobile Operator.

Contrary to classical mobile operators and to MVNOs, unconsumed minutes in a Bazile Telecom subscription are saved. This is an important benefit for older users, who don't like to waste.

Prescribers

The Bazile Handset and service aims to help older persons to live securely at home and outdoors. This target represents six million persons aged 75 and above. But also, Bazile Telecom may help two million visually impaired persons, 60% of whom are aged over 75. More than three million persons are handicapped in France, and in 70% of the cases, the handicap does not result from aging (Unadev, Union Nationale des Aveugles et des Déficients Visuels, and Insee HID 2000, in Bazile Telecom information dossier). Therefore, Bazile mobile phones and services are recommended by associations dealing with disabilities, such as the Unadev or Retina France, Associations for the Visually Impaired, 'Association Française pour la Myopathie', and other associations for handicapped persons.

Thanks to the Borloo law of July 2005, spending on tele-assistance and personal help at home is incentivized by a specific tax reduction. Bazile services are therefore registered and labeled as a 'Service to Persons' by the French government agency of services to persons (Agence Nationale des Services à la Personne, controlled by the French Ministry of Economics and Finance), enabling subscribers to deduct 50% of their subscription fees from their taxes, within a limit of €20 per month.

Competition

Direct competition comes from equipment makers, who market specific handsets for the elderly, but also from other mobile operators and MVNOs, who sell additional services for the elderly on top of their standard subscriptions.

- Mobile phone makers

Doro (Sweden) sells a range of 11 ergonomic mobile phones for the elderly, called 'Phone Easy', 'Handle Easy' and 'HandlePlus', equipped with large buttons, for example seven buttons in front plus an emergency button on the back of the phone (Handle Plus 334 GSM, €129). These phones have simplified functions for text messages, an FM radio and torchlight. Doro mobile phones are priced from €109 to €169. In France, the Doro range is listed in retail stores specialized in senior products and services, such as Celyatis, Facil&Co and hearing specialists. According to CEO Jerôme Arnaud, Doro mobile phones have won international trophies for their innovative design and ergonomics. Progressively, Doro phones are being sold in association with mobile operators such as Orange. Since 2010, users of Doro phones have had access to Bazile Service too (see the 'Bazile Classique' option mentioned earlier).

Emporia (Austria) sells a range of four mobile phones geared to older persons, equipped with large and easy-to-read buttons, such as Emporia Life (€125), Time and Talk. One model has an emergency button at the back. The phones are priced from €130 to €180. Two models are sold in association with the Prixtel 'Senior series' MVNO.

Exhibit 2.4 Dedicated phones for the elderly

Doro HandlePlus 324gsm

Emporia Life and EmporiaTalk

Source: Bazile Telecom (2010)

- Mobile Operators

Mobile Operators, such as Orange, SFR and Bouygues, retail in their stores dedicated handsets targeting older and impaired users. They also propose their own additional services on top of standard subscriptions. For example, with Orange, subscribers can be contacted at any time for €7 in addition to the standard subscription fee, and pay 0.37c per minute for communication (€13 for 30 minutes of communication). Orange sells these services in its five 'Arc en Ciel' boutiques and 165 'Solution Handicap' boutiques. Thanks to the SFR e-Care necklace device, a warning is sent if the subscriber falls; the device also reminds users of medication taking times (SFR's e-Rappel). In the 'Selection Handicap' range Bouygues adds 'Mobile Speak', vocal software reading what's written on the mobile screen. Indirect competition comes from fixed phones designed for the elderly and remote assistance devices, such as a tele-alarm and domestic emergencies warning.

- Fixed phones designed for the elderly

These fixed telephones are equipped with big buttons, photos of easy-to-reach persons, emergency button (Swedish Doro), sound amplifier (French Geemarc). Doro, for example, markets a range of ten models designed for older customers. They are priced from €10 to €200. Geemarc Phototel has a keyboard, which features ten photos.

Remote assistance

In France, 350,000 persons (three million in Great Britain) subscribe to a telemonitoring service. Tele-alarm devices must comply with the AFRATA (Association Française de la Téléassistance) chart. For example, the 'BipTranquille' service includes a full set of home help, for example, a sensing device signaling a domestic accident or a fall, and other services on request, such as nurse care, meals and help at home. This service is managed by AB-RAPA, an association that offers assistance and services to persons, and is located in Stras-

bourg (East France). As this device is mostly used for emergencies, most older persons leave it aside and forget about its location at the very time they need it urgently. Setting up the tele-alarm service in a home costs around €40, plus a monthly fee ranging from €25 to €50. As mentioned earlier, the Borloo law on Services to Persons authorizes the subscriber to deduct 50% of these expenditures from their tax amount.

Customer Behavior

Bazile had around 1,550 active customers at the end of 2009 and recruits approximately 150 new customers per month. In general, the subscriber is the user, whereas the buyer is a family member, an offspring in 85% of the cases, or a spouse (10%) or other relative (5%). Purchase often occurs when the user experiences a change of health status, a change of residence or the loss of a spouse. Bazile packs are sometimes offered at a family celebration (Mother's Day, birthdays, Christmas).

Seventy percent of customers are aged 75 and over. Most of them are 'active' women, still investing time in outdoor social activities, such as volunteer work. In couples, only one of the spouses is equipped. Their main motivation is to reach preferred contacts and to be reachable 24/7. The other 25% of the customers are visually impaired, and they are younger on average. The remaining 5% are physically handicapped persons. Both mentally and physically handicapped persons also find the Bazile phone very helpful. Sixty-six percent of the customers never had a mobile phone prior to subscribing to Bazile Telecom. Twenty percent of subscribers use 80% of the call center time. Bazile's churn rate is encouragingly low at around 12%, compared to the 25% to 30% defection rate, which is standard in the mobile phone industry. Those who cancel usually do so within five months of signing the contract. Fifty-seven percent of cancellations come from natural causes (death or inability to use the phone due to health degradation). Therefore, the average customer duration is six to seven years. Twenty percent of defections occur following dissatisfaction; the rest (23%) occur when customers face technical problems at the start, which is partly due to their lack of familiarity with the device and service. Weak or absent usage of service normally ends in cancellation, which is often prompted by offspring at Christmas time.

Table 2.2 Customer Basis from 2008 to 2010

	2008	2009	2010
Customer base at beginning of period	0	180	1550
Acquired customers	200	1760	3,000
Defection	20	210	550
Customer base at end of period	180	1550	4,000

Source: Bazile Telecom (2010)

Distribution of Bazile Telecom

Bazile packs are sold at brick and mortar retailers and on Internet sites. The retailers are diverse. Forty percent of them are specialized in products devoted to senior consumers, for example Audika Audioprothesist, medical equipment rentals, and specialized boutiques for the blind. The remaining 60% are opticians, mobile phone stores and pharmacies. On the Internet, sites devoted to seniors sell online medical equipment and furniture (Celyatis, Facil&Co). These retailers also have a few boutiques in Paris, Lyon and Geneva. Sixty percent of Bazile sales come from direct sales, through direct mail and telephone marketing. Teleshopping on TV was tested in September 2009. Forty percent of Bazile sales come from high tech stores such as phone boutiques, electronic retailers (Fnac) and stores specialized in equipment for seniors, such as Audika. It is worth mentioning that Audika has a network of 400 stores in France. The brand opened its first six centers in Italy in 2007 and had a network of 50 stores in 2009.

In the future, Bazile Telecom will also be looking at stores selling equipment for the disabled. So far, sales in mainstream phone shops (for example, a standard Orange phone store) have been disappointing, because the shops themselves are not geared to older customers. In most cases, the attendants are young and not used to an older clientele. These stores do not offer specific services to older customers. In December 2009, 250 points of sale listed Bazile Telecom services.

Promotional activity

The Bazile promotional budget amounted to €350,000 in 2009. From April to December 2009, Bazile ran a press campaign in targeted press magazines, for example in Notre Temps and Pleine Vie, but also in more popular newspapers, for example France Dimanche. The press campaign cost €200,000 (see GPRs below, measuring the effectiveness of the media campaign. It is computed as the percentage of reach multiplied by the frequency). TV was not an option in 2009, because the minimum budget to be effective is around €250,000. The start-up decided not to spend such an amount of money for the time being.

In December 2009, Bazile Telecom tested a radio campaign on RTL, the national leader, including 70 spots, for an additional €50,000 (in addition to the €350,000 initial budget). The campaign prompted 30 spontaneous calls and information requests per day from listeners. The second set of actions included a direct marketing program, costing €25,000. Bazile was referenced in Google adwords, targeting the elderly's offspring (50 years of age and over) having a high socio-economic status (CSP+). This referencing created 100–160 clicks per day, and cost an average of €0.7 per click. The campaign elicited more than 200 leads.

In 2010, Bazile Telecom advertised on television. The campaign focused on Bazile Classique and included 300 30-second spots. This campaign cost €250,000 and generated 1,700 calls from TV viewers and more than 500 subscriptions. Bazile also benefited from a 300,000 donor file belonging to Unadev, and sent a leaflet to its members, a majority of whom are aged 60 and over. Bazile Telecom only paid for the printing of the leaflets, which were

inserted in the Unadev quarterly newsletter and were sent on demand to the interested readers. The percentage of return was 0.1 (150 as of the end of September). The total cost for the campaign was less than €2,000.

Finally, teleshopping was tested in September 2009. Returns were not satisfactory, with only 20 sales during the first shot. A second test was carried out in December 2009. This campaign was costless for Bazile Telecom, because the TV channel charged a low flat fee per show. Other promotions included online editorials on devoted sites (e.g. lemarchedu-grandage.com), emailing, bus mailing – that is, a direct mail of several (10–20) promotional offers, and participation in senior marketing shows in Strasbourg, Paris, Dijon and Châlon-surSaône. The bus mailing promotion was sent to 15,000 prospects and Bazile Telecom had 172 returns.

Table 2.3 Press Media Plan in 2009

Press outlet	Type		Inserts	Period
Notre Temps	Monthly		5	April–June & September–December
Pleine Vie	Monthly		5	
Le Pélerin	Quarterly		10	
Sélection Readers Digest	Monthly		5	
France Dimanche	Weekly		5	September–December
Ici Paris	Weekly		5	
Age group	**GRP**	**% Reach**	**Frequency**	**Contacts**
50–64	171	43	3,96	19 965 000
60 and over	280	55,4	5,06	37 480 000

Source: Bazile Telecom (2010)

Press dossiers were sent to the medical professions, the specialized press, the visually disabled associations (AVH, Unadev, etc.) and to the relevant government organizations, for example the Mdph (House of Handicapped Persons). Bazile also advertised on senior websites run by gerontologists and pharmacists (e.g. orientationretraite.fr, clubseniors.com). The start-up has not yet run any marketing research program in order to save on costs. For example, an agency specialized in the elderly charges €8,000 for one focus group.

Results

Results so far are encouraging but lag behind objectives. Net Sales of first equipment amounted to 1,550 units at the end of 2009 against initial objectives of 4,000 units sold. Sales

were expected to increase to 10,000 by the end of 2010, which would have resulted in break-even for the start-up. Sales amounted to 4,000 units instead.

Costs, although too high, are expected to have declined in 2010. Despite its simple design, the handset cost €85 in 2009, whereas a classic mobile phone ex factory costs around €30. Due to increased volumes, this cost has decreased to €50 by the end of 2010. On average, the call center costs €3.50 per customer per month by the end of 2010. The communication cost includes the MVNO fee to a MVNE (Mobile Virtual Network Enabler) and the Orange communication cost. A MVNE (Mobile Virtual Network Enabler) is a service provider operating between the MNO Mobile Network Operator (for example: France Telecom Orange) and the MVNO Mobile Virtual Network Operator (for ex.: Bazile Telecom). In 2009, the marginal cost per hour included the cost of communication and that of the call center, plus 19.6% VAT. In 2010, the marginal cost decreased by 15%.

In addition, Bazile Telecom supported two one-time investments, which were: a) the connection to the Orange information system (the initial investment was app. €62,000); and b) portability, i.e. the ability for subscribers to keep their own mobile phone number while switching from one Mobile Operator to another (this one-time cost is expected to amount to €72,000 in 2010).

As the firm tests various tools in order to recruit new customers, marketing costs are high. For example, the average recruitment cost is estimated as €250 per customer. This includes the various tools implemented in 2009 (see above). Marketing is handled by CEO Yves Morel and by Marketing Manager Nicolas Roussel. They are helped by a marketing and communication assistant.

In 2009, these amounted approximately to €280,000, 65% of which represents compensation to retailers, for example, listing costs, rebates and promotional support. The remaining 35% corresponded to the cost of the direct sales activity (phoning). Sales are handled by five persons. Four sales persons are in charge of telephone marketing, one sells to distributors. In sum, Bazile Telecom incurred losses in the region of €1 million in 2009, representing the initial investment for its commercial launch.

Outlook and future developments

Bazile Telecom's top management identified a number of areas for development, such as complementing the service and the handset. Thanks to the MVNO status, Bazile Telecom can separate the handset from the service, and extend its product range by new mobile subscriptions, compatible with a large range of mobile phones. Bazile service could also extend its service with a remote monitoring offer. Bazile service may work with a permanent line. Each option has to be analyzed. Improving the handset performance and look is another option. For example, the handset itself, and the pocket cover, currently sold in one model at €14.90, could be available in several colors. One may also improve the ergonomics of the terminal.

Exhibit 2.5 Bazile handset pocket cover and docking station

Source: Bazile Telecom (2010)

To improve marketing expertise and efficiency, Bazile Telecom intends to develop partnerships in communication, including co-branding and co-marketing. The ideal partner is one object of debate: should it be a public subscriber? Local public representations, social services at the town hall, department offices and departmental agencies of the French social security need long lead times before making a decision. Other prescribers may offer a nice network and leverage too. Bazile Telecom will unveil a co-branding agreement with a major insurance company in 2010. Also, the mailing inserted in the Unadev newsletter was sent 'on demand' and Bazile Telecom has not run a classic direct mail campaign yet. Marketing efficiency needs reinforcing with a dedicated marketing staff, information system and decision aids. Basic surveys and user focus groups should be implemented in order to track customer feedback.

Efforts to improve sales efficiency are also intended. Recruiting prospects aged 75 and over requires gentleness and convincing arguments. Phoning is a good solution for those who won't surf on the Internet or go to the few boutiques listing Bazile. It may be crucial to reinforce sales force expertise in telemarketing and phoning. Presently, Bazile needs to enlarge the retail network. The senior boutiques channel is an option, but this channel is not very large anyway yet. Internet specialized sites offer good support, providing they display Bazile on their first site page. Direct at-home personal selling, 'à la Tupperware', could also be tested in various settings, such as associations and clubs for senior citizens. Tupperware recruits and trains hostesses. They organize at-home discussion groups with their friends about Tupperware products. Friends can order them through the hostess, who then receives a proportional fee of her sales. Gaining the support of subscribers is important in order to influence the user and the buyer of Bazile. The company has to set priorities between public (a public agency for example), commercial (a retailer) and personal influencers (a friend, a relative or a neighbor).

Aging is a growing concern in Europe, especially in Mediterranean countries (Italy and Spain), but also in French speaking countries such as Switzerland and Belgium. Facing demand of foreign markets, Bazile Telecom starts thinking of its international development, considering for its international range three main options: a) the handset only, its technology and the call center, relying on a local Mobile Operator; b) the service with phone operators only, relying on local mobile operator and available handsets; and c) a full MVNO offering the package of handset, phone operator service and communication time.

Student Assignments

At the shareholder meeting, Bazile Telecom marketing manager presents results, outlooks and strategy for the next two years to major shareholders.

Bazile management: We sell Bazile service through direct marketing, e.g. web, mailing, bus mailing, TV teleshopping, and through intermediaries, e.g. boutiques pure player, boutiques to senior clientele, and staff in services to person.

Shareholder: Sounds great, but are you assessing each marketing action? You use a large number of tools; it may be worth knowing what works best.

Indeed, the potential of the 'high-tech' simplified mobile (Joël Mori, 2009) targets the long-term growing end of the population, i.e. consumers aged 70 and over. How can Bazile Telecom, a start-up in mobile phone and services dedicated to seniors and dependent persons, take advantage of this trend?

1. Compute the net life value of a customer. Analyze the return on investment and identify the best cost-effective marketing tools tested in 2008 and 2009.
2. Write a SWOT analysis and a diagnosis for Bazile Telecom. Propose a strategy and a marketing plan for the next two years.
3. Propose a strategy of internationalization. In entering a foreign market, you may consider the three options mentioned above, i.e.

   a) handset only,

   b) service with the phone operator only,

   c) the full MVNO offer.

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3 Changing Media Regulation in Europe: VIASAT3 in Hungary

Mihály Gálik, Department of Media, Marketing Communication and Telecommunication, Corvinus University of Budapest

> **Yellow circle is to vanish from screen at Viasat3**
>
> The broadcaster of Viasat3 television channel in Hungary, Viasat Hungaria Ltd. asked the broadcasting regulatory authority named National Radio and Television Board (abbreviated as NRTB) to cancel Viasat3 from the registry of television channels by 1 May 2009. The move was initiated by Modern Times Group AB (MTG), the majority owner of Viasat Hungaria Ltd. Viasat Broadcasting UK steps in as new broadcaster for Viasat3 channel which will be registered by Ofcom, the British regulatory authority in London. [...] Neither viewers nor business partners are to experience any change: Viasat3 channel will be distributed on the same platforms as before. The only exception is the disappearance of the yellow circle from the bottom of the television screen as channels registered by Ofcom in the UK are not obliged to carry on the yellow circle symbol which indicates age rating of programs for viewers during all the programming time. [...] It's worth mentioning that TV6, another MTG owned channel in the Hungarian market, is also registered by Ofcom and has been distributed without any legal dispute in Hungary.
>
> ***Csaba Kalmár, Origo news portal, 28 April 2009***
> ***http://www.origo.hu/teve/20090428-eltunik-a-sarga-karika-a-viasat3rol.html***

3.1 Background

MTG, which has 95% interest in Viasat Hungaria Ltd., decided to finish legal disputes that had been going on between Viasat Hungaria Ltd. and the national regulatory authority (NRTB) regarding the Viasat3 channel for a long time. NRTB had fined the broadcaster many times since the launch of Viasat3 channel on 23 December 2000 due to the alleged violations of the Broadcasting Act passed in 1996 by the Hungarian parliament. The frequency of fines, one every second week on average, indicates the extreme regulatory activism in the Hungarian television market.

The continuous legal dispute between the broadcaster and the national regulatory authority got worse in the spring of 2007 when NRTB decided to change the status of Viasat3 from a regional channel to a national one; due to the provisions of the Broadcasting Act of 1996, this change was to put new regulatory burdens on the broadcaster. Viasat Hungaria Ltd. seemed reluctant to accept the resolution and filed a lawsuit against NRTB in the Capital

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Court, claiming that the national regulatory authority broke the law in having determined the area of reception (geographic market) of the channel. The two-step litigation process lasted for one and a half years and finally the Court of Capital Circuit ruled that NRTB really had broken the law in having classified Viasat3 as a national channel. The Court ordered the NRTB to carry out a new procedure in order to determine the area of reception of the Viasat3 channel but the broadcaster decided not to wait for it. It asked NRTB to cancel the registration of Viasat3 by 1 May 2009 and registered the channel at Ofcom in the UK on the same date. Since then, Viasat3 has been distributed in Hungary as a satellite channel registered abroad and the legal supervision of Viasat3's programming has been carried out by Ofcom.

3.2 Main features of the European television scene and common European television regulation

The age of state monopoly in television (and radio) broadcasting came to an end in the late 1970s and the early 1980s in West-European countries and in the 1990s in the post-communist emerging countries in Europe. Around 2000, the multichannel television model prevailed all over Europe; a great many channels had become available to audiences on different distribution platforms. For example, over 660 channels with potential national coverage were broadcast via terrestrial transmitters, satellite or cable in the EU-15 at the beginning of 2001, over 860 channels were active three years later (CEC, 2006).

The number of services available in the enlarged Community (EU-25) as of mid-2006 amounted to 122 analogue nationwide channels plus 1 335 digital channels available over cable, satellite, terrestrial and IPTV platforms (CEC, 2007). In addition, the number of television services targeting non-national markets has increased at an even faster speed: about 220 such channels were identified at the beginning of 2004 and 370 such channels operated in mid-2006.

Of course, thematic channels make up the overwhelming majority of new entries, reinforcing the trend of fragmentation of supply on the market. The digital revolution in info-communication technologies such as the rise of digital terrestrial television broadcasting (DTT), digital cable and digital satellite platforms and the delivery of television services over Internet Protocol (IPTV) have even quickened the proliferation of channels. As a consequence, hundreds of channels are distributed in most national television markets nowadays. The change from a 'frequency scarcity, few channels, devoted audience' era to a 'content abundance, flood of channels, attention scarcity' era is quite remarkable.

The shift from free television to pay television services seems to be the other important trend prevailing on the European television scene. The share of advertising revenues in overall turnover is diminishing while the share of subscription fees paid by the audience and the share of license fees paid by distribution platforms are increasing in the television industry as market data testify.

Free television channels have been seriously hit by the global financial and/or economic crisis of 2008 and 2009, and the business model based solely on advertising revenues is being questioned more and more vigorously even by prominent industry executives like Gerhard Zeller, CEO of the biggest European television company, RTL Group SA (Zeller 2009; Preuschat, 2009).

Satellite distribution of television services began in Europe in the early 1980s. The area of reception, the so-called footprint of satellite broadcasting covers not only one but many national markets that had been isolated from each other before. The introduction of new television services targeting non-national markets (trans-frontier television services) led to a kind of common European television regulation by the end of the decade. The European Convention on Trans-frontier Television was adopted on 5 May 1989 by the Council of Europe, and a couple of months later the European Community (today: the European Union) adopted a directive on the same field, too.

The latter regulation is officially called the Council Directive 89/552/EEC of 3 October 1989 on the coordination of certain provisions laid down by Law, Regulation or Administrative Action in Member States concerning the pursuit of television broadcasting activities, and it is popularly referred to as TWFD (Television Without Frontiers Directive). For the sake of convenience, this chapter deals with the common European television regulation as set by TWFD, which was amended in 1997 (97/36/EC) and in 2007 (2007/65/EC). One of the cornerstones of common European television regulation is the country of origin principle. Television programs that comply with the country of origin law and which are in line with the provisions of the TWFD may be freely distributed within the EU Member States.

The amendment of TWFD adopted in 2007 is called Audiovisual Media Services Directive (AVMSD). The AVMSD extends the scope of regulation beyond television services as we know it but this chapter focuses only on the television scene. Common European television regulation intends to promote different objectives like freedom of reception, scheduling more European works in programming, protection of minors, protection of human dignity, protection of consumers against the flood of advertisements in the program and against misleading and surreptitious advertisements, legal protection of broadcasters that provide services also in other Member States than where they are registered, etc. This list is far from being complete.

Provisions supporting the achievement of the objectives detailed above consist of, among others, the following:

- Member States shall ensure freedom of reception and shall not restrict retransmissions on their territory from other Member States;
- Member States shall ensure, where practicable and by appropriate means, that broadcasters reserve a majority proportion of their transmission time for European works and reserve at least 10% of their transmission time and/or of their programming budget for European works created by producers who are independent of broadcasters;
- Television advertising shall be recognizable as such and shall be kept separate from

other parts of the program by optical and/or acoustic means;

- The amount of advertising shall not exceed the 15% of the daily transmission time and 20% within a given one-hour period;
- Advertisements shall be inserted between programs with some exceptions like sports programs, events comprising intervals, feature films, etc. Where programs are interrupted by advertisements at least 20 minutes should elapse between each advertising break (at least 45 minutes as far as feature films are concerned);
- Advertising shall not use subliminal techniques and surreptitious advertising shall be prohibited;
- Advertising for cigarettes and other tobacco products, and medicinal products available only on prescription shall be prohibited;
- Member States shall take appropriate measures to ensure that television broadcasts by broadcasters under their jurisdiction do not include programs which might harm the physical, mental and moral development of minors;
- Member States shall ensure that broadcasts do not contain any incitement of hatred on the grounds of sex, race, religion or nationality;
- In the case of television broadcasts that do not comply with the provisions of the directive, Member States shall take appropriate measures to secure compliance of those broadcasters under their jurisdiction.

Out of the 27 articles of the TWFD, 12 detail advertisement and sponsorship rules, so the widely shared reasoning that the directive serves mainly to create and boost the single European television market does have support. Answering the developments of new advertising techniques such as split screens, interactive adverting and virtual advertising, on 23 April 2004 the European Commission adopted an interpretative communication to clarify the meanings of certain provisions of the TWFD (CEC, 2004).

In the field of advertisement and sponsorship rules, changes adopted by the AVMSD point toward liberalization and seeking of a balance between broadcasters' interests and other parties' interests. For example, the time period between two consecutive ad breaks was shortened from 45 to 30 minutes in feature films.

From a business point of view, the change in regulatory treatment of product placement seems to be the most important one: although product placement remains prohibited (AVMSD Article 3g 1.), there are numerous derogations from applying this provision which open the door for broadcasters (and program providers) to use this form of financing for production costs and/or to boost revenues. By the way, Hungary has failed to implement this change in its legislation up till now (mid-2010) although the deadline to bring into force the AVMSD expired on 11 December 2009.

Member states shall comply with provisions of the TWFD and/or the AVMSD and shall communicate to the commission the text of national law which they adopt in order to fulfill compliance obligation. Nevertheless, Member States are free to lay down more detailed and stricter rules in the area covered by the directives in question.

3.3 The Hungarian Television Scene at the Millennium

The basic transformation of the television scene began in Hungary in October of 1997 when the two national commercial television channels, RTL Klub and TV2, were launched. Before this date, Hungarian Television – the state broadcaster – dominated the scene with its two terrestrial channels, M1 and M2. Nevertheless, Hungarian Television had some small competitors, some private broadcasters with limited geographic coverage marketing television services via cable networks. They tried to satisfy people's demand toward more entertainment in the shadow of the big state broadcaster, increasing program choice available to the audience and offering new windows for advertisers.

These broadcasters were under-capitalized small companies and harbored high hopes to play a role in the upcoming process of privatization after the law was adopted. These hopes proved to be illusions as small broadcasters obviously overestimated the commercial value of the brand they had built and foreign professional investors showed no interest at all in using these brands. After Act I of 1996 on Radio and Television Broadcasting was adopted and came into force, two multinational professional investors managed to win the tender for the two commercial national television licenses and launched RTL Klub and TV2, both of them general entertainment channels, in October 1997 and have been operating with tremendous success.

In order to win the tender, the two bidders planned such a program structure that consisted of many public service programs as defined in the Act I of 1996:

"Article 2 (19): 'Public service program' shall mean a program serving the informational, cultural, civic and lifestyle needs of the audiences living in the area (national, regional, local) covered by the broadcaster, such as in particular:

a. artistic works or communication…;
b. dissemination of information serving educational and training purposes;
c. providing information on scientific activities and research results;
d. broadcasts serving the concept of the freedom of religion, and presenting church and religious activities;
e. children and youth programs, and educational and general information programs on child protection;
f. dissemination of information making everyday life easier…;
g. programs created for underprivileged groups…;
h. news services."

Later on they managed to modify the broadcasting contract with the national regulator (NRTB) to a significant degree as such a program structure had crossed their business interests and had not let them form the programming based on commercial logic, which re-

quires the provision of mainly entertainment to the audience. Regardless of the great success of RTL Klub and TV2 channels on the television market, they could not fully satisfy the audience demand toward entertainment so, following global trends, new thematic channels (movie, sport, cartoon, wildlife, scientific, etc.) gradually entered the market. It's worth noting that Act I of 1996 forbid national commercial terrestrial broadcasters to have qualifying (25% or more) interest in thematic channels.

3.4 The Launch of Viasat3 and its Positioning

The Swedish professional investor Modern Times Group AB (MTG) decided to enter the Hungarian television market in 2000. MTG's strongest business unit has been involved in providing television services. As of 2000, MTG was present – apart from Sweden – in the other three Scandinavian countries as well as the three Baltic countries and wanted to grow outside these two regions as well. In Hungary, MTG saw a market gap in the weakness of programs targeted at the young male audience. MTG decided to fill it by launching a general entertainment channel putting more emphasis on the sex genre and action movies in their programming compared to the two big channels and introducing new formats catering the needs of the same target audience, as well. By this time, the previous small general entertainment channels (TV3, Msat, Szív TV) had already gone bankrupt and left the market.

MTG founded Viasat Hungaria Ltd. with a 95% interest in the company (the remaining 5% went to two persons in management) and this company bought an ailing regional broadcaster, Alfa TV, distributing its program via terrestrial broadcasting in the most important geographic market, Budapest (the capital city of Hungary) and its region. Viasat3 channel was launched, after a test period, on 23 December 2000, just before Christmas with 18-hour programming and was also distributed via satellite broadcasting.

To extend the coverage, the new broadcaster offered the Viasat3 channel to cable distributors for free. Households' cable penetration was about 50% at the millennium and the cable industry had been in expansion, too. In addition, more than 11% of households had dishes for satellite reception (Direct-To-Home, DTH households in professional jargon) so the coverage of Viasat3 kept on growing.

Viasat Hungaria Ltd. inherited the regional broadcaster status based on the broadcasting contract between Alfa TV and NRTB. Alpha TV took part in a tender administered by NRTB for a license in Budapest region with two million or so inhabitants; NRTB awarded the license to Alfa TV and made a contract with it. Part of the contract is the so-called yearly broadcasting fee, which the broadcaster shall pay by law to the national regulatory authority over the ten-year duration of its license. At the same time, Viasat Hungaria Ltd. was also registered at NRTB as a regional satellite broadcaster. Act I of 1996 consists of criteria based upon the area of reception for broadcasters' geographic status and determines three categories, namely local, regional and national broadcasters. NRTB does not make contracts with satellite broadcasters; the national regulatory authority simply registers them and sets the

amount of yearly broadcasting fee as a resolution applying a pre-determined formula.

The business model of Viasat3 was built on advertising revenues. The extension of channel coverage has vital importance in this model and networking with local television broadcasters as an alternative to gain broader coverage was considered in the beginning but it was dropped later (the legal term of a network operator in the Act I of 1996 shall mean any broadcaster whose program is disseminated in a network of channels, and who is responsible for the broadcasting).

In addition, it turned out that young males form too narrow a target audience to attract advertisers to such an extent that revenues cover costs. The shift in audience targeting seemed inevitable, and the 18-49 age group with some skew toward women was chosen as a target audience like with other general entertainment channels. Of course, programming also changed, focusing on the needs of the new target audience.

3.5 Regulatory burdens on regional and national television channels registered in Hungary

The Act I of 1996 on radio and television, the media law in everyday use, orders regional and national broadcasters – except thematic channels – to fill daily broadcasting time at least up to 10% with public service programs as defined by the law [Article 8 (1)]. In addition, the media law orders them to broadcast public service programs during prime time for at least 25 minutes [Article 8 (2)] every day. On top of that, the media law orders that national television channels shall broadcast not less than twenty minutes of independent and uninterrupted news broadcasts during prime time hours. News material received from other Hungarian broadcasters may not exceed twenty percent of the news broadcast [Article 8 (3)].

The provisions detailed above seem to be rather strict compared to the provisions of broadcasting legislation in most European countries (OSI, 2005). In addition, the provision of TWFD that the amount of advertising shall not exceed 20% within a given one-hour period is interpreted in Hungarian media law as the amount of advertising shall not exceed 20% within a given hour period calculated in any way, i.e. within 60 consecutive minutes. The provision in this form is a hotbed for unintended violations due to the nature of programming. While control over advertisement time is an easy exercise if the meaning of one hour period is a time period of a given clock hour (let's say from 7:00 to 8:00 pm), it is a very difficult one if an hour period of time is interpreted as sixty consecutive minutes.

In the world of television business, these differences in regulation matter. In the case that the regulatory environment is clearly stricter in Hungary than in other European countries, broadcasters registered in Hungary may suffer competitive disadvantage in the market compared to broadcasters registered abroad. If the market is closed, this potential disadvantage is not real but if it is open, providing television services under Hungarian jurisdiction constitutes de facto a disadvantage in competition.

The market of terrestrial broadcasting is closed in the sense that the prerequisite of market entry is a license obtained from the national regulatory authority. On the contrary, the market of satellite broadcasting is open and satellite channels from abroad reach households directly or via cable without any regulatory intervention. Member States in the EU shall not restrict retransmissions to their territory from other Member States so if channels registered, let's say, in the UK or in Romania comply with the provisions of TWFD, they may be distributed in the Hungarian market, too.

In the case that broadcasters registered abroad and distributing programs in the Hungarian market do not pay a broadcasting fee, or if they do the amount of it is rather small compared to the broadcasting fee they ought to pay under Hungarian jurisdiction, they enjoy a competitive advantage in the market. The same is true for broadcasting public service programs and news detailed earlier. These regulatory burdens fall beyond the obligatory provisions of common European television regulation (TWFD) and may harm market players registered in Hungary.

One might say that this is a mere theoretical reasoning, but data testify quite the opposite. AGB Nielsen Media Research Ltd, the company providing audience measurement service in Hungary, registered 61 satellite channels in its people meter system in 2009. Out of the 61 channels, 42 are registered abroad and the remaining 19 are registered in Hungary. **Table 3.1** shows the main aggregated audience figures of terrestrial and satellite channels in Hungary.

Table 3.1 Aggregate viewing share (SHR) and average daily reach (RCH) of terrestrial and satellite television channels in Hungary in 2008 and in the first half of 2009 (4+ population)

Type of television channel	2008		First half of 2009	
	SHR %	RCH %	SHR %	RCH %
National terrestrial channels	56.9	71.0	53.8	71.2
Satellite channels registered in Hungary	13.0	42.7	14.6	45.4
Satellite channels registered abroad	21.2	45.0	23.3	47.2

Source: AGB Nielsen Media Research Ltd, 2009

Figures in **Table 3.1** show that the viewing share of satellite channels registered abroad is much higher than satellite channels registered in Hungary; one has to add that the difference has been increasing over the last decade. This may be partly explained by the logics of the television market, but it seems certain that outdated provisions of the Hungarian media law do have a very important effect on the state of art, too.

It's true to say that the common European television regulation consists of provisions on

broadcasters distributing their programs mainly in markets other than where they are registered. Member States may restrict the retransmission of such programs if they "manifestly, seriously and gravely infringe Article 22 (1) or (2) and/or Article 3b" [AVMSD Article 4 (2a)] i.e. if a given broadcaster manifestly, seriously and gravely infringes the rules on protection of minors and/or its program manifestly contains any incitement to hatred based on sex, race, religion or nationality. There have been a few cases brought to court on the ground of alleged circumvention of stricter rules and in some cases, the courts ruled to block retransmission (Castendyk et al ii, 2008: 361-363; CEC, 2006: 5-6) but these cases constitute exceptions rather than being common in implementing TWFD.

3.6 The growth of Viasat3

In the first years of market presence, Viasat3 remained a small channel: the 1.1 percent audience share achieved in 2001 could hardly meet the expectations of its owners. The company thus elected a new CEO in mid-2003, the third one in a row, who outlined a renewed business strategy. The new CEO reaffirmed that Viasat3 is to focus on a younger audience compared to the two market leader national commercial channels and to boost its viewing share providing science fiction and other series that attract young people. The crown jewel in the new program supply was to be the live coverage of UEFA Champions' League football matches.

Although Viasat Hungaria Ltd. treated the sum paid for live broadcasting rights of UEFA Champions' League matches for five seasons as a business secret, it had surely been the biggest investment since its launch. It turned out soon that these matches really attracted a much higher audience than on average, and, even more important, this was the first program that cable and satellite platforms regarded as a must have in their packages. Viasat3 coverage increased significantly, and this also reflected in the increase of audience share.

The management of Viasat Hungaria Ltd began to ask a license fee from platform operators, and this time succeeded. The change in business model, realizing two revenue streams instead of one, namely incomes from advertising and license fees paid by platform operators, helped the broadcaster to get out of the red in 2006.

Extending the brand name, MTG introduced two additional channels to the market. Viasat Explorer was launched in 2003, and Viasat History in 2004. Both of them are thematic channels registered in the UK. These channels do not belong to Viasat Hungaria Ltd; nevertheless the presence of two new channels may strengthen the position of the broadcaster when negotiating the terms of contract for distributing Viasat3 channel with cable and satellite platforms.

Table 3.2 Audience share of major Hungarian television channels in %

Channels	1999		2001		2005		2009	
	4+	18-49	4+	18-49	4+	18-49	4+	18-49[d]
M1[a, c]	13.0	13.0	11.2	11.2	13.8	9.1	9.5	6.4
TV2[a]	35.5	35.5	36.3	36.3	26,3	27.6	19.7	21.6
RTL Klub[a]	29.1	29.1	29,2	29,2	29.0	31.0	23.1	26.0
M2[b, c]	1.8	1.8	2.0	2.0	1.6	1.1	2.0	1.4
Duna [b, c]	1,6	1,6	1.6	1.6	2.7	1.6	2.1	1.0
Viasat3[b]	-	-	1.1	1.1	3.7	4.5	4.2	5.6
TV3[b]	4.5	4.5	-	-	-	-	-	-
Msat[b]	1.2	1.2	-	-	-	-	-	-

a: terrestrial channels, b: cable/satellite channels, c: public service channels,
d: 2008, source: IP and RTL Group (2009: 212)

Source: NRTB (2006: 226-227), NRTB (2010: 576)

MTG launched yet another satellite channel, TV6, on the Hungarian market in the autumn of 2007, which is also registered in the UK. TV6 is positioned as a general entertainment channel with a skew toward males in its targeted audience. Erotic programs form an important part of TV6's programming, and taking into account regulatory barriers they are broadcasted in the 11pm-5am time slot.

By the time of TV6's launch, the gender composition of Viasat3's audience had already shifted toward women due to the decision made earlier to reposition the channel. MTG decided to transfer the rights for live broadcasting of UEFA Championship League's matches to TV6 from Viasat3, and thus managed to secure a fair coverage for TV6 of about a fifth of television households to the new channel at the time of its launch.

Extending audience coverage of Viasat3 seemed to be vital for the broadcaster in order to become profitable, but at the same time led to a severe conflict with the national regulatory authority NRTB. According to data compiled in different surveys, Viasat3's coverage got extended beyond half of the population by the middle of the decade so the channel had grown out of the regional status as far area of reception is concerned and turned into a de facto national channel. This made the NRTB react after some time, opening a new chapter in the book of conflicts with the broadcaster.

3.7 Business as usual: from Conflict to Conflict

NRTB fined the broadcaster nine times in 2001 and eleven times in 2002 for the alleged violation of the media law during the program of Viasat3. This frequency of fines may be labeled as an average compared to other market players. Nevertheless, the two resolutions that ordered Viasat3 to darken the screen for 30 minutes in prime time got rather high publicity in the media: the reason behind these two fines was the alleged violation of human dignity of players performing in a reality show named Bar, broadcasted in the first months after the launch.

The frequency of fines set by NRTB increased steeply later on and amounted to 37 incidents in 2003 and 44 in 2004. As a matter of policy, Viasat Hungaria Ltd. never accepted these resolutions and sued the national regulatory authority on the ground of implementing the law in a wrong way. In order to put an end to litigation in courts, NRTB agreed to make a compromise with the broadcaster in the beginning of 2005. As the price paid for withdrawing lawsuits, the national regulatory authority lessened the amount of fines in a relevant degree, and the broadcaster paid them off. At the same time, Viasat Hungaria Ltd. promised to pay higher attention to comply with the law in the future, and the two parties agreed that if it seemed necessary, the broadcaster would seek to carry on consultations with the experts of NRTB regarding the age rating of programs in advance.

The compromise, however, did not lead to fewer regulatory sanctions in 2005; on the contrary, they increased to a record high level of 63 in that year. The frequency of sanctions attached to violating Article 8 (2) of the media law (regional and national broadcasters shall broadcast public service programs in prime time at least for 25 minutes every day) became more and more common. Of course, the interpretation of public service programs, as determined by the law, falls into the grey zone, so while implementing the law, the broadcaster kept on suing NRTB on the grounds of false interpretation of Article 2 (19) and asked the court to suspend the resolutions of NRTB in question.

Business as usual one might say, but litigation between the two parties took a new turn in the spring of 2007 when NRTB decided to change the status of Viasat3 from a regional to a national channel. As a consequence of this change, the national regulatory authority raised the amount of the yearly broadcasting fee from 19 million to 36 million HUF (the average HUF/EUR exchange rate was 264.27 in 2006 and 251.31 in 2007). Comparing the sum of the increased broadcasting fee to the broadcaster's net turnover in 2006, it amounted to a bit more than one percent, so it did not hurt the company badly.

The other main consequence of the new national channel status, however, threatened Viasat much more seriously. Article 8 (3), as cited earlier, orders that national television channels shall broadcast not less than twenty minutes of independent and uninterrupted news broadcasts during prime time hours. The costs to produce an evening news program that would correspond to the quality of the channel brand, were estimated at somewhere between 250-300 million HUF per year, corresponding to about the amount of profit made in 2006. Thus this requirement did not look viable for the broadcaster, so it sued NRTB again

on the same grounds: breach of the law in implementation.

The litigation process lasted about 18 months and ended in a peculiar way: The Court of Capital Circuit ruled that NRTB broke the law while determining the geographic status of the Viasat3 channel, annulled the resolution, and ordered the national regulatory authority to repeat the procedure to determine Viasat3 channel's legal status on the area of reception. This was good news for the broadcaster, who had lost five lawsuits filed against NRTN in the Court of Capital Circuit during the last quarter of 2008.

The broadcaster saw no reason to wait for the result of the new regulatory procedure and decided to apply for cancelling Viasat3's registration in Hungary as of 1 May 2009. Having no other choice, NRTB did cancel the registration of Viasat3. Consequently, the channel with the fourth largest audience share is no longer under Hungarian jurisdiction.

3.8 What went wrong? Questions for the Management

In preparation of this case, the management of Viasat Hungaria Ltd. was contacted for an interview and question answered by Bert Willborg, Head of Communication.

Q1: VIASAT 3 channel has been present on the Hungarian TV market since 2000. Taking into account only the full eight years in the 2001-2008 period, the Hungarian regulatory authority (ORTT, the abbreviation for NRTB in Hungarian) fined the broadcasters 254 times. Obviously conflicts between the broadcaster and the regulator had been frequent. Compared to the other countries where MTG AB is providing broadcasting services, do you regard the frequency of fines (in the Hungarian case: one every two weeks) as extremely high or just 'business as usual'?

A1: The frequency of the fines imposed by ORTT is indeed extremely high. What we consider particularly unusual is not the fines themselves, but the process of enforcing the fines, which seems different from other regulators' practices. *The only way for a broadcaster to argue against the method and procedure, which No 96 Law is not clear with, is to take ORTT to court, which is a relatively expensive and lengthy process.*

Q2: Comparing Viasat Hungaria Ltd. (the broadcaster) to the two market leader television broadcasters (RTL Klub, TV2) in Hungary, how do you judge the frequency of fines? Do the two national broadcasters cope with similar problems?

A2: We do not have detailed data about RTL's and TV2's fines. It is worth noting that unlike other regulators (e.g. Ofcom or the RTVV in Sweden who publish all judgments on all cases on their website and via newsflash emails), ORTT seems less transparent. There is the possibility to acquire such data, following a specific request to ORTT, but we understand that this takes time and makes judgments and law interpretations less transparent. It is very important for judgments to be public and easily available on websites and via newsletters, because this provides the broadcasters with a much clearer understanding on what the

rules' interpretation is by the regulator.

Q3: Grouping the fines in question, one realizes they have been attached to three subject matters, namely violating the rules on protection of minors, violating advertisement regulation, and violating the obligation in Article 8 (2) of the Broadcasting Act of 1996: "Public service programs shall be broadcast during prime time hours for not less than twenty-five minutes." Needless to say, the broadcaster contested the resolutions of the national regulatory authority (NRA, namely NRTB in Hungary) in most cases and filed a lawsuit against them. What did these lawsuits show?

A3: These lawsuits indicate that there are disputes in the interpretation of the law.

Q4: On average, how much money was spent on fines per year and compared to total costs, did the amount of fines represent a relevant item in overall costs?

A4: The figures are strictly confidential.

Q5: Some experts think that the broadcaster had been testing the tolerance of the national regulatory authority when violating some rules in the Broadcasting Act of 1996. Do you share this opinion?

A5: The interpretation of rules and regulations varies significantly not only from country to country but even within the same country. One rule can be interpreted fairly differently by a great number of people (often the judges or the regulators themselves). Take as an example the rule of not broadcasting content harmful to minors. In addition, interpretation of rules and what is accepted and not, goes constantly through a dynamic process, which follows the society and its reactions. Things totally unacceptable for the TV screens 10 years ago are often totally okay today. Also, many concepts or matters of our times were not even existent when certain rules were written. A broadcaster often needs to know to what extent certain things or new concepts are acceptable or to what extent they are covered by existing rules. At the same time, a broadcaster needs to understand how the interpretation of the rules change and to what extent it follows the society. This could sometimes be seen as testing the tolerance of the rules, but Viasat never aimed to breach any rules or regulations.

Q6: Although conflicts between the broadcaster and the NRA were permanent during this decade, the casus belli between the two actors seems to be clear: when the NRA ruled that the broadcaster's area of reception is nationwide the broadcaster might feel it had been enough and would not tolerate the ruling of the NRA any longer. Would you explain the reason behind this?

A6: NRA decided about Viasat3 being a nationwide channel without following the legal requirements. For this reason, we appealed and won the case, according to which Viasat3 is not a nationwide channel per Hungarian law.

Q7: How does the move of the broadcaster from Hungary to the UK fit the strategy of the company and the owner MTG AB?

A7: According to European Law, a channel is deemed to be established and regulated, and should accordingly hold a license in the member state where it has its head office and where the editorial decisions are taken. We have been looking at the operation of various channels around Europe which are under the control of Modern Times Group MTG AB (MTG) with the aim of improving efficiency by increasing centralization of our operations.

In the beginning of 2008 we made some significant changes in the programming management, partly as a result of this review. It became apparent more recently that for some time Viasat UK has been the broadcaster of the channel established in the UK, and consequently ought by law to acquire an Ofcom license for the channel, which we did with effect from the 1st of May 2009. More particularly, the head office for the channel has always been in London with Viasat UK. At the same time, more people have been employed in London with responsibilities related to the Viasat3's programming including editorial control and operations.

Q8: Don't you think that the move of the broadcaster from Hungary to the UK can be interpreted as a move to circumvent stricter rules in the fields coordinated by the directive 2007/65/EC (Audiovisual Media Services Directive)? It is quite obvious that the relevant market of VIASAT3 channel is the Hungarian market so the move in question has to bear legal scrutiny.

A8: The move of the broadcaster of the channel from Hungary to the UK is not a move to circumvent any stricter rules in Hungary. The channel is established in the UK along with many other channels. MTG and particularly its broadcasting division have a huge operation in the UK, which has been constantly growing since December 1987 when we launched our very first TV channel. Today, more than 25 channels are operated and broadcast from our London offices where more than 400 people work.

Student Assignments

Television broadcasting is a service, which can be provided for a target market from different locations.

1. Taking into account that trans-frontier television services in Europe have to comply with a common European regulatory framework (Council of Europe Convention and/or EU directive on trans-frontier television), what are the pros and cons when a broadcaster makes a decision on registering the service in a given EU member state?

Both general entertainment and thematic channels compete for the attention of a large audience.

2. From the point of view of marketing communication, what are the pros and cons for launching a general entertainment television channel and a thematic channel in a given television market?
3. What do you think of the provisions in Hungarian media law ordering regional and national television channels to broadcast a certain amount of public service programs including the rule to broadcast at least 20 minutes of news in prime time?
4. Given the information from the case regarding the core business decisions of Viasat Hungaria Ltd., how do you evaluate its timing for entry and subsequent changes in target audience and business model?
5. How do you judge the continuous litigations between the broadcaster and the NRA? Consider the arguments of MTG's chief communication officer Bert Willborg in your answer.

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4 Managing early and mature markets in Europe: The UniCredit Group

András Bauer, Marketing Department, Corvinus University of Budapest

> What we see right now across the region are the efforts of individual market participants to find the right strategy designed to counteract the rapidly deteriorating asset quality and higher funding costs. The scope of possible measures encompasses loan book re-pricing, cost savings, aggressive deposit gathering, non-core asset disposals, re-capitalization, and a slowdown of lending activities (combined with more selectivity). Still the major players in CEE remain committed to the region including more risky countries like Ukraine, Hungary, Romania and Russia.
>
> ***CEE Banking Sector Report: Rough Playing Field – Committed Players***

4.1 Banking in Europe

Banking has become a global – or at least regional – industry; this is especially true within the European Union which has pledged to provide the free movement of people, goods and capital. Despite this fact, banking is heavily regulated on national levels; regulations are converging. According to Dermine (2006), the level of banking integration has increased significantly due to joint regulations, institutional integration and further due to mergers and acquisitions.

These strategic choices can be seen as country specific. According to McCauley et al. (2010), banks have tended to follow a multinational direction over the last decades. Multinational, in this context, means a strategy of when banks expand through branches and affiliates and fund local positions from operations in the host countries. The opposite – termed international – is when a bank operates from its home country and makes mostly cross-border transactions. When, in a crisis, the international interbank business dries up, the tendency toward multinational banking becomes stronger. Despite the global trend, however, the authors claim a large difference across national banking systems. While Spanish banks tend to be operating more locally and decentralized, German or Japanese banks run centralized home-based operations. So, the variety of different banking systems is relatively high in Europe. One thing, however, is quite relevant for most mature market banks – they seek growth abroad, often in emerging markets.

The last two decades of the 20th century have witnessed tremendous change in Central Eastern Europe (CEE), both on political and economic levels. Communism collapsed as a

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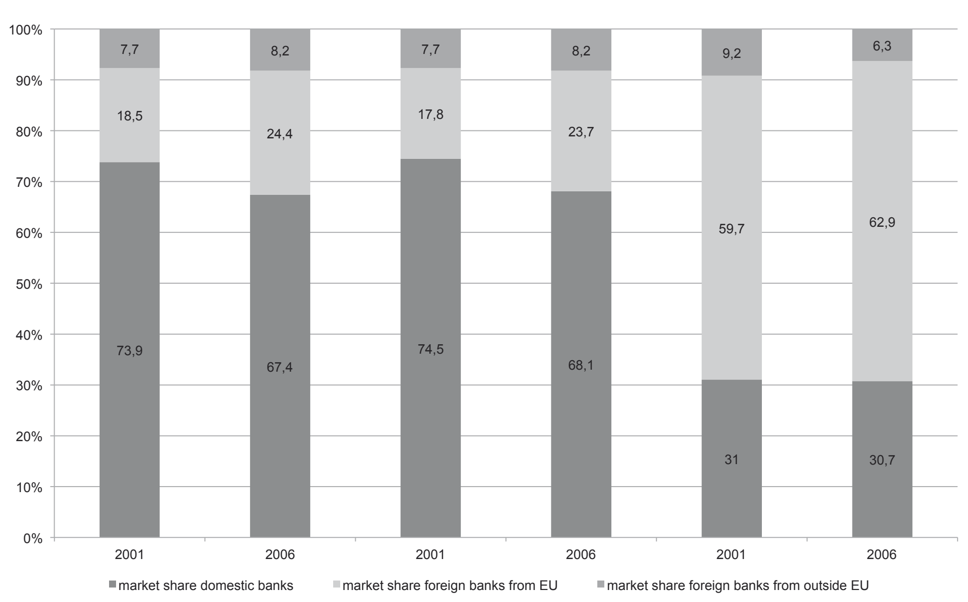
system and the previously communist countries decided to join the capitalist world. Based on the pursuance of mutual benefits, national governments opened their – previously relatively closed – markets and invited foreigners to invest. Investment in the banking industry opened growth opportunities for international banks, which faced several important strategic and marketing questions; these included:

1. Market entry and positioning,
2. Resource allocation decisions between their home markets and the newly built markets, and
3. The pursuit of firm-level efficiency gains, including the marketing domain.

While Europe is the birthplace of banking and even though several European banks are among the world's largest, banking tends to be a national issue in Europe. With some exceptions – take e.g. the HSBC group – European banks' focus is usually in their home markets, sometimes in adjacent markets, and rarely in some dedicated regions, such as the strong Spanish presence in South-America. Not too surprisingly, this is reflected in national market shares as well, as **Exhibit 4.1** shows.

Exhibit 4.1 Market Share of Domestic and Foreign Banks in the EU, 2001 and 2006



Source: Houben (2008)

As we see, most European markets maintain their home-dominance, except for Central Eastern Europe. This region opened up relatively quickly and turned previously state-owned banks into private hands, usually with the help of foreign investors. The landscape is dominated with small- and medium-sized European banks, usually from very specific countries. Geography, cultural closeness and previous ties all play a role here, so Central European banking is dominated by Austrian and Italian banks, while in the Baltics, Scandinavian (mostly Swedish) banks play an important role. One explanation of foreign domination in CEE is based on the privatization argument that due to lack of internal capital, formerly state-owned banks were sold to foreign investors. Even compared with other emerging markets, foreign ownership is high; **Table 4.1** seems to support this argument.

Table 4.1 Ownership structure of emerging market banks, 2009, percentages

Owners	Asia	Latin America	CEE	other emerging
Private domestic banks	38	44	21	79
Foreign banks	27	36	62	11
State owned banks	24	17	14	10
Other financial institutions	11	3	3	0

Source: Mihajlek (2010)

Foreign ownership opens up an interesting marketing dilemma of standardization: whether, if, and how much banks should follow marketing standardization across different national markets. We may believe that standardization may come from a production point of view in standardizing processes and ensuring that best practices are transferred across different markets.

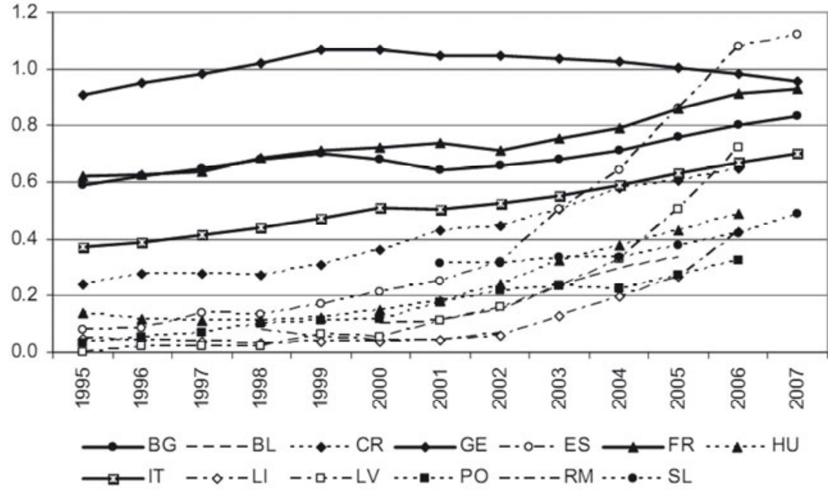
The CEE region had a relatively strong lack of development in bank intermediation and product variety. Due to pent-up demand, the previously less developed loan market started to grow at a high pace, often reaching 50% growth annually, albeit starting from a low base level. While the absolute figures had been much lower, loans started to play a major role in economic development and reached a comparable relative level as in Western Europe.

The loan to GDP ratios did not change heavily after 2007; however, the growth has stopped in emerging countries due to the contraction of lending, which was a consequence of the 2008-2010 financial crisis. In 2011, lending is slowly increasing but it has not reached the 2007 level.

Yet Eastern European markets are maturing. Overall investment has fallen from its peak and some foreign-owned have offerings which are tailored to small and midsize enterprises and their affluent owners. Citibank has cornered the credit card market in Hungary and Poland through greenfield investments. Italy's UniCredito, Germany's HVB, Austria's Erste

Bank, and Belgium's KBC Bank and Insurance have all built a presence in the region by acquiring local universal banks vying with high-performing incumbents such as OTP of Hungary.

Exhibit 4.2 Loan to GDP Ratios in Selected European Countries



Note: BG=Belgium, BL=Bulgaria, CR=Czech Republic, GE=Germany, ES=Estonia, FR=France, HU=Hungary, IT=Italy, LI=Lithuania, LV=Latvia, PO=Poland, RM=Romania, SL=Slovenia

Source: EUROSTAT (2009)

Competition is set to heat up in these still relatively fragmented banking markets, and further consolidation is expected soon. Banks continue to expand; others are leaving as intensified competition and convergence toward Western European market conditions begin to separate the winners from the runners-up. Western bankers will be familiar with the challenges; notably an ever-tougher battle for the all-important affluent-customer segment and a growing need to counter pressure on margins by reducing credit losses and improving cost efficiency.

4.2 Received Theory and Empirical Insights

Market structures change with market evolution, a fact that is easily observable in transition markets. Due to an interactive process of consumer learning and firm adaptation, marketing strategies are changing over time. To enhance consumer learning and to introduce

changes in the market, companies can use multiple tools such as new product introductions (Feick and Price, 1987), changes in advertising intensity and style (Chandy et al., 2001), and the alignment of distribution channels (Kabayadi et al., 2007).

Product Variety and Market Development

Consumer knowledge and product variety highly depend on market evolution, albeit culture may have an influence. Product formats are introduced at different times and while a certain product is a novelty in one market, it may be a mature one in another market. This creates an interesting perspective on efficiency transfers whether it be brand positioning, channels or advertising. Firms tend to use what works and avoid cost duplications by utilizing best practices.

Product portfolios can vary according to market development and market size. A better developed product market usually attracts a wider and deeper portfolio since consumers can identify their needs clearly and go after specialized offers that suit them perfectly. It is easy to see the backside of this approach; however, fragmentation may lead to product proliferation that increases costs. In parallel, firms have to take market size into account as well. A niche strategy is often only feasible if the total market size is large enough and would allow for profitability. In the European banking market, the difference is striking, as reflected in **Table 4.2**.

Table 4.2 Product Portfolio and Revenue Differences in European Banking

Region	Number of products owned by customers	Share of day-to-day revenues, %	Share of credit based revenues %
Northern Europe	3.2	59	41
Western Europe	5.4	49	51
CEE	2.1	34	66
CIS	1.7	28	82

Source: Angoulvant (2009)

In mature markets, where banking intermediation has reached a very high level, there is a share of wallet battle going on; banks have penetrated the market with several products and consumer own many of them. On the contrary, in early markets, where the penetration is relatively low, consumers only own a couple of bank products. Clearly this sets objectives for product strategy; cross selling is the way to go in early markets. This insight is further supported by a recent study of Ernst and Young (2010), which concluded that in mature European markets 91% of customers bank at least with three banks and one quarter of all customers have 2-4 products with second banks.

Table 4.3 Revenue Differences in European Banking (Euro)

Region	Income Customer	Growth Rate	Fees Income %	Interest Income %
Northern Europe	630	2.9	59	41
Western Europe	750	4.7	49	51
CEE	190	14.0	34	66
CIS	110	61.9	18	72

Source: Angoulvant (2009)

Pricing

The right pricing strategy has to assure that firms optimize their revenue, taking market segmentation and market development into account. Firms therefore have to take price sensitivity into account and make sure they find the right product/price combination. Not too surprisingly, revenue sources across markets may show great differences as **Table 4.3** shows.

Bank revenues are heavily dependent on consumer needs; in Northern and Western Europe, day-to-day banking revenues (commissions and fees) have a high share, while in Eastern Europe banks make mostly money from credit-based interest. This is not too much of a surprise as we consider the product structure in different regions.

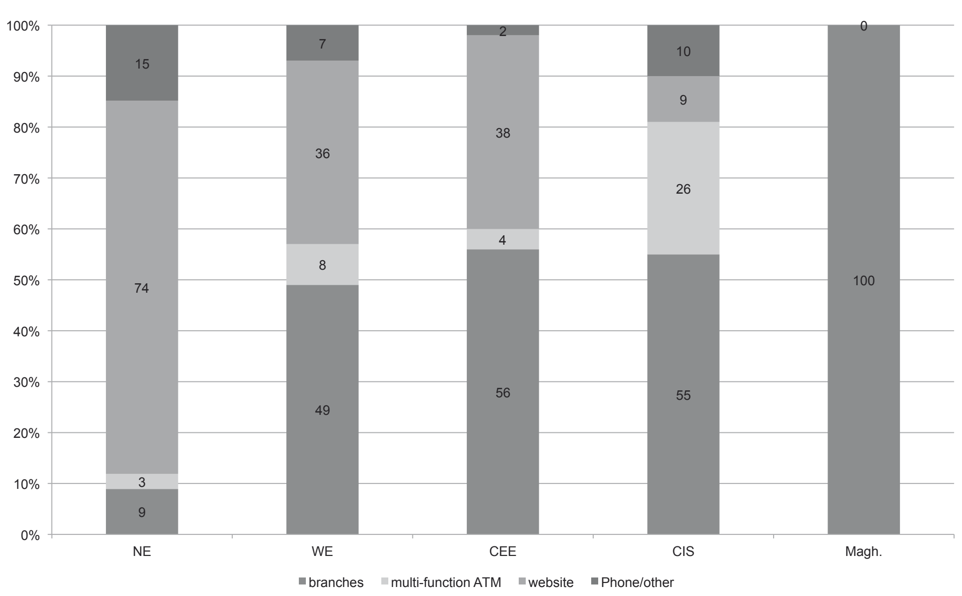
Distribution

In developing access points, firms may consider multiple issues including efficiency, culture and geography. A further dimension relates directly to market development. In early markets, most consumers can be considered as novices that face high risk in purchasing from new product categories. Face-to-face channel solutions usually do much better in this respect due to the unstructured nature of consumer problems. Salespeople are effective in reducing the risk of novelty through product demonstrations and personal advice. If we consider the Dell phenomenon, we notice the Dell Computer became highly successful with its indirect model when consumer knowledge reached a certain level and consumers did not need the personal service any longer.

The same can be true in the banking industry. The higher the financial sophistication, the lower the need for personal advice; or personal advice is mainly sought when consumers are buying complex products, while simple products are sold over indirect channels. Van Birgelen et al. (2006) found in the Dutch banking environment that consumer requirements towards distribution options depend on product complexity. Simpler products are often purchased online and consumers want efficiency, while they do not mind spending time on more complex issues personally, usually tied to complex products, such as investments. However, there is a clear notion – at least in the insurance industry – that sophisticated consumers are apt to use indirect channels.

Further, there are cultural elements as well. One could argue that Northern and West European consumers are similar in financial sophistication, but the channel picture does not support this argument, as can be seen in **Exhibit 4.3**.

Exhibit 4.3 Distribution Channels Across Different Regions, 2008



Source: Angoulvant (2009)

Clearly we may have cultural influences in this distribution. However it is clear that CEE and CIS customers are favoring physical branches over traditional indirect channels such as phones. Branch opening – despite the cost – is still the major direction in less developed markets due to the importance of face-to-face contacts in buying new products.

For routine services, our findings suggest that behavioral intentions are most strongly influenced by satisfaction with office-related performance factors. For non-routine services, satisfaction with service employee performance is the most significant driver of intentions (van Birgelen, 2006). However, cost is not the only issue in this respect; channel effectiveness can be more important. Bauer and Carman (1996) e.g. argued that in an emerging market, retailers may forgo their cost efficiency advantage and use quality differentiation instead. This, we believe, is still a considerable argument. Depending on positioning, companies with a clear quality advantage may not use cost-efficient channels, such as the Internet, even in the insurance market.

Despite the cultural differences, one can clearly see that while in mature markets branch distribution is scaled back due to cost reasons (the number of branches decreased), in CEE and CIS banks pursue a branch opening strategy to serve clients directly.

Advertising

Consumer knowledge has a strong impact on advertising style. As Chandy et al (2001) have pointed out, expert consumers process information in a quite different way than their novice counterparts. Due to their knowledge and product experience, advertisers may create differences in multiple areas, including the type of appeal, its prominence, appeal frames, and consequently appeal source. In younger markets, consumers lack product information and are therefore more willing to learn from advertising and accept arguments rather than emotional elements. Similarly, negative frames can be used in creating advertising messages since consumers face problems every day, and do not mind being confronted with problems in commercials when a solution is offered later. While in mature markets consumers often reject it when experts play a role in advertising messages, in younger markets, central elements of advertising work well.

Chandy et al (2001, p. 400) have argued that response to advertising can be quite different in established and new markets. In defining the market they argue: "Market age refers to the lengths that the product or service has been available and advertised in a particular market. For a particular product or service a market is said to be older than another if the product or service has been available and advertised longer in the first market than in the second. Thus, a young market is one where the product or service was introduced only recently; an old market is one where the product or service has been available and advertised for a long time. We argue that different cues work differently in younger markets than in older ones because of intrinsic differences in consumers' motivation and ability to process information in those markets. Knowledge of these differences can help marketers to assign ads that are tailored to the age of individual markets."

Overall, one could argue that consumers in younger markets are often more involved in the same product category than in mature markets. This definitely represents an interesting challenge for international players: Since they have to build markets often from scratch, advertising has to provide basic benefits for consumers that may jeopardize their positioning or at least their advertising style in more mature markets. This also means that advertising standardization is difficult if not impossible, or it should rather take place in media planning and not in creative solutions. Another challenge derives from product assortment issues. Mature and early markets can have different product portfolios and advertising's role changes accordingly.

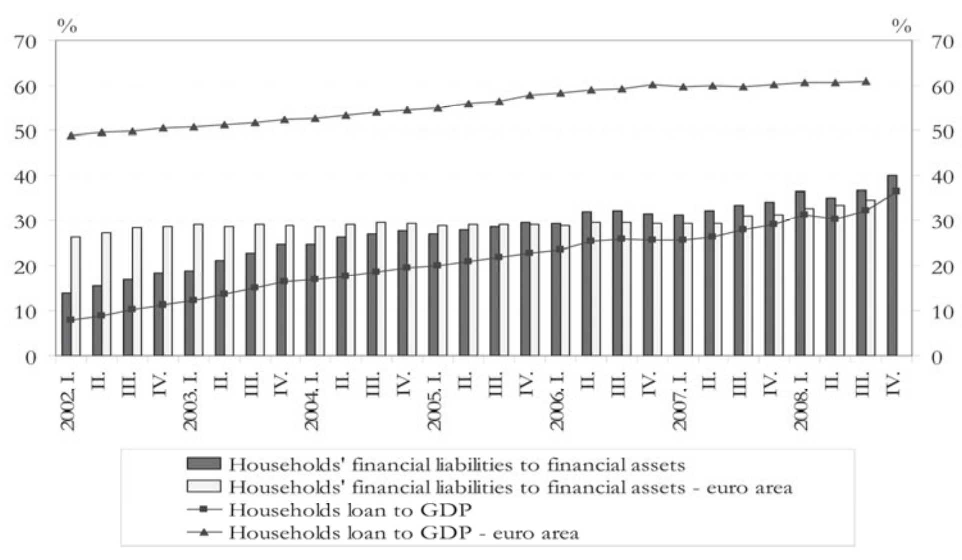
Consumer Behavior

Consumer learning is an important driver of market development. During a trial-and-error process, consumers learn product features, price-value relationships, quality aspects, and by receiving market feedback rules of consumption. According to Hoch and Deighton

(1989), there is an important difference in how experts and novices learn due to motivation, product domain knowledge and the marketing environment. Novices – often found in a large number in early markets - have a disadvantage in structuring problems and finding the right sources. Consequently their learning tends to be shallow and can easily be manipulated by the ambiguous marketing environment.

Learning can especially be quite intensive in situations when information becomes abundant after a relative scarcity. Due to their constraints, CEE consumers have not been overwhelmed with market information for a long period. Only after the system change and with the advent of market economy did they get access to a wide variety of stimuli, including new products, services and advertising messages. This has created major confusion as many customers are not able to unlock marketing language, including that of advertising. This is reflected in suboptimal consumption decisions including some important ones. In Hungary – which is not an exception in CEE – consumers got heavily indebted by taking loans. This phenomenon can be seen in **Exhibit 4.4**.

Exhibit 4.4 Household Liabilities to their Financial Assets in Hungary



Source: Hungarian National Bank (2009)

Household loans started to grow and while it did not reach the Eurozone average, the risk element was embedded in the loan constructs that were based on foreign currencies (mainly euro and Swiss franc). While the national currencies of the CEE countries were stable, this created no problem. The 2008 crisis, however, led to national currency devaluations,

partly by the increased risk premiums. Consumers who had taken foreign-currency based loans previously were now facing huge hikes in their monthly installments and many of them defaulted on their loans. This represents a heavy lesson in consumer behavior for many families.

During the process of improving consumer skills, consumers learn from multiple sources, including advertising and word of mouth. Word of mouth is an important factor, especially in product categories where social aspects are strong. For any national market there is an interesting question to be asked: How willing are consumers to share market information with each other?

Partly based on diffusion of innovation and word-of-mouth research, Feick and Price (1989, p. 85) coined the term 'market maven', meaning those "individuals who have information about many kinds of products, places to shop, and other facets of markets and initiate discussions with consumers and respond to requests from consumers for market information." In later studies, several authors picked transitions countries, including some in CEE, to study the nature of spreading market information in young markets. The insights from this research suggest that while CEE consumers in general are less educated in finance, many young consumers are both willing to acquire and share market information.

Market entry and international organization

Firms handle international expansion in different ways. These decisions can be assessed mainly from two perspectives: standardization and efficiency. The standardization literature usually focuses on how demand is handled in multiple markets. The globalization school is basically focusing on demand homogeneity and consequently emphasizes economic (e.g. economies of scale and scope) and perceptual advantages that can be reached in a globally orchestrated way. Localization is embracing market heterogeneity and focuses on the effectiveness argument that is supported by unique consumer behavior and institutional setup.

Organizational issues, such as market entry modes and on-going operations, are usually discussed from an efficiency perspective. Anderson and Gatignon (1986) argue that asset specificity and the existing governance structure in foreign markets will define the most efficient entry mode. Unclear governance will increase the propensity of firms choosing high-control entry modes. This notion is supported by Erramilli and Rao (1993) arguing that service companies, such as banks, may favor high-control entry modes due to their highly asset-specific knowledge based assets. In CEE the high control entry mode is clearly observable. Hryckiewicz and Kowalewski (2010) report acquiring existing banks was the most preferred entry form in CEE and, with much less frequency, the establishment of subsidiaries. Entrants were mainly attracted by market size and profit options, but interestingly having the same legal system in the host country played an important role as well. CEE countries with German or French legal systems attracted entrants that preferred one or the other system.

Beyond entry form, banks have to make decisions about how they organize for international expansion and how they integrate new units into their organization. According to Douglas and Craig (2011), companies have to rethink their global strategies due to different market saturation, cultural diversity and operational issues. They predict the emergence of semiglobal marketing strategies that can bring some kind of regionalization into the global setup. In CEE banking entrants often cluster emerging markets together and sometimes use one dedicated developed country, such as Austria, as headquarters for these operations. We would argue the regional approach can be seen as one transitory step towards standardization. Emerging markets are managed at the beginning as individual units sometimes with special rules, but later on become fully integrated parts of the mother organization.

4.3 The UniCredit Group

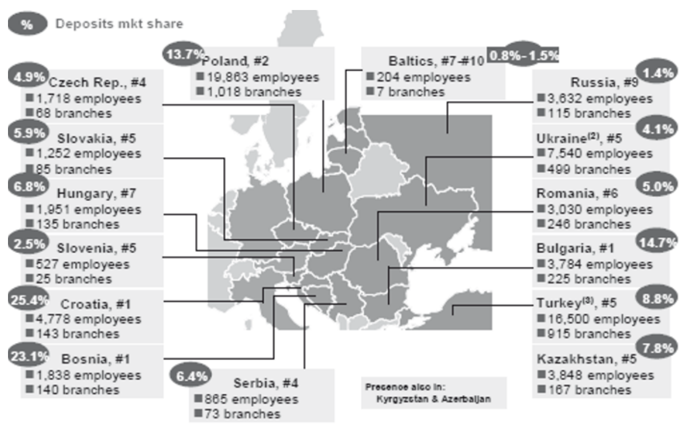
The UniCredit Group was the outcome of the 1998 merger of several Italian banks including, among others, Credito Italiano, and Unicredito and the subsequent combination with the German group HVB and Italy's Capitalia (Banca di Roma, Banco di Sicilia and Bipop Carire). In 1999, UniCredito Italiano, as it was then known, began its expansion in Central and Eastern Europe with the acquisition of Polish Bank Pekao. Growth continued over the next few years with the purchase of the Pioneer Investment group, and the subsequent formation of Pioneer Global Asset Management, and further strategic acquisitions in Bulgaria, Slovakia, Croatia, Romania, Czech Republic, and Turkey. In 2003, UniCredito Italiano completed its reorganization plan, S3, by forming three banks in Italy, for individual market segments (UniCredit Banca, UniCredit Banca d'Impresa, and UniCredit Private Banking) and with the creation of the New Europe Division. This reorganization process made UniCredit the first bank in Italy to adopt a business model based on its divisions; this model is still operational today.

In 2005, UniCredit merged with the German group HVB, itself formed in 1998 by the combination of two Bavarian banks: Bayerische Vereinsbank and Bayerische Hypotheken-und Wechsel-Bank, resulting in a single, major European bank. Integration with the HVB Group, reinforced by the merger with Bank Austria Creditanstalt in 2000 and its territorial establishment in many areas of the new Europe, enabled further growth for UniCredit Group, thus building on its own European vocation. Bank Austria Creditanstalt is Austria's largest banking group. Bank Austria Creditanstalt is a major shareholder in Bank Medici AG. Following news on Friday, 2nd January that the Bank Medici had invested $2 billion with Bernard Madoff, Vienna appointed a supervisor to run the private bank. In 2007, by combination with the Capitalia Group, the third-largest Italian banking group, UniCredit Group consolidated and strengthened its position in one of its most important domestic markets, Italy. Capitalia was established in 2002 from the integration of two pre-existing entities, the Bancaroma group (in turn the result of the merger between the oldest Roman banks: Banco di Santo Spirito, Cassa di Risparmio di Roma, and Banco di Roma), and the Bipop-Carire Group. Apart from these two banks, the Group also controls the Banco di Sicilia Group, one of the oldest Italian banks, with a well-established base in Southern Italy;

MCC (formerly MedioCredito Centrale); and Fineco, the first direct bank and first online broker in Italy.

After a series of mergers and combinations, the UniCredit Group has reached new dimensions: it operates by far the leading banking network in the region with about 4 500 branches in 19 CEE countries and over 10 000 branches in total. CEE contributes about half of the group's profit and large country markets (Poland, Turkey, Russia) provide more than half of the CEE revenue. A key issue for UniCredit is the creation of a leveraged business model across the corporation, which has helped the bank to decrease cost of operations especially during the critical years of 2008-2010. The bank established 'product factories' that develop best practices across business lines in the following areas: leasing, asset management, consumer credit, mortgages and investment banking.

Exhibit 4.5 UniCredit presence and position in CEE, 2010



Source: Ghizzoni 2010

Bank operations are done in four divisions: Families and SMEs, Private Banking, Corporate & Investment Banking, and the separate CEE Division which includes 19 countries in emerging markets. Operations are considered to be a mixture of global and multilocal ways, the latter allowing local businesses to meet customer needs optimally. A local country chairman is responsible to carry out corporate strategy locally while engaging in management of the main business entities in the given country. To better understand CEE operations, **Exhibit 4.5** provides an overview of how UniCredit is positioned in the CEE region and how much some of the markets are developed, e.g. in the extent of financial intermediation (share of customers having bank contacts in a country).

Branding of the Bank

Shortly after the mergers took place, the bank decided for a regional branding strategy: The Group is now adapting its brand architecture to this new dimension. The CEE brands will be closely linked to the umbrella brand 'UniCredit Group' to emphasize the strength and opportunities the network offers to its customers. Therefore, most of the CEE banks will operate under the new brand name 'UniCredit Bank'. The new brand values create a clear and consistent brand image that emphasizes unity within the region. The branding strategy took the market positions into account: In countries with a strong leading position, the UniCredit name only plays a supporting role to the acquired local brand. So, Zagrebacka Bank (Croatia) and Yapi Kredit (Turkey) kept their names, while Tiriac Bank in Romania became UniCredit Tiriac Bank. More coherence is served through the unique lettering and the use of the bank colors. Interestingly, most mainstream competitors share a similar branding approach, with the exception of the clearly positioned, niche players, such as Citibank, or ING, banks carry their original brand name in CEE countries.

Table 4.4 Major Players in Central Eastern Europe Banking (17 countries, based on assets, 2010)

Bank	Origin	Countries Present	Leading Position in Market (1-3)	Share of CEE Assets in total
Citibank	U.S.	3	0	
Commerzbank	Germany	3	0	
Erste Bank AG	Austria	5	4	30
GE Capital	U.S.	3	0	
ING	Netherlands	5	0	
IntesaSp	Italy	6	4	7
KBC	Belgium	4	3	20
Nordea	Sweden	3	0	
OTP	Hungary	4	2	100
Raiffeisen	Austria	11	3	54
SEB	Sweden	3	2	
Société Generale	France	6	2	6
Swedbank	Sweden	3	2	
Unicredit	Italy	17	5	12

Source: Company Homepages and UniCredit Strategic Analysis

Competition

Growth opportunities have attracted multiple players into Central Eastern Europe. Several banks and financial institutions felt the need to find fast growing markets where they could leverage their assets and take early market share. Beyond the numbers an interesting choice of market is observable. Some banks have a specific regional focus, such as Scandinavian banks are only active in the Baltic region (Estonia, Latvia and Lithuania). French banks, such as Société Générale, concentrate on countries where the language and the legal system are similar. Most foreign banks use their home-based brand-names with the exception of KBC (Belgium).

Competitive development and UniCredit reaction

Until 2008, the markets almost exploded, as can be seen in **Table 4.5**. While the level reached only about third of the EU 27, the tendency was quite clear: strong market growth was driven by foreign banks utilizing their assets generated in their home countries.

Table 4.5 Mortgage Market Development in Selected Countries, % of GDP

Country	2000	2005	2009
Bulgaria	0.4	4.6	12.6
Estonia	4.6	23.4	44.5
Hungary	1.4	10.5	16.7
Poland	2.1	4.7	18.2
Slovenia	0.3	4.8	11.4
EU 27 average	36.0	46.5	51.9
U.S.	70.0	88.8	81.4

Source: Hypostat (2009)

In essence foreign banks – including UniCredit – were redirecting their lower cost savings revenues from the home or Western-European markets into CEE and converting them into loan products. Due to the home based reputation advantages of local banks in acquiring clients, foreign banks had to use higher marketing expenses to balance the reputation effects. Banai et al (2010) report that in the Hungarian market they spent around five to six percent of their banking revenue for marketing, while local banks only spent around four percent. This changed dramatically after the global financial crisis. When the 2008 financial crisis reached Europe, many of these banks had their problems at home and had to ask their own governments for help. This dried up the resources for CEE lending and made the market players change their strategy in focusing on deposit collection rather than providing loans. The financial crisis hit CEE hard; it can be seen as a two way process. On the one

hand, financial contagion from developed markets spread into CEE, but it was complemented by the contraction of GDP in almost every country. After the collapse of Lehman Brothers, interbank lending in the world almost stopped. According to Moreno and Villar (2010), international debt markets for emerging market issuers closed and trading collapsed. In some CEE countries (especially Hungary, Poland, Russia, Latvia and Lithuania), exchange rates changed in a volatile way, while member countries of the Eurozone (Slovenia and Slovakia) suffered little in this respect.

Banks in different CEE markets had to find different solutions to financing shortages. An overall approach taken was the cutting of the lending activities both for the corporate and the consumer market. Because Western European parent banks have suffered greatly in their home countries, cross-border lending was not as strong as before. This gave a strong push to change the product scope and focus on local currency and foreign currency deposit taking. Saving products and a more selective loan expansion seem to be the key areas for the second decade of 21th century.

Nonetheless, Eastern Europe will retain its particular challenges and it will be essential to master them. The region's affluent customers, for instance, tend to be young, entrepreneurial and in need of loans. But banks are grappling with loan loss provisions four times higher than those in Western Europe, a task made more difficult by a lack of the type of credit information taken for granted in Western countries.

A final word from a banker...

"Today, more than ever, the banks must be able to determine quickly the current needs of their clients and, just as quickly, provide solutions for them in terms of products and services that are truly able to meet these needs.

In such a delicate phase of the economy, banks should offer products that are simpler than in the past, completely transparent and easy to price."

Alessandro Profumo, CEO UniCredit Group, February 2009

... and a quote from a recent report

"We continue to expect GDP gains this year for CEE as a whole, of almost 4%, with all countries in our group posting positive gains for the first time in 4 years. Data released to date for 2011 is supportive of this view."

UniCredit CEE Quarterly, March 2011

Student Assignments

1. Describe the marketing differences in early and mature banking markets.

   Are these differences relevant to all players?

2. UniCredit Bank has quite different market positions in different CEE countries. What are the consequences for country level marketing? How much standardization would you recommend in this domain?

3. How would you advise a new entrant into the CEE banking market?

   What kind of marketing entry strategy options may a major or a niche player rely on?

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Part 2

Acknowledging and Managing Diversity in Consumer Behavior in Europe

5 Nostalgic Branding in Central Europe

Petr Král, University of Economics Prague, Czech Republic

Socialism is over, decided the Industrial Property Office:

Kofola´s brand does not belong to everyone.

January 5th, 2010: The Company Kofola will keep its most valuable asset, its brand 'Kofola', which ranks among the most valuable brands in the Czech Republic. The Industrial Property Office refused a proposal of the company's competitors to use the word 'kofola' as it was in socialism as a general name for some non-alcoholic beverages and not as a brand. Now there is just one Kofola and the company has the right to protect its brand and use it exclusively, decided the Office.

Kofola bought the brand in 2002 for CZK 215 million (app. EUR 8.4 million) and has since invested heavily into the brand. Today, Kofola ranks among the most valuable brands in the country and is the most popular Czech brand among Facebook users, with 167 thousand fans (some 120 thousand more than Pilsner Urquell – the second most popular Czech brand on Facebook).

Article in online news: Aktualne.cz

5.1 Background

Kofola once was a response of the Czechoslovak centrally planned economy to the increasing popularity of Coca-Cola and Pepsi. The history of the brand dates back to 1962 when the national pharmaceutical company Galena Opava started to distribute Kofo-syrup to producers of non-alcoholic beverages in former Czechoslovakia. The Kofo-syrup was used as a key ingredient for the Kofola drink. Since the 1960s, Kofola has been gaining popularity all over the country with various producers producing the drink.

After the Velvet Revolution in 1989, the brand almost disappeared from the market, as well as many other 'old communist brands', as its market share was taken over by the global giants Coca-Cola and Pepsi. Consumers in former communist countries at that time preferred imported Western products over national brands, as they perceived them as of higher quality and more trendy. Kofola reentered the market in 2000 when the newly established company Santa nápoje started the production of Kofola again. In 2002, the re-launch of Kofola was supported by a TV advertising campaign in the Czech Republic and Slovakia. Kofola soon regained its lost popularity, and today is a respected competitor of the global market leaders in the Central European markets.

T. Rudolph et al. (Eds.), *Diversity in European Marketing*,
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The example of Kofola demonstrates a current trend in consumer behavior in Central and Eastern Europe, as consumers in those former communist countries return to their traditional national brands after more than a decade of preference of imported Western products. This chapter elaborates this trend in a European context by introducing the concepts of nostalgia and retro branding. Key success factors that help marketers re-introduce old and sometimes almost forgotten brands and different target groups for nostalgic brands are discussed. Limitations of this specific branding concept are also considered and the future perspectives of those brands in Central and Eastern Europe and their chances to also become popular outside their home country are outlined. The example of Kofola will be used along other Central European brands to illustrate the findings.

5.2 The Concepts of Nostalgia and Retro Branding

Nostalgia and retro branding are not just a Central and Eastern European phenomenon. In the 1990s, many old brands were re-launched in Western European markets and in the USA. Many of them soon gained popularity and therefore attracted the interest of marketing researchers who wondered what made these old brands so popular in times when continuous innovation and trend-following were generally considered to be the key success factors in marketing.

Some authors argue that a kind of 'nostalgia-boom' is always characteristic for the turn of centuries and therefore the turn of the millennium attracted just more attention from consumers. At such times, people usually look back and commemorate also the brands that were connected with the 'better' past. Such classic brands not only embody the moral values of craftsmanship and lasting value, but also hark back to a time when the world seemed safer, more comprehensible and much less commercial (Brown, Kozinets, and Sherry 2003). In today´s world, when people worry about so many things, such as terrorism, job reduction or global warming, an old brand gives people the feeling of comfort and security and reminds them of times when they felt better (Lamb 2009).

One can identify two types of nostalgia, personal and communal, which are strongly interconnected in marketing. Personal nostalgia refers to people´s personal experience. As consumers get older, they often look back to their young years, while communal nostalgia refers to epochal changes on the societal level. Long established brands evoke not only former epochs, but also former selves (Brown, Kozinets, Sherry 2003). These two kinds of nostalgia may explain why Generation X consumers started to purchase the brands of their youth again, but they fail to explain why these brands also appeal so much to the younger Generation Y, which usually considers everything related to former generations old-fashioned. Nurko (2003) suggests that Generation Y consumers purchase retro brands because they enable them to mix the 'cool' things of their parent's generation with the technology of today. Earle (2004) supports this idea by stating that for younger consumers 'old' has become 'classic' and classic has become cool.

Representatives of such brands that succeeded with the combination of an old brand name and new technology are, for example, the New Beetle by Volkswagen, Mini by BMW, the New Fiat 500, the New Chrysler PT Cruiser or Nike's retro sneakers. Such retro brands should be distinguished from pure nostalgic brands. Retro branding refers to the revival or re-launch of a product or service brand from a prior historical period, which is usually, but not always, updated to contemporary standards of performance, functioning or taste. Retro brands, on the other hand, are distinguishable from nostalgic brands by the element of updating. They are brand new, old-fashioned offerings (Brown, Kozinets, Sherry 2003).

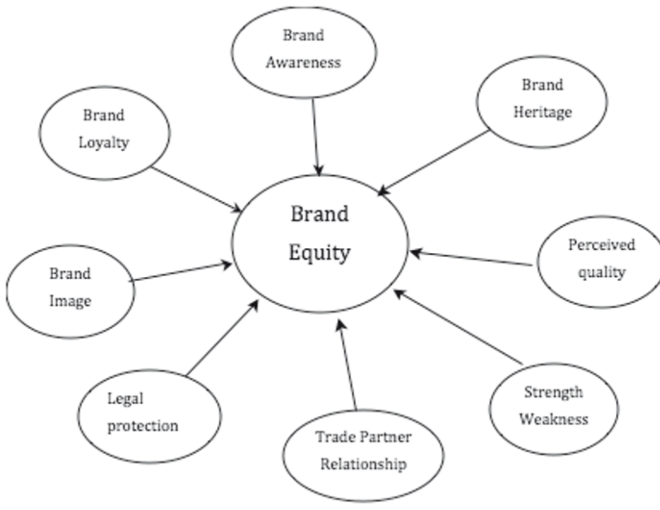
Yet it is not just the consumers' desire to bring back the old good times that drives the retro trend. For marketers, retro brands represent a relatively safe and less-costly way to introduce a new thus offer a useful way of limiting the risk of failure. A new product can be introduced bearing an old brand and therefore connecting itself to a successful predecessor. The brand values are already set and the target market knows them. In consequence, the probability of success is much higher.

The general model of brand equity may be applied to retro (nostalgic) brands to show the main benefits an old brand may bring when used to launch a new product. Brand equity can be defined as a set of brand assets and liabilities linked to a brand, its name and symbols that adds to or subtracts from the value provided by a product or service to a firm and/or to this firm's customers (Aaker 1991). **Exhibit 5.1** shows the main elements of brand equity.

Brand awareness represents the ability of the consumer to recognize the brand and to link it to a certain product category. A retro or nostalgic brand can benefit from its past market presence and from the fact that a certain group of consumers remembers the brand from the past. *Brand loyalty* describes the probability that the consumer will purchase a certain brand. Old brands that disappeared from the market years or even decades ago have no loyal customers at the moment of the re-launch but they might be able to gain back those who were loyal to them product to the market (Earle 2004). The launch of a new brand incurs huge investments: A new brand name and logo must be created and tested among the target group and a new slogan and communication campaign have to be launched to introduce the new product with a new brand to the target audience. All these steps incur cost and time and despite detailed and sophisticated marketing research, a marketer can never be sure of success. Retro brands in the past. *Brand image* represents any associations (positive or negative) that the consumer has towards the brand. It is clear that companies that revive the old brands always do so only with brands with strong positive associations from the past. *Brand heritage* represents the associations towards the brand that the brand gained in the past. Brand heritage is therefore a key component of the brand equity of retro and nostalgic brands and a key motivation of companies to reintroduce such brands.

Perceived quality could be defined as a perception of the overall quality of the products or services that bear the brand name. Retro brands must offer the same or higher quality of products related to today's needs than they offered in the past to be successful on the market. If the nostalgic or retro brand should be successful today, it needs to fit the modern needs to exploit the nostalgia opportunity (Ridgley 2009).

Exhibit 5.1 Brand Equity Elements



Source: Machková, Lhotáková, Král (2010)

Legal protection is essential for the company as a brand is an important intangible asset (see the article at the beginning of this chapter) and therefore must be protected so that no one else can use the brand on the market. The advantage of retro brands can be that the brand is usually already registered and legally protected and the company therefore has almost no additional costs related to the necessary registrations. Finally, *relations with trade partners* refer to existing contracts with distributors and retailers. Brands that are widely distributed are more valuable for the company than those that are not so welcomed by the distributors and retailers. Retro brands usually have no existing distribution channels at the beginning, but can attract more attention of retailers who are confronted by thousands of new entrants every year. Earle (2004) suggests that brand heritage can virtually open the door to existing distribution channels with lower effort if compared to totally new brands.

An analysis of brand equity shows that under certain circumstances, retro or nostalgic brands can have better chances to be successful. The key success factors are: keeping the promises, image and values of the past (the values that the brand stands for should not differ from those in the past) together with meeting the new technological standards and the needs of modern consumers. Marketers today are rather skeptical about the sustainability of retro or nostalgic branding. Lamb (2009) warns that most revivals are just short-lived. Ridgley (2009) stated that nostalgia arrived in waves every three to five years and that marketers today therefore should concentrate on identifying the size of the potential market for nostalgic brands and make sure that the personality of their brand corresponds with con-

sumer´s needs and expectations. Lamb (2009) concludes that brand managers should not look at nostalgia as a trend, but as part of their holistic brand history.

5.3 Branding in Central Europe

In order to fully understand the current trend of reviving old brands in Central Europe, one needs to look back and discuss the role of brands in communist times as well as the changes in consumer behavior and in the perception of national (local) brands since the early 1990s.

In communist times, brands and factories producing branded products were publically owned (by the state, communities, etc.). This fact determined the role of brands in those societies. Brands were not considered intellectual property (as we consider them today), but rather played a role of identification for a certain product. Therefore, it often happened that more independent factories produced the same or just a slightly different product under the same brand name. Given there was often just one single brand offered in certain categories, this limited offer in retail stores impacted the role of brands. On one hand, brands did not help differentiate a product from its competitors, as there were no competitors at all; and on the other hand, some brands gained almost a monopolistic position within a certain category and were used as a common name for a whole category of products (for example the word 'Jar' – a brand name of Czech washing detergent today produced by Procter and Gamble – is still used today in the country as a general name for the whole product category; Procter and Gamble today, of course, takes advantage of this fact). Therefore, companies were not forced to invest into brands, because customers had just very limited choice.

This situation dramatically changed after the fall of the Iron Curtain. Western European and American producers entered the newly opened markets with their brands, and customers, who were bored by the very limited choice, took advantage of the incredible variety of products and brands. In this new situation, local brands had very limited chances to successfully compete with the established and financially strong Western brands, which consumers generally perceived as higher quality. Many Western brands were already known in Central European countries and – thanks to intensive advertising campaigns that local competitors were not financially able to compete with – soon gained leading positions in certain categories. Consumers generally perceived local brands as old-fashioned, connected with the past and with inferior quality. Moreover, local producers did not have sufficient financial resources or educated marketers with some experience with how to build a brand or how to communicate in an open and free market.

Many local brands therefore soon disappeared from the market. On the other hand, some local brands were overtaken in the process of privatization by international players and thanks to their financial investments and transferred marketing experience kept or soon regained their positions in the market (such as Škoda Auto as a member of the Volkswagen group). Many Western European and American producers decided that it would be easier to keep and develop the already known brands than to invest in building new brands in those markets. Some internationals later changed their strategy as local markets developed

more towards Western Europe and re-branded their products under their global brands, while some of them decided to still keep local brands in their portfolio.

At the end of the 1990s, Central European markets were already dominated by global brands that competed with local brands owned by international companies and just a few really local brands. Up to today, local brands are developed by international companies mostly just as regional or national brands for Central European countries and their position is generally weaker than that of their global and international competitors. The Interbrand listing (Interbrand 2010) shows the weak position of Central European brands in the global environment. Among the TOP 100 most valuable brands worldwide, there is no brand that originates from Central or Eastern Europe.

Table 5.1 10 most valuable Czech brands according to marketing experts

Rank	Brand	Industry	Established	Owner
1.	Škoda Auto	Car production	1925	Volkswagen Group
2.	Pilsner Urquell	Brewery	1898	SAB Miller
3.	Budweiser Budvar	Brewery	1895	State owned
4.	Baťa	Shoemaker	1894	Bata Shoes
5.	Kofola	Drinks	1962	Kofola Holding
6.	Jan Becher	Liquor	End of 19th cent.	Pernod Ricard
7.	Mattoni	Mineral Water	1867	Ronaldsay
8.	Česká pojišťovna	Insurance	1827	Generali PPF
9.	Staropramen	Brewery	1870	InBev
10.	Česká spořitelna	Bank	1825	Erste Bank

Source: IHned (2007)

Branding, as a new management and marketing category in these markets, is still relatively underdeveloped and even today it is hard to find a standardized evaluation of brands in any of the Central and Eastern European markets. The brand listings in those countries are usually based on evaluation and opinions of experts and not on real statistical and financial reports. This is also the case of the following listing that shows the most valuable Czech brands according to the opinions of respected marketing experts. The experts provided the publisher with their opinions about valuable brands, but simultaneously rejected estimation of their financial value. The listing shows clearly important facts about the Central and Eastern European brands. The most valuable brands are those with a very long tradition (most of the listed brands have a tradition longer than a century) and most of them are owned by international companies. From the TOP 10 most valuable Czech brands, only

Kofola is owned by a Czech company and Budweiser Budvar is owned by the Czech state. All other brands are owned by international companies and are not widely marketed outside the home market (with the exception of Škoda, Baťa and Pilsner Urquell) and therefore have just a limited chance to become global.

5.4 Changes of Consumers' Attitudes towards Local Brands

At the end of the 1990s, the attitudes of consumers in Central Europe towards local and international brands started to change slightly. Consumers who preferred imported products and foreign brands for almost a decade started returning to local brands. There were several reasons for this change of consumer behavior.

First of all, many consumers became disappointed by the imported products and found that their quality was generally not as superior as they had expected. Many people realized that the imported products and foreign brands had just pushed the old brands out of the market and that in the end, the choice in supermarkets remained almost as uniform as it had been a decade ago. Foreign brands just replaced the local ones on the shelves, but did not bring the expected added value. Some customers, mainly the younger generation, also tried to search for a way they could become more original and differentiate themselves from the majority of customers who purchased international brands.

Secondly, consumer attitudes towards their own countries changed. After the first economic problems and downturns appeared in Central Europe at the end of the 1990s, some consumers felt obliged to somehow support their home economy and searched for local brands again in order to help protect local jobs and support local entrepreneurs. In some countries, this shift towards national brands was also supported by politicians who promoted the consumption of domestic products as a part of every citizen's responsibility for the future of their country.

Thirdly, but not lastly, the situation changed in the traditional companies that formerly produced local brands. After years of cost-cutting and staff reduction, these companies started to seek a way to succeed in a market dominated by big multinationals; one of the options that they had was to revive the old brands but with a renewed positioning and updated marketing strategy. Also the financial situation of some of these companies changed positively and enabled them to hire new marketing professionals and to invest into branding activities and marketing communication.

These changes led to a new trend of reviving old local brands in countries across Central Europe that will be discussed in detail in the following text. This trend started in the late 1990s but the real 'nostalgia boom' spread over Central Europe after the beginning of the new millennium. Although today most market categories are dominated by big international companies and their brands, local brands must now be considered as serious competitors in many categories.

East Germany

Nowhere else in Central Europe did local, traditional brands face such abrupt changes in consumer behavior as in former East Germany. The established East German brands lost their market almost overnight after the fall of the Berlin Wall and many of them simply disappeared from the market. After the fall of the Wall, East Germans turned to Western brands for the same reasons as other Central Europeans. Eastern brands were perceived as low quality and old fashioned, while Western brands enjoyed the perception of being high quality, modern and must-have products.

While the attitudes towards Western and Eastern products in East Germany were similar to those in other countries of the region, the changes in buying behavior were much more abrupt. No language barrier existed between the former Eastern and Western Germany, and therefore Western brand names sounded familiar to the majority of consumers in the East. Another important factor that played a role was the fact the consumers in East Germany (or at least in some parts of the country) were able to receive the broadcasting of West German TV stations and therefore knew the Western brands from their commercials. Modern and colorful commercials contributed to the perception of Western brands as modern and trendy, and after the fall of the Wall, consumers simply wanted to try them.

The last barriers for Eastern consumers to purchase Western products fell in 1990 as the German Mark (DM) became the official currency also in East Germany when the two countries reunited. Thanks to these events, consumers from the former GDR (German Democratic Republic) could buy Western products with their own salaries and savings without the need to exchange currency. Consumers in the former GDR also perceived the purchase of Western brands as a contribution to the reunification of the country. While in other countries in the region the traditional producers were (at least at the beginning of the 90s) protected by the local inconvertible currencies and their unfavorable exchange rates, former GDR brands could not benefit from such advantages and thus lost their market very quickly.

The trend towards consumption of the West German brands was also supported by the retailers who did not want to distribute Eastern brands at all. Local retailers just followed the trends in consumer behavior and wanted to offer the Western brands that were demanded by consumers, while the big retailers from the West, after overtaking parts of the existing distribution, simply used their business models from the Western part of the country which did not include any Eastern brands.

Nevertheless, still some old brands survived those dramatic changes, and today, they can be found on the shelves; they also benefit from the current retro trend even though their number is rather small. The study 'Und sie leben doch!' (And they are still alive!) found altogether just 127 former GDR brands that survived the dramatic changes of the market environment and that can be found in the stores across Germany today (Absatzwirtschaft 11/2009). Through interviews with the brand owners, the study identified the following main factors that contributed to the survival of those brands: trust/brand awareness from

the times before the fall of the Wall, quality, innovation, local origin, performance, flexibility, and continuity.

The study supported the idea that the nostalgia trend contributed significantly to the success of the former GDR brands as consumers´ trust and the fact that the consumers knew the brand from the times before the fall of the wall was mentioned as one of the main success factors by 80 percent of brand owners (Absatzwirschaft 11/2009). On the other hand, nostalgia alone cannot help to succeed in the long-run. Therefore, it was no surprise that the quality of the products scored as the second most important success factor with 54.3 percent and innovation in the third place with 30.9 percent (Absatzwirtschaft 11/2009). On the other hand, continuity as a success factor was mentioned just by 17.3 percent (Absatzwirtschaft 11/2009) of the brand owners, which again supports the idea that just a few brands can be successful in the long-run due only to the nostalgia trend, i.e. without significant modernization and innovation.

Flexibility, as one of the success factors, stands for the ability to react quickly to the changing requirements of the retailers. For many of the former GDR brands, flexibility also means the personal passion of the owners, managers and employees for the brand who were able to support their brands in difficult times after the changes and believed in their future success.

The example of the sparkling wine producer Rotkäppchen (with more than a century of company history) clearly demonstrates the importance of flexibility for the success of a brand. After the fall of the wall, the brand lost its distribution channels in East Germany almost overnight, as the retailers did not wish to distribute its products anymore. In reaction to this, company employees drove all over the country in their cars and sold the wine on the streets directly to the customers. This flexible reaction to market changes was crucial for the future comeback of the brand. Consumers did not forget the brand or its products and the brand was able to survive the first half of the 90s without almost any presence in the 'official' distribution channels (Rotkäppchen 2009). Today, Rotkäppchen holds the position of the most consumed former GDR brand with 48.3 percent of consumers in the former GDR who consumed the brand within the last three months (Absatzwirtschaft 11/2009). The trend towards the old 'good' brands improved the financial results of the company so much that it was even able to take over its West German rival Mumm a few years ago (BBC 2009).

The nostalgia trend in East Germany was mainly driven by older consumers who remembered the brands from the times before the fall of the wall and who returned to their brands after the period when they experimented with the Western brands. But recent research findings have showed that also the younger generation of East German consumers who were not even born at the time when the wall fell down purchase those products. The young generation purchases those products because of familiarity (they know the brands from the stories of their parents and grandparents) and also because of the ongoing retro trend (Absatzwirtschaft 11/2009 and BBC 2009).

While the young generation of East German consumers seems to be convinced about the qualities of the former GDR brands and thus provides positive promises for the future of those brands, the problem to develop into 'all German' brands still remains. Even the most successful East German brand, Rotkäppchen, is consumed by only 9.5 percent of consumers in the West while in the East this number reaches almost 50 percent (see above, Absatzwirtschaft 11/2009). The differences with other successful East German brands remain even bigger. The washing powder Spee is regularly used by 31.6 percent of the households in the former GDR, but by only 7.8 percent of those in the West. The popular East German Vita-Cola is purchased by 14.1 percent of the consumers in the East, but by only 1.1 percent of the West Germans (Absatzwirtschaft 11/2009).

One of the main reasons why former GDR brands are much more successful in the East than in the West – besides consumer preferences and brand awareness – might be found in the marketing communication strategies of those brands. While the successful Western brands use mainly mass media for their marketing communication, former GDR brands prefer more personal communication tools, such as personal contact and point of purchase promotions, which are generally limited to a certain geographical area.

To conclude this subchapter, we can say that the main challenge for the East German brands for the near future is to enlarge their market towards the Western part of the country and to become nationwide players. This is definitely not going to be an easy task considering that even Florena, the hand cream today produced by international giant Beiersdorf (producer of Nivea) and one of the former GDR brands that according to experts has the best chances to become a nationwide brand, is still purchased just by 5.8 percent of West Germans while in the East this number easily reaches 25 percent (Absatzwirtschaft 11/2009).

Czech Republic

Although the changes in the Czech Republic after the Velvet Revolution (November 1989) were less abrupt than those in East Germany, the traditional Czech brands did not have easy times in the early 1990s. Czech consumers preferred Western brands and did not want to purchase the local brands anymore. Still the local brands were at least protected by the unfavorable exchange rate of the Czech currency, which made imported products far more expensive than local ones.

On the other hand, many traditional brands were acquired in the process of privatization by foreign investors who either invested financial resources and marketing experience into modernization of the brand values and re-launched the old brands successfully on the market with new more modern positioning or simply eliminated the old brands and replaced them with their international brands keeping the advantages of local production for lower costs. Some internationals even created specific brands for the Czech market or re-invented very old regional brands that were almost forgotten even in 1990, and turned them into national brands with a sophisticated marketing strategy. This was the case mainly in the categories in which consumers seemed to be more conservative preferring national

brands (such as food and beverage production). Those new or re-introduced Czech brands received professional marketing and financial support from their international mother companies and were therefore able to manage to become key players or even market leaders in a relatively short period of time.

For example, Tchibo – the German coffee producer – re-introduced the almost forgotten regional coffee brand Jihlavanka and turned it into nationwide brand with Czech positioning and traditional values. The traditional positioning that stressed the long history of the brand and traditional values helped the brand to become market leader in the country; this would not have been possible for Tchibo´s international brand.

At the same time, traditional brands that were not acquired by international players had difficult times. They did not have sufficient financial resources to invest into their brands, and they also lacked marketing knowledge and experience. Therefore, it was extremely hard for them to compete with strong international brands or national brands supported by international players and most of them either disappeared from the market or survived only thanks to cost cuttings and deployment.

Their main competitive advantage at the time was their lower price and partly the brand awareness originating from the past. But with the appreciation of the Czech currency and the increase of production costs, many of them realized that this would not be a viable long-term strategy. Therefore, the producers were forced to re-think completely their strategy and to strive to find new competitive advantages that would enable them to differentiate themselves from the international brands and to create specific value for their customers. The following example of Czech watch manufacturer Prim clearly demonstrates the changes that the traditional Czech producers were forced to implement when they wanted to survive in the changed market environment. The retro or nostalgia trend also significantly contributed to the success of the company.

The production of clocks and watches in Eastern Bohemia (Czech Republic) has a long tradition, which dates back to the 19th century. The production of wristwatches under the brand Prim started in the former Czechoslovakia in 1949 when the recently established national company Chronotechna took over the nationalized local producers of watches and clocks. In 1969, the company's name was changed to Elton, but the brand Prim for watches remained unchanged. In addition to wristwatches, the company also produces alarm clocks and household clocks under the Prim brand.

In the centrally planned economy, the position of the company and its brand was almost ideal. With no local competitors and just very limited imports from other countries of the Eastern bloc, the brand was virtually the only option for Czechoslovak consumers. Thanks to its monopolistic position, the brand was not forced to innovate and was usually the first wristwatch that consumers possessed. The production increased steadily and reached almost half million watches annually just before the Velvet Revolution (Idnes 2009).

After the Velvet Revolution, the market situation changed dramatically. Consumers did not want to purchase the Prim watches anymore; furthermore, the distribution channels re-

fused to distribute them. The market split into two segments leaving no free space for Prim. The upper segment was taken over by traditional Swiss producers who enjoyed the perception of highest quality products with long tradition, while the lower segment was occupied by no-name cheap products originating from Asia. Surprisingly, even the Asian watches were found as more modern and of higher quality by the majority of the consumers than those produced by Prim. In response to these market trends and changed consumer behavior, Prim introduced a new product line of classical manual watches but this attempt was not successful at all and production was ceased after a few years.

In 2000, the company changed its production, marketing and distribution strategy completely. Instead of competing with mainstream products in the overcrowded market, the company shifted its production and consequently its pricing, distribution and communication strategy towards the upper segments of the market. The new strategy is based on its long tradition and on the fact that almost all components of the watch are produced by a European producer, which is rather an exception today. Most competitors today just assemble the watch from components imported from Asia. The awareness of the Prim brand played a crucial role in the new strategy, as even today the brand is the best known watch brand in the Czech market (Prim 2009), as for the majority of customers, the Prim watch was the first one they ever had. Also the changed perception of imported and domestic products contributed to the revival of the brand. Many consumers were bored by the imported mass products and searched for some original products that would correspond with their personality.

The cornerstone of the new strategy is the individual approach to each customer. Prim introduced new collections of watches that were prepared in cooperation with carefully selected designers with the respect to the tradition of the brand. All watches can be adjusted to the wishes of the individual customer and therefore represent the customer´s personality. Customers can choose the material that the watch will be made of (such as stainless steel, gold, silver or platinum), the type of the watch, the color and material of the watch strap and can even have his or her monogram on the watch. All products are tailor-made and therefore the company does production after the customer places a firm order and pays the deposit.

The shift towards a tailor-made production subsequently changed the overall marketing strategy. Products are no longer distributed through conventional distribution channels, but customers contact the company directly in order to be able to specify their wishes regarding the quality and personality of their watch. Also the pricing strategy underlines the new positioning of high quality hand made products. The prices range from almost 600 EUR for a watch from the standard collection to almost 40,000 EUR for the highest model offered, a watch made completely from platinum.

In communication, the brand does not use mass media, but communicates rather on a personal basis. The main communication tool is the website of the brand where customers can find all information about the offered products, can adjust the products to their wishes and place an order. For communication with the broader public, the brand uses mainly PR activities such as articles in newspapers and information about celebrities who wear the Prim

watch. The celebrities are then used as peers influencing the rest of the public. The brand, for example, gave an individualized platinum watch from the limited collection (just 50 pieces were produced) to Czech President Vaclav Klaus. President Klaus, as a traditional supporter of old Czech brands, seems to be the right person to communicate and spread the message of the brand. Almost all media covered the small ceremony during which the president received this present, covering all details about the product and its qualities and celebrated the revival of the almost forgotten brand. The brand cooperates also with the government office and thus the Prim watch is given as a present to important state visitors. So, for example, French President Sarkozy and American President Obama were presented with Prim watches. The brand naturally uses those prominent customers in its communication, mainly through PR.

Prim is one of the few old brands that was able to totally change its strategy and made the successful shift from the price-oriented mass market towards the upper market segment where price is not considered of such importance for the customers and where it could fully use its competitive advantages, namely skilled workers and its long tradition. Today 70 percent of the brand´s turnover comes from individual tailor-made watches, 25 percent from the standard collection and just five percent from the production of simple quartz watches (Prim 2009). From this perspective, Prim could be considered as a brand that fully used the nostalgia trend in Central Europe, but added innovation and sophisticated marketing strategy in order to keep its competitiveness for the times when this boom is over.

5.5 Kofola as an Example of a Revived Brand

This chapter opened with the brand Kofola and after having summed up the relevant theoretical findings and practical information about the Central European markets and their recent changes, it now returns to this brand to discuss its success story in more detail. Kofola´s story can no doubt be used as a benchmark of a successful Central European company that used the nostalgia trend to start again, but that developed its strategy continuously in order to become a real market leader.

Kofola´s brand history dates back to 1962 when Kofo-Syrup was introduced for the first time into former Czechoslovakia as a response to global players Coca-Cola and Pepsi. The drink that was produced by mixing the Kofo-Syrup with carbonated water soon gained popularity in Czechoslovakia and was produced under the name Kofola by dozens of producers across the country. After the Velvet Revolution in 1989, the Kofola brand almost disappeared from the market, as its position was taken over by Coca-Cola and Pepsi, which were preferred by both consumers and retailers.

The comeback of Kofola to the Czech market started in 2000, when the company Santa nápoje (founded in 1993 as SP Vrachos) acquired the license for the drink under the brand Kofola from its owner company IVAX. From this moment, the development of the company has been interconnected with this brand. In 2002, Santa nápoje purchased the brand Kofola for 215 million CZK (app. 8.4 million EUR) and started with heavy investments into the brand. In this year, Santa nápoje changed its company name to Kofola and re-launched

the product in the Czech and Slovak markets. Kofola introduced its first TV advertising campaign with the catchy slogan "If you love her, nothing else matters." This TV campaign played an important role in the comeback of the brand. Firstly, it reminded the older generation of consumers that the brand they knew from the past was back; however, it also introduced the brand to the younger generation as a fashionable and friendly one. The advertising campaign was a huge success in terms of brand awareness and re-introduction of the brand. TV as media for the campaign was also a good choice. Kofola showed clearly with this campaign that it was back not as a poor old brand, but as an ambitious market player that could afford to invest into prestigious TV advertising. TV was and is traditionally the most influential and prestigious media in the Czech Republic. This fact was crucial mainly for the young generation of consumers who understood that Kofola could really be considered as an alternative to global brands.

In the following years, Kofola continued its expansion in the Czech and Slovak markets. The company acquired other almost forgotten brands, such as TopTopic in 2001 and Vinea in 2008 and reintroduced them to the Czech and Slovak markets. In 2003, Kofola started its international expansion by establishing a subsidiary in Poland, followed in 2004 by a subsidiary in Hungary. Since that year the brand has been operating within all Central European countries. In 2005, a new production plant was opened in Poland which represented the biggest Czech direct investment in the Polish market. Through a merger with Polish company Hoop and entry into the Warsaw stock exchange, Kofola became one of the main players in the Central European market with production capacities in four countries (Czech Republic, Slovakia, Poland and Russia) and distribution in five countries (Czech Republic, Slovakia, Poland, Hungary and Russia). Although the company does not report sales numbers, estimations show that Kofola holds important positions in Central European markets being number three in the Czech market after Karlovarske mineralni vody (Czech producer of mineral and bottled water) and Coca-Cola (Vizjak 2009), number one or two together with Coca-Cola in Slovakia (Vizjak 2009) and number three in the Polish market (Kofola 2009).

Today, Kofola is the most popular Czech brand on Facebook having 167 thousand fans (Aktualne 2010), and it is the fifth most valuable Czech brand (see subchapter 2). In 2007, Kofola scored for the first time in the Czech TOP 100 listings of the most admired companies in the country (in eighth place); in 2008, it scored third and in following year, fourth (Kofola 2009). This listing proved that Kofola succeeded not only with its customers, but also with the broader public and future employees who perceived the company as stable and developing. In 2007, Kofola scored also internationally gaining the 174th place in the prestigious Europe's 500 listing – published by the Economist – of companies that contributed to the development of European economy (Europe's 500 2007). The annual turnover of the company reached 350 million EUR in 2008 (Kofola 2009).

The success of the brand and of the company itself was based on various factors: The successful revival benefited from the nostalgia trend in Central Europe at the beginning of the new millennium. The brand Kofola was not unknown and could therefore soon gain back its lost position in the market in the Czech Republic and Slovakia. The existing brand

awareness opened the gates of the minds of older consumers who remembered the brand from the past, while the TV advertising campaign introduced the product to the younger generation. Logically, Kofola concentrated in the first years on the two former home markets Czech Republic and Slovakia and entered new markets such as Poland and Hungary only after it had gained a certain position in those home markets.

In the product and branding strategy, Kofola follows its vision to be present in every Central European market with at least two brands that will be either market leader or number two within their market segment. Kofola therefore respects the local specifics of each market and carefully selects the products and brands that are introduced into those markets. The company strives to be present with its products in every relevant category which means that it needs to have a relatively large portfolio of products ranging from bottled waters to juices to cola-based beverages. In the categories where there was a successful predecessor in the past, the company acquired the brand and re-launched it in a way similar to Kofola's re-launch such as with Vinea and TopTopic, while in the categories where there was no such predecessor, the company created a new brand and used the power of its flagship brand Kofola to push the new brand through the existing distribution channels such as with the bottled water brand Rajec.

Kofola respects the local specifics of its markets and that is why the drink Kofola was introduced first in the Czech Republic and Slovakia and later on also in Hungary, while in Poland the company still uses the local brand Hoop Kola which was acquired through the merger with Hoop (E15 2009).

The communication strategy is different in every market. Kofola wants to keep the local positioning for all of its products, and therefore advertising campaigns are prepared separately for each market creating another competitive advantage of the brand against its global competitors. While Coca-Cola uses global Christmas campaigns with Santa Claus also in Central Europe where actually Christmas presents are not brought by Santa, Kofola connects its brands with local Christmas traditions and rituals.

Pricing and distribution strategies underline the overall marketing strategy and respect the strategic goal to become one of the market leaders in the whole region. Kofola strives to build intensive distribution covering virtually all market segments in every country it is present. The distribution today covers the main retail stores in every country and the current investments aim to gain the same position also in restaurants and other on-trade distribution channels. Regarding pricing, Kofola´s goal is to offer top quality products for affordable prices. Therefore, the prices of the products are a little lower than those of Coke and Pepsi, but significantly higher than those of non-branded products and private labels.

Permanent innovation is another important part of the company´s strategy. Kofola is steadily widening its portfolio by adding newly created or acquired brands covering uncovered categories and innovating its products in order to follow market trends and consumer wishes. The new sugar-free Kofola was introduced to satisfy the trend towards a healthier life style, Kofola with lemon flavor to satisfy mainly the younger generation of innovative

consumers, and a special Christmas edition of Kofola (Barborkova) aimed at offering something special for the Christmas table.

Although Kofola can be considered an example of a successful Central European company, there still remain challenges that the company must be ready to face in the near future: After years of high growth rates (2004-2008) when the sales of the company grew on average by 24 percent annually and profits by 20 percent (Vizjak 2009), the company will surely face slower growth rates in the immediate future. Also, the consolidation of international activities and wide brand and product portfolio could be considered as a challenge for the upcoming years. But internationalization of the brand, which started few years ago, will remain the main challenge for marketing managers. Kofola is already very successful in the Czech Republic and Slovakia and relatively successful in Poland. Yet Hungary does not contribute much to the overall success of the company so far.

Student Assignments

Retro and Nostalgia Branding

1. Given the information from the case study, would you consider retro or nostalgia branding as a company's sustainable marketing strategy?
2. What are, in your opinion, the market conditions that enable successful nostalgia branding?
3. What are, in your opinion, the key elements of successful nostalgia branding strategy?
4. Identify the main pros and cons of nostalgia branding. Take one brand that you know that followed the nostalgia branding strategy and discuss the benefits and disadvantages of this strategy.

Internationalization of Central European Brands

1. Given the information from the case study, try to estimate the chances of brands originating from Central Europe to successfully enter foreign markets. Discuss the key factors of a successful market entry strategy.
2. Select an example of a Central European company which already successfully entered foreign markets (e.g. car maker Škoda, brewery Pilsner Urquell, ski producer Elan) and identify the key success factors.
3. Which target markets, in your opinion, should Central European companies concentrate their efforts on? Please suggest a marketing strategy and support your opinions.

Additional Readings

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On nostalgia branding:	Brown, S., Kozinets, R.V., Sherry, J.F.Jr. (2003): Teaching Old Brands New Tricks: Retro Branding and the Revival of Brand Meaning
On Central European brands:	Kofola-Company´s website: www.kofola.cz

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6 Diversity in European Retailing

Thomas Rudolph and Jan Niklas Meise, Institute of Retail Management at the University of St.Gallen, Switzerland

> **Aldi sets eyes on Romanian market**
>
> German-based company Aldi, the world's tenth-largest retailer, which boasts a global turnover in excess of 39 billion euros, has entered the Romanian market by setting up a firm that is entirely controlled by an Austrian subsidiary of the group, Hofer. Market sources maintain that the German retailer is looking at the Romanian market for future expansion; however, the entrance project remains in the early stages of development. The new Bucharest-based Aldi Stores company headquarters, in which Hofer (Austria) holds 100 percent of the share capital, was legally registered approximately one month ago. As a result of the recent move, the Aldi company joins its main international rival on the Romanian market, Germany's retailer Lidl, which plans to carry out investments worth approximately 150 million euros in a network of more than 100 stores by 2011, according to market sources.
>
> ***Press Clipping in Ziarul Financiar on 08.08.2007***
>
> ***(As of 2011 Aldi has not yet opened any stores in Romania)***

The Romanian market entry marks yet another step in the internationalization of the German discount icon Aldi, who started venturing outside its home market in 1967 and to date generates almost half of its revenue abroad, with Europe accounting for the majority of this percentage (Planet Retail 2008). This is particularly remarkable as the European retail market and especially food retailing are very diverse and face retailers with countless challenges in their striving for European cross-border expansions (de Mooij and Hofstede 2002). Consumer preferences vary considerably across Europe and it is even hard for local stores to keep up with ever-changing and highly fragmented consumer tastes and needs.

In this chapter we will elaborate on the diversity of the European retail market and introduce you to the basic concepts of retail strategy, differentiation and internationalization of retailing. You will learn that retailing across Europe is subject to vast diversity in consumer behavior and that especially food retailers are challenged to respond to this diversity in retail management decisions. What works in one country, may fail in another. Retailing strategies cannot be extended to other countries without adaptation. Therefore, we devote special attention to the central issue of standardization and adaptation in the internationalization of retail operations. To illustrate these concepts, we will describe the business model and European internationalization of Aldi, a hard-discounter who bases its strength on strict standardization, but yet had to learn to adapt to diversity for international success.

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6.1 European Retail Diversity

The world over, shopping is a local experience and habit. Increasingly, scholars find that tastes and preferences diverge largely across different cultures, countries and regions and predict consumer behavior to become even more heterogeneous given cultural differences (de Mooij and Hofstede 2002). Europe enjoys the highest cultural density and diversity on the globe. This diversity translates into a myriad of distinct consumer segments, impeding foreign players catering to the customer base of another country. Consumers shape retail markets, as their consumption patterns determine the product offering and shopping environment. Retailing is hence a very local business and requires a deep understanding of local tastes and preferences. Diversity in consumer behavior has led to diversity in retailing across Europe. Only a handful of food retailers have been successful across multiple countries, while many ventures failed or fell short of expectations.

Diversity across European Consumers

Consumers differ not only in the usual ways (by age and gender, education and occupation, marital status, and living arrangements) but also in their activities and interests, their preferences and opinions, the foods they eat, and the products they buy (Schiffman et al. 2008). Effectiveness in marketing and retailing means adapting to cultural values. This is especially the case in Europe. While international marketers would like one to believe that in the 'new Europe' with a single currency, consumers will become more similar, increasingly eat the same food, wear jeans and sneakers, and watch the same television programs, reality is likely to be different. There are large differences among the value systems of consumers in different European countries, value systems that are strongly rooted in history and that appear to be very resistant to change (de Mooij and Hofstede 2002). Despite globalization and the numerous theories of conversion of markets and consumer needs, there is evidence that consumer behavior is actually diverging in Europe as reflected in the consumption, ownership, and usage of many products and services.

De Mooij and Hofstede (2002) explain that the wealthier countries become, the more manifest is the influence of culture on consumption. When income levels are such that consumers have satisfied their basic needs and wants, they will spend their discretionary income on what best fits their value systems. The stereotypic ideal of Americans is a five-car garage, the Dutch will buy more luxurious holiday trailers, and the Spanish will eat out even more than they do now. In the new century with increased wealth, predicting and explaining consumer behavior differences across countries is indispensable for international retailers. When countries converge with respect to national wealth, cultural variables start to explain more of the differences in country-level consumer behavior. This has certain implications for marketers and retailers. Expanding operations to countries with different cultural values than one's own without adapting to these differences can lead to serious losses. This applies to the retail format used as well as to sourcing for different cultures. In collectivist cultures in Europe, for instance, people allocate a higher percentage of consumption expenditures to food than do people in individualist cultures, perhaps because food has an

important social function in collectivist cultures. In supermarkets, the variation and display of food needs more attention in collectivist cultures than in individualist cultures, where people are more focused on convenience and fast food. The European diversity in consumer behavior has thus a strong impact on the European retailing landscape.

Diversity in European Retailing

The impact of diversity in European consumer behavior on the European retailing landscape is illustrated by the data compiled in **Exhibit 6.1**. We computed the combined market share of the ten biggest retailers in each country and the share of domestic versus foreign influence thereof. Our classification of domestic and foreign retailers followed the rule that regardless of local subsidiaries, foreign retailers' operations originate in a different country. Though Lidl may, for instance, set up a local Swedish business, it is still considered a foreign retailer in Sweden.

One thing becomes immediately obvious analyzing the left part of **Exhibit 6.1**: High market density and dominant national players apparently come together. In Scandinavia and Western Europe, market concentration is highest and domestic players dominate. This is best illustrated looking at the German market, notorious for its competitiveness and accordingly low retail margins. Indeed, the top ten retailers in Germany are completely made up of domestic players. In Sweden, Finland, Switzerland and France the case is very similar.

Conversely, Eastern Europe is lacking this high influence of domestic retailers. The retail scene in the Czech Republic almost exactly mirrors that of Germany with only foreign-based retailers among the country's top ten. Given that retailing was only introduced and developed in Eastern Europe after the fall of the Iron Curtain, there simply has not been sufficient time for domestic retailers to emerge and reach the same degree of professionalism as their European counterparts. In addition, local consumer preferences were limited given the restricted choice and access to consumption under the Communist reign. Consumers strive for Western products and thus adapted quickly to the European retail formats entering the Eastern European markets.

Not all retail sectors are impacted by the diversity in consumer behavior in the same way. While diversity appears to be less eminent in non-food retailing like fashion, the sector with the highest diversity is indisputably food retailing. This is due to the high fragmentation of consumer preferences and tastes even within national borders, such as local tastes in Bavaria and Northern Germany. In their research covering the world's top 250 retailers, Deloitte Consulting (2009) found that while the fashion retailers of this sample were, on average, operating in ten countries, the world's biggest retailers of fast moving consumer goods (food retailing) had a presence in merely five countries, making it the least geographically dispersed sector. The right columns of **Exhibit 6.1** therefore take a special look at food retailing in Europe. Again we calculated the share of each country's top ten players as well as the domestic and foreign influence. As expected, market concentration is much higher in food retailing with the top ten players making up as much as 90 percent of the market in Scandinavian countries. Apart from a few exceptions in Eastern Europe, the top ten retail-

ers generally constitute over half of the grocery market. Concerning the domestic and foreign influence, a similar picture to the general retailing scene is obtained with national dominance in most Western European and foreign dominance in Eastern European markets.

Exhibit 6.1 Market Concentration and Internationalization in European Retailing

Country	Top 10 Retailers' Share (%)	thereof national (%)	thereof foreign (%)	Top 10 Grocery Retailers' Share (%)	thereof national (%)	thereof foreign (%)
Austria	36.4	16.4	20.0	75.5	27.6	47.9
Belgium	29.7	16.2	13.5	56.6	32.4	24.2
Bulgaria	15.3	12.0	3.3	24.6	13.9	10.7
Czech Republic	35.7	0	35.7	74.5	0	74.5
Denmark	52.2	46.9	5.3	82.7	69.6	13.1
Finland	56.6	54.8	1.8	97.2	92.2	4.9
France	40.0	37.0	3.0	73.3	66.7	6.6
Germany	36.3	36.3	0	75.2	75.2	0
Greece	15.3	6.0	9.3	29.1	9.9	19.2
Hungary	41.5	8.0	33.5	74.3	14.5	59.8
Ireland	48.7	31.9	16.8	83.7	51.3	32.4
Italy	22.1	18.6	3.5	52.0	43.6	8.4
Netherlands	32.5	26.3	6.2	66.6	54.4	12.2
Norway	49.6	38.9	10.7	92.8	76.3	16.5
Poland	26.3	4.4	21.9	41.9	5.5	36.4
Portugal	35.0	16.5	18.5	58.7	28.4	30.3
Romania	23.3	2.7	20.6	37.1	5.1	32.0
Slovakia	32.0	10.0	22.0	59.1	18.9	40.2
Spain	28.1	23.0	5.1	48.3	38.1	10.2
Sweden	47.8	46.7	1.1	83.3	76.5	6.8
Switzerland	45.9	42.2	3.7	68.2	63.1	5.1
United Kingdom	42.0	35.1	6.9	76.3	58.5	17.8

Source: compiled by authors from Datamonitor 2010/09 Retail Country Reports (2010)

Internationalization of Retailing in Europe

The internationalization of retailing has two main elements: sourcing and selling. International retail sourcing has a long tradition and is by no means a new phenomenon. Howard (2004) notes that even if their stores are entirely domestic, many retailers have been buying goods from foreign countries for a long period. For the better part of two decades, the push toward internationalization of retail store operations has been deemed imminent. While many retailers have ventured abroad, many have not. Moreover, many have found the terrain far more challenging and not quite as lucrative as originally anticipated.

Exhibit 6.2 compares the relative importance of international activities conducted by the ten largest European grocery retailers. In fact, turnover outside the domestic market exceeds 50 percent of total turnover in only four cases. Yet, the reasons to venture abroad have not disappeared, but have rather been reinforced by recent events: In developed countries, retail spending growth is weak and, due to a combination of demographics and shifting economic structure, this is likely to remain so. Apart from gaining market share at home, Europe's leading retailers will only find strong growth by moving into new markets, especially into fast-growing emerging and less developed retail markets.

Exhibit 6.2 Share of Domestic and Foreign Sales of Top 10 European Food Retailers

	Retailer	Sales in 2007 (USD mn)	Domestic Sales in 2007 (%)	Foreign Sales in 2007 (%)
1	Carrefour	140.966	45	55
2	TESCO	103.400	73	27
3	METRO Group	75.538	42	58
4	Kaufland LIDL	71.406	48	52
5	ALDI	65.460	51	49
6	Ahold	63.736	25	75
7	Auchan	63.071	52	48
8	REWE	56.251	68	32
9	Groupe Casino	55.952	62	38
10	EDEKA	51.267	95	5

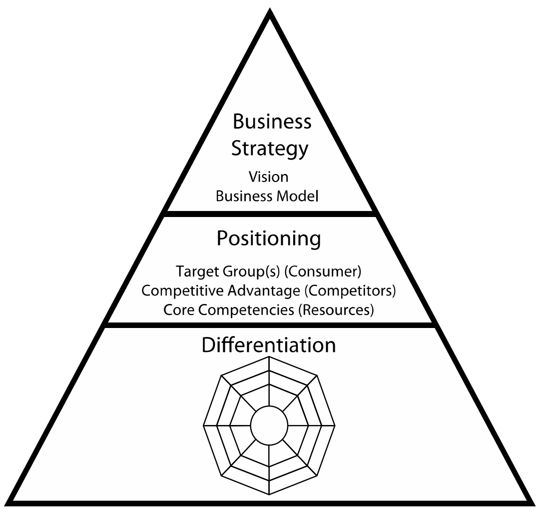
Source: Planet Retail (2008)

It should not come as a surprise that European diversity is also reflected in consumer preferences across countries and therefore retail markets. As this introductory section has shown, market concentration in the retail sector is rather high in most European countries with only a few retailers making up a substantial part of the market. Oftentimes, established national players control a major share of the market, which adds to the difficulties for foreign retailers to venture abroad. While this is mostly the case in the Scandinavian and Western European countries, Eastern European countries have offered rather attractive opportunities for European retailers to expand, as these markets were lacking strong national players.

6.2 Introduction to Retail Strategy

In order to cope with the outlined challenges concerning consumer tastes and preferences as well as dense competition and market saturation, retailers are in need of a clear business strategy. One just cannot copy-paste one store design or merchandise mix across all countries (de Mooij and Hofstede 2002). One rather has to understand local consumers and build customized models for each community one operates in. In the 21st century, effective retailing will require understanding differences among consumers across borders. Instead of just reacting, a well-defined strategy allows to actively plan ahead and focus on one's goals. As outlined in **Exhibit 6.3**, this section provides a brief guideline with tools for developing a retail strategy, deciding upon the positioning of the retail business and, most importantly, its differentiation from competitors.

Exhibit 6.3 Retail Strategy Development



Source: Rudolph (2000)

Business Strategy

When starting the strategy process, the general approach to the business in terms of its vision and business model has to be defined. The vision may be seen as the main value proposition of the retailer and should be clearly communicated to consumers and fully understood and followed by the company (Rudolph 2000). To illustrate this, consider the value proposition "we buy the best for less, so you can too" of the hard-discounter Aldi (Aldi 2010). It provides guidance to both consumers and employees (Hayes 1985) and exerts motivation within the company. Consumers know what to expect of Aldi and employees what to strive for. The vision should be easily understood and not too narrow in focus.

The search for an apt business model to deliver the chosen value proposition marks the next stage in the definition of the overall business strategy. Based on the three most important drivers of customer value in retailing, i.e. price, product, and service, we distinguish three generic business models: the global discounter, the content retailer, and the channel retailer. Each model comprises a distinct vision and its implications for operations, management, and required competencies. As outlined in **Exhibit 6.4**, the global discounter tries to minimize costs through optimized sourcing, logistics, and sales in order to be price leader, while the content retailer encourages product innovation to become product leader. Through service offerings, the channel retailer focuses on solving consumers' problems to create a unique shopping experience (see Rudolph 2000 and 2005). Note that these models are generic and require certain adaptation.

Exhibit 6.4 Three Generic Business Models in Retailing

	Global Discounter	**Content Retailer**	**Channel Retailer**
Vision Value Proposition	"minimize cost"	"foster innovation"	"provide solutions"
Strategy	cost leadership	product leadership	customer relationship
Operations Core Competencies	efficient purchasing, logistics, and sales processes	market research, product development, innovation and trend research	relationship management, industry collaborations, service focus
Business Structure	standardized and simplified processes	agile and decentralized network structure	high empowerment of employees
Management	reliable and fast repeat transactions following defined benchmarks	building and maintaining unique assortments	apapt offering to consumer needs and problems
Expansion	organic growth	organic growth	mergers and acquisitions

Source: Rudolph (2000)

Positioning

Having defined the value proposition and chosen an apt business model, the positioning should be defined. This concerns the target groups, competitive advantages, and core competencies of the retailer. A retailer may specialize and only cater to distinct groups or it may focus on a broader crowd. Either way, to deliver the value proposition, certain competitive advantages are needed, which the retailer will obtain through its core competencies. Aldi initially catered to consumers in need of saving money, but increasingly expanded its target group to almost any type of consumer in search of fairly priced quality products (Steenkamp and Kumar 2009). This is achieved through Aldi's core competencies of volume buying and cost-control with a network of private label suppliers.

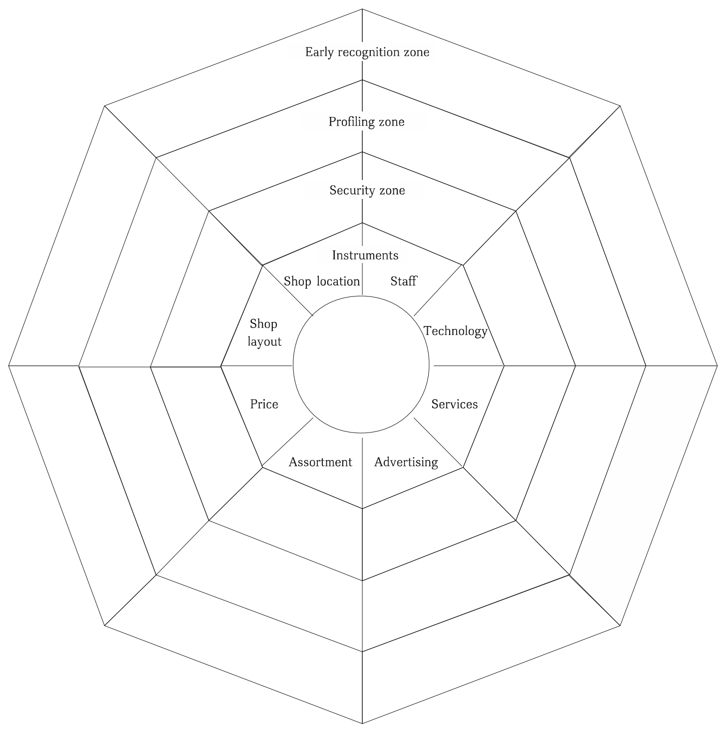
Differentiation

Successful differentiation is the key factor for retailers that do not just want to react and defend, but act and increase their market share. With a clear profile, retailers avoid becoming replaceable and will be able to achieve competitive advantages in increasingly difficult markets. The zone model of differentiation (as depicted in **Exhibit 6.5**) contains eight key instruments through which a retailer may differentiate its offering from the competition. These important areas are staff, technology, services, advertising, assortment, price, shop layout, and shop location.

In determining the differentiation strategy, the emphasis to be placed on each area should be defined and activities developed accordingly. For each instrument, we suggest three zones of intensity. The security zone contains must-haves and does not provide any market differentiation. Initiatives in the differentiation zone, however, help retailers create a distinct image and enforce the value proposition. The early recognition zone contains activities responding to early signals of future trends. At Aldi, high emphasis is placed on the price. In accordance with its value proposition to offer at low prices, Aldi has in place many measures to reduce costs and increase efficiency in all operations. Staff, however, is not used to create a distinctive image. This aspect remains within the security zone. As we will explain in more detail in the next chapter, retailers may accentuate different differentiation instruments in each market they operate in to better respond to diversity in consumer behavior and cater to local tastes.

The successful operations of retail companies in non-domestic markets revolve around one main principle: Only companies that have proven themselves in a highly competitive domestic market have a chance of earning money abroad. An attempt to escape into foreign markets, because of weakness in the domestic market, will fail (Liebmann and Zentes 2001). According to Murphy (1999), American and British retailers in particular tend to ignore cultural differences when expanding to offshore markets and tend to forget that retailing is a very localized concept that requires great sensitivity to local tastes and habits. This illustrates the importance and need of a thoroughly planned and executed retail strategy.

Exhibit 6.5 Zone Model of Differentiation

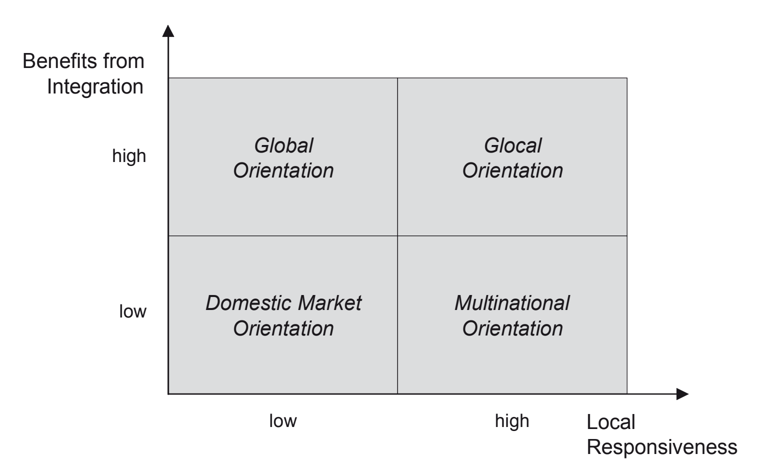


Source: Rudolph (2000)

6.3 Internationalization Strategies in Retailing

As with international marketing, the major question in international retailing is that of standardization vs. adaptation. Just as with brands and products, some retail concepts work in foreign markets with virtually no adaptation. This is what is meant by standardization. Most retail concepts, however, need some changes in the assortment composition or promotion strategy to fit new markets (Sternquist 1998). Helfferich et al. (1997) and Zentes et al. (2007) distinguish four basic options with regard to the level of standardization vs. adaptation of retail formats: domestic orientation, global orientation, multinational orientation, and glocal orientation. The corresponding matrix is shown in **Exhibit 6.6**. Benefits from integration refer to standardization, whereas local responsiveness means adaptation.

Exhibit 6.6 Internationalization Strategies in Retailing



Source: adapted from Helfferich et al. (1997) and Zentes et al. (2007)

Transferring a retail concept from the home market to other countries without major changes (low adaptation) leads to a unified program and standardized operations. While the benefits drawn from this standardization are minor in the domestic market orientation cell, they increase with the number of ventures a retailer is pursuing abroad. Global orientation is characterized by focusing on exploiting similar markets across the world and benefiting from economies of scale. In contrast to the domestic market approach, a global retailer seeks homogeneous markets across the world; these are the basis for developing a retail strategy or concept. Retailers following a global approach, among other criteria, consider to what extent there are shared customer aspirations and similar infrastructures (logistics, media, norms, governmental regulations) in different nations, in order to implement a relatively standardized strategy that conforms to these needs (see Zentes et al. 2007). The Spanish fashion retailer ZARA is highly standardized around the world. Except for seasonality, the store in Tokyo vastly resembles the one in Madrid and any other store of the chain. The same goes for the Swedish furniture store IKEA, who relies on the same store proven retail concept, store layout and assortment around the globe and only minimally adapts to local markets in pricing or its advertising approach. ZARA and IKEA may both be characterized as true global retailers.

In heterogeneous markets, such as the European retail landscape, substantial adaptations to retail concepts may be necessary, leading to definition of a specific strategy with different assortments and pricing policies for each market. The multinational orientation thus largely focuses on country markets. For this strategy, the market size or the spending power and competitive environment are primary considerations in market evaluation (see Zentes et al. 2007). Given the fact that the retail concepts operating within the multinational approach

considerably differ across countries, limited benefits may be drawn from a common brand, which is why many retailers have resorted to operating local brands across various countries. The Dutch food retailer Ahold, for instance, operates various supermarket chains in the United States and Europe, which each carry a unique brand. The glocal orientation, on the other hand, follows the idea to think global and act local by moderate adaptations to heterogeneous markets. In this approach, the retailer brings together economies of scale through standardization (efficiency) and a concentration on country markets (effectiveness). The approach of the German discounter Lidl may be considered a glocal approach, as Lidl simultaneously seeks the advantages from high standardization of operations (store layout, logistics) and local adaptation (assortment, pricing).

Retailers that internationalize must define the degree the business model and strategy need to be adapted to the new market and its local requirements with regard to the four basic types of international retailing. Entering a new market, each of the eight instruments of differentiation should be considered and carefully evaluated. While it is important to adapt to certain local aspects, the retailer should not deviate from its core strategy and business model too much in order to sustain its competitive advantage to leverage the core competencies. For a content retailer with an assortment composed of strong store brands, selling branded products in the new market would deteriorate its competitive advantage. For any retailers following that business model, a market entry to a country where consumers primarily value branded goods would not be advisable. The upcoming case of Aldi's learnings in Great Britain will illustrate these theoretical considerations.

6.4 More with Less – The Aldi Approach to European Retailing

6.4.1 Introduction

Aldi is a leading global retailer and one of the world's largest privately owned companies with about 8,877 stores in currently 18 countries (Euromonitor 2010). The company is mainly renowned for its simplistic approach to retailing, offering a limited assortment of great quality products at low prices. Industry experts consider Aldi the bellwether of the discount world and its strategies a powerful indicator of where the discount channel is heading due to the width of tactics it typically employs in the markets where it exists (Steenkamp and Kumar 2009).

Two German brothers, Karl and Theo Albrecht, founded Aldi in 1946. They named their company Albrecht Discount or Aldi for short. In 1960 the two brothers split the company into Aldi Nord (North) and Aldi Süd (South) over a dispute whether to stock tobacco products. With a mutually exclusive geographic presence across Europe, North America and Australia, Aldi Süd operates approximately 3,900 outlets, whereas Aldi North has about 4,300 stores (Wikipedia 2010). New stores open at a weekly pace, which makes keeping count a challenge. Germany, France, Netherlands, Belgium, and Austria have the highest

number of Aldi stores followed by the United Kingdom, Denmark and Spain. In Germany, Aldi Nord has a larger number of outlets than Aldi Süd due to its expansion into the Eastern part of Germany after the German reunification in 1990. While Aldi Süd has its own stores in the United States, Aldi Nord controls the Trader Joe's supermarket chain, which focuses on more upmarket exotic products and health food and operates under a structure separate from Aldi. Amongst the Eastern European countries, Aldi Süd is present in Slovenia where, like in Austria, it uses the Hofer brand name. Aldi Nord recently entered Poland in 2008.

The Albrecht family still privately owns the company. Aldi does not disclose any financials, but sales per square meter at Aldi are estimated at about 8,650 EUR, whereas traditional supermarkets struggle to cross the 4,000 EUR mark (Mitchell and Sachon 2006). Aldi is by far the world's largest operator in the discount channel, in which it accounted for 19 percent of world value sales in 2007, with a number one position in Western Europe (Euromonitor 2010). Aldi's 40 million shoppers and its competitor Lidl's 60 million shoppers combined outnumber the cumulated shoppers of all other retailers across Europe (AC Nielsen 2007).

6.4.2 Consistently Simple – The Aldi Business Model

The concept of Aldi's approach to food retailing has remained largely unchanged since the late 1940's. Aldi's philosophy is to focus on the indispensible and avoid the unnecessary in order to pass resulting savings on to its consumers. Aldi aims at offering the best quality products at value prices by simplifying the shopping experience and stripping out any redundant costs. Steenkamp and Kumar (2009) report that Aldi's cost only add 13% to the procurement price; 2% each for logistics, rental, overhead, and marketing, plus about 5% for staff. Both the grocery industry and consumer media frequently confirm the quality of Aldi's products with the highest praise and top awards. Aldi describes its value proposition as follows:

"We buy the best for less, so you can too – Our day-to-day items cost less because we buy them in great volume. And because we buy them from the same, hand-picked suppliers (whose products are sold under our own labels) we are able to negotiate substantial discounts – savings that we then pass on to you." *Source: www.aldi.co.uk*

The Aldi sales system is characterized by a limited product range with goods of best possible qualities that reflect basic consumer needs and by easy handling of these goods in terms of operational requirements. Both these points result in the lowest possible sales prices. It is the result of low overhead, high volumes, and heavy use of private goods that enables Aldi to underprice its competitor by 20 to 30 percent while maintaining a higher profit margin (Rudolph 2003).

Limited Assortment and Private Labels

The central idea that makes Aldi's strategy work evolves around the limited assortment concept. A typical Aldi store has four aisles, three to seven employees and approximately

1,000 products; a far cry from the typical European supermarket with 10 to 20 aisles and 15,000 up to 30,000 items (Steenkamp and Kumar 2009). Aldi specializes in selling staple products like food, beverages and household supplies consumers shop for on a regular basis. The assortment is strictly focused on the most needed and most often used products for the average home. Twice a week, these basic offers are enriched by special buys where customers can find anything from DVD players to clothing and kitchenware at great value. Special buys have limited numbers and are sold on a first come, first served basis.

Choice is limited at Aldi with minimal or no duplication of products. Aldi offers an average of just seven items per category with each item clocking sales of over 10 million EUR annually (AC Nielsen 2007). This ensures streamlined operations, efficient sourcing, and better shelf utilization. The resulting tremendous savings enable greater price compression. By limiting the number of items, Aldi manages to ensure that suppliers produce sizeable volumes of each item in a single run and extract even greater economies of scale. Faster turnover and logistically efficient pallets result in greater product freshness and even more profitable inventory management. Private labels are central to Aldi's low-price strategy, with private label products accounting for around 95% of sales (Euromonitor 2010). Only very occasionally when the private label product does not meet Aldi's high standards, a branded product is offered. None of the company's private label products are sold under the Aldi name. Hence, it is likely that many consumers, particularly in new markets, do not realize they are purchasing private label products.

A notable aspect of Aldi's assortment strategy is that it is constantly reviewed and revised to ensure that only the highest selling items remain listed. On average, Aldi tends to introduce 350 new or strongly modified items per year though the total number of items in the assortment remains unchanged (AC Nielsen 2007). Factors such as rising consumer health-awareness and increasing concern about environment and ethical issues are creating opportunities for Aldi to attract a larger consumer base and generate higher margins by repositioning some of its offer up-market through developing more premium private label ranges (Euromonitor 2010). Across Europe, Aldi initiated a greater segmentation of its product range by offering gourmet, health-orientated, Fair Trade, and organic products through developing private label ranges such as Grandessa, Bio, and Specially Selected. This segmentation helped improve the quality perception (Retail Week, 10 Jul 2008).

Simplifying the Shopping Experience and Operations

With a marked emphasis on offering low prices, Aldi strongly focuses on operating efficiency. Ruthless cost control is the leading principle. Many details contribute to the unmatched efficiency Aldi has reached in all its operations, including sourcing, distribution, replenishment, in-store handling, and sales. The shopping environment at Aldi is simple, clean, and highly functional. All unnecessary costs that would be transferred to the customer are removed. An Aldi store does not have service counters such as bakeries, butchers, fishmongers, and deli counters, so it does not have the associated costs. Products are stacked on pallets or in the boxes they arrived in, which cuts out the associated shelf stacking costs. When stock has to be replenished, it is wheeled into the store on shipping pallets

and the carton is simply cut open. None of Aldi's employees need to unpack individual packages or decorations. Aldi did not introduce refrigerated items until the refrigerator cases and cardboard boxes matched its requirements (Brandes 2005); the cases had to have an enormous capacity and the boxes to be the right size to be placed into the cases neatly without any wasted space.

In-store costs are kept to a minimum. Aldi is a self-service retailer requiring customers to unload their items at the checkout and pack their own bags. Shopping trolleys require a coin deposit. Hence, there are no additional costs for bag packers and trolley collectors. Customers buy carrier bags or bring their own. Aldi explains (Aldi 2009a): "Many retailers add the cost of free carrier bags onto the prices paid for products, so customers pay for them indirectly whether they use them or not. Charging for carrier bags furthermore encourages their re-use, delivering benefits to the environment." No music is played in stores; to cut costs, Aldi does not buy music licenses. At nights, the stores only keep the emergency lights on in order to save on electric bills. Although Aldi's advertising strategy is traditionally based mostly on low-cost media such as a small weekly newsletter leaflet Aldi informiert… ('Aldi informs…') providing details of that week's special buys, it was the second largest spender in advertising in 2008 among retailers, after Metro's Media Markt/Saturn chains, which dispels the assumption that discounters keep advertising spending to a minimum (Euromonitor 2010). Outside Germany, Aldi is also increasingly using TV advertising.

Aldi operates a lean staffing with an average of five to eight people: a store manager and two assistants are usually the only full time employees. Most Aldi locations are quite hectic and staff is expected to be swift on its feet. All personnel unload the stock, clean the store, watch for shoplifting, and work the registers. Store managers are also actively involved in all store operations and will help with customer checkout at peak times. Aldi's checkout is considered the fastest in the industry; one Aldi clerk checks out 42 items per minute versus 15 items per minute in a conventional supermarket (Mitchell and Sachon 2006). In return, the retailer pays above-average wages, which helps limit staff turnover; even still, Aldi's personnel costs are three percent of sales versus nine percent of a regular supermarket (Brandes 2004).

Aldi stores are a standard size and layout adding to efficiency. All store fixtures are purely functional. There are no in-store decorations, and economic building materials are used for flooring, ceilings, and shelving. Properties of the generic store format for new Aldi outlets concerning shelves, lanes, and possibly even the length and width of the store itself are determined solely in terms of logistics (box size, pallet size, maneuvering space needs for forklifts, and similar matters). Reordering is made simple by allocating shelf space to hold one more or less one week's supply (Kumar et al. 2007). Thus, on average, the whole inventory of a store is completely renewed after one week. Aldi stores receive new goods daily from decentralized regional logistic centers. These depots are in contact with mostly medium sized vendors, together making up a unique replenishment system hard to replicate.

Regarding distribution, Aldi is organized in cells of unique legal entities to improve logistics. Each cell consists of 50 to 80 stores and generates its own financial statements (Brandes 2004). Adhering to the principle of discreteness, this structure permits the company to avoid publishing financial results (under German law, companies of a certain legal form and below a certain threshold in sales do not have to make their financial statements public) and hence no consolidated financials are published for the Aldi group. The cell structure also supports Aldi's quest to decentralize and simplify. Using a hub-and-spoke distribution system, the distribution center supplies all stores within a radius of 50 kilometers (Kumar et al. 2007). About 90 percent of the goods entering a distribution center are immediately cross-docked and placed on trucks for shipment to the stores; approximately five percent of all goods go directly to the stores (Regani 2007). Most goods are shipped in opened boxes so they can be immediately placed on the shop floor.

The whole concept behind Aldi makes it easy to plan and order far in advance. Aldi primarily focuses on permanent customer needs and not too much on actual consumer demands. In Germany, Aldi has evolved into a cultural institution. As the BBC (2000) once declared: “Aldi is more than just another food store. The true character of the German lifestyle and zeitgeist can be found in only a few places. Aldi is one of them.” There is no magic formula to the success of Aldi, but paying attention to small details over decades has resulted in probably the most efficient and optimized operations in retailing.

6.4.3 Taking Aldi Abroad – Adapting a Standardized System to Local Needs

The internationalization of Aldi followed the company’s key principles of simplicity, high quality, frugality, and confidentiality. As with growth within Germany, all of Aldi’s international expansion was financed through retained earnings due to Aldi’s fast cash-to-cash cycle and solid profit margins (Mitchell and Sachon 2006). Aldi’s international strategy involves entering markets substantial enough to support its hard discount concept through a combination of acquisition and organic growth ensuring a solid retail infrastructure. To date, Aldi has not exited any markets it entered, even though its entry into various countries often has sparked anxious debates about price wars and smaller margins.

Aldi has cumulatively increased its store count on a continuous basis. In terms of store density, there is one Aldi store for every 20,000 inhabitants in markets that Aldi entered during the early phase of its existence such as Austria, Belgium, Germany, and the Netherlands (AC Nielsen 2007). If Aldi did attempt to match this store density in each of the other European countries that it is currently present in, the number of Aldi stores would triple. This indicates a lot of space for Aldi to expand within countries it has entered more recently (see **Exhibit 6.7**). However, Aldi’s approach to market entry and store expansion has been rather conservative: while its main competitor Lidl has increased its stores by a multiple of ten over a 15 year time frame, Aldi has only seen a doubling of stores over the same period (AC Nielsen 2007).

Despite its growing presence, Aldi's progress is not uniform across markets. In some countries it has managed to garner a significant share of trade whereas in other markets it seems relatively under-represented. While it has managed a high single-digit or double-digit share of trade in markets like the Netherlands, Germany, and Belgium, it seems less popular in markets like France, the United Kingdom, and Ireland (AC Nielsen 2007). Aldi's turnover per store too reflects this with a higher turnover for Belgium, Germany, and the Netherlands, but a relatively low per store turnover in France and Ireland (Euromonitor 2010). According to AC Nielsen (2007), this can be attributed to differences in both the number of stores across countries as well as variations in consumer demand for the discount channel (Ireland) or more intense competition within the discounter channel (France).

European Internationalization

Aldi's internationalization (as depicted in **Exhibit 6.7**) began in 1967 with Aldi Süd's purchase of the Austrian Hofer chain. After the take-over, it encountered resistance from the Austrian government trying to pass a law forcing food distributers to stock milk, dairy products, and bread; this legislation would have diluted Aldi's then exclusive focus on dry goods (Kumar et al. 2007). Aldi Nord first ventured abroad in 1975 and opened stores in the Netherlands, which were soon followed by stores in Belgium and Denmark. In 1988, Aldi Nord entered the difficult French market, which was dominated by domestic chains and their popular hypermarché concept. The United Kingdom was added to Aldi Süd's portfolio in 1990, followed by Ireland in the year 2000. Aldi Nord meanwhile completed its Benelux operations by putting Luxembourg on the Aldi map in 1998. Following the millennium, it then set about conquering the Iberian Peninsula through entering the Spanish and Portuguese market. Aldi Süd also ventured further south by opening stores in Switzerland and Greece in 2005 and 2008, respectively.

Exhibit 6.7 Aldi's European Internationalization

Source: graphical representation by the authors

Aldi's focus on expansion into Eastern European markets began in 2005 with Aldi Süd opening in Slovenia and continued with the 2008 market entry into Hungary and Poland. There are future plans to open stores in Romania. In Slovenia, Aldi managed to run 35 outlets at the end of 2007 before its rival Lidl followed; in most other Eastern European countries, Lidl is already present. The first Aldi in Poland opened in March 2008, following a delay. Initially, Aldi had planned to open in the summer of 2007, but it had struggled to find the appropriate ten sites it was seeking before rolling out its first outlets, and in addi-

tion, it had difficulties in obtaining licenses to sell alcohol. Aldi's long-term objective in Poland is to have up to 1,000 outlets; in Hungary, Aldi initially opened 26 outlets in the first half of 2008 and has a long-term goal of around 400 stores (Euromonitor 2010). Aldi's Austrian subsidiary Hofer manages this market; the proximity of the two markets helped to have a good knowledge of market conditions prior to the opening of the first stores.

Considering Local Market Needs

The clearly defined and simple concept based on efficiency to achieve low prices facilitates Aldi's expansion into new international markets, as the concept is relatively easily shaped to their demands. In general, only limited marketing is needed to familiarize new consumers with Aldi. Yet, Aldi very carefully adapts certain elements of its concept to each new market. In newer markets where the brand image is not very strong, Aldi deviates from its strict limitation concerning marketing efforts and a greater focus is placed on advertising campaigns. In the United Kingdom, Aldi seeks to improve its brand perception by promoting the chain's premium products through the advertising campaign 'Spend a Little, Live a Lot' launched in 2005 and including TV commercials – an unprecedented format for the stingy retailer (LZ, 23 Feb 2006).

Given the key role of the limited assortment in the Aldi approach to business, the retailer very carefully assesses local tastes and consumer preferences to offer an equally attractive assortment to consumers across countries. At the same time, caution is exercised in deviating from the standardized processes to guarantee the same efficiency in operations across countries to match the cost target. Although Aldi offers a small selection of products across most markets where it operates, its private label offering is largely adapted to local markets. The assortment is predominantly local with an extremely limited presence of branded goods. When branded goods do get listed, it is usually with just one item. While Lidl has a central core set of private labels found in every country, Aldi's private label assortment is more country specific. For example, in the United Kingdom it offers jammy dodgers biscuits and locally brewed bitter beer, while in France, it sells ready meals such as Cassoulet as well as frozen snails. In Slovenia, the Hofer stores sell traditional Slovenian foods along with local dairy and vegetable products (Euromonitor 2010).

Aldi's efficient supply chain relies to a great extent on local sourcing. Up to 60% of its fruit and vegetables are sourced locally where possible (Aldi 2009a). Bread and morning goods are bought locally and delivered into stores fresh every day from local bakers. This has clear implications on the cost advantages related to sourcing, since a centralized approach would provide better economies of scale, while a localized approach customized to local tastes may improve the rate of off-take and hence sales volumes. When entering a new region, Aldi usually establishes the supply chain and warehouses first before opening stores. When a critical mass of 60 to 80 stores exists in one area and the distribution center has reached its maximum capacity, Aldi creates a new regional entity, complete with its own regional distribution center, administration, and accounts (Brandes 2004). Thus, distances between warehouses and stores remain short, which allows for rapid and responsive distribution.

The following section will take a closer look at how Aldi deals with diversity and local differences. When entering the British market, too much emphasis was initially given to keeping the German business model and focusing on efficiency and costs. The neglect of local consumer needs resulted in a severe image problem, which Aldi is trying to resolve with massive advertising efforts and high adaptations of its strategy to the British market.

6.4.4 From Cheap and Commonplace to Chic and Convenient: Aldi in the United Kingdom

The first Aldi store in the United Kingdom opened in Birmingham in 1990. During the mid-1990s, Aldi successfully exerted price pressure on the domestic grocery retailers via its hard discounting strategy (Euromonitor 2004). Sticking closely to the German discount protocol, the majority of Aldi stores were located in mostly second-rate locations in suburbs of low-income townships to save on rent (LZ, 02 Oct 2008). In the United Kingdom, where social class still matters greatly, this created the impression of Aldi being a store for the socially deprived. Snotty Brits refused to shop at Aldi and those who had done so tried to avoid showing it by covering their purchases in bags of up-scale chains such as Waitrose when carrying home their purchase (LZ, 2 Oct 2008; Retail Week, 28 Aug 2008a). Paul Foley, managing director of Aldi Stores Ltd. in the United Kingdom since the year 2000, recalls (LZ, 23 Feb 2006): "Across the globe, Aldi is recognized as a retailer providing good quality at a cheap price. In the United Kingdom, we were just considered cheap and commonplace." As British supermarkets responded to Aldi's low prices by introducing own discount ranges, they easily regained ground. Consequently, after enjoying a moderate growth during the mid-1990s, the significance of Aldi declined and contrary to its other European ventures, Aldi's market-share in the United Kingdom lingered around two meager percent for a decade (Planet Retail 2008). An ambitious expansion and repositioning plan announced in 2005 was about to change this.

Repositioning Aldi

Purchasing motivation in the United Kingdom is not just driven by price, but also by other factors including the quality and convenience of the shopping experience (Euromonitor 2004). Consequently, Aldi is attempting to stage a comeback by improving consumers' perception of its store's value and quality of products. Aldi will be repositioned as an up-market retailer, targeting more affluent consumers. At the same time, Aldi's prospects for growth in the UK and Ireland are significant with up to 50 new stores planned annually over the next four to five years, reflecting the fact that its geographic coverage is still incomplete and will be increased. Following an investment of £1.5 billion over the next five years, the current number of about 400 stores would thus increase to 1,500 (Aldi 2009a).

Employing the claim 'Don't change your lifestyle; change your supermarket,' Aldi is increasingly drawing in new crowds to its stores and shedding its commonplace image in light of the unfavorable economic conditions (Finch 2008). Aldi's philosophy of offering an outstanding combination of incredible quality and unbeatable value has made an increas-

ing number of people switch on to the Aldi message and make Aldi their first port of call for their weekly shopping. Having neglected most of the local market trends, consumer tastes and expectations for the past decade, Aldi is thus shifting its approach towards the British market from a strategy of high standardization with close to no local adaptation towards a highly tailored one, taking into consideration local preferences in almost all of the elements in the zone model of retail differentiation.

Catering to a Broader Audience

The effort to move upmarket and attract more middle-class consumers with high disposable income required Aldi to increase the depth of its assortment and provide a certain product choice. As a consequence, the product range was expanded from 700 to 1,050 products, excluding non-food and seasonal merchandise. Between the year 2000 and 2004 Aldi had already expanded its fresh food range from 150 to 240 items (LZ, 23 Feb 2006). With the 2005 launch of the Specially Selected range, Aldi drew the focus on private label items with a more upmarket positioning introducing a number of premium health and beauty products, cosmetics as well as spirits and chilled ready-to-eat meals. These products included quality ham and lamb, pesto, and foiegras (Euromonitor 2010). To visualize the qualitative up-trade, product packaging was redesigned and more exclusive materials used (LZ, 23 Feb 2006). It was reported that the development of these premium private label products helped Aldi perform extraordinarily well over the 2007 Christmas period, recording a 12.1 percent growth thanks to the success of its seasonal range under the Specially Selected label, and strong sales of fine wines and champagne (Retail Week, 11 Jan 2008).

Educating the Consumer

Aldi is aware that teaching consumers how and why Aldi operates as it does is a vital part of the store's long-term acceptance in the United Kingdom (Retail Week, 10 Jul 2008). Inside the stores, Aldi has installed extra signage to explain its processes, such as the policy of customers loading their shopping back into the trolley at the checkout and then packing their bags at benches at the back of the store. As part of the huge 2005 repositioning, Aldi rolled out the professional advertising campaign 'Spend a Little, Live a Lot' in an attempt to attract wealthier customers and boost its market share to 5% (Finch 2008). The TV commercials created portray Aldi as a high-quality retailer. The campaign is estimated to have cost about 8.8 million EUR (LZ, 23 Feb 2006). Yet, in 2007, Aldi went even further and entered a long-term partnership with popular BBC-chef Phil Vickery, who is developing a range of recipes and advising Aldi on its product range. Aldi already introduced 40 additional products on Vickery's recommendation (Retail Week, 03 Sep 2008). Aldi is hoping that Vickery's celebrity status will pull in shoppers. The cost of this campaign is estimated at about 12 million EUR (LZ, 05 Sep 2008) and emphasizes how Aldi is now adapting to the local market; especially taking into consideration that its more up-scale competitor Sainsbury employs the renowned chef Jamie Oliver for advertising and product endorsement. Employing a professional publicity agency to promote Aldi's quality awards and achievements in the press and media marks another milestone and deviation from the company's general closed-lipped attitude and secrecy principle. In no other country does Aldi operate

an online press center and answer consumers' and media question as openly as in the United Kingdom.

New Store Format with Convenience Focus

To complement its core offering and demonstrate its new positioning, Aldi is also making changes and local adaptations concerning its shop locations and store layouts. In 2006, it launched a new store type in the small town of Rugby in Warwickshire with upgraded lighting, graphics, merchandising, and an easy-to-navigate store layout (LZ, 23 Feb 2006). The more attractive architecture allows more natural light to enter the store. High walls like those in a market hall create a pleasant atmosphere. Lower shelves and bigger signage facilitate orientation and allow for an immediate overview of the store. All stores in the United Kingdom and Ireland subsequently underwent an extension or refurbishment until the end of 2008 (Euromonitor 2010). These efforts are ongoing; in Ludlow in Shropshire, Aldi is currently constructing its first eco-store with an environmentally friendly roof covered with alpine plants to prevent water running off and retain heat (Retail Week, 05 Mar 2008).

Aldi furthermore seeks to open more outlets at city center locations following the success of a first test store opened in Manchester in December 2006. The 1,000 square meters store is directly accessible from the Arndale Centre, a downtown shopping mall featuring tenants such as Lacoste, H&M, and BHS department stores. The Manchester outlet differs from other Aldi stores thanks to a more upmarket feel, including a more elaborate layout and a focus on more premium products of the Specially Selected and Be Light ranges (Retail Week, 28 Aug 2008a). Instead of selling pre-packaged sets of six items, Aldi is offering single apples and bananas as well as ready-to-eat fresh produce. The store thus marks a deviation from Aldi's standard trolley-only model with the launch of a new lunch range in a grab-and-go format, featuring a premium selection of locally sourced sandwiches along with chilled coke and champagne (Euromonitor 2010; LZ, 16 Mar 2007). This focus on convenience reflects the current British shopping attitude and follows formats developed by competing British chains such as Marks&Spencer and Tesco. Both the improvements of shop layout and location are important steps towards the goal of appealing to Britain's more affluent middle class, who by tradition values quality and shopping experience, but is increasingly struggling to make ends meet.

Sustainable Success?

Though Aldi's repositioning campaign is still underway, first signs of success soon showed. It was reported that Aldi UK increased the sales volumes of fresh vegetables five-fold in 2007 (Retail Week, 11 Jan 2008). In November 2008, TNS World panel figures revealed an extraordinary increase of Aldi's market share by 23.9 percent over the past twelve weeks. As a consequence, Aldi finally pushed past the three percent mark of the British grocery market (Retail Week, 11 Nov 2008). Discount competitor Lidl only achieved an 11 percent increase during the same period of time, showing that not all discounters equally benefit from the economic downturn. In 2008, the UK operations of Aldi were honored with the

coveted 'Outstanding Achievement of the Year' prize at the 2008 Retail Industry Awards (Aldi 2009a). Unanimously voted winner by the leading experts of the British retail sector, Aldi impressed the judges with its ongoing drive, expansion program, and commitment to offering consumers something extra special at an exceptionally low price. Consumers appear to agree, as in early 2009, Aldi came 7th out of 96 retailers in the country's biggest survey of high street shops. Members of the independent consumer group praised the quality of food available at Aldi, highlighting that lower prices do not have to mean compromising on quality (Aldi 2009b).

Industry experts credit the rapid growth mostly to the credit crunch, which led to a change in shopping habits. Along that line, polls suggest that Aldi and Lidl are no longer dirty words for the consumer (Retail Week, 22 Aug 2008) and that shoppers are unlikely to desert value grocers even when the economy picks up, as "snobbery is ditched" (Retail Week, 28 Aug 2008b). Yet despite the praise Aldi received, growth slowed in 2009. With a growth rate of 83 percent during the past three months of July 2009, Aldi only grew slightly more than market average (6.2 percent). During the same period in 2008, growth had still been at 17 percent (LZ, 13 August 2009). In consequence, Aldi surprisingly announced the immediate replacement of UK and Ireland Managing Director Paul Foley with Armin Burger in August 2009. The sudden stop in growth leaves one wondering if Aldi may not have overstepped the line in the UK and moved too far away from its discount roots in stretching the discounter ethos towards premiumization and convenience.

Student Assignments

Aldi in Romania

Given the information from the case about the European internationalization of Aldi, how would you judge the company's decision to enter Romania?

How might the experience in the United Kingdom help Aldi prepare their market entry to Romania?

What would you recommend Aldi do concerning local tastes and shopping habits?

Aldi in the United Kingdom

Considering the recent changes Aldi has subjected its UK business to, discuss whether the company seems to be deviating from its glocal approach to internationalization towards a more multinational one or not.

What problems might Aldi face if it were to change its internationalization approach?

Provide evidence for your arguments from the case and strategy section.

Internationalization Strategy

Draft an internationalization strategy for a local retailer from your country starting with the definition of its business model, value proposition, and differentiation profile.

Based on these criteria and the chosen target country, which approach should the retailer follow concerning standardization and adaptation?

Which areas of the zone model of differentiation should the retailer try to adapt to the local market and which ones require standardization?

Base your answers on the retail strategy, competitive advantage, and core competencies of the chosen retailer.

Additional Readings

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7 Private Label Strategies in Europe

Isabelle Schuiling, Louvain School of Management, UCL

Renaud Cogels, Executive Vice President Delhaize Group, retired

> **Private label gains market share across Europe, PLMA's 2010 Yearbook reports**
>
> (Amsterdam)—Private label has reached record market shares across Europe as retailers rely more than ever on their own brands to offer value to shoppers, according to PLMA's 2010 International Private Label Yearbook. For the first time, private label accounts for at least 40% or more of all products sold in a total of five countries. Overall, private label gained in 14 of the 20 countries tracked by Nielsen for PLMA's Yearbook.
>
> ***PLMA's World private labels – May 2010***

7.1 Private Label Evolution in Europe

In this chapter, we will first review the overall evolution of private labels in the world. We will elaborate on the differences between Europe and the US and understand the reasons for the growth of private labels. Next, we will review what are the objectives followed by retailers in the development of private labels and the different types of private labels that retailers have created over the years. We will then highlight the branding strategies these private labels have adopted to fuel their growth. After this, we will understand which categories have private labels with high shares and review the key differences by country. We will also analyze what is the perception of consumers regarding private labels and identify the companies that are producing private labels. We will finally illustrate this development with the case of Delhaize, an international retailer based in Belgium, which has used private labels as a way to gain a strong competitive advantage in the market.

The growing sales of private labels are a global phenomenon. Private labels account for 14.9% on a global basis but Europe is the region with the largest private label share at 35% (Nielsen 2011 report). This compares to 17% for North America. Private label development varies significantly by country, by retailer and by product category. In Switzerland, the level of private labels is the highest in the world with 46% in 2009 as indicated by Nielsen. In the UK, the level is also above 40% with a 44% share. This is followed by Germany with a 32% share, Spain with 29% and Belgium at 28%. In Italy, the level is relatively low at 14%.

Interestingly, private labels are also present in Eastern European countries where private label development is starting to become important. We find a 22% share of private labels in Slovakia, 18% in Czech Republic, 17% in Hungary and 12% in Poland.

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Key differences between Europe and the US

Key market differences explain the variations between the European and US situations. Some are structural and will not change in the medium term. The share of private labels in Europe at 35% compares with 17% in the US. There are key structural differences. First, retail concentration is much higher in Europe. Retailers have the scale to drive scale efficiencies and the brand equity to gain trial and loyalty. Second, there is a far greater presence of hard discounters in Europe that have created the need for value brands; and third, European retailers have developed sophisticated private labels. This has led to broadened appeal across consumer segments and across a broader range of categories. Sub-branding for example has been critical to the success of European private labels (IRI 2008). In the USA, there is actually a strong consciousness that a private label is a must, and some major retailers are developing very strongly, like Kroger. The strong growth of Aldi in the USA will also be a reason for acceleration of private labels.

The evolution of private labels over the last three decades

The role of private labels has evolved over the years. In the 70's, private labels were created as a response to the introduction of hard discounters, but they did not have a lot of success. These private labels were plain white, no frills packaging without any product name (produits libres de Carrefour in France, produits blancs de GB in Belgium). The quality was significantly lower than national brands and the prices were around 40% lower than national brands.

In the beginning of the 80's, the use of private labels was viewed by retailers as a defense strategy to reduce the power of manufacturers. At that time, substantial price increases happened on national brands. This was fuelled by several leveraged buyouts over the decade. In the 90's, private labels were used more as a way to increase the profit margins of retailers and to introduce new products and ranges that were weak or absent in the brand manufacturers and improve the differentiation versus other retailers to enhance retailer image. The world of private labels has changed over the last three decades. If, in the beginning, private labels were seen as me-too products, over the years the quality of private labels has increased, and now retailers offer premium store brands that offer quality that equals or even surpasses manufacturer brands. They began to innovate on value, using sourcing and supply chain efficiencies to offer lower prices without compromising on quality (Kumar, Steenkamp 2007). They also started to manage their store brands more strategically and introduced price segmentation.

A good example is Tesco in the UK (see **Exhibit 7.1**). There are many proposals in the special private labels' segment, such as "Tesco organics", organic food from cookies to sausages, or "Tesco Free from" for products that are gluten, wheat or milk free. There are also "Tesco Healthy Living", products with reduced fat, sugar and sodium, "Tesco Carb Control" low carb products, certified "Tesco Fair trade" products and "Tesco Kids" products.

Exhibit 7.1 Tesco brand architecture

Source: J.W. Grievink in Kumar and Steenkamp, (2007)

Reasons for steady growth of private labels in Europe

The success of private labels is attributed to different factors, such as the growing concentration of the retail industry (see **Table 7.1**), the growing presence of hard discounters, an improvement in the quality of private labels over time, the increasing efforts of retailers put in their private labels programs (Lamey et al. 2007), and the economic crisis.

Table 7.1 Retailer Concentration

Country	Private Label Value Share	Retailer Concentration
Switzerland	46%	86%%
Great Britain	44%	65%
Germany	32%	65%
Spain	29%	60%
Belgium	28%	80%
France	26%	81%
Netherlands	24%	64%
Denmark	22%	89%

Source: Nielsen (2009)

The growing presence of hard discounters – Aldi and Lidl are present in every European country. Within Aldi, private label products account for 95% of sales. As hard discounters continue to grow and gain shares, so do private labels. Also other retailers are becoming simpler and "discounted", like Mercadona in Spain, Carrefour with Express format and Auchan with "Simply Market", all with more accents on their private label.

Regarding an improvement in the quality of private labels and increasing effort of retailers in the private label programs – Retailers such as Tesco in the UK have added premium private labels lines (Tesco Finest) and are developing sub-branding strategies.

Regarding the poor economic situation, Lamey et al (2007) have shown in their study that consumers buy more private labels in economic recession, but some of them keep buying these store brands when bad economic times are long over. This is confirmed by a 2010 Nielsen study on more than 27,000 respondents in 53 countries that shows that 50% of consumers surveyed said that they purchased more private labels brands during economic downturn and that up to 91% said they will continue to do so when the economy improves. The top four countries where consumers have claimed to buy more private labels are the ones that were more hit by the economic recession: Spain, Greece, Portugal and Ireland. In view of this, manufacturers should invest more in promotions to support their brands. We see, however, that the contrary happened; manufacturers cut their support in times of difficult economic conditions while at that time most retailers invest more strongly in their private label programs.

Strategic objectives of private labels

The advantages of private labels are numerous. This explains the success of private labels over the last decades. First, private labels generate more profit than manufacturer brands. If no marketing costs are dedicated to private labels, the cost price between brands and private labels can reach up to 30%. In the beginning, when private labels were imitating national brands, they had less investments needed in the R&D and communication. This would give them higher margin because of these lower costs. Second, it builds and maintains consumer loyalty. If a brand is available only at a particular retailer, the consumer must go to that retailer to purchase it and that enhances consumer loyalty. It also creates traffic as more consumers will come to that store. Third, it creates differentiation versus other retailers. This will also enable the retailer to build its retailer image. Fourth, it permits increased negotiation power of retailers versus manufacturers.

Types of private labels

Over time, European retailers have had very different approaches for their private labels. They have used a more sophisticated segmentation approach over the years. The actual existing strategies are still very different by company and market approach.

Mono-line or “1-tier”: One product by segment, of high, medium or low quality and price, depending on the retailer’s strategy. The best examples are Aldi and Lidl in Europe, Mercadona in Spain, Pingo Doce in Portugal, Mega Image (Delhaize) in Romania.

2-tier: A very common approach in the 80's, where besides the main private labels, mainstream retailers created an offensive low price or "first price" range (Carrefour with Les Produits Blancs), or a defensive one to fight against Carrefour and the internationalization of Aldi (Derby at Delhaize). Today, there are numerous retailers who have a "mainstream" private brand completed by a "first price" range. Germany has many retailers following this strategy.

3-tier: Launched by Tesco UK in the 90's, where besides the medium, brand comparable Tesco range, you find in the same categories at the one side low price products, i.e. "Value", at the other side more upscale and/or innovative products, "Finest". Today, other examples include Carrefour in Europe, Leclerc, Casino and Système U in France (Bien vU - produits U - Saveurs U), Delhaize in Belgium, Ahold in the Netherlands and Esselunga in Italy (Fidel - Esselunga - Top Esselunga).

Multi-tier: Besides the now quite common 3-tier approach, a number of retailers have added other more specific private label ranges, such as Saveurs de France (Carrefour), Reflets de France (Leclerc), and Close to Greek Nature (Alfa Beta Delhaize Greece) for authentic regional food. In many cases, specific brands are used for organic food (Delhaize Bio, Loblaws Organics, U Bio) and environmental friendly products (Eco Delhaize, U Ecologique).

The no-brands approach with only private labels, where Marks & Spencer UK and until recently Migros Switzerland are unique examples. Even Aldi and Lidl now have international brands.

Finally, the no-private label strategy is not common anymore. Kwik Save, a UK discounter, became a big failure. One positive and very interesting example is Konzum in Croatia. Instead of pushing their private labels, they gave enormous support to the national (Croatian) brands and manufacturers, which they use "against" the international brands.

The most obvious advantages (and disadvantages) of the different approaches are:

- The fewer lines, the better the buying power and the lower the handling costs and the levels of inventory.
- The more lines, the more differentiation, innovation, loyalty, margin, contribution.

Branding strategies of private labels

Retailers have adopted different branding strategies for their brands. Single brand names, unique brand name per category or different brand name approaches have been used over the years. Following is a list of the branding strategies having been used over times.

Monobranding: one brand for all the private label products, mostly the store brand. Two examples are Carrefour and Cora, both in their home country and abroad.

Brand per broad category: a different brand per category. Sometimes the "core" categories (food for example) have the store brand. Other categories like detergents, health & beauty

have other brand names; examples include: Mercadona (Hacendado for Grocery, Bosque Verde for Home care, Deliplus for Beauty care), Delhaize (Delhaize for Food, Care for Non-Food, sometimes called "Near-Food").

Different brands by product or product type: The best examples are Aldi and Lidl. In these cases, the retailers aim to create brands and designs that are comparable to the international brands of multinational manufacturers. They also avoid the risks on cross-contamination in case one of their bands faces quality problems.

For multi-tier private labels, the retailers who have this approach can use the same or different brand by tier, even if they add the signature of the store brand on each of them. Well known examples are Tesco (Tesco Finest, Tesco mainstream, Tesco Value) and Delhaize (Taste of Inspirations, Delhaize mainstream and 365), Système U (U Saveurs, U mainstream, and Bien vU).

Private labels of other European retailers: Here, Delhaize in Belgium has been quite unique, having sold Sainsbury's private label from UK, Esselunga from Italy (still now) and of course Alfa Beta private label from Greece (part of the Group). Alfa Beta Greece and Mega Image Romania are selling Delhaize Belgium private label in their companies.

International private labels: Carrefour, Tesco, Aldi and Lidl are the leading pan-European retailers selling the same brands everywhere, also because the store brands are the same everywhere. Delhaize is an exception, selling their 365 brand in the other European subsidiaries, even if the store brands are not common.

Two additional examples of not very common practices are Waitrose UK, which exports its private labels to some countries, and Migros Switzerland, which has its own factories for yogurt, cheese, chocolates, biscuits and detergents among others, and is selling products to other countries (including to Delhaize in Belgium).

Price of private labels

Price is a major driver of private label trial and adoption. The economic situation has served to amplify the impact of price on consumer attitude and behavior. The UK demonstrates the largest price gap versus national brands with a 51%, while the private label discount is smallest in Italy at 21% (IRI 2008). Every retailer has its own pricing strategy: EDLP (Every day low price) means no price promotions; EDFP (Everyday fair prices, the same but a bit higher); High-Low, with price promotions. There is also a large difference of price differentials depending on the category.

Countries with high private label shares

As indicated in the introduction, the strength of private label varies widely across the countries from 46% in Switzerland to 14% in Italy. The variations of the share of private labels in Europe can be explained by different factors. First, countries with a highly concentrated retail structure tend to have higher private label share positions. In several European coun-

tries such as Spain and the UK, a limited number of retailers exert an important influence on the retail market place. Dominant retailers have the brand equity and consumer loyalty necessary to build private label trial and adoption. Second, category dynamics also play a role. Some categories are dominated by a few brands. These brands have great equity and invest heavily in branding and promotion. Innovation tends to be high and private labels share tends to be lower. Third, retailer strategies play also a role. They have been shown to have a profound impact on private label share (IRI Times and trend 2008).

Exhibit 7.2 Value Share of Private Labels by Country

value share of private label in percent

Country	Value share
Switzerland	46
Great Britain	44
Germany	32
Spain	29
Belgium	28
France	26
Netherlands	24
Denmark	21
Italy	14

Source: Nielsen report (2011)

Switzerland: The high contribution of private labels is due to the dominance of Migros and Coop Switzerland on the Swiss market. Migros has been the leader for decades with also a very high share of private labels. Coop, as number two, has a slightly lower penetration but is still high. The recent arrival of the hard discounters such as Aldi in the country is even pushing private label market shares further.

Great Britain: With a share of 44% in the UK, private labels are strong and growing fast. The British retailers have always been ahead in developing quality private labels. Marks & Spencer, Sainsbury and Tesco have played a major role as they have invested heavily on private labels. But also smaller retailers like Waitrose took the lead in private label innova-

tion, and have even been able to sell them in other countries, such as Asia. A Sainsbury survey showed that 53% of their shoppers feel that national brands are losing importance and 73% are satisfied with private labels alternatives (IRI 2008).

Germany: Private labels in Germany are strong with a 32% share. Hard discounters dominate private labels in Germany. Aldi is a clear market leader with an estimated 20% share of the market. Lidl is also present and 50% of its sales are coming from private labels. Retailers Rewe and Edeka are important in the German economy. They are covering more the mid-tier end of private labels spectrum. Today, it is the premium end of private labels that is the fast growing tier.

Spain: Private labels are quite strong in Spain. The structure of the retail market is very concentrated with Mercadona being a dominant player. Private labels represent 50% of Mercadona's sales and therefore have a big impact on the Spanish economy. Price is also playing a major role in Spain with prices offered at a 38% discount versus national brands; growth of private labels is also attributable to an extension of private label lines. In retailers such as Alcampo, Caprabo and El Corte Ingles, the value and economy tier offerings have been extended (IRI 2008).

The Netherlands: The Dutch market is very peculiar. Dominated by Albert Heijn (more than 30% market share), the country has a lot of regional retailers who are, in general, member of buying groups. The most important regional retailers are: Jumbo, Dirk Van den Broek, Sperwer, Jan Linders, Deen, Plus, Poiesz and others. The most important buying group is Superunie with almost 15 members. Albert Heijn has the strongest share in private labels, as the regional retailers often use private labels created by the buying groups. But things are changing quickly; as the regional retailers are becoming more national, they are more confronted with each other and have started launching their own private brands.

Belgium: The country has three dominant retailers – Carrefour, Delhaize and Colruyt. Carrefour and Delhaize have a very high contribution of private label compared to other European retailers. Colruyt has some, but is more dedicated to selling branded products at very low prices. Carrefour's international private label development was rolled out in Belgium, and Delhaize built its own.

France: With 26% share of private labels, they are well developed and growing. Private labels grew in France as it is the republic of the hypermarkets. Having the space in their stores, they developed a lot of products and the particularity in France is that the private labels of most of the retailers (Carrefour, Auchan, Leclerc, Intermarché) are often made by the same manufacturers and thus are very similar. The differentiation is probably not as strong as in other countries.

Italy: Private labels are at a low 14% in Italy, but they are growing at double digit rates in this country. Retailers are using private labels more and more as a way to differentiate themselves from competitors. The need for low priced private labels is not yet very strong. Concentration and competition have been quite low in the country and the presence of

hard-discounters is still much lower than elsewhere. The leader in private labels is Esselunga, a leading retailer in Lombardy. Their products are of good quality, and some of them are made in their own factories.

Categories with high private label shares

Different factors explain the difference of private label levels in different product categories. The level is influenced by:

1. The technology used to develop the product. If the product is simple and the technology not sophisticated, it will be easier for the retailer to develop a private label;
2. The size and growth of the market. If the volumes are attractive, it might attract the retailers;
3. The presence of a strong national brand or several strong national brands. In the case of Coca- Cola or Kellogg's, it is very difficult for a retailer to develop strong private labels;
4. Innovation. If the innovation is critical in the category as it is in the diaper category, it is more difficult for a retailer brand to grow;
5. The level of advertising spending, and
6. Consumer implication in the category. Categories such as perfumery and cosmetics are difficult for retailers. On the other hand, the kitchen towel category is very much dominated by retailer brands.

In some categories, private label development is below average. In these categories, large manufacturers are dominant players. These categories are, for example, carbonated beverages, cereal, coffee, and laundry detergent. Within these categories, brand investment – in terms of promotion and innovation – is significant (IRI 2008).

Table 7.2 Low Share Categories

Category	France	Germany	Netherlands	Italy
Carbonated beverages	7%	5%	14%	5%
Cereal	20%	13%	21%	6%
Coffee	15%	6%	26%	5%
Laundry detergent	10%	6%	15%	6%

Source: IRI (2008)

Categories such as frozen foods, milk, paper towels and toilet tissue have the highest share of private labels.

Table 7.3 Staples Categories

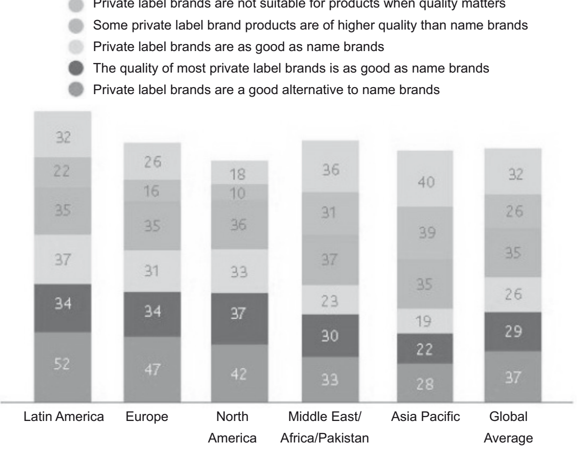
Category	France	Germany	Netherlands	Italy	UK
Bread and Rolls	30%	9%	43%	26%	22%
Frozen Vegetables	65%	38%	50%	54%	N/A
Milk	40%	54%	57%	13%	74%
Natural Cheese	35%	N/A	42%	17%	59%
Paper Towels	56%	24%	60%	33%	60%
Toilet Tissue	60%	55%	53%	23%	46%

Source: IRI (2008)

Consumer perceptions of private labels

The IPSOS MORI research based on 3,000 shoppers in France, Germany and Great Britain shows that young shoppers, aged 16-34, are more frequent purchasers of private labels than middle-age and older shoppers. They benefit also from a higher awareness. The research shows also that the percentage of shoppers that claim that they will buy more private labels far exceeds those who claim that they will buy fewer private labels. Shoppers believe that private label products perform as well as manufacturer brands.

Exhibit 7.3 Global Perception of Private Label Brand Quality



Source: Nielsen (2010)

According to the latest Global On-Line Nielsen survey (2010), 37% of global consumers perceive private label brands to be a good alternative to national brands. Twenty-nine percent think the quality is as good as a national brand and 35% believe that some private labels are of higher quality than national brands. The report also indicates that 40% of consumers said that private labels are usually extremely good value for money. Another Nielsen study in 2009 indicates that private label users are heavy buyer people, with large families and children, and the retail brand buyers are not low budget people, but rather affluent and more educated buyers.

Producers of private labels

When private labels were mostly cheap copies of the manufacturer brands, many private labels were made by brand manufacturers, who of course never supplied their best or more innovative products. The motivations of the manufacturers to produce private labels were the following:

- Use idle capacity: When providing products for retailers, this was a good way to increase volume and get economies of scale in the production area.
- Create a better relationship with the retailer: This was a way to improve the contacts with the retailer when the relationships were not easy.
- Prevent a competitor from entering the market: Some manufacturers preferred to provide retailers with private labels themselves rather than see their own competitors do it.

There were of course several risks:

- Loss of market share: National brands may lose market share when private labels have too much success.
- Possible conflict between different departments at the manufacturer: It is difficult to manage internal competition when some are selling national brands and others are developing private labels.
- Price war: If the private label brand has more success than the national brand, there is a danger that the national brand has to reduce its price, which could then start a price war.

Later, more and more manufacturers specialized in private labels, especially when the relation with the retailer became a long-term one, or if the supplier had many customers. As an example, we will consider: Senoble, a dairy manufacturer in France, is supplying a big number of international retailers without having a significant brand of its own. Today, more and more small and medium enterprises are also suppliers of retailers for specialized products, where in the past the door was closed for them.

There are different approaches for the sourcing of private labels: retailers may own factories for a significant number of products, such as Migros in Switzerland; they may have exclu-

sive agreements and heavily control factories, such as Marks & Spencer in Great Britain; they may enter into very long term relations and often audit the suppliers, such as Mercadona in Spain, and they may regularly control product quality.

Similarly, different approaches for buying and the loyalty of retailers to suppliers exist: contracts may be negotiated every year and possibly incur new suppliers (e.g. Aldi & Lidl); retailers may enter very long-term relations with commitments (e.g. Mercadona); or employ a mix of the two, such as Carrefour and Delhaize, who enter long-term relations for a big number of suppliers, but they rely on yearly negotiation for the low price ranges.

Conclusion

Private labels have achieved a high level of share in Europe. The level is much higher than in the US due to major structural differences between the two regions. The growth has been continuous over the last 30 years. This trend started in the 70's with minimum success, was been reinforced in the 90's, and is still in a growing phase today, especially now with the economic crisis.

The situation varies depending on the countries and the categories. Switzerland and the UK have the highest shares in the world, followed by countries such as Germany and Spain. A country like Italy remains at a low level. This is, however, an exception. Concerning the product categories, the level is also very different. This depends on the pace of innovation in the category, the presence or not of strong national brands, and the level of advertising spending.

In terms of branding strategies, the retailers also follow different branding models. Some retailers have mono-lines of private labels while others pursue a strategy with multi-tier private label brands. It is interesting to see that there is not a unique business model in the retailer industry. Different strategies can lead to success. In terms of level of internationalization, there are also big differences. Some retailers push the internationalization level such as Carrefour, while others remain regional like Mercadona in Spain or even local like Colruyt in Belgium.

7.2 Private Labels at Delhaize, Belgium

7.2.1 Delhaize's 142 years of History

Two Delhaize brothers and their brother in law Vieujant founded the Delhaize Frères & Cie in 1867 in Charleroi, in the south of Belgium. With 100 Delhaize-le-Lion stores in 1880, they moved to Molenbeek in Brussels to create a head-office, distribution center and factories. Before World-War II, they had 744 stores of their own and 1,500 affiliated stores all over the country. In 1957, inspired by the USA, they opened the first "supermarket" in Europe. Having 80 supermarkets in 1974, but limited by a new law restricting new openings, they decided to invest in the USA, and acquired a small retailer in North-Carolina, Food Town Stores, who later became Food Lion, a very fast growing company. In 1980, they started a

joint venture with Pingo Doce in Portugal that ended in 1992. In the 1990's, dynamic expansion started in Europe and Asia: Czech Republic in 1991, Greece in 1992, France in 1994, Slovakia in 1998 and Romania in 2000. Also in Asia, the company started in Thailand and Indonesia in 1997 and Singapore in 1999. In 2000, Hannaford in New England joined the group, and later other American regional retailers like Harvey's and Victory's. In 2002, a trial was done in Germany, but it was not convincing. From these countries, some were abandoned, other were strengthened. In Greece, in particular, aggressive expansion by acquisition and organic growth is going on.

Delhaize Group today

Today, Delhaize Group is a Belgian international food retailer with activities in six countries on three continents. Delhaize is listed on Euronext Brussels and the New York Stock Exchange. The current CEO is the great-grandson of founder Jules Vieujant, and the family owns around 20% of the shares. At the end of 2008, Delhaize represented: 2,673 stores, with revenue of 19 billion euros, 467 million euros net profit and 141,000 associates.

The USA represent the largest market for Delhaize, with 1,587 stores and revenues of 19 billion US$ under different banners (store brands) – Food Lion (1,319 stores) and Hannaford being the largest. Belgium is the group's historical home market and has a multi-format network of 789 stores and revenues of four billion euros and 17,000 associates. Greece, with Alfa Beta Vassilopoulos, is now a national retailer with 203 stores, revenue of 1.3 billion euros and 9,000 associates. Romania, with Mega Image, is actually very strong in Bucharest with 40 stores and 1,900 associates. Finally in Indonesia, Super Indo operates 65 stores mainly in Jakarta and other cities on Java, with 4,500 associates. In 2009, Delhaize acquired Prodas in Romania and Korifi in Greece. The latest big acquisition was Delta Maxi Group in Serbia in 2011.

A unique model

Even being an international retailer, Delhaize Group has a unique approach to its markets and companies compared to other pan-European retailers such as Tesco and Carrefour. Different store brands are maintained, national or even local ones (five store brands in the USA), because great value is given to the local market situations and customers, local decision making, local management and local products.

In some cases (Food Lion, Lion Super Indo, Mega Image) only the "Lion" symbol is used besides the local store brand name. This is especially done because the Lion is represented on many private labels that are shared in between the different companies. The group operates a comparably small head-office in Brussels with less than 100 people. On the other hand, there is a high degree of cooperation, synergy and exchange of best practices among all the companies, which makes it a strong, coherent group. The market share evolution of Delhaize Belgium went from 24% in 2000 to 25.7% in 2010.

7.2.2 Development of Private Labels in the Delhaize Group

As the mission of the founders in creating the company was going directly from producers to the consumers, private label has always been part of the genes of the company, as this was and still is another way to cut costs and intermediaries. In the 1880's, Delhaize started importing and producing a wide range of own label products: coffee, biscuits, chocolate from Congo, ham coming from the USA, sponges, soap, brushes, liquors with their own distillery, and wine bottling.

In the 1930's, more "Delhaize" brands were launched, no longer only manufactured by them. For the most part, they were not Delhaize branded, but rather branded with exclusive brands, different by category: Panier d'Or for canned vegetables, Mariana for coffee, Silver King for canned fish and Del Rio for canned fruit. A low price range was also launched, Derby, in response to the crisis and the severe weakening of the population's purchasing power. At the end of 1950's, when Delhaize started to develop supermarkets, the Delhaize brand was strongly expanded, and the other brands slowly abandoned, including Derby. At the opening of the first "supermarket" (one of the first if not the first in Europe), Delhaize redesigned and extended the "Delhaize" branded private label, with the main purpose to increase margins and loyalty.

In the late 1970's and early 1980's, Derby – the "first price" range, was relaunched to fight against the upcoming international expansion of the hard discounters (Aldi) and the lunch of the "Produits Blancs" (White Products) by GB in Belgium. Around 300 products were launched in a very short time from 1978 on. The packaging was very simple and not even attractive. The quality was average. In the 80's, a more offensive relaunch of store-branded private labels was done, but more to increase margins and to reduce the power of multinational brand manufacturers than to differentiate. In 1985, a revamping of Delhaize products with a new uniform design by well-known Landor design company was done; this provided a much higher visibility and penetration of the private label. Still the private label was a copy and paste of the brands, with equal quality, but with prices from 10 to 15% lower. At that time, many private labels were often produced by brand manufacturers at a "marginal" production price. The quality was good, but certainly not better than the branded goods of the same factories.

1990's: from basic needs to added value

Delhaize started innovation with private labels. The evolution of private labels in the UK over many years has been very inspiring for Delhaize; Marks & Spencer, J. Sainsbury, Tesco, and Waitrose have been and are still at the forefront of private label innovation and penetration. Thanks to the easier direct import from other European countries and to diffusion by the media of many new eating habits (Italian, Spanish, British, Japanese, North-African food), there was a large extension of the Delhaize range, with a lot of innovative products and ranges, but still with the same brand and pricing approach. The three pillars were: discovery, convenience and health. Fresh ready meals, mozzarella, Italian and Spanish hams, organic products, and new frozen ranges were launched exclusively under private label, in categories with few or no presence of brands.

Private labels became a real vehicle for innovation and differentiation. The relations with suppliers and the suppliers themselves changed. A lot of small and medium enterprises became private label suppliers from Belgium and other countries, as well as companies who became fast growing thanks to private labels and thus specialized in their production. A strong example is Senoble, a manufacturer for fresh dairy for a large number of European retailers.

2000's

Delhaize was at the forefront of organic food in the early 1990's focusing more on fruit and vegetables. But a more ambitious development of organic products brought them to launch a Delhaize Bio brand in 1998 and it quickly became a well-known brand on the Belgian market. In 2004, a big move was done with the launch of "365", a low price but good quality range (at least as good as the Aldi products) replacing Derby with a more attractive packaging. The range was launched in all the European branches of Delhaize and all the languages were present on the packaging (French, Flemish, German, English, Greek, Czech, Slovak, Romanian...); 365 is much more offensive than the defensive Derby. In 2006, a private label dedicated to Health and Beauty and other "near food" ranges was launched under Delhaize "Care". Naturally, the private label became "multi-tier", not really as a strategy, but because of the need for different brands to make a clear communication.

During that period, there was huge development of European Buying Alliances: Agenor, Coopernic, EMD, AMS and others, regrouping non-competitive retailers from different countries and leading to joint negotiation with brand manufacturers, but more important, to common sourcing of private labels and bi-lateral exchanges of products, ranges and suppliers. Delhaize was part of EMD from 2000 until 2008, and then it joined AMS. Members of AMS are, among others: Migros Switzerland, Ahold Netherlands, ICA Sweden, Morrison's UK, Dansk Denmark, Esselunga Italy, Système U France and Jeronimo Martins Portugal.

2010's

From the end of 2008, a new more structured and clear strategy was born: From the end of 2008, a full review and restructuring of the private labels has on the way, leading also to renaming private "labels" by private "brands". Over the last 20 years, a multi-tier private label was built empirically based on the needs to market different types of products. Some confusion was the consequence, where no clear message came with each product. Today, a very clear role for each private brand is given, for the customer and for the company.

The mission of the new private brands is: "We are supporting and developing strong brands which serve as the reference for consumers by offering a broad and innovative range ensuring the best quality/price-ratio for different consumer needs and different levels of price sensitivity."

All the products have to fulfill the following customer expectations:

- to save money without giving up quality,
- to feel like a smart shopper,
- to discover innovative items and be proud of it, and
- not to feel disturbed or ashamed to show that they buy Delhaize brand products.

A new definition for 'what are private brands' was decided; this was done to harmonize between the group's companies and with retail in general. "Private brands include all products that are exclusive to our stores for an extended period, six months at least." The private brand penetration (or contribution) is the sales of private brand products divided by the sales of all products in the local currency (excluding VAT and prescription drugs). The Delhaize Group definition of private brands seems to be unique from all comparable definitions found, which makes comparisons difficult.

There are mainly six brands, which all respond to the following common goals:

- to differentiate themselves and to strengthen the Delhaize brand,
- to boost Delhaize customers' loyalty,
- to maximize sales and margins (with a penny profit higher than the national brand), and last but not least,
- to give the retailer a higher independence in decision making on assortment, pricing and margins.

All six brands also respect the same rules, i.e. high quality standards, audit by an internal quality team or external auditors, and strict procedures for the selection of the suppliers and the products.

Delhaize mainstream

Products under this label offer to the customers a wide variety of private label quality products with the best quality/price ratio (great value). Customers see the Delhaize brand as a range of trustworthy products with a quality equivalent to leading national branded product and cheaper for the same quality. The products are selected from the world's best producers, with a demanding "cahier de charge" for quality, applied on all products. Besides that, there are innovative products you cannot find anywhere else and they are available at reasonable prices and not "gourmet" ones. The target audiences are consumers who are aware of the fact that you can get the same quality as national brand products at a lower price. It is more a matter of state of mind than an economic need. The pricing strategy is to be at least 15% cheaper and in line with the price of the competitors' private label products. If there is no comparable national brand product, the product will be at "a good price level for its category".

Delhaize bio

The objective is to offer customers a wide variety of organic quality products from the private label with a great value for money. The attributes of bio products are:

- Responsible: A responsible choice towards nature: products originating from environment-friendly production and agriculture,
- Healthy: Organic products suggest a healthy choice,
- Taste: "Bio" product have the pure taste customers expect from organic food,
- Contemporary: Organic products fit in with a modern way of living.

The suppliers have to be certified "bio" suppliers and are audited by an independent instance. If possible, they use environmentally friendly packaging. The consumers of bio are concerned about the environment (man, animal, agriculture) and/or have adopted a healthy lifestyle. The certified "bio" quality products are sold at an affordable price: more expensive than conventional products but cheaper than "bio" national brands. The consumers feel that they don't have to pay too much for bio products and that they contribute to the well-being of their family and respect the environment.

This penetration seems very low, but it is even higher than in most European countries. The exception is Germany, where some retailers have a much higher share of bio. An example is Tegut, a 300 store chain in central Germany, where bio is represented in a large number of categories up to 20%. Traditionally, German consumers are much more sensible to organic food.

Delhaize Eco

This range offers the customers a wide variety of environmentally friendly quality products with a great value for money. They want to provide an answer to the growing concern of customers regarding impact on environment. The attributes are:

- Responsible: Limiting the impact of production and consumption on the environment, and
- Contemporary.

Ecological products fit in with a modern way of living and respond to the growing awareness regarding the impact one has on the environment. The suppliers are certified eco-friendly suppliers and are audited by an independent instance. The packaging has to be as eco-friendly as possible. Their consumers are concerned about the environment and the impact their consumption has on the environment. The pricing strategy is to be more expensive than conventional Delhaize products but at least 15% cheaper than ecological national brands and in line with competitors' price.

Delhaize Taste of Inspirations

This new brand and range, already existing in sister-company Hannaford (USA), is to offer customers a range of unique products of superior quality. The attributes are:

- Gourmet: A range of products of superior quality and great taste, especially designed for food lovers,
- Originality: The unique Taste of Inspirations products take customers through a real sensory discovery,
- Authenticity: Original products, based on authentic and delicious recipes and with high-quality or unique ingredients.

The products are selected from the world's best producers. They are unique, of superior quality and are very innovative products. The target audiences are consumers that are looking for superior quality food products and/or that want to discover new flavors. The prices are in accordance with the product's quality yet affordable. The consumers buy these products to indulge themselves with a quality and very tasty product.

Delhaize Care

This brand and range offer the customers a wide variety of private label ranges of non-food (or "near food", meaning non-food related to food or to what is related to food shopping) products comparable to national brands, offering quality products with the best quality/price ratio. The attributes are good quality and great value: at least 15% cheaper for the same quality than the comparable national brand products. They aim to be contemporary with an attractive modern look and create emotional feeling, generate warmth in the heart of people. They are stylish and functional products. They include body & beauty care products and some textiles. They can also be innovative items on the market with a price at a reasonable level. The target audiences are consumers who are aware of the fact that you can get the same quality as national brand products at a lower price. It is more a matter of state of mind than an economic need. In these categories, especially among the strong brands in health and beauty, private brand has still a weak position.

Delhaize 365

They offer the customers a range of basic products to respond to basic consumer needs of a modern family, as an alternative to hard discounters basic products and at a discount price. Their attributes are:

- Economical: 365 stands for affordable and valuable products,
- Minimal basic quality.

The target audiences are customers who are budget-sensitive and who are looking for the best prices for basic products. The pricing strategy is defined by the competition. If the product is available at Aldi, the Aldi price will be applied; if not, the price will be the same

as the main other discounter. The main consumer benefit is to stick to a tight budget.

The evolution of total contribution of private brands to sales went from 55.80% in 2006 to 59% mid 2011.

Private brands by category

Penetration of private brands is extremely different by category; it may vary from 99% in fresh fruit and vegetables and meat, 45% in some frozen categories like potatoes, 25% in grocery, 15% in fresh dairy to 5% in health and beauty care. It depends on the consumers' addiction to the brand, trust in the Delhaize brand, habits, and marketing by the manufacturers.

Suppliers of private brands

The relationship and procedures are very different with the private brand suppliers than with the brand suppliers. If for the latter the intention of best buying conditions and margins are the essence, for private brand suppliers, a much larger set of criteria play a role, and can lead to more long-term and collaborative relations. A large number of small and medium enterprises are suppliers of private brands. Even in some cases, preference is given to local (Belgian) manufacturers. Full transparency is key to building loyal relations. But for many Delhaize mainstream products, and especially for 365, the sourcing via tenders through the AMS Buying Alliance is the rule. The common sourcing with other Delhaize Group operating companies and bilateral collaboration/negotiation with other AMS-members (Système U, Esselunga, Albert Heijn, Migros, etc...) are also very often ways to source the products.

Marketing & Communication

The marketing plans for the private brands are driven by the marketing strategy of the banner. The base for the marketing of a private brand is the commercial plan, which gives commercial activities every week and every season of each year, the weekly shopping being considered as the most common behavior of the customers, and the season influencing the way customers shop. Every week, the link is kept; every season, the accuracy of Delhaize's offer is reinforced. A specific commercial plan for the private brands is developed and implemented:

- In-store communication: head of gondolas, special displays, tastings,
- External communication: weekly communication in the national newspapers,
- Direct mail,
- In-house magazine (Le Lion) every month or quarter,
- Internal Communication: A significant visibility is given to private brand products to all associates via all available channels: Delhaize News and IntraNews.

Private Labels at Alfa beta Vassilopoulos in Greece

Alfa Beta has a very similar strategy in private labels as Delhaize Belgium. Six brands are part of the private labels: Alfa Beta, Care, 365, Alfa Beta, Choice for chilled products, Alfa Beta Close to Greek Nature and Alfa Beta Bio. The contribution to sales is now close to 20%, the highest in Greece if we don't consider the hard discounters.

Private Labels at Mega Image in Romania

The strategy of Mega Image is slightly different and more adapted to an emerging country, even if, in Bucharest, consumption patterns are evolving very quickly to European standards. There is no Mega Image private label, but the European 365 brand is their mainstream private label. Around 400,365 products represent 10% of the total assortment. To offer more affluent customers of Bucharest a wider choice, they have added 400 Delhaize private labels, 300 "Near food" products under the European care brand, 100 Greek Alfa Beta's private labels and 60 Bio Delhaize private labels. The total private label sales represent 12% of total sales, double that of 2007.

7.2.3 Conclusion

Delhaize Europe is an important player on the private label market, with strategies well adapted to their local market, but also with a lot of exchanges in between the different companies of the group. In the future, all those private labels will be more and more European as soon as a proper and efficient supply chain is working to ensure quick and cost-effective transportation between the different regions of Europe. The Delhaize Europe Private Label strategies are on the way to giving the American companies strong private label development as well. Delhaize's strategy is a current winning strategy, but other – very different – strategies are winning as well. It is crucial to give clarity, externally and internally, to the chosen strategy.

Student Assignments

1. What are, in your opinion, the market conditions that enable successful development of private labels in Europe?
2. Do you think, based on the European experience, that the US private labels could grow to a similar extent?
3. What can explain the big difference of private label development per product category?
4. Given the information form the case, do you think that six different types of private labels can generate extra growth?

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8 The Consumer as a Co-Producer and Prosumer: Convenience Food Marketing

Sigurd V. Troye, NHH Norwegian School of Economics

Magne Supphellen, NHH Norwegian School of Economics

Alexander Jakubanecs, Institute of Economics and Business Administration

> "Our Toro-brand is facing competition on several fronts. First, our dinner kits and other bases are competing with convenience food like frozen pizza, TV-dinners and other ready-to-heat meals offered by other manufacturers. Second, we are to some degree competing with food-interested consumers who seek authenticity and self-fulfillment and – at least from time to time – want to indulge in the luxury of preparing meals from scratch. For some of our customers, ready-made solutions like dinner kits may even compete with fast-food restaurants and student cafeterias. Health concerned people may – sometimes for the wrong reasons – prefer fresh food and other types of convenience food to our products, which are mostly based on dehydrated food."
>
> ***Stang Volden, Chief Marketing Officer at Toro***

8.1 Background

The history of the Toro brand and Rieber and Son can be traced back to 1839 when Paul Gottlieb Rieber founded a vinegar factory in Bergen, Norway. Since then, the Rieber and Son group has grown into a major food corporation nationally and internationally. The company now owns 25 brands, employs 1 200 employees in Norway and 2 400 internationally with manufacturing facilities in Norway, Sweden, the Netherlands, Poland, the Czech Republic and Russia. Through export it serves consumers and industrial customers in 16 more European markets. In a typical full-assortment food store in Norway, more than 500 food items will be from Rieber & Son; in the Czech Republic, the number is 300. The Toro-brand operates in the convenience food market. The brand name was registered in 1946 and two years later it launched its first product, Toro Kjøttbuljong – Toro Meat Bouillon – a beef bouillon cube. Toro Meat Bouillon was gradually built into one of Norway's strongest brands in food products. In 1964, Toro created another national bestseller – Bergen Fish Soup. The dehydrated powder-based fish soup was one important addition to the gradually growing convenience categories and it has become one of Toro's best-selling products over the more than 40 years that have elapsed since its introduction. Both Toro Meat Bouillon and Bergen Fish Soup have become signature products of the Toro brand. Building on its initial success, Toro has evolved into a producer of dehydrated-powder based soups,

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sauces, stews and casseroles in addition to pasta dishes, spices and bouillons. They also offer a variety of products that are not based on dehydrated powder, such as ready-made sauces.

8.2 History of Convenience Food

Convenience food has a number of different definitions and connotations. According to one definition, it refers to "any packaged dish or food that can be prepared quickly and easily such as by thawing or heating" (www.thefreedictionary.com) and – we might add – simple operations such as stirring and frying. Any food solution that reduces customer effort relative to what a similar home cooked dish or meal made from scratch would require can thus be classified as convenience food. The various solutions differ both in substance and technological base and include:

- TV-dinners that can be heated and served,
- Delicatessen – or ready-to-eat food, takeaway food intended to be eaten off the premises, and
- Ready-mixes or commercially packaged solutions containing all ingredients needed for consumption.

Most of the Toro convenience food is based on dehydrated meats, fish and or vegetables. The origin of dried food dates back to Mrs Dubois and William Cookworthy of London who, in 1756, won a contract with the Royal Navy to produce "portable soup" made from reduced, degreased and dried stock. In fact, most of the foundation of modern convenience food includes products and technologies developed for the military to fill its need for storable, portable and easy-to-prepare food. A method for canning food was thus invented in 1809 by the Frenchman Nicolas Appert in response to a request by Napoleon Bonaparte who offered a prize competition for a method to preserve food for the army. Appert opened the world's first canning factory in the French town of Massy in 1804 (five years before his invention was officially acknowledged) and is also credited for having invented the bouillon cube in 1831, which almost 80 years later in 1904 was first commercialized by Maggi. Modern convenience food started after World War II in the United States. After the war, many commercial food companies, being left with surplus manufacturing facilities, developed new lines of canned and freeze dried foods that were designed for use in the home.

The tension Mr. Stang Volden refers to in the opening vignette is demonstrated by the historic development of the food industries with respect to inventions of food products and advances in new business concepts, logistics, marketing and technologies. The advent of fast food restaurants, such as McDonalds, Kentucky Fried Chicken and Pizza Hut in the late 1940s, 50s and 60s, allowed families convenient alternatives to homemade meals. The commercialization of different types of convenience food (e.g. frozen pizza, bread, pasta, instant coffee) provided reasonable alternatives to fast food restaurants and convenient alternatives to more elaborate meals prepared at home. The introduction of tools and equipment (e.g. refrigerators, espresso makers, bread making machines, and food processors) on the other side facilitates consumers' self-production of meals and dishes that can

also be purchased ready-made or eaten in restaurants. The growing number of cooking shows on TV from the 1940s, new food magazines, and later, Internet sites and chat groups for food, have also contributed to the knowledge base and motivational support needed for consumers' self-production – consumers' active involvement in producing meals and dishes. Convenience food, ranging from more or less complete dinner kits to individual side dishes, can compete with "old fashioned" home cooked meals as well as facilitate self-production by simplifying some of the operations needed for a complete meal.

Convenience food, e.g. dinner kits, can mean different things to different people. To housewives, dinner kits can be a convenient way to save time and effort rather than preparing food the traditional way. To students and other one-person households, dinner kits can be an economic alternative to eating in a restaurant or cafeteria. What role convenience food plays for consumers will most likely be different from one market to another, reflecting the prices of eating at home relative to taking meals at restaurants.

Criticism of the food industry

The increasing trend of convenience has been criticized for a number of reasons. Critics have been critical of using single serve packaging and plastics that cause environmental concern both with respect to how it is produced and transported and how it contributes to solid waste. Health organizations have drawn attention to the high levels of salts, fats, additives and preservatives in some of these products, which can contribute to obesity and other health problems. This criticism may not be entirely valid for all types of convenience food. Thus, food based on dehydration will typically require elimination of fat (that otherwise might oxidize); this allows the manufacturer to eliminate the use of additives for conservation.

However, the food industry in general and the convenience food industry in particular have been criticized for their use of the taste enhancer monosodium glutamate (MSG), which by many is believed to cause health problems especially for people supposed to have developed an intolerance to MSG. The main component of MSG, glutamine acid, is naturally occurring in proteins. A human body weighing 150 thus consists of about 1.8 kilos of glutamine acid, and mother's milk has a particularly high content of it. Furthermore, according to several reports (Freeman 2006; Geha et al. 2000), no statistical association between the intake of MSG and a number of alleged MSG-induced symptoms has been demonstrated under controlled conditions.

Other criticisms claim that convenience food corrupts food culture. In 1986, the Arcigola association was formed in Piedemonte to defend the Italian wine and food heritage (and to protest the opening of a McDonald's near the Spanish Steps in Rome) by promoting "slow food" (symbolized by a snail). This local initiative has spawned an international movement that (as of June 2010) includes 100 000 members with chapters in over 132 countries (including Norway). The movement promotes "taste education", educates people about the risks of fast food, is lobbying for programs to preserve family farms and organic farming and encourages ethical buying.

8.3 Recent Food Trends in Norway

Norwegians spend less time in the kitchen than most other nationalities on the European continent. Less than 40% report (2009) spending more than half an hour making dinner mid-week, whereas between 50 and 60% spend more than half an hour each day during the weekend. Time spent preparing dinner over the weekend has been fairly stable over the last decade, but time spent mid-week has dropped. The success of Norwegian chefs in Bocuse d'Or and other international food championships over the last 10-15 years has spawned a fairly high interest in cooking and close to 60% in the survey claim to be "very interested" or "quite interested" in cooking. Most dinners are eaten at home (on the average between 280 and 290 days per year) and, on the average, only 10-12 times in restaurants. The age group 20-24 spends almost four times as many days per year eating their dinner while they watch TV than persons in the age group above 60. Norwegians' use of cook-books has remained fairly stable over the last decade (close to 60% report using one frequently), and a moderate drop in the readings rates for magazine articles on food has been more than offset by a sharp increase in the usage of the Internet; seven times as many (more than 40%) reported (in 2009) using the Internet for recipes on a regular basis than eight years earlier. With increasing obesity and occurrence of diabetes II in the Norwegian population, more and more people are concerned about their intake of fat and sugar and – to some degree – carbohydrates. Vegetables demonstrate increasing popularity particularly among women. However, the willingness to pay a price premium for ecological products has declined (between 40% and 50% would not pay a premium in 1999).

While the dehydrated food products offered by TORO until recently have demonstrated increasing popularity, the sales of dehydrated food products in general have been fairly stable over the last 10 years in Norway. Dehydrated sauce-bases are, according to an ongoing panel study, used at a steady average of about 30 times per year, and the demand for powder-based side dishes has also been stable (average usage rate of 10-12 times yearly). Kits for casseroles and stews have furthermore shown a fairly steady usage rate of about 15 times a year, whereas dehydrated soup bases have declined from well above 20 times to about 15 times.

White meats (chicken, turkey) have become much more popular over the last 10 years. One example is the usage rate per year for chicken filet, which has almost quadrupled from 1999 to 2009. This trend might reflect another trend: The concern for fat and obesity. Soup, as a dinner dish, has declined in popularity, whereas oatmeal porridge as a dinner dish has had a remarkable increase in weekly usage rates. Homemade pizza has increased in popularity over the last decade (usage rate of about 15 times a year in 2009), whereas other delivery modes (carry-out and frozen) have declined in popularity. This trend might have been facilitated by the availability of ready-made pizza crusts and pizza kits. Fresh convenience food and ready-made dishes purchased in food stores have become more popular over the last year, most likely at the expense of deep-frozen alternatives that have decreased in popularity in the same time period. Both rice and dried pasta have shown a remarkable increase (about 30%) in usage frequency per year over the last 5-10 years; this reflects a gen-

eral increase in popularity of Asian and Italian food. The high popularity of ethnic food is partly explained by Norwegian vacation patterns and the presence of ethnic food restaurants (e.g. Chinese, Indian and Italian). Norwegians have a very high loyalty to domestic food brands; this partly explains why the German food chain Lidl's venture into the Norwegian market failed. Within less than four years of operation, they sold (March 2008) their 50 Norwegian stores to the domestic Rema 1000-group.

8.4 Rieber & Søn and Toro's Product Portfolios and Strategies

Rieber & Søn entered a particularly vibrant phase in the development of its food business in the early 1990s when it made a number of national and international acquisitions, particularly in Central and Eastern Europe. Many of the acquired brands have gradually been integrated with the operations of Rieber & Son. The Norwegian brand, Mr. Lee (Asian noodle dishes), was bought in 1996 followed in 2003 by the acquisitions of Nopal AS – the producer of Ming and Geisha – brands of rice products, Black Boy – a brand of spices, Trondhjems – a brand of canned food, and Sopps – a brand of pasta. In 2004, a Swedish brand of Asian food, Mrs Cheng's, was acquired. All of these brands have been integrated into the Rieber & Son's business division. Toro's operations have also been coordinated with the operations of the Czech company Vitana (acquired in 1992) and with the Polish company Delecta (acquired in 1996).

One of the strategic pillars is to acquire, develop, and strengthen national brands and achieve synergies through joint product development and procurement (e.g. of packaging concepts). As a non-EU member, Norway has high customs and taxes on meat and produce to protect domestic producers; products with such contents will be subject to high tariff rates. For this reason, it is virtually impossible to achieve synergies of production by outsourcing manufacturing of products in the Norwegian product portfolio to Rieber & Son's foreign subsidiaries. Most products in the Toro product line are consequently manufactured in Norway. Many of the products in Rieber & Son' portfolio are due to acquisitions, but Toro has developed a strong corporate culture of continuous innovations in product development and brand building. For instance, the company was the first in the Norwegian market to launch a Lasagna mix. In addition, Toro was among the first to introduce Asian food to the Norwegian public by launching an Oriental Casserole as early as 1975. Because of the company's knowledge of the market they serve, combined with strict quality control, new products offered by the Norwegian branch of Rieber & Son have an average survival rate of 6.5 out of 10 – a remarkably high score for the industry.

In 2000, a new corporate strategy was adopted by the board of Rieber & Søn under the title "The Local Taste Champion". The new strategy emphasized greater adaptation of the company's products, including Toro's, to the local consumer taste in each international market. The strategy would be a central element differentiating branding strategy such as Toro from the multinational food brands of e.g. Unilever or Nestle. Furthermore, continuous focus on product development and brand building has resulted in annual organic sales

growth of 9% in the last 25 years (data from 2003). Today, Toro is a very strong brand in the Norwegian market with over 250 products in its various categories. Every year around 50 new products are launched; 30% of the turnover comes from products launched in the last ten years.

The product development strategy of Toro is characterized by a rapid cycle of revitalizations and new launches. Some highlights of the development of Toro reflecting this strategy over the recent years are the following:

- Toro Gourmet Pasta Sauce was launched in 2001 in four varieties. In the same year, a series of gluten-free products were launched as well as Toro Brownies mix.
- A series of seven pasta and Asian sauces in glass jars were launched in 2002.
- In 2003, Toro Wraps were launched in Norway; these are a combination of wheat tortillas, marinade mix and dressing mix. Tortilla Wraps have been selected as one of the most successful new launches of the year by AC Nielsen.
- Toro was selected as "Supplier of the Year" by the Norwegian retail chain Norgesgruppen in 2003.
- A series of in total 25 Asian products were launched in 2004, e.g. Indian, Chinese and Thai dinner kits. The Toro Wraps were launched onto the Swedish market using the marketing communications used earlier in Norway.
- A Toro barbecue sauce series as well as Boil-In-Bag rice and Pizza Pronto – pizza dough were launched in 2005. The company started putting more emphasis on convenience in developing new products to counteract the growing pressure from private labels.
- Toro launched a new series of frozen meals ("Velbekomme") in 2006. Toro's signature series "Rett-i-koppen" ("straight-in-the-cup") was developed into a new product type – Soup-To-Go in plastic microwavable cups.
- In 2007, Toro launched a new product type – Toro Menuett frozen cakes, building on the expertise of the acquired Swedish cake manufacturer Frödinge. The Norwegian series Velbekomme was launched in Denmark. The new communication concept "Good Food is Important. Regardless." was introduced to make the brand more focused and relevant for consumers.
- An extensive corporate change program was launched in Rieber & Son in 2008 under the new leadership focused on making the supply chain more efficient, focusing on core activities and on product innovation. The new strategy implied a significant change from the original strategy of Rieber & Son by diversification of risks through investment in different, sometimes loosely connected industries. The new strategic initiative had profound consequences for Toro's operations. A new record in market share for the Velbekomme series was set in 2008. Finally, the new Tandoori Chicken Casserole variety was launched in the Velbekomme series.
- The soup series "More of the Good Stuff" was launched in 2009, including Rich Provence Chicken Soup – a thicker soup variety with healthier ingredients.
- On their homepage, Toro brought up the issue of Monodium glutamate (MSG), the flavor enhancer commonly used in dehydrated food. Despite the lack of scientific, empirical evidence regarding its alleged detrimental health effects, Toro stated that the

company would stop using the additive in new products and would gradually phase out its use in existing products.

The overall strategic goal of Rieber & Son in the years to come will be a combination of top line bottom line improvement. The recipe is profitable innovation and further development of brand equity in established brands. A key strategic concern is how to position their most important brand, Toro, in order to attract the modern consumer and strengthen brand equity. A core issue in this discussion is the role and impact of self-production. When the brand was launched, self-production mainly served the purpose of saving time and money. The standard of comparison was homemade meals based on fresh ingredients. Thus, self-production facilitated by Toro stimulated perceptions of convenience. Toro enabled consumers to spend less time in the kitchen. Consequently, until 2006, the brand essence defined by the marketing department was "Toro cooks good food for you". However, to the modern consumer, self-production in the food domain may serve multiple purposes, including self-expression and customization. Recent research sheds light on the psychology of self-production and its implications for branding of convenience food products.

8.5 The Toro customer as a prosumer and the possibility of "I-made-it-myself-effects"

Products offered by Rieber & Son and the Toro brand more specifically range from solutions that hardly need any activity on the part of the consumer (other than heating) to multi-step kits that require some customer effort and allow individual adjustments by the consumer. In addition, some of the products (e.g. spices, pasta, and sauce bases) target customers who prepare food more or less from scratch. Thus even consumers of convenience food are to some extent active producers.

According to Xie, Bagozzi and Troye (2008), marketing and consumer behavior literature has, however, traditionally limited its attention to what consumers purchase, and has not been concerned with what they do with the products they buy. This artificial separation of production and consumption, which undergirds contemporary economics and marketing research (Firat and Venkatesh 1995), implies that the consumer is not considered a creative actor in the value creating process but rather a passive responder.

The emergent "service-dominant" logic suggested by Vargo and Lusch (2004) challenges the view of buyers as passive consumers and includes buyers in the value creation process by asserting that the customer is always a co-creator of value (Vargo and Lusch 2004, 2006). In this perspective, goods (e.g. a piece of meat or dinner kit) acquired in the market place are merely intermediate products that are used by customers to create value (e.g. nutrition, psycho-social benefits, relaxation). In the present context, consumers use their competence (e.g. cooking skills and health knowledge), tools (e.g. food processors), raw materials (e.g. potatoes and dinner kits), and sometimes professional services (e.g. cooking classes) to produce meals. The realization that consumers are actively involved in creating value and benefits for their own consumption is aligned with the concept of the "customer as a part-

time employee" (Bowers et al. 1990) and is consistent with the notion of "prosumer" (i.e. as one who pro-duces and con-sumes, see Toffler 1980; Kotler 1986). Prosumption implies that buyers produce products (e.g. food dishes) for their own consumption. A growing body of literature is challenging the rather limited perspective of the customer as value destroyer rather than value creator. The emergent orientation towards consumers as active value creators reflects a confluence of theoretical and methodological advances on one side and trends and developments in society and marketing practice on the other. Thus, outsourcing of certain aspects of production and delivery to customers (e.g. like having them slice the ham themselves), increasing availability of advanced household tools (meat slicers, steam ovens, etc.) and increasing discretionary time are some of the factors that pave the way for consumer value creation.

From one perspective, prosumption-like behavior is not new. Most products require some activity by consumers to provide value: Chewing gum needs to be chewed and cars need to be driven, maintained, and serviced in order to provide the desired benefits. Likewise, food items intended for a meal have to be assorted, combined, transformed, and presented in order for the nutritional and psychosocial values of various kinds to be produced. One could say that prosumption is not so much a new phenomenon as it is a new perspective of the role of consumers.

Which are the implications of prosumption for manufacturers of convenience food brands such as Toro? Let us first ask why customers might be willing to assume more responsibility for production than they have to. Why should they cook themselves rather than using catering or restaurant services? One reason is the cost of using professional services relative to the alternative cost of their own labor – homemade meals are cheaper than a restaurant meal in most countries. Another justification is that self-production may allow customization to the person's own needs and desires. Thirdly, people can seek self-expression through producing their own products and experiences as a matter of pride, self-identity enhancement (Holt 1995), and self-fulfillment. Fourthly, some may simply enjoy cooking whether the outcome is good or bad. A fifth reason is transparency and authenticity (see Supphellen and Troye 2008; Troye & Supphellen 2010) as consumers can verify the contents of dishes they make themselves, rather than having to trust the manufacturer.

Beyond its potential impact on the objective quality of the outcome, prosumption can have psychological effects on the evaluations of the outcome as well. Thus consumers may perceive and evaluate the same outcome (e.g. a dish) differently depending on whether it is made by themselves or by somebody else. There are several reasons why such effects may occur: One is that experience-based information (e.g. sensory information like taste) is ambiguous and therefore has the potential of becoming biased. Another reason is that self-production can increase the consumer's sense of "psychological ownership" (Beggan 1992; Fuchs, Prandelli and Schreier 2010; Mittel 2006) and thereby lead to inflated perceptions of self-produced outcomes.

Although most commercial products require some productive activities by the consumer, marketers typically have some flexibility with respect to how much productive effort is

required or possible. Thus, cake mixes may not require the addition of eggs or a casserole mix may not necessarily call for extra red wine or cream for an optimal result, but manufacturers may still suggest or recommend such additions in order to increase the consumer's sense of "ownership" with regard to the dish.

There are several potential strategic consequences of outsourcing part of the production to the customer. First, one obvious consequence is that it increases customer effort and hence to some extent decreases convenience – the very reason for offering convenience food. Second, the more the customer is made responsible for the outcome, the more the manufacturer has to relinquish quality control. A third potential consequence is that according to self-serving bias theory (Campbell and Sedikides 1999), consumers may claim responsibility for successful outcomes of their own effort, and attribute failures to the manufacturer. The homemaker may therefore put his or her signature on a successful dish and forget about the brand, which could then possibly reduce the value of the brand. Fourth, to the extent consumers evaluate self-made outcomes (say a meal) higher than similar ready-made meals, this could lead to higher evaluations of the brand used as input as well. One reason for such an effect is that the only basis for evaluating many input products (like e.g. a cake-mix) is the end product to which the consumer contributes him- or herself, or to put it in another way: "The proof of the cake-mix is in the eating."

Some recent empirical studies of customer coproduction suggest that self-production may tend to positively bias consumers' evaluation of the end-result. In a study of Franke, Schreier and Kaiser (2010) consumers who were allowed to design T-shirts, scarves, skis, watches and cell phone covers using mass customization toolkits on the Internet, reported higher willingness-to-pay for self-designed products compared to ready-made alternatives of similar design quality. They found that consumers who took part in their experiment, for example, were willing to pay 6.85 Euros for a t-shirt they designed themselves, but only 4.74 for a t-shirt of similar design quality designed by manufacturer. They furthermore found that a feeling of accomplishment mediated (or explained) this effect. They also found that consumers were willing for pay a premium for a self-designed t-shirt whether the design was of high or mediocre quality (a premium of 4.95 Euros for a high design quality and 1.94 Euros for an unattractive design). In one of their experiments, Franke, Schreier and Kaiser found that willingness to pay a surcharge for self-designed watches was moderated by the amount of freedom that the self-designed kit allowed. More specifically, the more freedom and fewer restraints, the higher the price the consumers were willing to pay (30.34 Euros when design freedom was high versus 19.21 Euros when low). In a different study, Fuchs, Prandelli and Schreier (2010) found that people who believed they were empowered to partake in the selection of t-shirts to be marketed were also willing to pay a premium.

The evidence cited above suggests that consumers might be willing to pay the manufacturer for the work they do themselves when they participate in the design and selection of t-shirts and watches. Can we expect similar findings when consumers produce food themselves using dinner kits? Will for example a consumer who contributes to the outcome by adding ingredients and engaging in a number of activities enjoy the taste of the outcome more than a consumer who just opens the package and heats the content?

8.6 The Tikka Masala Experiment

To examine whether self-production leads to a positive bias in consumer evaluations of self-produced compared to ready-made meals, an experiment was carried out using a Tikka Masala dinner kit offered by Toro on the Norwegian market. The details of the procedure are described below.

To manipulate and calibrate quality, a professional chef prepared two variants of the dish (high and low quality). The high quality variant was prepared as prescribed on the package. To further improve the quality, some cream was added. For the low quality variant, the chef used more water than prescribed and left out some of the coco milk. To increase the difference between the two qualities, some vinegar was added to the low quality variant. In a blind test on four experts and twelve consumers, all participants selected the high quality variant and indicated high choice certainty. Also, all 16 participants agreed that the low-quality variant was eatable (mean=5.4 on a seven-point scale). In contrast to previous research, which has relied on scenarios to manipulate prosumption (e.g. Bendapudi and Leone 2003), we let participants engage in real prosumption by having them take part in food preparation. A professional research company recruited participants randomly from Bergen, Norway (n = 98; 52.4 percent females, mean age: 33). The study used a 2 (low/high quality) by 2 (low prosumption/high prosumption) design. The experiment took place in a laboratory kitchen with eight pairs of ovens. In the low prosumption condition (n = 47), the food was ready-made and participants only heated and stirred the food. In the high-prosumption condition (n = 51), participants were asked to fry meat and prepare the meal as prescribed on the product package (the package contained coco milk and dehydrated sauce and rice). To allow for more creativity and active involvement in the task, we included seven additional spices and instructed participants to use at least three of them; the spices were selected by a gourmet chef.

On average, participants used about 25 minutes to prepare the food. Participants were only allowed to taste once during the cooking session. Participants in both prosumption groups were randomly assigned to low and high quality outcomes. Before tasting the food outcome, participants filled in a small booklet of measures on perceived prosumption level (manipulation check) and demographic questions in an adjacent room. While participants filled in this questionnaire, the dishes they prepared were secretly swapped with either the high or low quality food prepared by the chef. Participants were led to believe that they were going to taste the food they had prepared themselves. Next, participants were instructed to taste the food. After the taste session, participants responded to a questionnaire with their initial thoughts regarding: tasks, evaluation of the outcome, evaluation of the Tikka Masala kit, perceived taste quality, product domain (cooking) involvement, and the degree to which the respondents attributes the outcome to themselves. Product domain involvement was measured by three items (very interested in food, spend a lot of time on cooking, spend a lot of money on cooking). In the thought-listing task, participants listed up to six thoughts that came to mind when tasting the food. Upon completion of all tasks, participants were debriefed and awarded 40 Euros.

Table 8.1 Mean Scores for Outcome Evaluation

	High Involvement		Low Involvement	
	Low Prosumption	High Prosumption	Low Prosumption	High Prosumption
Low Quality	3.1	5.5	4.8	3.9
High Quality	5.0	5.6	5.1	5.3

Results are shown in **Table 8.1** and **Table 8.2**. As we see in **Table 8.1**, respondents highly involved in cooking who made the dish themselves were more satisfied with the outcome (taste) than those who just stirred and heated (means: 5.5 vs. 3.1 for low quality, 5.6 vs. 5.0 for high quality). For those less involved in cooking, the results are not so clear. In fact, individuals who tasted the low quality version were less impressed when they tasted the version they believed they had made (mean: 3.9) than those who only stirred and heated (mean: 4.8). For high quality there was virtually no difference (5.3 vs. 5.1).

Table 8.2 Mean Scores for Input Evaluation

	High Involvement		Low Involvement	
	Low Prosumption	High Prosumption	Low Prosumption	High Prosumption
Low Quality	3.7	5.6	4.9	3.8
High Quality	5.1	5.9	5.0	5.6

Table 8.2 shows how prosumption affects the respondents' evaluation of the Tikka Masala kit. As we see the pattern is more or less the same as for outcome or taste. Those highly involved in cooking and who made the dish themselves appear to inflate the evaluation of the Tikka Masala kit (means for low quality: 5.6 for high prosumption vs. 3.7 for low prosumption, means for high quality 5.9 vs. 5.1). Less involved respondents that tasted the high quality version had a slightly higher evaluation of the dinner kit when they had actively used it than if they had just stirred and heated it (5.6 vs. 5.0, not statistically significant). We also analyzed the relationship between evaluation bias and tendency to attribute the responsibility to the consumer him/herself or to the Tikka Masala kit. There was no indication that consumers tended to take credit for high positive evaluations of the outcome and to blame the brand and input product for low evaluations. Additional experiments (see Troye and Supphellen 2010) show the same pattern: Self-production tends to positively bias the evaluation of the outcome and input product (the Tikka Masala kit). Furthermore, the brand (in our case Toro) also appears to benefit from this bias.

8.7 Toro and the Competition

Over the last decade, the number of competitors for the Toro brand has grown considerably. This is not due to new brands entering the "convenience dinner" category, but due to the fact that Toro has launched many new products relevant to other need situations. In particular, new products have been launched to compete in the following two categories: "in-between meals (ready in a few minutes)" and "Saturday evening family meals". Major products for families on Saturday evening are pizza and Tex-Mex products (tacos, fajitas, etc.). Santa Maria (Tex-Mex) is a main competitor in this meal situation. Just a few years after the introduction of the Tex-Mex line, Toro had earned a leading position with about 30% of the market preferring Toro products. Because this meal situation is more emotional and often tied to experiences of excitement (watching films on DVDs or family shows on TV), the stronger link between Toro and Saturday evening meals has strengthened brand liking and made the Toro brand more "modern and exciting" (higher score in the 2006 survey than in 2002). Compared to the competitors, Toro scores as high as Santa Maria on "modern and exciting", but somewhat lower on "quality". Lower quality perceptions seem to be related to the core Toro-associations "economical" and "convenient". The strongest determinants for preference in this situation are "taste (the whole family likes it)", "quality", and "modern & exciting".

In the "in-between meals" situation, Toro is present with several of its most easily-prepared products, including soups and spaghetti in small plastic cup portions ready to be heated in the microwave oven after the addition of water (preparation time of 2-3 minutes). The competition in this meal situation is versatile and consists of a number of brands and products ranging from ready-made products such as hot dogs and bakery products to fruits and spread bread. The strength of Toro products is convenience and low prices or a high value/price ratio. The brand scores lower than several competitors, in particular ready-made alternatives, on taste and quality perceptions. Another brand in the portfolio of Rieber & Son, the noodle-brand Mr. Lee, has improved its position in this meal situation. Salient associations to this Mr. Lee are "convenient", "exciting", "youth", and "funny" (referring to the commercials and the brand character – Mr. Lee – a spirited and charismatic Asian-looking endorser and original founder of the brand).

In the traditional Toro meal situation, "everyday dinner ready in 30 minutes", Toro keeps a strong position and is recalled as a relevant choice alternative for about 40% of the market. Compared to 4-5 years ago, "good taste", and "modern and exciting" have become stronger determinants of brand preference in this meal situation. These factors are now as important as "convenience". Toro scores higher than its main competitor, Knorr, on "modern and exciting", and equally high on "convenience" and "good taste". The 2006 survey shows that perceptions of "bad content" (salt and preservatives) now have a weak negative effect on preferences for Toro in the everyday dinner situation.

Student Assignments

The research reviewed above has several important implications for positioning the Toro brand. The strong empirical evidence of positive "I made-it-myself" effects suggests that Toro should provide ample opportunities for self-production. One way of growing the top-line and meeting the new demand for self-production would be to launch new products that allow for greater participation on the part of the consumer. On the other hand, several of the motives involved in self-production are not necessarily congruent with the notion of a convenience brand.

The Toro brand is still strongly linked to convenient solutions for everyday dinner situations (Toro survey 2006). The flagship products most closely associated with the brand are casseroles and soups for dinner meal situations. However, the 2006 survey showed that Toro has become more than a convenience brand. "Ethnic food" and "Saturday evening meals" have become salient brand associations (Toro survey 2006), though less so than "convenience" and "everyday dinners". Moreover, after 2006, several new dinner toolkits and various ingredients for ethnic meals have been launched under the Toro brand. These products are less linked to convenience situations and probably activate other self-production motives than saving time and money. Moreover, the 2006 survey shows that Toro scores higher on "excitement" perceptions than in 2002. While this development may attract some consumers, it may also lead to a common problem for brands with a range strategy: brand opacity (Kapferer 2004). The meaning of the brand could become blurred, thus reducing brand equity.

The value of brands is strongly related to the relevance and clarity of their positioning in the minds of consumers (Keller 2009). Thus, Keller (2009) suggests that brand managers explicitly define points-of-differentiation (POD) and points-and-parity (POP) for their brands. PODs are brand associations (such as "quality of ingredients") that are both relevant for choice and differentiate the brand from those of competitors. Parity associations (POPs) are important factors for choice (e.g. "price") for which a brand scores equally high as competing brands (parity). In addition to company history, company resources, overall corporate strategy, and consumer behavior trends, a primary concern when defining PODs and POPs for the future is the current positioning of the brand compared to the competition.

1. Define relevant points of differentiation (PODs) and points of parity (POPs) for the Toro brand. Explain your choices.
2. Decide which kinds of self-production should be central and peripheral to the Toro brand.
3. Which criteria should be met in order for a product to be included in the Toro portfolio?

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Part 3

Responding to Diverse Marketing Environments and Managing Diversity in Europe

9 How companies organize their European Business: The Role of Regional Headquarters

Bodo B. Schlegelmilch, WU Vienna University of Economics and Business, Department of Marketing, Institute for International Marketing Management

Björn Ambos, WU Vienna University of Economics and Business, Department of Global Business and Trade, Institute for International Business

> **Adidas Group to Create New Organizational Structure**
>
> The [Adidas] group... has decided to take out one complete level of management, the regional office [emphasis added]. This means that going forward the group will no longer operate regional headquarters in Europe and Asia. Instead, it will strengthen the direct interaction between the global organization and the local markets.
>
> To support their own retail business, which is an integral part of the group's controlled space strategy, the group plans to set up a dedicated global retail organization under the leadership of a chief retail officer. The group will also carry out a review of underperforming retail store locations in the coming months.
>
> The restructuring will also see the wholesale part of the business, where products are sold and distributed via retail partners, consolidated under the leadership of a chief sales officer. All group functions such as operations, finance, HR, legal and IT will also undergo changes to reflect the new organizational structure while identifying shared service opportunities to drive further efficiencies.
>
> Although all project details have yet to be finalized, it is management's goal that upon completion these measures will lead to annual cost savings of more than €100 million as well as a contribution to the top line.
>
> ***Published by Datamonitor, 06 May 2009***

9.1 Do Regional Headquarters Matter?

The Adidas example illustrates that regional offices (or regional headquarters) are not uniformly welcome. Indeed, some companies have abandoned regional headquarters all together. In contrast, companies like Citibank see the issue rather differently. In March 2008, it announced the following organizational change: “Citi has established a regional structure

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to bring decision-making closer to clients. It is empowering the leaders of the geographic regions with the authority to make decisions on the ground" (Reuters, 2008).

So who is right: Adidas in abolishing regional headquarters or Citibank in establishing a regional structure? When do regional headquarters make sense? And, from a wider perspective, does a regional strategy make sense?

Below, we are reviewing the arguments supporting regional strategies, showing the interactions between regional strategies and regional structures, and sharing some of our research findings on the role of regional headquarters in Europe. The research was conducted over a period of four years and involved personal interviews with senior managers from Europe, the USA and Asia as well as an extensive quantitative study; for a detailed description of the methodology, please see Ambos and Schlegelmilch (2009). Embedded in this discussion is a case study that we developed on Puma in Europe. Taken collectively, this chapter demonstrates the challenges in aligning strategic objectives and organizational architecture.

Internationally operating companies are constantly striving to find the middle ground between local responsiveness and global synergies. Consequently, the key question is not, whether companies should centrally coordinate all their activities worldwide, but which activities and which components of the products and services they offer should be centralized or decentralized, standardized or adapted. Finding this "right" middle ground involves the design of an intricate mesh of organizational structures and processes in which regional structures and regional coordination and control processes usually play an important role.

There are relatively few scholars who focus on the regional dimension of international business. One such scholar is Pankaj Ghemawat, who coined the phrase "semiglobalization" in his work on corporate strategy. In his view, differences between countries are far larger than generally acknowledged and companies that presume complete integration are emphasizing standardization and scale expansion too strongly (Ghemawat, 2003, 2005, 2007; Ghemawat and Ghadar, 2006).

Other scholars who stress the importance of regions are Alan Rugman and Alain Verbeke (Rugman and Verbeke, 1992, 2004; Rugman, 2005, 2007). In his analysis of Fortune 500 companies, Rugman (2005) points out that even among these large MNCs, over 80% generate more than 50% of sales in their home region. In fact, according to Rugman and Verbeke (1992, 2004), only 2.4% of these MNCs are global in that they derive at least 20% of sales from each of the three triad regions. While other dimensions of globalization should also be considered, notably the globalization of the capital base, the globalization of the supply chain and the globalization of the corporate mind-set (Gupta and Govindarajan, 2004), the inevitable conclusion of these scholars is that a regional strategy matters.

There are also a number of other arguments that underline the case for a regional strategy, namely cultural affinity, limits to economies of scale and scope, the concept of liability of foreignness, the region-centric orientation of management and the sheer organizational complexity of global structures.

The concept of cultural affinity zones was introduced by Usunier and Sissmann (1986). These zones are said to display similar characteristics in terms of language, religion, family life patterns, work relationships and consumption patterns. Adding other factors like the regulatory system, industry structure and competition, marketing infrastructure and the organizational heritage that connect companies to particular regions, it is very likely that differences in the external environments and factors connected to the organizational heritage become more acute when companies cross regional boundaries.

In many industries, such as the car industry, factory automation has lowered scale economies. This enables companies to supply regional and even local markets efficiently (Douglas and Wind, 1987). Moreover, marketing costs, transport costs and administrative and overhead costs may increase rapidly when operations cross regional boundaries (Nachum and Zaheer, 2005). Finally, economies of scale and scope may also be optimized at a regional level, since the transfer of ideas, experience and knowledge is limited by increasing differences between regions (stickiness of knowledge) (Szulanski, 1996; Von Hippel, 1994).

Liability of foreignness is another concept that emphasizes the importance of regional strategies and structures (Zaheer, 1995; Zaheer and Mosakowski, 1997). The key argument posits that there are a series of costs that place foreign companies at a competitive disadvantage. These include costs directly associated with spatial distance, for example the cost of travel, transportation, and coordinating, as well as firm specific costs such as unfamiliarity with and lack of roots in a local environment. While liability of foreignness is clearly present each time a company crosses national boundaries, we argue that liability of foreignness becomes more acute when companies cross regional boundaries. Within Europe, of example, it is easily possible to arrange a face-to-face meeting in one of the capital cities where participants fly in and out at the same day. In contrast, the same would not be possible if participants from Europe, Asia or the US were involved. Even phoning colleagues is more complicated when different time zones are involved.

The regiocentric orientation of management is another argument lending support to the development of a regional strategy. Howard Perlmutter (1969) developed the EPRG framework to capture the worldview of corporate management. EPRG stands for ethnocentric, polycentric, regiocentric and geocentric. In a company with a regiocentric orientation, management views regions as unique and seeks to develop an integrated regional strategy. Where more than one region is involved, the strategic and organizational logic of the company will mainly center on regions. Wind et al. (1973) discuss this issue with reference to the development of international marketing strategies. Similarly, Malhotra et al. (1998) argue for a regional perspective on the grounds that cultural factors still inhibit the development of homogeneous markets. Given the cognitive and emotional embeddedness of managers within a particularly region such as Western Europe, it is likely that managers will find it easier to conduct business in their home region and will mostly also be more efficient and effective in the way they carry out their work.

The organizational complexity of global structures provides a final argument supporting a stronger emphasis on regional strategies. Even very large companies struggle with organi-

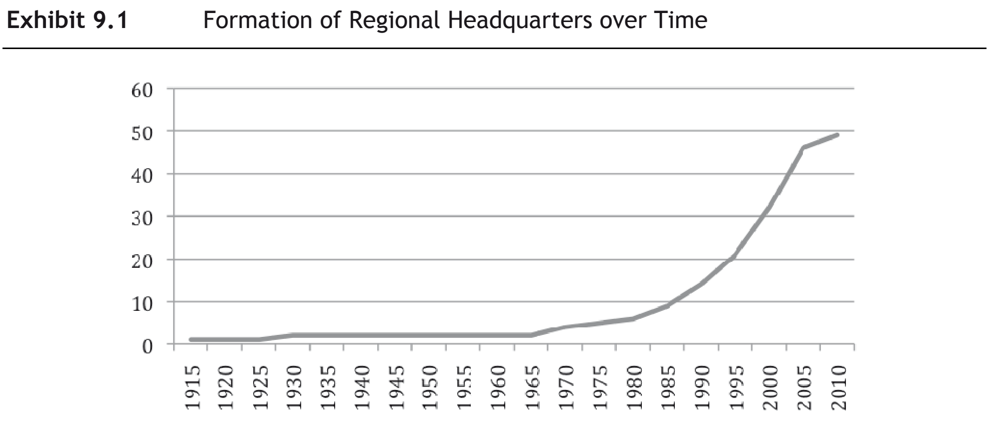
zational complexity. Procter & Gamble (P&G), for example, attempted to shift primary profit responsibilities from four regional organizations to seven global business units ("GBUs"). In addition, the company created seven market development organizations ("MDOs") responsible for implementing global strategies. Yet another dimension was added in the form of a global business service unit ("GBS") that coordinated transactional activities such as accounting, human resources or IT. And to obscure the organizational structure further, specific teams and task forces are woven into the structure (Bartlett, 2003).

For the majority of small- and medium-sized corporations, such examples raise the question of whether or not the potential gains of a tightly integrated global organizational structure are offset by the inevitable organizational complexity. Expressed differently, for most firms there appears to be an argument supporting the development of strong pan-regional structures, while keeping inter-regional structural links at a minimum.

9.2 How Regional Strategy Can Add Value

Evidence from our research (Ambos and Schlegelmilch, 2009) reveals that regional strategy and structure often go hand in hand. In fact, our data reveals a substantial increase in the number of regional headquarters within Europe over the last decade (**Exhibit 9.1**). This data clearly demonstrates that regional headquarters, at least within Europe, have become an increasingly important structural response to dealing with the global-local dilemma.

Exhibit 9.1 Formation of Regional Headquarters over Time



Source: Own Data, RHQ Survey

Being an intermediary located between the global headquarters and the local subsidiaries, for regional headquarters the answer to the value question apparently has two sides. On the one hand, regional headquarters organize the economic activity within the region they are responsible for; as such, they fulfill the classic role of a parent. Consequently, the advantages that the regional headquarters brings to the organization should be similar to that of

other corporate parents. In this context, Campbell and Goold (1995) identify two questions driving such "parental advantage": (1) Does the parent understand the business of its local subsidiaries? And (2) Can the parent contribute to the resource and capability endowment of the local subsidiaries? Parents that neither understand the local businesses nor are in a position to contribute to local operations in any meaningful way are operating in what the authors call "alien territory".

From the perspective of the corporate headquarters, regional headquarters may be viewed as a bundle of unique capabilities that may create superior value for the MNC. Thus, in addition to the strategic impetus dictated by limited economies of scale and scope, regional headquarters have also been found to add considerable value in their own right. In fact, the knowledge advantage of regional headquarters within the region is consistent with the criteria for the parenting advantage spelled out above. To this end, one could easily make a case that regional headquarters are, in fact, the unit with the largest potential to add value because they possess the most relevant knowledge and capabilities to govern the local subsidiaries within a region.

Possessing relevant knowledge is crucial, as much of the knowledge needed to operate globally is local, or regionally bound. Thus, making informed decisions from a distance becomes quite difficult for corporate headquarters. In this respect, regional headquarters fulfill the important mission to translate global headquarters' targets into successful strategies for local markets. Regional headquarters may serve as important competence centers within the corporate network; they provide valuable services to local operations. On the one hand, the regional headquarters receive valuable knowledge on the global operations from the global headquarters and then filter and channel this knowledge to the individual subsidiaries within the region. On the other hand, the regional headquarters take information from local markets and provide the global headquarters with accurate information on the region, which enables the latter to make more informed decisions. Finally, the regional headquarters may add value by transferring knowledge from subsidiary A to subsidiary B and, by doing so increase the performance of all actors within the region (Ambos, Schlegelmilch and Brenner, forthcoming).

Asakawa and Lehrer (1999) pointed out that the intermediary role of regional headquarters may also help to alleviate the tensions between the global needs for integration and local needs for adaptation. In this sense, a regional headquarters may function as an "organizational pressure valve".

In addition to relieving tensions, the intermediary role that regional headquarters play also helps reduce the span of control for the corporate parent. In this way, the regional headquarters help the organization to direct its attention to directions that are most useful for the whole group (Birkinshaw, Bouquet and Ambos, 2007). In large multi-regional organizations, this becomes important as managerial attention becomes a scare resource that needs to be optimally managed in order to avoid dysfunctional priority setting.

9.3 Developing Regional Strategies and Structures

So far, we have made the case for developing a regional strategy rather than a pure global or multi-domestic strategy. Now, we are looking at how managers can actually build successful strategies for a region such as Europe. This involves a number of questions; consider for example: Which countries should be combined into a region? Should a regional headquarters be developed? Should the region be managed virtually or from the home office? How should the region itself be structured? How should the company manage the regional operations?

We will first focus on the structural and strategic questions involved in developing a regional strategy and corresponding organizational architecture and then look at how to manage regional operations.

Defining the Region

Throughout our conversations with managers in headquarters, regional offices, and local subsidiaries, no single question triggered as much interest as how to figure out what should constitute an optimal region. If nothing else, the managerial interest in this "seemingly obvious" question clearly indicates that the common practice to divide the world into three triad markets (North America, Europe and Asia) does not do justice to the managerial problems at hand (Ohmae, 1985). Many companies, for example, extend their European region very far eastwards to include countries like Kazakhstan and Uzbekistan. Quite a number of US MNCs bundle their African and European Business into a so-called EMEA (Europe, Middle East and Africa) region. What constitutes a region to the individual MNC and which countries are managed by the individual regional headquarters is therefore not as clear-cut as it appears.

Our research revealed five defining factors for the scope of a regional headquarters: geographic proximity, market similarities, managerial consideration, political consideration, and cost efficiency. In reality, many of these factors are interlinked and firms take more than one of these factors into consideration when creating their regions. However, for the sake of conceptual clarity, let us present them one by one.

Geography: Few managers we talked to actually organize their regions on a purely geographical basis. This is not to say that geography does not matter – quite the contrary. Grouping geographically proximate markets eases transportation and logistics, which is particularly an issue for firms that sell similar products in multiple markets as setting up a joint distribution center saves costs.

***Market similarity*:** It seems obvious that market similarity should constitute a main driver in deciding which markets to group. It has become custom to define market similarity by antonym distance (see for example Håkanson and Ambos, 2008). Ghemawat (2001), for example, talks about cultural, administrative, geographic and economic distance and relates these distances to the optimal scope of the firm. Where consumer preferences align, a

similar marketing approach and penetration of the region makes a lot of business sense. The existence of common administrative bodies constitutes another reason for grouping similar markets. Within the pharmaceutical industry, for example, jurisdiction and drug approval processes have become vital parameters for firms' considerations of how to structure their global operations. Finally, similarities in the economic development of countries may constitute other grouping criteria for firms seeking similarities within their region. Fast moving consumer goods ("FMCG") manufacturers build their grouping decisions in part on the relative purchasing power of the consumers in the respective markets. This argument holds also for the banking sector, where many banks bundled their CEE operations into one emerging market segment.

Role of Management: While a limited span of control, information processing capabilities and the ability to reconcile conflicts already helped to explain why regional headquarters exist, they arguably reveal only a little about how to structure the regions they create. Managers, however, also use structure to devote attention to specific issues. In this sense, the grouping of markets is very often a reflection of the relative importance or attention headquarters wants to devote to individual markets (Birkinshaw, Bouquet and Ambos, 2007). Nearly all big pharmaceutical companies in Europe, for example, maintain direct reporting lines to the big five consumer markets (Germany, France, Italy, Spain and the UK), while often grouping the other markets into one or two other sub-regions.

Political Considerations: In some cases, our research revealed groupings and allocations that were merely a matter of political considerations. In 2005, for example, Unicredit acquired HBV Group, a German Bank with large operations in CEE that were coordinated and managed from the bank's regional headquarters in Vienna. After the acquisition, Unicredit left the regional reporting structure and responsibilities of the Vienna office largely unchanged with the exception of one market: Poland. National pride on the side of the Polish subsidiary and interventions by the Polish government forced Unicredit to establish a direct reporting line to the Italian headquarters, bypassing the regional hub located in the much smaller Austria.

Cost considerations: Even when firms realize that consumer preferences favor a further fragmentation and adaptation of marketing activities within a region, costs may render such approaches unfeasible. McDonald's, for example, stopped its initial local adaptation of its breadcrumbs formula on its Chicken McNuggets (which used to be coarser in the alpine region), back to a worldwide-standardized product, purely for cost efficiency reasons. Many firms use the same copy of a television advertisement in multiple countries despite the fact that subtle language differences may cause some animosity among some local conscious consumers.

Deciding on the Organizational Structure

To play devil's advocate straight away: It is, of course, possible to pursue a regional strategy without a regional structure. Indeed, there are many examples of firms that manage their regional business successfully without developing a clear supporting structure within

the region. In his article "Regional Strategies for Global Leadership" (2005) P. Ghemawat in fact argues that by centering scholarly investigation on regional headquarters rather than regional strategies, previous research has come closer to studying the wallet than its content. And while Ghemawat has a strong point to make, one should not ignore that even those firms he considers home-base centered do possess a "center" within that region managing the business activity. Thus, in reality we will see only few firms that do not have a structure to support their regional business activities. Samsung, for example, has achieved fairly balanced global sales within its memory chip division without a designated regional headquarters structure (Ghemawat, 2005). Helmut Schütte (1996) calls this form of regional management a "regional headquarters for the region" (as opposed to the alternative which in his terminology would be a *regional headquarters in the region*.) In this setting, the MNC acknowledges the importance of regional differentiation, but the managers responsible for the region sit at global headquarters. Thus, regional management is simply added as a function of global headquarters.

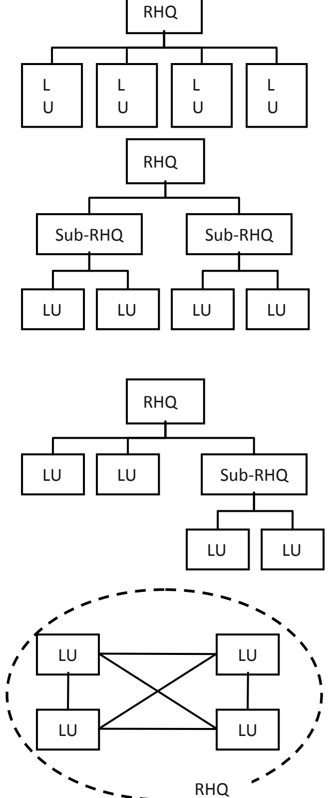
A headquarters for the region has a set of advantages for firms. The most obvious is that firms do not need to duplicate many of the supporting functions in a second physical location. Key functions like human resources, IT and other internal services can be shared with global headquarters operations. Co-location with the strategic apex of the firm also usually ensures a smooth knowledge flow between headquarters staff and regional management.

A latent risk of a headquarters for the region is the apparent lack of market embeddedness that is often closely tied to market knowledge (Andersson and Forsgren, 1996). As customer intimacy becomes important or competitive pressure requires quick reaction, a physical presence in the region becomes a necessity. To this end, many companies decide to build up designated regional headquarters in the region.

However, deciding in favor of a regional headquarters in the region and defining what constitutes "your region" does not solve all the structural issues a firm has to consider. This is particularly evident when multiple considerations need to be taken into account. For example, a common outcome of a company's analysis may be that a region should encompass Germany, Austria, Sweden, Finland and Norway from a market development point of view. Distribution and logistical considerations, however, would suggest splitting the three Nordic countries from the two Germanic nations. While yet again, managerial considerations would imply a separate reporting for Germany, while grouping the rest into one sub-region.

In our research, we found that managers deal with these challenges by selecting a structural option that best caters to their specific problem. The different options are as follows: (A) Single market approach, (B) Sub-regional HQ approach, (C) Mixed approach, and (D) Virtual network structures. **Exhibit 9.2** gives a graphical account of each of the four approaches.

Exhibit 9.2 Four Different Approaches to Structure the Region



(A) Single country market approach
The RHQ acts as a **central hub** for the region.
All local units are only connected through the RHQ (i.e. they have **few linkages** among each other).

(B) Sub-regional approach
The region is divided into **several sub-regions** (i.e. sub-regions are country-clusters of single markets that are linked together).

(C) Mix of single market and sub-regional approach
The region is divided into **single local units** that are directly linked to the RHQ **and** into sub-regions.

(D) Regional / Virtual network
Regional **responsibility is shared** across different countries and functions.

Source: Ambos and Schlegelmilch (2010, p. 74)

In a *single market approach,* all country markets report to one regional headquarters. We found firms to favor a single market approach when the span of control was relatively small, the markets were of equal importance, or consumers were quite homogeneous across the whole region. Asics, for example, sells a set of very standardized products in Europe: running shoes and sports apparel. Given the size of Asics' operations in the market (many European countries are still serviced via independent distributors), a single European headquarters, located in Amsterdam, seems most feasible for the operations at hand.

In a *sub-regional headquarters* structure, country markets are separated and grouped together in homogenous sub-groups that then report to a regional headquarters. We found this approach to be most common in firms with large operations within an otherwise heterogeneous region. Nike, for example, further segments the market into coherent consumer mar-

kets (such as, for example, with Austria, Germany and Slovenia). The objective of all these approaches is to remove variances within the region by grouping subsidiaries with different needs into different sub-regions.

In the *mixed structure approach,* firms place some units into sub-regions while other units maintain a direct reporting line. We found this approach to be the predominant one in unbalanced firm portfolios or in situations where a few markets require special attention (either due to their impact on the bottom line, special development [growth] goals or interests of political stakeholders). In our study on European management, almost all pharmaceutical companies followed this approach.

In the *virtual network structure,* firms do not physically assign a regional headquarters function to a specific location. Instead, the regional management tasks are divided and carried out by the individual subsidiaries in a shared manner. Thus, the headquarters is a mere virtual concept to which the competencies and functions of individual units contribute. The primary benefit of this approach is to ensure a higher engagement of individual subsidiaries given that the structure tries to achieve some degree of regional specific management without adding another layer of hierarchy to the organization. This might be a particular asset for firms with relatively mature country operations, where the establishment of a designated regional headquarters would cause a serious dispute in the existing power structure of the MNC. The downside of this approach, as with all self-organizing systems, is high coordination intensity.

Deciding on the Location of the Regional Headquarters

Economists usually suggest that location of economic activity within a region can be determined by looking at a discrete set of hard (e.g. taxation) and soft (e.g. quality of life) determinants. Looking at regional headquarters within Europe, such a relationship does not hold. In fact, the rank-order correlation between location of regional headquarters in Europe and country attractiveness, as measured by key indicators of the International Institute for Management Development (IMD) world competitiveness index, is close to zero; We used IMD data from the World Competitiveness Index and location information on regional headquarters in six countries to compute a correlation between location choice and competiveness score. This lack of a relationship made us curious to find out what drives location decisions of regional headquarters. In total, our interviews revealed three different motivations: power leverage of individual managers, personal preferences of senior managers and historical accidents.

Power Leverage: For most of the multinational firms we studied, the regional headquarters did not constitute their first engagement in Europe. Thus, with many national subsidiaries already in operation, the decision on where to locate the regional headquarters was not foremost in selecting a greenfield site but, to declare one subsidiary within the region to assume a leadership role and host the regional headquarters. This background might help explain why power leverage of individual subsidiaries turned out to be one of the most prominent location drivers. Limiting the location choice to a set of established subsidiaries,

power levels, such as competence profiles, unit or market size and relationships to global headquarters has become more important than pure economic drivers.

Personal Preferences of Top Management: The importance of quality of life is also a common driver in deciding where to locate regional headquarters. As Jim White, President of Ecolab's regional headquarters, remarks:

"After undergoing an extensive evaluation process to find the ideal location for Ecolab's EMEA Headquarters, we are pleased to have our home in Zurich. Zurich was chosen because of its consistent ranking as one of the best business locations in the world, as well as the outstanding quality of life it offers our associates."

Historical Accident: While personal preferences and power leverage often play a role in deciding on the initial location decision, managers also quite often revealed to us that the initial location decision was nothing more than a historical accident; take, for example, the case of Ford of Europe. When Ford started in Europe, for example, they established their first regional headquarters close to London Stansted Airport. As one vice president (VP) at the regional headquarters points out:

"There was no particular reason for establishing our first regional headquarters in the UK. We had been there for more than 40 years before we decided to move the RHQ to Germany."

9.4 Managing Regional Headquarters

When dividing layers between global headquarters and local subsidiaries, managers at regional headquarters potentially have to deal with severe tensions. Local subsidiaries often challenge the charter of regional headquarters, insisting that they do not need an additional layer of hierarchy dictating what to do. Global headquarters will ask for justification of the performance of a whole region, thus putting regional headquarters under pressure to deliver on their performance expectations; a detailed discussion of these issues would go beyond the scope of this chapter, but it can be found in Ambos and Schlegelmilch (2009). In this context, we merely allude to the various activities commonly performed by regional headquarters (see **Table 9.1**) and counter balance the impression that regional headquarters are only fulfilling administrative tasks.

After discussing some of our research findings on the role of regional headquarters and regional strategy in general, we are now turning to a case study on Puma in Europe in order to highlight some of the managerial challenges involved in aligning regional strategy and structure.

Table 9.1 Common Functions Performed by European Regional Headquarters

Function	Objective	Company Example
Pooling of Activities		
Regional Distribution Management	Joint warehouses to cater to the region or sub-region.	Asics European distribution center in Amsterdam
Regional Marketing	Joint marketing for the region	P&G DACH region
Key Account Management	Central management of key or pan-European customers	Unicredit Banca, for corporate customers in the region
Regional Product Development	Shared R&D Center to adapt or develop products for the European market	Ford's European R&D centers in Germany, Spain & the UK
Back-office Management	Joint human resource and legal services	Henkel's CEE headquarters in Vienna
Regional Manufacturing	Build-up of central plant to cater to multiple markets	Toyota's manufacturing plant in Wales
Regional IT Management	Managing a joint IT platform for the region	Tiffany & Co's IT center in Munich
Coordinating Activities		
Budget Allocation	Financial control and management of budget allocation process	Puma RHQ in Salzburg
Control of Subsidiaries	Ensuring compliance and control within the region	Boehringer Ingelheim
Regional Strategy Development	Developing and adjusting the market strategy for and within the region	P&G European headquarter in Geneva
Regional Benchmarking	Performance and best-practice benchmarking across the region	Boeringer Ingelheim, CEE
Entrepreneurial Role		
Regional Issue Selling to Global HQ	Representing a regional voice in the corporate governance councils	Honda's VP Europe sits on the Board in Japan
Intra-regional Knowledge Sharing	Sensing useful practices in one national market and transferring them to another within the region.	Unicredit Banca, Transfer of practices across the CEE region
Regional Opportunity Seeking	Development of new markets within the region, introduction of new brands/products into the European markets	Henkel CEE, Development of new markets in Asia (i.e. detergent business in Kazakhstan)

Source: Ambos and Schlegelmilch (2010, p. 94)

9.5 Puma and the Virtual Matrix Structure

On 22nd November 2009, the Financial Times quoted a senior manager of Pinault-Printemps-Redoute (“PPR”) saying: “Instead, he (Mr. Pinault) wants the new PPR to become a `lifestyle company´ focused on clothing and accessory brands with two centers of gravity – one at the luxury end around Gucci Group and the other a high volume business built around Puma, the German sportswear company.”

PPR, a French luxury goods retail conglomerate, purchased a 69 percent stake in Puma in 2005. Financial analysts favorably agree that PPR´s potential transformation into a pure play luxury/lifestyle company could create better value for the conglomerate with Puma as one of its main business anchors.

Puma has proven to be a success story. Its corporate philosophy “to be one of the world´s leading sports lifestyle companies” is a pragmatic strategy that began in 1993 under the leadership of Jochen Zeitz. A four-stage expansion strategy was the foundation for Puma´s growth during the last few years. Management´s passion and creativity was possible through their continuous response to market changes. A fluid corporate structure is the crutch that supported Puma´s expansion strategy. How did such a corporate structure evolve? What parameters led to Puma´s virtual matrix structure? What intrinsic role does the regional headquarters have today?

Company Development: The early years

Puma initially began through the efforts of the two brothers in 1924 with the formation of the “Gebrüder Dassler Schuhfabrik”. Its main products were slippers and outdoor shoes. The brothers worked hand in hand, with Rudolf handling the business and Adolf handling the production and technical operations. Within a few years, the Dassler brothers decided to focus entirely on manufacturing sports footwear with emphasis on track shoes and football boots. Soon several top athletes started to wear the Dassler shoes in main sports events. With its new found image, the company grew despite the Great Depression in the late 1920s. It started to sponsor star athletes in order to enhance its reputation, e.g. Jesse Owens, the track star who wore Dassler track shoes in the Berlin Olympics in 1936. By the late forties, the firm was split into Adidas, which became Adolf´s business, while Rudolf set up the Puma Schuhfabrik Rudolf Dassler. From that point, the two newly created companies would be competitors in the sports shoe industry.

The Puma brand would gradually gain recognition with star athletes. In 1950, German soccer players wore the Puma “Atom” shoe at the first international soccer match post-WWII. In the Helsinki Olympics (1952), track athletes wore Puma shoes. The American women’s 400-meter track team wore Puma track shoes when they won the Olympic gold medal in the 1952 games. The soccer star Pele also wore the Puma “King” shoes during the height of his sports career. By the late 1950s, Puma was a brand identified in 55 countries on five continents.

The fast growth led to the formation of a family owned partnership in 1959. By this time, Austria was already the first licensed producer outside Germany. The international export business covered 100 countries by 1962. During the next few years, Puma products were valued for their innovative features such as the "vulcanization" process for soccer shoes. This process "joined the soles to the uppers". All other sports shoe manufacturers were to adapt this new technology in the coming years. Puma also developed a "uniquely shaped sole for running shoes that supported the natural movement of a foot when in motion." Puma was the first sports shoes manufacturer to use the Velcro strap.

When Rudolf Dassler died in 1974, Armin Dassler, his son, took over the management of the company. He had managed the Austrian subsidiary in Salzburg since the early 1960s. The company continued to thrive under Armin´s management and eventually went public in 1986. Innovation was still an essential ingredient for the success of the business. The S.P.A. technology was introduced by Puma in the mid-1970s; this enabled sports shoes with a higher heel thus relieving tension on the Achilles tendon. The Puma Duo flex sole, developed by Armin Dassler in 1982, allowed the foot better mobility using special slots. In 1989, the Trinomic sport shoe system, which cushioned the runner´s foot with hexagonal cells between the sole and shoe, was introduced. The Puma brand continued its momentum as star athletes in tennis, track and football wore Puma products. Despite its strong brand name, Puma´s net earnings gradually declined during this period. The Puma brand's athletic footwear still had high brand name recognition, but fifty percent of sales originated from the lower priced range footwear sector. Product innovation required research and development costs. Marketing expenses for new footwear models further diluted profit earnings. The result was low product margins and negative profit for almost a decade.

By 1991 Puma International was founded. This served as the holding company for Puma´s operations in Australia, Austria, the Far East, France, Germany and Spain. Each area was independent of the other. In the same year Proventus, a Swedish conglomerate, purchased Puma´s outstanding common stock traded in Frankfurt and Munich while injecting DM 50 million of fresh capital.

Similar to Adidas, Puma repositioned itself by focusing on the high end, premium priced footwear markets. Its main competitors became Nike and Reebok. This change in marketing strategy resulted in further financial losses as well as decreased sales. Market share position likewise decreased for Puma in the early 1990s. In addition, new product innovations such as the Puma disc further deteriorated Puma's already weak financial position.

The Four-Phase Business Strategy

There was an urgent need for a change in management. Jochen Zeitz became Chief Executive Officer in late 1993. He immediately implemented a long-term business strategy. Phase I (from 1993 to 1997) was a restructuring of the company. During these years, Puma underwent "market oriented" changes such as major cost cutting measures and organizational restructuring. Zeitz aimed to streamline functions and develop a corporate culture of entrepreneurship. The purchasing and product development departments were merged. A cen-

tralized distribution system was established replacing independent warehouses. By late 1996, Puma had re-established itself as a profitable and successful market driven company. Shareholders received dividends for the first time as the company achieved its highest sales in three years.

During Phase II (1998 to 2001), new alliances and higher investment in international marketing and product development were the emphases of the company. Puma started to concentrate on international business with emphasis on building the "sports lifestyle name" brand globally. An Italian subsidiary began operations in 1997. A new subsidiary was established in the United Kingdom in 1999. During this period, the United States became the most important market for Puma; here it sponsored world-renowned tennis star Serena Williams. It successfully landed long-term contracts as the official supplier for shoes and textiles for the Women´s Tennis teams in 1998. The Japanese market was another important strategic market where license fees were still 10 percent. Puma continued to grow over the next few years. The corporate strategy seems to have worked as Puma´s sales increased, especially in the United States. By 2001, Puma had repositioned its brand as "one of the most desirable sports lifestyle brands in the world".

Phase III commenced in 2002. It is referred to as the Momentum Phase (2002 to 2005) with the goal to "further explore the potential of the brand by generating desirable and profitable growth" (Puma Corporate History). Profits continued to grow. There were several direct investments in key markets in Eastern Europe, Japan and South Asia. Strategic alliances with distributors were established. Retail became a critical function for Puma. Expansion of "in-store" merchandising was a priority. The launch of store openings in high-density cities was another important step to extend the Puma brand's visibility.

Compared to its competitors, Puma continued to be a small player in terms of the global sports merchandising market. Football and running were the key sports for Puma. The management board knew that Puma had to be innovative and progressive for the future. They had to select a unique approach for the Puma brand and identify other areas in sports that would add value to the company´s goal "to be a desirable sports lifestyle brand". "Sports lifestyle is the challenge for a new market which realizes that consumers are demanding sporty products and styles that they can wear not only in the fitness studio or the pitch, but also in their free time" (Santjer). This was critical for the continued success of Puma as a company and the Puma brand.

By 2004, the Puma brand was identified as one of the most influential brands globally. In June 2005, consolidated sales increased by 13.3 percent in Euro terms with global brand sales reaching €1.2 billion. Gross profit margin was above 53 percent with net profit margins stabilizing at 12 percent similar to the previous year.

In the fall of 2005, Puma had successfully positioned itself for the next phase of its corporate strategy. The next year Phase IV (2006 till 2010), called the "Expansion" phase, was implemented. This meant (1) the expansion of product categories, (2) the expansion of the non-Puma brand, and (3) a regional expansion. During this phase, Puma started to invest in

majority ownership of joint ventures with former license partners in Japan for the apparel business, China/Hong Kong, Turkey and Argentina. Puma has established fully owned subsidiaries in India, Dubai for the Middle East, Korea, Romania and Zagreb in Croatia. The expansion into other sports areas such as golf and sailing continued. Puma also focused its expansion in Africa through sponsorships of soccer teams and strengthening its operations in South Africa. Despite the current global recession, Puma has "weathered the downturn much better than its rivals" (Financial Times 2009). Year-end consolidated sales for 2008 (adjusted for currency differentials) stood at €2.5 billion while net earnings of €232.8 million.

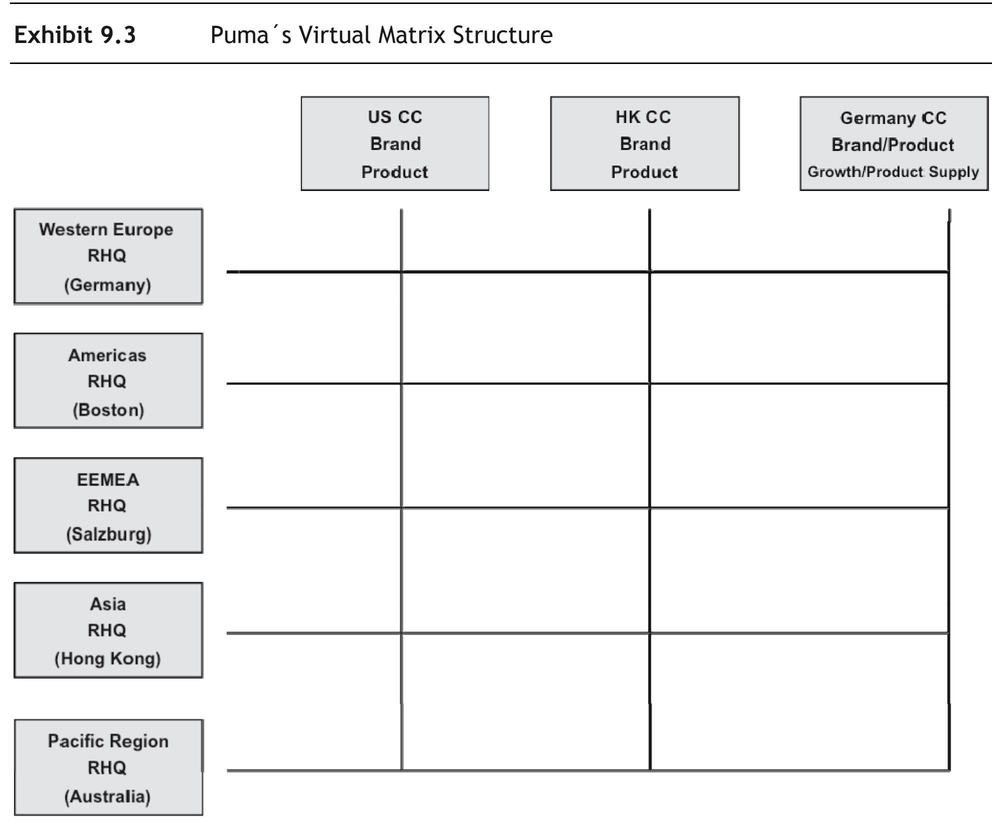
Puma´s Virtual Matrix Structure

In order to be responsive to constant changes in the markets Puma developed a multilevel virtual matrix organizational structure as part of its Four Phase corporate restructuring. The matrix is defined by geographic regional hubs (vertically) and by "competent centers" (horizontally). A competence center ("CC") is basically a virtual headquarters, which is responsible for one of seven corporate functions and is located in the U.S.A. (Boston), Germany (Herzogenaurach) or Hong Kong. The functions are located in any of the three virtual CCs depending on where the management experience and talent as well as strategic specialty arise. The functions are: Products, Brand, Product Supply, Growth, Structure, Culture and Brand Value. All virtual CCs and functions are then further subdivided by product category of apparel, footwear and equipment.

The function Product refers to research & development and sourcing. The Brand function is for the marketing and strategic planning of the brand. Product Supply function involves logistics, warehousing and supply services. The Growth function implies sales, after sales service and general distribution. Finance falls under the strategic planning sub function. The geographic distribution further ensures the subsidiaries´ interaction with each competence center. The five regional hubs (or regional headquarters RHQ) are located in Hong Kong for Asia, in Boston for the Americas, in Australia for the Pacific region, in Germany for Europe and in Austria for Eastern Europe, Africa and the Middle East. The regional hubs are critical for being close to the market.

In an interview with Klaus Bauer in 2006, the then chief operating officer for Puma stated that regionalization is shaped by the similarities in the market conditions and cultural practices. In his view, regionalization is possible when there are economies of scale, similarities in market conditions and practices, product harmony, price stability, complementary discount structures and an accounting system as a control mechanism. Regional hubs have central market competence in the region. A regional general manager ("RGM") must have a feel for how the regional market operates and how to lead the team. Regional marketing strategy and regional product management are important functions to have close to the market. The RGM must be able to identify the right product mix for markets within his area of responsibility. His leadership in managing each market as part of a whole region is critical to the success of the business.

Exhibit 9.3 Puma´s Virtual Matrix Structure



Source: adapted from Ambos and Schlegelmilch (2010, p. 441

Therefore, human resources, finance, logistics and technology functions all support the structure of the region. There are five core elements needed at the regional level: operating strategy, distribution systems, marketing strategy as applied at the national level, product strategy (which products can sell at the national level) and retail. Klaus Bauer, former chief operating officer, Puma Headquarters explained in 2006:

"The process and market demand for each country works differently. Centralizing processes was not simple for Puma as it has had a presence for a long time in these European markets. If we create regions, then we carefully structure the systems taking into consideration the demand of each market. Standardization is difficult as each of the European countries has a different market structure and composition."

Regional Headquarters in Salzburg, Austria

Puma AG owns 100 percent of Puma Austria. Puma Austria serves as the regional hub for Eastern Europe (EE), Africa (A) and the Middle East (ME). As a RHQ, Puma Austria over-

sees the activities of Puma´s subsidiaries, distributors and licensees in EEMEA. Its main responsibility is the continued development of regional business operations as well as identifying opportunities in new, emerging markets. According to Martyn Bowen, the current regional manager, Puma Austria's footprint covers approximately 40 countries (telephone interview with Martyn Bowen, RHQ Head, Puma Salzburg, 15 November 2009).

RHQ Background and Erwin Kaiser

The main role of Puma Austria as a regional headquarters is to support the development of business operations in its geographic area. The RHQ was to expand the business operations in each country and identify opportunities to complete business deals. The RHQ found suitable distributors and showed them how Puma does business and imprinted the "Puma way". All distributors in EEMEA and India fell under the auspices/responsibility of Puma Austria.

In the early 1990s, Erwin Kaiser undertook the task of developing the Eastern European countries. Austria was chosen as the regional base due to the similarities in history and culture with the Eastern European countries. It was a time when Eastern Europe was coming out of the communist era and the Cold War. The economic situation in these countries was still uncertain and unstable for a multinational like Puma. It was difficult to do business given the eco-political situation. Kaiser decided to approach each market based on customer demand and adjusted selected products to local market conditions. The goal was to first set up a marketing and sales operation in the local market for each country. In most cases, 70 to 80 percent of the sales were based on the international collection. The remaining 20 percent are goods adapted for local market preferences.

Under the leadership of Erwin Kaiser, Puma Austria successfully gained experience and management know-how as the "specialist" to establish Puma as a new business in emerging and difficult areas. Unlike other Puma RHQ heads, Kaiser felt he had the management freedom to carry out certain decisions. Puma Austria eventually served as the holding company for the Middle East and South Africa. Other subsidiaries were later established when the sales volume in a specific market grew. As a manager from Warsaw explains:

"The Austrian advantage is that these guys have existed in these markets for ages. …And my colleagues in Austria know much more about the market in Eastern Europe than my colleagues in Herzogenaurach. This is clear because they have been responsible for this market for over 15 years."

"Ideal" Structure

The RHQ supports the EEMEA subsidiaries and affiliates in all functions such as marketing, retail, logistics and finance. Martyn Bower, the current RHQ head, describes Puma Austria:

"We have a regional finance manager, a purchasing manager, a sales manager, a marketing manager and a merchandising manager in Salzburg."

Each regional functional head is in touch with the functional heads in the subsidiaries such as Poland, the Czech Republic, Hungary or South Africa. The budget and major strategic decisions for the EEMEA subsidiaries are discussed with Puma Austria RHQ. At the same time, R&D, sourcing and brand management continue to be central functions under the auspices of the virtual hubs or CCs. Each country's general manager in the EEMEA region reports directly to the manager of the regional headquarters.

Finance and Budget

Finance and budgeting for the EEMEA is centralized in Puma Austria. Each country reports its proposed budget to Puma Austria. The financial budget for the region is combined into one report for corporate headquarters in Herzogenaurach, Germany. Approval for each country budget is determined at Puma Austria RHQ. If a country's general manager (GM) wants to make changes to the existing budget during an operating year, then there will be a consultation between the GM and the regional finance manager. If there is an issue regarding capital investment, then it is essential to inform Martyn Bowen as manager of regional headquarters and the head office finance director in Germany.

Financial control for subsidiaries and affiliates remains at the level of the regional headquarters for the EEMEA. Costs and expenses are the responsibility of each country operation. The GM files the budget and is then in charge of expenditures. In order to manage the flow of financial information and general data, RHQ installed similar information and computer systems in all EEMEA subsidiaries.

Sourcing and Logistics

Puma Austria is responsible for the regional sourcing and logistics for the EEMEA region. In 2006, there was a "custom free" central warehouse in Austria that facilitated all purchases of the subsidiaries in the Eastern European area.

Marketing

There is a global marketing competence in Boston and regional marketing is centralized in Salzburg. In the event of a conflict and/or difference of opinion, then critical marketing issues will be referred back to Boston. Day-to-day administration for marketing operations is handled at the regional level. For example, the concept for advertising campaigns is generally developed by a central creative team in Boston. The regional hubs have the task of executing the campaign. The advertising campaign is then adapted to the European style and subsequently launched in each country with the necessary changes in language and/or wording. Coordination becomes imperative. A senior manager says:

"We have become a company of meetings. There are unending meetings where each functional group meets with the regional functional specialists to discuss numerous issues."

Summary

As the company adapted its strategy through the restructuring years, the organizational structure of Puma gradually evolved to what it is today. The competence centers continue

to be the basis for technical and/or talent knowledge. Information sharing, timely coordination and communication through the matrix is imperative as Puma moves forward into the next phase of its corporate development.

9.6 Conclusion

Taken collectively, our research findings as well as the Puma case point to one very important fact: To achieve global advantages, firms need to know how to win regionally. Europe, one of the key regions of the globe, is no exception. After having taken a detailed look at the integration responsiveness dilemma experienced by many multinational firms, we outlined the common organizational responses to manage this dilemma. Based on this debate, we developed the argument that the quest for superior performance is largely determined at the regional level. This suggests that firms venturing beyond their home regions may gain by tilting the global matrix towards a more regional approach that is consistent with regional strategy.

Recognizing the need for superior regional performance is one thing; achieving superior regional performance is something else entirely. To develop a stellar regional strategy, multinationals need to resolve a number of pertinent questions. This starts with the rather mundane sounding question: What is a region? Evidently, companies answer this differently. Some split Europe into EU and Non-EU; others divide into Western Europe and Central & Eastern Europe (CEE), while some even create entities called Europe, Middle East & Africa (EMEA), into which they merge all of Europe.

Having settled on their particular definition of a region, multinationals need to decide how to manage it. Should companies manage the region with a regional headquarters or without? Would it make more sense to have a regional desk at corporate headquarters outside Europe? If the company opts for regional headquarters within Europe, where should it be located? And what about sub-regions – which companies need them and which do not?

Although the answers to these questions are largely idiosyncratic to the companies involved, we also demonstrated that managers need to follow some general rules in order to make these important decisions. Our data shows that in addition to market similarities, managerial considerations constitute the main drivers for the grouping of individual markets. In fact, the structure a multinational firm adopts to manage the region tends to reflect the maturity and diversity of the business. More mature organizations usually adopt a more fine-grained sub-regional or mixed market approach within Europe; smaller organizations go for a single regional headquarters structure. Leaving questions of location and structure behind us, we then briefly looked at the tasks commonly undertaken by regional headquarters.

In the last part of the chapter, we have fleshed out the discussion with a detailed case study focusing on the major operator in the Sports Shoes & Apparel industry, namely Puma. The case study provides a concrete example on how firms actually manage their regional operations.

Overall, we demonstrate that multinationals can, and do, develop region specific advantages. The organizational architecture selected to serve the region is a crucial element in delivering these advantages. Although regional headquarters fulfill an administrative function, their entrepreneurial role is arguably more important. Passing on best practices, encouraging subsidiaries to adopt new business models, and developing innovative products and processes turns well-managed regional headquarters into what we like to call “dynamic competence relays”.

Student Assignments

1. Why do the regional headquarters play an essential role in MNC's strategy building? Describe the intermediation role of the regional headquarters.
2. By what criteria would you judge whether a regional headquarters has succeeded or failed?
3. What kind of tensions may the managers of regional headquarters have to cope with? Identify and discuss the managerial challenges associated with regional headquarters.
4. The text presents four approaches to structure a region, namely the single market approach, the sub-regional HQ approach, the mixed approach and the virtual network structures. Describe and discuss for which type of companies these approaches may be particularly suitable as well as the advantages and disadvantages of each approach.
5. The Puma-case demonstrates how regional operations can be managed. Discuss the possible reasons why Puma came to implement the virtual matrix structure.
6. What could be the motives for abolishing regional headquarters for companies such as Adidas?

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10 Managing consumer's experiences: Design as a solution for transformation

Tore Kristensen, Copenhagen Business School, Department of Marketing

Dóra Horváth, Corvinus University of Budapest, Institute of Marketing and Media

> "… represents **a creative form of interaction** between those who go and those who left behind, between human beings and the forces of nature", therefore transform.
>
> (Ottagono Italy, July-August, 2009, p. 60.)

10.1 Introduction

In our article we present an unusual case study in the sense that we don't present a single corporate case, but we present you a new notion, transformation economy – its characteristics: creative elements, domain and field, furthermore we show where transformations may take place: in person, physical environments, organizations and technology. We take you to a cultural tour in order to let you understand where transformation economy stems from and then invite you to find your experiences of transformation examples. We illustrate the idea of transformation economy with two design award winning cases where transformations occur with the owner, in the product and with the environment – the examples are very distant and close at the same time – one is a collection of maternity clothes for pregnant women transforming through time, the other is a new concept of tombstones that reflects time, environment and people.

10.2 From experience to transformation economy

Since the German author Gerhard Schultze (1992) wrote his book about the "Erlebnisgesellschafft", forecasting that a major force of growth of the Western World would come from experiences, politicians, decision makers and researchers have flocked around this assumption. It may have peaked with Pine and Gilmore's (1999) bestseller about the experience economy, where work is theatre, and every business a stage. Furthermore, public investment followed reports like in Denmark where the experience economy was predicted to become a major force of growth from 2005, although at the time it only accounted for 5.3% GNP, 16% export, mainly as tourism and some entertainment. The growth of the experience economy was strongly affiliated with Richard Florida's (2005) studies of the "creative class". Political debates implied that the growth of the creative class, which actually in-

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cluded most people with a longer education, would support the expansion so this sector could counter the "flagging out" of the manufacturing industry to the Far East. Would it not be great if that was so?

Politicians would invest in research, education and regional policy. The population could rest because responsible politicians would secure what was lost and industry would soon be won back by the creative sector. In 2006, the Finnish statistician Aku Alanen (2006) wrote a critical article attacking the assumptions of the concept creative industries. Although there was seemingly agreement among many countries, Alanen found the concepts flawed. While there seems to be no doubt that the economy develops as a result of creative forces (Schumpeter 1950), Alanen's attempts to find the concepts useful and clear failed. Not all creative industries are creating wealth in terms of profits. For example, the term is limited to certain sectors of the economy, even though many more sectors use creativity. A major sector is the "copyright industries", where some firms get legal protection of some conditions of their innovations. Even here "open source providers" like LINUX and Wikipedia who do not protect their works do not seek revenue and guessing how much value they create is very difficult. In the construction industry, not only the architects are creative, but also the joiner, carpenter, and bricklayer find new solutions and therefore are creative. Also, as argued by Alanen, the demand for cultural products is kept out of the equation although it is an important determinant of the outcome. Even the education and research industries fall, to a large degree, outside the concept of creative industries, although both patents and partial secrecy may be ways to protect the solutions from copycats.

Pine and Gilmore (1999) open an escape door in their book and identify a potential shift in the mode of value creation, which they call "personal transformation". They believe this already exists, but the phenomenon will grow in the future. Here experiences are replaced by personal transformations. It may seem premature to guess what this may be like, but there are signs in the existing culture which may be explored to suggest possible futures for the transformation economy. The reason is that if the transformation economy stands a chance of becoming a major factor of wealth creation, it should already be here.

This article aims at giving an explanation of the lack of growth and paints a picture of what a transformation economy may look like. Finally, the article provides some suggestions for marketing practices and conceptual development.

Why did the experience economy fail before it got started?

Periods in history were labeled according to the major technology and material dominating a long period such as stone, bronze and iron. Even periods which meant important and relatively speaking swift transformations of a society like the Gothic (1140 – 1480), Renaissance (1430 – 1530) or Baroque (1570 – 1770) were long periods, and they varied across Europe. Even the dating of these historically important periods may be debated. Every period that was replaced carried something over to the next period and became embedded in the next period, at least for as long as the customs of building and making were carried by some. Even today, there seems to be a general agreement that modernity started around

1770 and still persists, although numerous authors claim we are living in a "late modern" or even "post-modern period". The persistent influence from Friedrich Nietzsche (1844 – 1900) is still provoking doubt in the belief in reason, progress and democracy, which are usually seen as the pillars of modernism. When authors today try to label our time, the concepts may differ from information economy, knowledge economy, creative economy, or cultural economy, according to who says what and the agenda. Not the least political discourses are "post-modern" changing terms according to whatever may sell the message.

Bearing in mind that we are trying to label the period we are experiencing right now reduces the credibility of the labeling itself. Only new generations in the wisdom of history may actually be able to label what best characterizes the age we live in.

Taking the claims of Alanen (2006, 2007) we may even find good economic reason for them. The Nordic countries are among the richest in the world. While poor countries are struggling to meet the day, produce and procreate, the Nordic countries are blessed by the people's need to actualize themselves. Although, there are less fortunate people, even some living in poverty, a major part of the population is fine. Put differently, it seems that the experience economy has already peaked. The capacity is utilized and there seems to be little room for new waves of tourists, event making and entertainment; it is already there. Then what will happen? Will there be a new phenomenon to take over? According to Pine and Gilmore (1999), the new is what they call the "transformation economy".

10.3 Transformation Economy

10.3.1 What is transformation economy?

The highest level of value creation is, according to Pine and Gilmore (1999), based on the individual search for improvement, physically, spiritually and not least individually. Transformations are one-time experiences that changes the character of need-satisfaction. This means that those customers or users who are subject to it will be changed. The user becomes more critical, demanding, and a competent user of a class of products, objects or service. It means converting the demand function for a class of goods. By means of diffusion of the new competency (Rogers 1995), the altered demand function may spread in the economy. Often this concerns the consumption of culture; good examples would be Florence in the 14th century (Csikszentmihalyi 1996) and Vienna in the 17th and 18th centuries. A competent and critical bourgeoisie were able to set the highest standards for art.

Having set new standards for demand, the suppliers have little choice but to improve the quality of their offerings. The general idea is that the economy undergoes a transformation based on influencing the consumers by giving them both new competencies and the chances to raise their voice or threaten to exit (Hirschman 1970). This means to influence the system, rather than be loyal to a brand.

10.3.2 What constitutes a transformation?

How does a transformation create value? A transformation is a personal experience where the "aspirant" temporarily accepts the authority of somebody else to stage the experience and for the aspirant to become whatever was promised. The aspirant can be a student who accepts the leadership of faculty members, accepts their authority and becomes a graduate the day the exam is passed. Very often less formality is executed. A course in self-improvement, storytelling or losing weight requires a new practical way of living, but there are few formalities like a doctoral degree required.

In principle, a transformation is a one-time phenomenon. It cannot be undone and no consecutive experience will be the same. A transformation changes the character of the need satisfaction. Giddens (1991), however, casts serious doubts about the irreversibility and claims that in a late modern society, eternity may in fact be quite a short time. Even formal transitions like a doctoral degree or a license to practice medicine may "expire" if not used in the proper way and the candidate is continually "updated" in the domain.

Transformations are business. There seems to be few or none which exist for purely altruistic reasons. Business models are the basic foundation for management of transformations. In principle, a business model is a breach of economic equilibrium, where the monetary streams are altered in a way that creates a profit for the business. A business model becomes sustainable when the disequilibrium becomes long-term by keeping the formulae secret, by patenting and other forms of legal protection or by reducing lead-times or simply a loyalty towards the business (or its brand). Examples of transformations which are good business are found in education, fitness and even religious businesses. In particular, universities have succeeded by getting transferred from the governments, charging for tuition from students and firms and a few have succeeded in alumni organizations to give economic and political support. Artistic organizations like museums apply considerable amounts of work to secure their funds in similar ways to bond with their users, give special entries to openings and lectures to invited dignitaries and supporters.

Creative elements

Three basic elements are essential in understanding a transformation economy (e.g. Csikszentmihalyi 1996). There must be creative individuals with imaginary capabilities. Then, there must be a "domain" consisting of the "mechanisms" containing rules and symbols. Finally, and that is the major force in this reasoning, there must be a "field" consisting of the customers and also other stakeholders such as critiques, experts, organizers and administrators who influence the management of resources.

Creative individuals are encountered in cultural institutions and as a large group of designers and artists who try to gain assignments and a reputation. The group is however much larger because being creative is not restricted to the groups who are educated in design schools and schools of art. Very similar to the creative people with a degree would of course be chefs, musicians, architects and all kinds of people who just act creative with "no

license". *No license is needed to become creative*. Anyone who feel like it, feels having a talent, has some financial resources and dares take the opportunity can enter a creative mission.

Domain

The second basic element is the domain. A domain can be made up by a discipline or it may be a set of rules and mechanisms constituting a system. Entertainment, art and religion are broad examples of such systems. Access to talented people and places to perform are such elements. In addition, there are the rules of the game defining the practices. In regulated areas such as education and religion, certain forms of authorizations must be achieved through relevant education and exams. In entertainment, admittance is free and only the market forces regulate who is in and who is not.

In experiences, the rules are very open and interpreted many ways. Transformations may be seen as a special area within experience where a personal change is part of the process.

Field

The field consists of the people who act as gatekeepers to the domain. The degree of formalism differs, but there is usually a selection process which itself is a transformation. In "mob" terminology, the rhetoric uses the term "a made man", which means that to be an accepted member of such a criminal organization, the aspirant must serve as an aspirant or "hang around" for a time and usually commit a particular deed to become a full member, sanctioned by the older members. Although the principles may be the same, there are big differences in consequences whether a particular organization is on one or the other side of the legal divide.

The rituals may be a part of the transformation the user wants to achieve. It is not the transformation itself, but a formalization that it has incurred. The hand-out of diplomas, where university candidates wear old-fashioned uniforms is only an end statement confirming that they have passed. Yet it may be of utter importance because the gradual transformation taking place over several years may itself be intangible, but the ceremony is distinct. Then the aspirant becomes a candidate and is accepted as a member of the field.

10.3.3 How is value created?

The creation of value is traditionally based on the disequilibrium in the economy, where money is invested in production and the price paid exceeds the inputs and therefore constitutes a profit. This yields value to both the producer and to the customer since the price paid must exceed the value gained or else the transaction will not take place. The production is replaced by a staging of the transformation and the user is treated individually.

Value is created when a scarce raw material is transformed into a new concept and materialized. In the case of transformation, the person becomes the materialization herself. Then following Giddens (1991), the concern becomes to which extent this is so; it is a sustainable value creation. A whole line of different transformations may fit the scheme, and it may be

practical to distinguish between personal, physical environmental, organizational, and technological transformations.

10.4 Personal transformations

The most basic form of personal transformations is probably the experience of education. This takes the novice or aspirant from a stage as pupil to a higher stage of skills and knowledge. There is a whole line of consecutive transformations built in a hierarchical manner with no apparently top level. Even with the finest accreditations in art, business or crafts or a doctoral degree, or even a Nobel Prize there seems to be an extra dimension or level one could reach. Such transformations are probably the prototypical form of transformation. Each step seems to open new places in a societal hierarchy with their associated privileges. Such transformations also form a society.

Transformations include borderline physical experiences such as jumping out of an airplane with a parachute, recovery from injury or illness, or a fitness experience. These transformations may give the feeling of catharsis, which means becoming clean or purified. Such an experience may be called "autotelic" in the sense that it has a limited reward or direct consequences outside itself.

Other personal transformations may come from a culinary or cultural experience, which may be a feeling of being in contact with the physical or cultural context. Becoming an art collector may be a genuine example of a transformation where the assets acquired may at least in principle be turned into financial assets. In addition, the collector is likely to learn from the objects acquired as well as often enjoy other forms of art. For example, a collector of paintings may also enjoy music and opera. Therefore, the learning of culture may accumulate while the collectors also gain economic status. Totally, this may become a good transformation. Even so, it may be lost. Bad investments whether in art or in other fields may mean a loss. Falling in love is a special transformation which will usually have very strong implications, positive or negative. It is usually not staged although some influence may be exerted. For a complete picture, the following examples will be discussed.

10.5 Case 1: ILLE-OLLA maternity clothing

One of the biggest transformations for a woman is becoming pregnant and giving birth. This transformation is reflected in OLLA dresses. One of the nicest stages and periods of life for a woman is her pregnancy. The brand name OLLA refers to this stage. It stems from the Finnish word „olla raskaana" (being pregnant). It is not only its literary meaning but also its round letters too, which also refer to this very special state, the beginning of a new life.

Exhibit 10.1 ILLE-OLLA Maternity Clothing, Designer Illési Lenke

Source: Hungarian Design Award (2009)

According to today's fashion, an expectant mother no longer needs to hide her belly. The growing belly of pregnant women is a challenge for fashion designers. OLLA dresses for pregnant women are created with a special cut, which is different from usual, traditional forms of cut, like the inserted elastic element at the front of the trousers at the belly, or special loose cut T-shirts under the breasts. The beautiful, natural folds of OLLA dresses make these pieces enjoyable to wear.

The newest collection is created in a way that the dresses maybe worn before, during and after pregnancy, making it comfortable to the owner to transform. The dresses are created in many styles – elegant, sporty, loose or tight – from skirts to trousers, which can be combined all together.

10.6 Transformation of physical environments

The physical space may concern the location inhabited, such as a house or flat. Such a place may be under the influence of domestication to become a "home". The process of domestication means that the place is taken and one gives it a personality by re-design, patina, accretion and or organizing objects and borders.

A physical transformation can take place in a literal sense by moving to a new location, e.g. in the country, at a resort, in a city or wherever. The place or location can be ecological in the form of a special landscape (Appleton 1979). Doing this usually means seeking protection from predators or enemies seeking refuge. Prospects are also, according to Appleton (1979), a major cause to relocate based on the evolution of our ancestors' survival and how their physical needs may have been left as feelings or preferences for certain landscapes. Although Appleton clearly meant an eco-system or similar environment, the term asylum may imply that a shelter from hostile powers may be an urgent transformation.

Organizational transformation

This means that the aim of a transformation may be to change the position within an organization. A basic one is the family, where age, certain rituals and marital status or economic status turns one's positioning into a transformed one. A work transformation is one typically located in the "pitch" as described above. Certain action, interpreted as success according to the nature of a business, will usually lead to an improved status, whether informal or formal.

Fraternities, alumni and secret society, such as freemasons, odd fellows, secret police or religious groups build on an assumption that the aspirant is selected to a special situation and gives an oath to keep the transformation or a major part secret from others than the members of a higher rank. Such organizations are usually hierarchic (Levitt and Dubner 2005).

Technological transformation

This topic is probably a more controversial issue. "Cyborgs" come from the science fiction literature, where human and technology grow to form a new creature. Clark (2003) on the other hand claims that it is here and has been for some time. Electricity, telephones, telegraphs, faxes, and later the Internet and mobile communication including SMS may be much less intrusive, but in cognitive terms, they are natural extensions of the human body and brain which increase our reach to a considerable degree.

Whereas these remote connections were associated with control of the human being by robots or cruel beings, the new view is one of a human being who is transformed into an omniscient and communicating everywhere creature who exerts control over his/her own environment.

10.7 Case 2: The SEEYOU project

Seemingly, this is a very strange case and a project; however, it shows what transformation means: interaction and transformation between architecture and nature, families and among people dead or alive.

Phenomena and elements of nature are invited to be involved in creating an interaction. The look of the object changes over seasons and time. The water in it reflects the outer world; the mossing gives a beautiful appearance even if nobody cares. The tomb is not only a connection between the departed and the bereaved, but it helps families in togetherness. It is designed to be completed by the owners and nature.

21st century taboo

In the not very distant past, death was a taboo subject even among developed societies. By insulating themselves from death, the living deprive themselves of opportunities to be better prepared to face their own mortality.

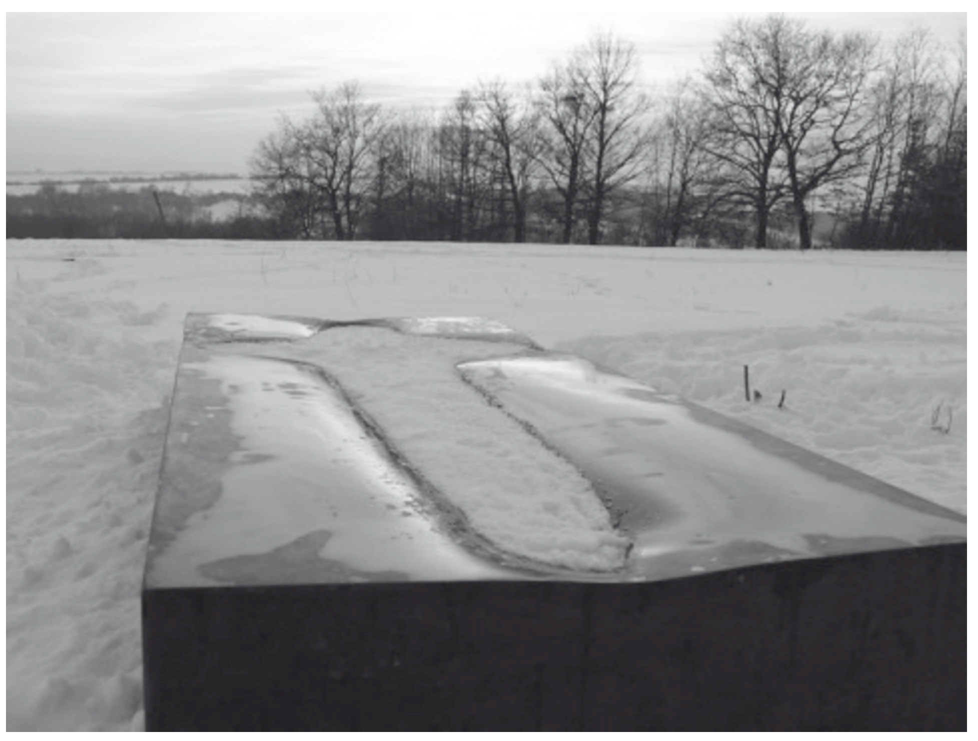
Architecture and design for life AND death

Death is one those subjects people tend not to like talking about; however, it still comes to us all in the end. Tombstones haven't changed much over the last few centuries – that is until now with some moves to shake up the architecture and design of death. Death used to be a nice line of work for architects. It generated the tombs and pyramids of Egypt, the Taj Mahal and countless other magnificent structures. The great achievements of modern architecture and design have brought stunning forms to our built environment – yet these qualities often seem to have been kept away from objects and spaces and for burial. The living want new houses, new spaces, new furniture, new objects of desire; they don't want to bother much with the dead.

Reflections and personal remembrance

Forming a circle around the grave, looking at the tombstone, it is the ancestor that connects the family. A father can recognize his forefathers by looking at his son. Descendants can see their ancestors in themselves. When look closer into the surface of the water you can catch sight of yourself. The cross shaped hollow becomes saturated with water, leaves, sand, snow, and then decreases, and so on. The object is always reflecting on the outer world and environment. It is exposed to nature and to the concern of family members.

Exhibit 10.2 Seeyou gravestone in winter



Source: Hungarian Design Award (2009)

The cross form

Cross forms were used as symbols, religious or otherwise, millennia before the Christian era as marks of identification or were significant for belief and worship. The designers' intent was to create a universal object that reflects on the European milieu and rich culture we live in. The cross is thus both a sign of Christ himself and a universal emblem of faith. The cross is also interpreted as a human form. This well-known element has been suited for helping the object’s deeper messages to be understood. Seeking a contemporary interpretation of traditional meanings and timeless values, designers created a new representation of the cross.

Exhibit 10.3 Seeyou gravestone in autumn

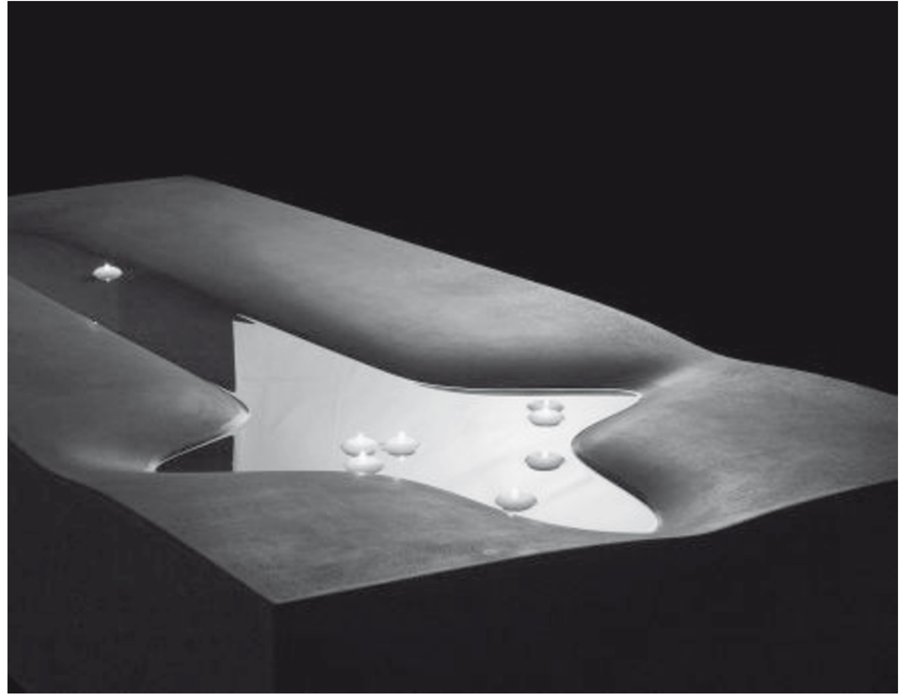
Source: Hungarian Design Award (2009)

Material: concrete

To create an object, a building or a structure means to create space. Space must be pleasant to man and well integrated in its environment because earth participates in everything. Indeed, lots of importance is to be addressed in the materials and their use. Through its firm structure, heavy weight and durability, concrete transports the idea of passive strength by its resistance of external forces as a perfect complement of the active force, life energy of every living being. Dual beings are forming one organism coming together for one purpose, resulting in a harmonious outcome.

Concrete not only has an ancient history as a durable material, but its versatile character makes it the perfect medium of creative expression as well, a vanguard raw material as much for its appearance as for its flexibility of use. Unlike its primary carcass and form-work function, this material suddenly takes on fluidity, stylishness and panache.

Exhibit 10.4 Seeyou gravestone with candles



Source: Hungarian Design Award (2009)

Technology: a shot of fluid in motion

Concrete's robustness is accompanied with an active force within that expresses the material's contradictory states of fluidity and cast solidity. Concrete construction projects are antistatic, and can be defined as a shot of fluid in motion. Concrete's plastic characteristics – from fluid to solid, allow for the production of complex forms. Unlike solid slab materials that may prove difficult to tool into more complex shapes, concrete has sculptural features. Pouring the mix into a mold – negative form of the gravestone – it can take its shape without producing any waste material.

Traditions and history form 'cradle to grave'

Planting the deceased for later renewal is the earliest known human ritual. Between 20,000 and 75,000 years ago, Neanderthals began to bury their dead. Evidence of many of our contemporary customs appears at Neanderthal sites. Both rituals and monuments for the dead played an important part in everyday living.

10.8 Discussion

Two important issues concern the value of transformations. Similar to a sustainable competitive advantage for a firm, a transformation is assumed to become sustainable in order to create a permanent value. Additionally, the value must be positive in some sense.

Degree of sustainability

It is assumed that a transformation is totally irreversible and that once it has changed, the character of need satisfaction is created and this can go on. The question is whether this holds in reality; even when it does not, it may not mean that it is completely lost. Even fragile transformations may make value in the sense that the outcomes are positive, at least on a temporary basis. If a transformation leads to an increase in field status, this seems to be itself a case for sustainable value, at least for the person. Such a position is "stickier" than a financial gain and may be used in order to get a second chance.

Valence and traumatism

Sennett (2006) describes the new consumption of travelling from city to city or maybe rather between identical shopping malls, buying almost identical brands is more a depowerment than creation of value. Yet most transformations seem to offer a potential for empowerment, although it may need some degree of security, and it can be lost. Empowerment seems to be a general norm in a modern society and when it is not safeguarded, it may be lost.

A careful conclusion is that transformations of the kinds expressed in these unusual case studies may have the potential for value creation for the individual and for society. The latter occurs when the character of need satisfaction changes for consumers to become more critical, competent and demanding.

Student Assignments

ILLA OLLUM Maternity Clothing

1. Try to find similar or dramatically different objects, i.e. products that make it possible to transform together with their owner(s). Explain why these transformations are valuable?
2. Explain your point of view about whether the possibility of a product to transform together with its owner can be a strong differentiating tool for its marketers, meaning that users will prefer these products over the former ones that fulfill one need in a static way.
3. Try to think of non-existing product concepts where the potential for transformation could bring extra value. Do this task with a group of other students and potential users and use projective techniques (association techniques) in order to bring unusual and unexpected ideas.

SEEYOU Project

1. Try to find similar or dramatically different pieces of architecture and design in your environment; show how they interact with their environment and audiences, and therefore create transformation in themselves and the environment.
2. In your opinion, is this design an incentive of transformation of people or their environment? Explain what you agree and disagree with.

Questions and Tasks

1. Search for examples where empowerment of the consumer brought success. What was the key to success?
2. Search for examples of product failures which might be explained by the depowerment of users, audiences, and places.
3. Think of your country and other cultures you have visited; can you explain situations where the empowerment of the user gets different meanings?
4. Search for good examples that reflect to the idea of a transformation economy as in the cases we presented. What are the major strengths of these examples?

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11 European Market Entry — The Case of DeLaval

Henrik Glimstedt, Stockholm School of Economics,

Upgrade marks 10th anniversary of first DeLaval milking robot

The robotic milking stations have been upgraded to incorporate the latest technological benefits of the voluntary milking system. This will support dairy farmer Walter Kessler in boosting productivity without investing time and resources in a new robot. "We see upgradability as a major customer benefit. Our goal is that VMS farmers don't have to buy a brand new station to get the best of the system," said DeLaval vice president Andrew Turner. Walter said: "Over the last decade my two robots have operated nearly 100,000 hours, which equals 47 years if working five days a week, eight hours a day. Without VMS, I would not be milking today. "What DeLaval is supplying, the possibility of upgrading my stations to incorporate the latest in milking automation, provides yet a new degree of accuracy for making financial decisions. I'm as excited now to be a frontrunner in trying out the new technology as I was 10 years ago."

New smart features and even more cost savings and flexibility make the latest system, VMS 2011, even better. Thanks to updated DelPro software and the touch screen, VMS 2011 allows farmers to instantly see an overview of their herds as well as track performance data, including individual cows' locations in the barn. "Upgradability, system integration, herd management, on farm analysis and serviceability are key to our customers. VMS is an investment in automation which works immediately and can always be kept up to date," said Andrew Turner.

With VMS, farmers can check milk quality automatically and weed out any that doesn't meet standards. VMS 2011 also provides the highest hygiene levels, through individual teat washing and disinfection, helping to ensure milk quality and healthier cows. VMS uses less water, detergents and energy. As a result, the system significantly cuts operating costs and helps farmers reduce the environmental impact of their operations.

Press clipping from Southwest Farmer, 25th March 2011

11.1 Introduction

On October 25th, 2008, Benoît Passard, Vice President Marketing and Communications with DeLaval, the Swedish international market leader in dairy farming equipment and automation, prepared for a meeting with the company's executive team concerning "how to go to

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markets." The backdrop for the meeting was a mix of good and bad news. On the one hand, the company's investments in robotic high-tech solutions for dairy farming had been crowned with success, confirming the company's dominating market position with its cutting-edge technologies. On the other, DeLaval was facing a shift in the pattern of growth from the company's core markets to the emerging ones. For the years to come, business volumes were expected to grow slowly in the old markets like Europe and North America, whereas by the production and consumption of milk in China, India, Brazil and Russia was predicted to grow on average around 3-4% annually leading to substantial investments. While the estimated growth of milk demand and dairy farm consolidation pointed towards favorable conditions for dairy farm automation solutions, the company still faced a real obstacle, being unsure of its capacity to interact with the new types of customer in the emerging markets.

As expected from a more than century old multinational enterprise, DeLaval's approach to the market was structured through a long evolutionary process of dealing with dairy farmers in the company's core markets, consisting of mid-sized dairy farms in Europe and relatively large farming operations in the North American market. DeLaval knew these types of dairy farming operations inside and out, but Benoît was not sure of the level of competence of the company towards new types of dairy farm businesses that were developing in the emerging economies. In countries like China, India, Latin America and Eastern Europe, the market was seeing different approaches to dairy farming, with cases of external investors entering the business with an industrial approach to operating farms with herds between 5,000 and more than 20,000 animals, alongside cases of very small dairy farmers - often with no more than five cows – that were making initial investments to begin to sell milk to dairy product processors on more commercial terms, leaving traditional 'third world barter trade' behind for the first time. In some cases, small farmers were experimenting with cooperative milking stations, or even more advanced solutions, while in other cases multinationals like Nestlé were promoting their own concept for local farm consolidation in order to secure an ample supply of milk for their processing operations. As a result, very large industrially sized operations were now developing side-by-side with the various attempts by very small farms, adding to an already complex dairy farm structure.

As the meeting was approaching, Benoît couldn't help but ask: was there a need to develop a new approach to 'go to market', given the on-going transformation of the international dairy product value chain?

11.2 Company Background

"We drive progress in milk production. We aim to be at the cutting edge of the industry, to pre-empt farmers' needs through superior resources, technical expertise and service second to none. We will focus our attention on dairy farming as a whole and each individual farmer, whatever size of their business and whatever environment they are working in."

The story of DeLaval dates back to 1878, when a Swedish engineer, Gustaf de Laval (1845-

1913), patented a centrifugal cream separator that revolutionized dairy production by allowing the user to separate cream from milk with improved efficiency compared to earlier methods. The machine was such a technological breakthrough that it was awarded, in 1879, with six top prizes in agricultural shows and 18 in the following year. By 1881, over 300 machines had been sold by the simple sales company founded in 1879 by de Laval together with Oscar Lamm, also a civil engineer. In 1883, the original sales company, known as Ingenjörsfirma Oscar Lamm Jr., was incorporated in the limited liability company AB Separator.

Like other firms with small domestic markets, the young company grew internationally almost immediately. Already in 1879, 37 separators were sold abroad out of a total of 54 units sold. Only few years later, in 1885, out of a total of 826 separators manufactured in Sweden, only 24% were sold in the domestic market, while the rest was exported mainly to Germany (32%), the Nordic countries (13%), France (8%), Great Britain (8%), but also to Australia and New Zealand (13%). In the same year, 394 separators were manufactured and sold in the United Stated. By 1914, AB Separator was exporting as much as 90% of its output.

The attention to the customers' needs and to the wellness of the animals involved was also a priority in the eye of Gustaf de Laval. As a result, 1894 was marked by the acquisition of Hamra Farm, in Tumba, 20 km outside of Stockholm, Sweden. Immediately turned into a test and demonstration center, the farm was to remain in the company to our days and continuously play a role as a major source of inspiration, research and development.

The leaving of both Oscar Lamm (1886) and Gustaf de Laval (1897) did not impact the ability of the company to be at the cutting edge of the industry. While the separator was being modified to meet the consumers' increased needs, the first milking machine, known as De Laval Milker, was introduced in the market in 1917. Once again, the machine proved to be successful in responding to the needs of the farmers, by offering an efficient way to extract milk from the cow without hurting the animal. Five years later, in 1923, more than 600 machines had been delivered in all milk-producing countries. In 1931, the plate heat exchanger was introduced, a new type of milk pasteurizer that was to become another of the company's key product lines, but also an important component in the paper industry, and in the chemical and marine sectors in the 1950s and 60s. By late 1940s, AB Separator could offer a wide range of products to help the dairy farmers in all their needs, from milk extraction to responses to the increasing hygiene demands, not only for cows, but also sheep and goats, thereby dominating the world market for dairy barn equipment.

When the hand separator stopped being produced in 1962, it had just registered its peak of 125,000 units sold in one year and accounted for more than three-quarters of total turnover. By the early 1960s, however, the milking machine was generating more revenues than the hand separator and it became one of the company's most important products. 1963 saw the introduction of another technologically advanced product, the Hydropulse, which secured the company's position as market leader in equipment for the dairy farmer. Meanwhile, as a response to the farmers' needs for functioning systems, the company was moving to-

wards a more complete and advanced offer of products. As a result, in 1977 'AlfaFeed' revolutionized the farming industry by making it possible to tailor the amount of feed each cow received, while in 1993 'ALPRO' brought together feed and milk yield into one system. Finally, it was possible for the farmers to fine-tune the management of the livestock and exploit the full milking potential of their herds, as the machine could not only automate the feeding process and optimize the relationship between feed and yield, but also record additional information, such as for instance when a cow last calved, when she was in heat or ill and so on.

While advancing technologically and confirming its leading position in the market, the company was going through a series of internal changes. In 1961 the headquarter of the company was moved from central Stockholm to Tumba, just a few hundred meters away from Hamra Farm, which at that point was already a world-leading development and training center. Two years later, in 1963, the first change of name was registered, from AB Separator to Alfa-Laval AB. A few decades later, in 1991, Alfa-Laval changed ownership after years of weak financial performance through a friendly takeover by Tetra Pak, Sweden's international giant in diary product and beverage packaging and distribution systems. The merger gave birth to a group that was able to offer a complete system for food supply – from cow to consumer. Two years later, after a restructuration organized around the need of the customers, four groups were formed: Tetra Pak International, responsible for fluid foods; Tetra Laval Food, responsible for non-fluid food products; Alfa Laval, supplier of industrial separators and Alfa LavalAgri AB, treated as a fully independent entity and responsible for dairy farmers. The change in name of this last group gave birth in 2000 to the DeLaval brand, with a name chosen to show the inheritance from Gustav de Laval, while the Greek alpha logotype in the logo of the company was left to show the continuity from the Alfa Laval brand.

11.3 DeLaval in 2008

Since the very beginning, the competitive advantage of the company had been based on technological advantage and a high price/high quality competitive positioning, a stance which had been carried over into the modern engineering company of DeLaval in 2008. DeLaval also has a unique presence through its service organization with 24/7 availability, which differs from most of the competition. In line with AB Separator, innovation and international market penetration were still at the heart of the company over 125 years later, making it a truly global corporation, with operations in more than 100 national markets.

Following its tradition, the company still had its strength in milking systems, but the field of operation stretched into every corner of dairy farming. The main product, called Voluntary Milking System (VMS) was truly to be considered a farmer's best friend. Introduced in the market in 2000, with a second generation improved version presented in 2006, the VMS was an innovative machine that allowed cows to be milked without any direct human intervention, therefore freeing the farmers from the daily chore of milking, twice a day, come rain or shine, 365 days a year. Designed to run around the clock and equipped with a

touch-screen user-friendly interface, the machine could guarantee the highest standards of hygiene and provided the farmer with knowledge and control over their herd health by proactively monitoring the SCC (Somatic Cell Count) level of every cow at every milking in a cost efficient way. DeLaval provided its customers with systems for herd management, stalling, automation, milk extraction, vacuum, feeding, cleaning, pipelines, cooling and manure handling, as well as products and services for animal care, water provision, feed additives, surface coating, pasture management, filters, liners and tubing.

Table 11.1 DeLaval in 2008

Revenues	€ 0.8 Billion
Employees	4,381
Local sales organizations	54
Manufacturing units	18
R&D units	3
Dealers	1,240
Shops	1,210
Sales reps (Service technicians and sales representatives including independent dealer staff)	1,409
Service technicians	4,155
Mobile shops and trucks	571

Source: DeLaval, 2008

The products were available not only for cows, but also for sheep, goat and buffalo dairy farms. Known for its reliability and excellent maintenance services, DeLaval represented a partner that could supply any product or service that was needed to efficiently run a dairy farm. In addition, DeLaval's assortment also includes a wide variety of after-market consumable goods, including: animal feeding, detergents and other hygiene consumables, plus barn equipment ranging from complex ventilation systems and light systems to simple consumables like scrappers and protective clothing. The consumable products are just as important as the complex milking systems, for which the company is known, because after-market products – which in many cases are sold by service technicians – underpin the permanent business relation between DeLaval and its customers. The traditional service and maintenance of the milking equipment is also an important base of the DeLaval name and credibility in the market. With an increasing number of cows to take care of, no farmer in the world can afford to get back to manual milking because a vacuum pump was out of order!

By 2008, DeLaval's executive management team could look back at a decade of growth, with the exception of two weak years in 2003 and 2004. Clearly, the company's decision to invest in automatic robotic milking systems contributed to the growth, generating strong revenue streams from the mid-1900s onwards.

At the basis of DeLaval's strategy in 2008 was the prediction that the global production of milk would continue to grow. Whereas growth in North America and Europe was slow or negative, that demand was replaced by increasing substantial growth in the emerging markets of Eastern Europe, Asia and South America. (See the following section on global milk below.) This new growth was accompanied by considerable consolidation and modernization of farming over time, even though the vast majority of milk farms in those areas still remained very small by comparison. The increasing demand for safe and healthy production of dairy food products was driving this transformation, which translated into an opportunity for high-tech solutions, automation and integrated software based quality control systems.

Integrated automation was believed to shape the future of dairy farming, and DeLaval had identified three key areas that would unlock great new possibilities for the industry: automated milking or smart farming, consisting of systems for small and big farms based on the existing VMS solution; total herd management control and monitoring of cow and herd levels based on biomodels; and smart automated feeding systems, capable of adjusting feed rations to maximize profit per cow and reduce feeding costs. The overall integrated system presented by DeLaval could not only analyze and present data to farmers, managers and advisors, but it was also based on biomodels capable of estimating risk of diseases and generating prevention and proposals for action. All of this was available in a system that was being implemented both on-farm and remotely. As Andrew Turner, Vice President of Product Area Milking Systems, stated in 2008: "Our vision is an on-farm integrated system where we can apply automation even further. We know that the farmer needs to boost profit, milk yield and quality, and reduce feed and labor costs. Our goal is to contribute to the peace of mind for future generations of dairy farmers." In the mature markets, emphasis was placed on being a 'one-stop-solution' for dairy farmers, building on the company's policy of 'Being Your First Solution – Everyday' in order to boost sales of after-market products.

DeLaval believed that a key goal to secure market shares in all markets was to be closer to the customer. Following this reasoning, the company was promoting a new policy called 'First to Serve the Customer', aiming at forging closer relationships with the end-customers in the dairy farming industry to understand their needs and to build brand loyalty. Following a traditional approach, the customers were grouped into the company's organization according to the type of milking system installed, or milking solution, in four entities:

Table 11.2 Customer Segmentation

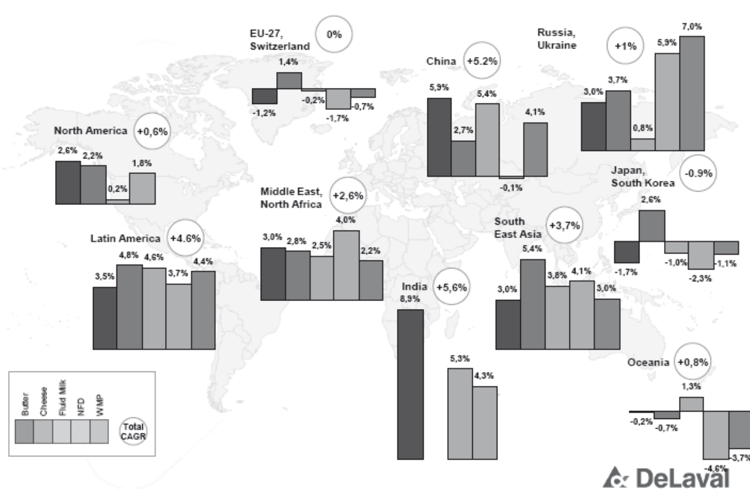
Segment	Description
Grassland	A solution for cows with access to grass feeding all year round. Grassland farming included farms where the cows were predominantly fed and housed on pastures. Climatic demands played a very important role in products and solutions to suit this style of farming, which explains their presence mostly in regions like New Zealand, Australia and South America. Grassland farmers were looking for cost effective solutions that optimized their profitability and labor management while maintaining cow health.
Heady Duty	Dairies that were typically used very intensively, up to 24 hours per day, located mainly in North America, but also Germany, Russia, Ukraine and the Middle East and expanding into areas that were seeing rapid consolidation. Cow housing typically consisted of free stall to large, open dry-lot corrals, and was often (but not always) dependent upon climate. In these cases, farmers were looking mainly for dependable, cost-effective solutions that helped them achieve their business goals and manage labor in the parlor for maximizing herd health, cow-throughput and production.
Tied Up	Stanchion barns (or Tied Up barns), where cows had their own, individual places where they could eat, rest and be milked. These types of stalls were still the predominant solution and were therefore very common all over the world. In these cases, DeLaval technologies enabled profitable business in tied up farms and provided ergonomic and comfortable solutions for people and animals.
Loose Housing	Stalls where the DeLaval solution for robotic milking was combined with 'loose housing', meaning that cows could rotate freely between different stations of the barn, where they were fed and rested and then either gathered to be milked in a milking parlor or visited a milking robot. Central to the latter case was the DeLaval Voluntary Milking System (VMS) and the customers in this segment consisted mostly of European family farms with 50-70 cows.

Source: DeLaval (2008)

11.4 The Global Milk Business

After a few years of stagnation, the global demand for dairy products was estimated to recover and grow with an average of 2.4% annually for the period between 2008 and 2012. In key demand markets, like China, the demand was increasing exponentially at an average of 8.5% per year until 2013, while in other strongly developing markets, including Russia, Ukraine, Mexico, Algeria and India, growth in demand was estimated to be strong but slightly lower, with an annual average between 1.5% and 6.5%. In sharp contrast, the demand for dairy products in the large and dominant European and North American markets was estimated to be negative until at least 2013, see **Exhibit 11.1**.

Exhibit 11.1 Dairy Consumption Growth (2006-2010)



NF= nonfat dry milk; WMP= and whole milk powder

Source: DeLaval (2008)

On the production side, global milk production was estimated to expand by 2.5% to 710 million tons in 2009, a far slower pace than in previous years. Growth prospects had been affected by a number of factors as international markets had been responding to the historically high international levels of feed price and opportunity costs for pasture in the previous few years. Moreover, new issues related to food safety concerns had surfaced in some areas, clouding the dairy outlook.

South America and Eastern Europe were expected to play a dominating role in milk exports thanks to ample supply of cheap land and labor. Forecasts for North America, India, New Zeeland Australia, Russia and Argentina suggested steady moderate annual growth between 1.5% and 3%, while in China the production of milk was predicted to grow with an average of 4.2% annually in the period between 2009 and 2013. Although this Asian country was indeed the center of growth in world milk production, China was not expected to play a role in the export markets due to the political nutritional goals set by its government.

Since the 1960s, milk production in the largest producing areas of Europe and North America had been based on two basic types of dairy farming: large and medium-sized farms. The European medium-sized farms, with herds typically around 50-100 cows, were generally family owned/operated capital intensive units with a high degree of automation. In many cases, mid-sized farms were modernizing not only through investments in new generations of milking equipment, but also through increasing herd-size. A clear trend following the degree of modernization was the increasing level of commercial professionalism and com-

petence, which was generating new demands on the suppliers of dairy farm equipment and services in terms of more support for technologically advanced solutions, training and investment advice. While the owners/operators of mid-sized dairy farms had traditionally been served by technicians, sales representatives and retailers of feed as well as less complex equipment, the new integrated technological platforms placed demand on the sales and service sides in terms of need for expert advice. On the other hand, at the lower end of the mid-sized farming, farmers were struggling with making the necessary minimum-level investment to stay in business. Their service needs were often met by the traditional sales representatives and existing retailer chains, but with the increasing diffusion of robotic milking systems and software-based solutions also the low-end of the mid-sized farms was starting to require specialized support.

The North American market, dominated by large farms with an average of about 1,000 cows each, was experiencing a strong stream of farm consolidation. As a result it was estimated that in 2007, 90% of the milk production in the region was produced by less than 3% of the dairy farms, data that reflected the investment boom that had interested the dairy farming industry in the previous years. The combination of increasing demand for milk products and the tendencies to international market de-regulation over the previous decades had underpinned the in-flow of investments into the industry. Since the 1990s, these financially driven actors had been speculating in balancing lower milk prices with increasing efficiencies in dairy farming to the end of winning export market shares in competitively priced milk. To balance lower prices with increasing efficiencies, financially driven investors had channeled their investments towards new levels of economies of scale in dairy farming.

Such a trend had been on-going for many years in other markets typified by low land prices and inexpensive agricultural labor, namely Latin America, the Middle East and Eastern and Central Europe, including Russia and Ukraine; this was helped also by the investments made by multinational actors such as NZ Farming and Al Safi International. In addition, the major international processors, e.g. Fonterra, Danone and Nestlé, had embarked on a vertical integration strategy in order to secure supply of low-cost milk for their processing business, reinforcing the trend towards large-scale farming. With financially driven large scale farming entering the industrial approach to an even higher degree than that of the professionalized dairy farms, operators of this type of farms expected specialized support from their suppliers. Just as with the industry more generally, there was a trend within large scale farming to look for turn-key solutions and first-tier suppliers.

The soaring demand for milk was also driving another type of dairy farming business, namely small 'entry line' family farms. Typically embedded in the system of 'informal' milk production in the third world, with only a few cows and/or buffalos and production of milk for barter trading, producers were starting to make investments in milking equipment to sell milk to the 'formal' sector of milk processors in the dairy product industry. This type of dairy farmers were also forming cooperatives to share the financial burden investing in clean and safe milking stations to which the farmers were taking their cows and buffalos for milking on a daily basis, therefore guaranteeing a stricter level of quality control.

11.5 The Supply Side: Dairy Farm Equipment Industry

On the supply side, the market was just as fragmented, with small local producers specialized in one particular segment of operation covering up to 50% of the market. Although these producers, defined by DeLaval as 'grey competitors', could not compete with the Swedish company in terms of global distribution and product range, they could still limit the market penetration of DeLaval in some specific segments of the market. Some form of competition was also coming from so-called 'global specialists', meaning big global players that would compete directly with DeLaval in specific sectors. One such example was Ecolab, a world-leading provider of cleaning, food safety and health protection products and services for the hospitality, foodservice, healthcare and industrial markets.

The closest competitor for the Swedish company in the global market was the German Westfalia Surge. Even though its market share was only half of that of DeLaval, Westfalia Surge was more similar than the local competitors in terms of product portfolio, offering a wide range of products in the fields of milking, cooling, feeding, herd management equipment and dairy supplies. Westfalia Surge was part of the GEA group, a global technology group that ranged from food, chemical and petrochemical industries, the energy sector, air treatment and shipbuilding as well as pharmaceutical and cosmetic industries, owning more than 250 companies in 50 countries with a total of over 19,000 employees and generated sales of EUR 5.2 billion in 2007. Other global competitors offering milking systems and other similar products were the Dutch Lely, the Belgian BouMatic and the English Fullwood. Relying on independent dealers that were not always exclusive, DeLaval was aware that in some cases their products were presented to the customer together with some of the competitors' products. At the same time, the Swedish company could count on the widest distribution network and the most efficient customer service, which resulted in a high level of loyalty among its distributors.

11.6 How to go to Market?

The market for dairy farm equipment was changing rapidly. With the new levels of consolidation and the alterations in the entry-line farming, the need for continuous increases in productivity and quality was high. In many respects, DeLaval was well positioned to benefit from the current transformations typifying dairy production. A need for greater efficiency, monitoring of sanitary conditions and milk quality, modernizing of feeding systems and cost control all resonated with DeLaval's previous and on-going investments in integrated automatic dairy farming solutions. This growing segment of the market presented DeLaval with favorable conditions, as the new type of customers (e.g. industrialized large scale farming, entry-line cooperatives, and dairy farming closer to urban centers in China) all represented consolidation and demand for modern equipment with a focus on quality and food safety.

At the same time, reaping profits from these favorable circumstances was conditioned by the company's ability to approach and serve the needs of the emerging investors. While the

company had a very good understanding of how to approach farmers in their traditional core markets, an increasingly complex technology base and new markets called for upgrading of the sales channels. In Europe and the US, high tech offerings and the importance of software-based information systems created a need to ramp up the knowledge of sales and service reps to face the demand of high tech solutions. As indicated by the difficulty to be successful in both capital goods and aftermarket and consumables, there was still plenty of room for improvements concerning the group's strategy for how to best approach and serve dairy farmers. Furthermore, DeLaval knew that one possibility to substitute volumes from dairy equipment was to make increased efforts to get sales volumes from aftermarket products and services, including feed, feeding system, advanced barn equipment and health related products and services. Also, the aftermarket products and solutions required in-depth specialized knowledge to the end of selling advanced products.

DeLaval's leadership depended on 125 years of innovation, but reaping the innovative investments was dependent on the company's ability to interact with the end customer. In DeLaval's situation, the B2B-offerings investments were substantial relative to the farmer's business volume, and the returns needed to be calculated over many years. Each investment decision reflected a calculation of the balance between input factors like feed price, water availability and land price, and an informed view about the often complex national and supra-national regulations and political trends on which farming depended more generally. To raise the confidence levels, dairy farmers often turned to trusted business advisors with which they had long-term ties. Among those advisors, the sales representatives were often among the most trusted for the simple reason that the relationship between buyer and seller dated back many years.

Over the past few decades, DeLaval's sales process has been governed through a 'three-tier' system involving both direct and indirect sales channels. Following this approach, the company was represented in the front line by about 1,409 sales representatives and 4,155 service technicians working directly or indirectly for DeLaval. Apart from the wholly-owned local sales organizations and shops, the company was selling through 1,240 independent dealers, who had historically played an important role in driving the sales of DeLaval's products and services in a wide array of national markets, such as in North America. In total, independent dealers were employing 77% of the total of sales representatives and service technicians interacting directly with DeLaval's customer base (see **Exhibit 11.2** and **Exhibit 11.3**). It is noteworthy that the typical dealers were not big national dealer chains, but rather small-size family business operations or regional farmer cooperatives. (For dealers, see http://www.delaval.com/Sales_Contacts/)

Exhibit 11.2 World Milk Production (2006-2010)

Source: DeLaval (2008)

Exhibit 11.3 Direct and Indirect Sales

Source: DeLaval (2008)

Hence, the network of dealers represented a historical evolution as well as the specific strategic position taken by the company. Historically – because of the diverse and far flung markets – the company's strategy was to view the dealers as the proper end customers. From that point of view, each individual dealer willing to buy and market DeLaval's products was seen as a welcome addition to the customer list. Exactly how each dealer interacted with the dairy farms was outside DeLaval's strategic scope. On the front line, thus, DeLaval was represented by both its Local Sales Offices (LSO) and the independent dealers offering four main sales channels.

The front line people were supported by the second and third line of back-office support functions. The network of regional and national sales offices (companies) represented the 'second line', which mainly supported sales representatives in direct contact with customers with deeper level of technological expertise.

The regional sales offices constituting the second line were also responsible for carving out and reinforcing the overall approach to the local markets, e.g. product strategy and tools to adapt technologies for local demand, and customer programs. Four customer solutions centers and eight teams of product specialists made up the third line. Product specialists, representing the company's different product portfolios (VMS, Milk Quality & Animal Health, Farm Supply & Barn Equipment, Service & Spares, Cooling, Nutrition), were co-located close to the main R&D activities and the HQ in Tumba, Sweden. Their role was to develop portfolios and applications based on the company's R&D. Product specialists also provided product training to DeLaval's sales organizations. The product specialists worked closely with solution centers. Being located closer to customers in Europe, North America and Oceania, the responsibility of the customer solutions centers was to adapt products and solutions to local farming conditions typifying the local markets. Typically, third tier employees typically university graduates with advanced degree, many of them with PhDs, within the agriculture, engineering, veterinary, nutritional, biology, or the field of business.

With regards to DeLaval's varied product catalogue and service offerings, particularly the front line had a specific set of strengths and weaknesses. As suggested by past achievements, the first line had specialized decades before in marketing automatic machine milking system to mid-size and large family-owned farms in the EU and US markets. Competitors had often cited DeLaval's distribution system, or more precisely the company's network of dedicated sales representatives, as a barrier to entry. As long as the long-term relation between the sales representatives and the dairy farmers remained trustful and close, there were few chances for the competitors to establish similar customer-relations.

By 2008, however, managers within the company had started to feel that the strategic positioning of the company as selling to dealers made less sense than a decade ago. All dealers were put in the same basic category and offered basically the same contract with few if any modifications on the notion that 'one size fits all'. In essence, DeLaval did not discriminate between more important dealers that it worked closer with and less important dealers operating at arm-length relations, nor had it established a set of criteria for segmenting dealers. With no differentiation among the dealers, there were few incentives for dealers to specialize their sales. Therefore, the dealers were agnostic about brands and tried to keep a neutral profile, offering DeLaval's equipment side-by-side with their main customers.

Stefan Bergstrand, a senior dairy expert with DeLaval, offered a clear view of the disadvantages: "DeLaval has the same issue with dealers as all companies that are going to the market through indirect channels. We have not yet developed a good set of tools and incentives for the dealers to prioritize our equipment in their marketing strategy." But there were also additional problems. In particular, the high-tech turn in the industry required firms to get deeper insights into the practices of dairy farming. Stefan Bergstrand, again said: "Al-

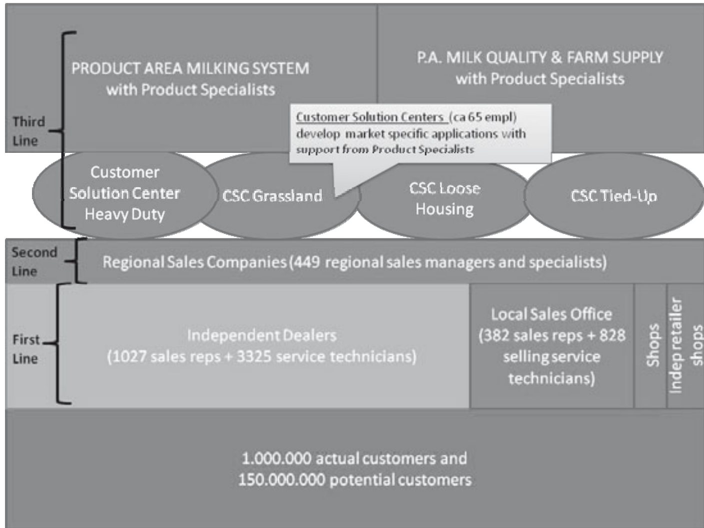
though the dealers are doing a good job many times, we have lately experienced that dealers can represent a filter between us and the farmers we need to be close to. This problem is becoming more and more difficult because the development of our new product lines and service offerings require closer cooperation with farmers working under different conditions. Indeed, we are part of the problem and need to find better ways to work with dealers." Furthermore, DeLaval has not issued the right support to dealers, making it hard for the network of dealers and sales representatives, in certain parts, to cope with marketing DeLaval's new high tech product offerings, such as herd management software and the company's range of nutrition products like feedtech silage, calf feeder, feed stations, etc.

Table 11.3 The Front Line

Channel	Description
Sales Technicians	Covering a role of the service technicians goes beyond supplying technical services on installed equipment; technicians have gradually become important sales channels for after-market products as well as advisors to the farmer. The typical ST is male, around 50 years of age and has some kind of technical training but does not have a university degree. Internal training and on-the-job experience provide the backbone in the STs training.
Sales Retailers	A role tied to the core business that is the selling of traditional and automatic milking systems to mid-sized farms. In the business, the forging of close personal relationships had always been necessary. In this respect, SRs were also covering the role of consultants to the farmers, needing therefore to have deep knowledge about the individual customer's farming business as well as the key changes in the business environment. On average, SRs were also at least 50 years of age and lack university level education; therefore, internal training was very important. Very often, the SR had been with the company for most of his career.
Shops	Independent retailers played a major role in the sales of the basic after-market commodities. Shops were an important interface to the customer, but increasing consolidation of retailing was increasing the purchasing power of independent retailer chains, farmer cooperatives included. In this context, DeLaval products were exposed alongside those of the competitors, a problem that the company had overcome in some markets by developing a fleet of truck-based 'mobile shops', which allowed improved margins in the after-market sales.
Internet	DeLaval was in the process of implementing a strategy for Internet B2B-services. The website partly aimed at promoting DeLaval's solutions, partly at facilitating peer-to-peer discussion. It also aimed at implementing an e-commerce function for the company's wide assortment of after-market products. The company was also considering implementing telemarketing.

Source: DeLaval (2008)

Exhibit 11.4 Sales Support – the First, Second and Third Lines



Source: DeLaval (2008)

11.7 Outline of a Customer Centric Go-to-Market Strategy

Just a few days before, Benoît had proposed a plan for a drastic overhaul of DeLaval's policy for channels as well as the company's customer segmentation model. According to Benoit, the company needed to 'own' the relationship to the customer in order to be able to capitalize effectively on trends in the dairy farming industry in the years to come. Therefore, Benoit had proposed replacing the functional model of customer segmentation (i.e. segmenting customers on the basis on type of milking systems in use) with a new customer segmentation model that would take into consideration both the size of the farm and the key factors affecting the customers' decisions.

Moreover, Benoit's plan involved a structured way matching customer type with channel type, according to an estimation of customer service demands and important characteristics of the sales channels. By taking the point of departure in the customer needs, the model highlighted the need for upgrades in service offerings for large and investor farms. The focus on industrial logic and high through-put in large scale farming, called for a service level that the conventional channels have problems meeting. In particular, the expectancy of on-time delivery of after-market products and services has been a weakness. Also, service technicians, with their limited experience with advanced chemicals, software solutions,

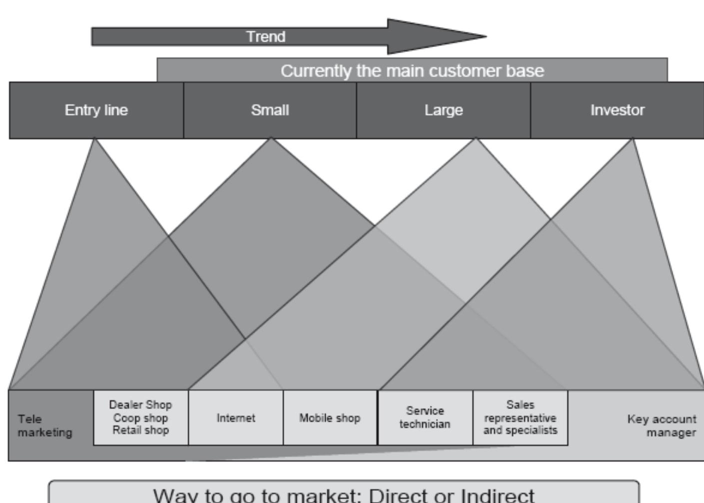
etc., call for innovation within the channels (e.g. key account managers and specialized sales and service functions).

Table 11.4 Outline of a New Customer Segmentation Model

	Entry-Line Farm	Small Farm	Large Farm	Investor Farm
Type of Business	About to enter formal milk production. Making their first investments. Small scale, but coopera-tives may increase size.	Traditional family farms lagging behind. Must improve effi-ciency and size to remain in business.	Modern family-owned farms with a high degree of compe-tence, carefully planned operations and already high degree of automa-tion.	Financially motivated external investors. Industrial approach.
Key Factors in Customer Decisions	Cost Value–Performance As little as possible	Price / features & benefits No frills Local Relationship Value–Performance	Brand loyalty and relationship must be proven competitive in the long-term. Service & support Trust, reputation, reliability	Max throughput Low Price/High value 24/7/365 perfor-mance Economies of scale – ROI
Key Dimensions of Value to Customer	Key Dimensions of value to customer Low cost and early return to investment key.	Require support and business advice on how to modernize their farm to be financially viable in the future. Also need advice basic farm manage-ment skills. Often multi-skilled operators capable of servicing their exist-ing set-up, but need training on more advanced products.	Require training for advanced products and systems. Expect a high-degree of service and busi-ness advice for complex system investments. Focus on family business and the family's long-term ROI. High expectancy on coordination of their technical support and business contacts.	Focus on turn-key solutions and struc-tured sourcing sys-tems. Deal only directly with 'first tier' supplier Focus on ability to demonstrate industri-al logic with focus on short-term financial performance.

Source: DeLaval (2008)

Exhibit 11.5 Integration of New Customer Segmentation and Front Line Channels



Source: DeLaval (2008)

With the meeting ahead of him, Benoit was wondering how DeLaval's go-to-market-strategies needed to evolve to meet the new demand and how the implementation of the more newly segmented multi-channel approach needed to be customized. Even though he believed in the new plan in general, there were still numerous outstanding issues he could see in front of him.

As he reflected on the company's ambition to lead innovation and be the first to serve the customer, he could not help thinking that the company had evolved faster than its sales force. There was, it seemed to Benoit, a gap between the high-tech profile of the company and its aging sales force. With respect to the independent dealer networks, he asked himself how the relationship to the dealers was going to evolve when the company's strategy would aim at 'being the first to serve' the customer'? Could the relations to dealers be re-formed, or did Delaval need to move to more drastic solutions?

Moreover, DeLaval had little experience in large scale farming, since its own sales representatives were mainly specialized on family farms. In this line, Benoit wondered how the company could acquire competence and implement a channel with key account managers, targeting the large-scale farms and entry-line cooperatives. The task lying head was not just to grapple with these questions one-by-one, but to review all the options and to put together a specific recommendation building on a set of well-argued, clear priorities.

Student Assignments

DeLaval is a relatively small multinational. However, it addresses a large number of national markets. Given the company's size and the on-going transformation of the milk markets, outline an idea for a makeover of the company's method of going to market.

References

The case study builds on several interviews the author conducted with DeLaval in 2008 and was compiled from privileged access to privately held company information, which are prohibited from further disclosure.

12 Growing with the Wind: The Case of Vestas

Rolf Wüstenhagen, Good Energies Chair for Management of Renewable Energies, University of St. Gallen

Wind Power: Vestas' Fortunes Hinge on the U.S. Wind Market

Everybody's waiting with baited breath to see how the U.S. wind-power sector develops this year, but few more so than Vestas, the world's biggest wind-turbine maker and a sector bellwether. Vestas, which just reported its best-ever sales and profit numbers, is hedging its optimistic 2009 outlook based on what happens in the U.S., which is by far Vestas' biggest market. The company expects a 19% jump in sales this year to 7.2 billion euros – but only if wind orders pick up substantially in the first quarter.

"We feel more certain other markets will do their part…where in the U.S. the jury is still out," Vestas chief executive Ditlev Engel told Dow Jones Newswires. If the wind market doesn't recover from the near-total "collapse" in the fourth quarter, Vestas said, the company will rethink its planned 1.2 billion euros in capital spending this year, including expanding three U.S. factories. If orders don't pick up globally, Vestas warned it would have to "seriously consider" layoff. (…)

The U.S. renewable-energy sector, led by wind, is grappling with the fallout of the credit crunch, which has choked off financing for many new projects, even as clean energy enjoys growing political support. "The political climate has never been better, while the financial climate has never been worse," Mr. Engel said at the earnings presentation. (…)

Wall Street Journal, February 12, 2009

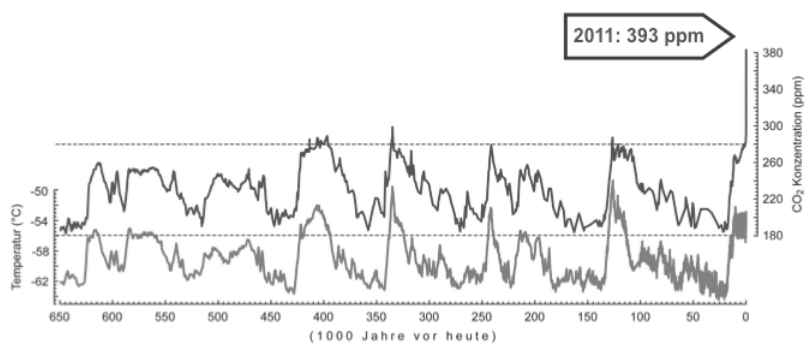
12.1 The Wind Energy Industry – Leading the Transition to a New Energy Economy

Countries around the world have increasingly become aware of the challenges of climate change and global warming. The Intergovernmental Panel on Climate Change (IPCC) has provided clear scientific evidence that the concentration of greenhouse gases, such as carbon dioxide (CO2), is much higher today than ever before in the last 600,000 years (see **Exhibit 12.1**). As a conclusion, IPCC estimates that the level of global CO2-emissions needs to be reduced by 80% before 2050 in order to avoid dangerous changes in the earth's atmosphere. Burning fossil fuels such as coal, oil and natural gas for power generation, heating and transportation is the most important source of manmade greenhouse gas emissions.

T. Rudolph et al. (Eds.), *Diversity in European Marketing,*
DOI 10.1007/978-3-8349-6976-7_12, © Gabler Verlag | Springer Fachmedien Wiesbaden 2012

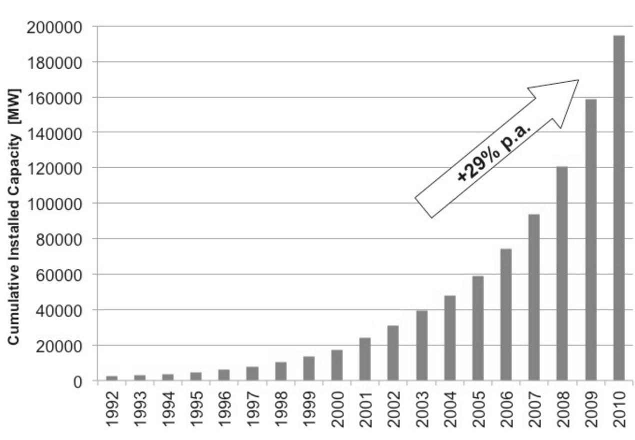
More than 80% of the world's energy supply comes from non-renewable sources, and about 66% of global oil reserves are found in a small number of countries around the Persian Gulf.

Exhibit 12.1 650,000 years of GHG Concentration and Temperatures



Source: adapted from IPCC (2007)

Exhibit 12.2 Historical Growth in Worldwide Wind Energy Capacity 1990-2010



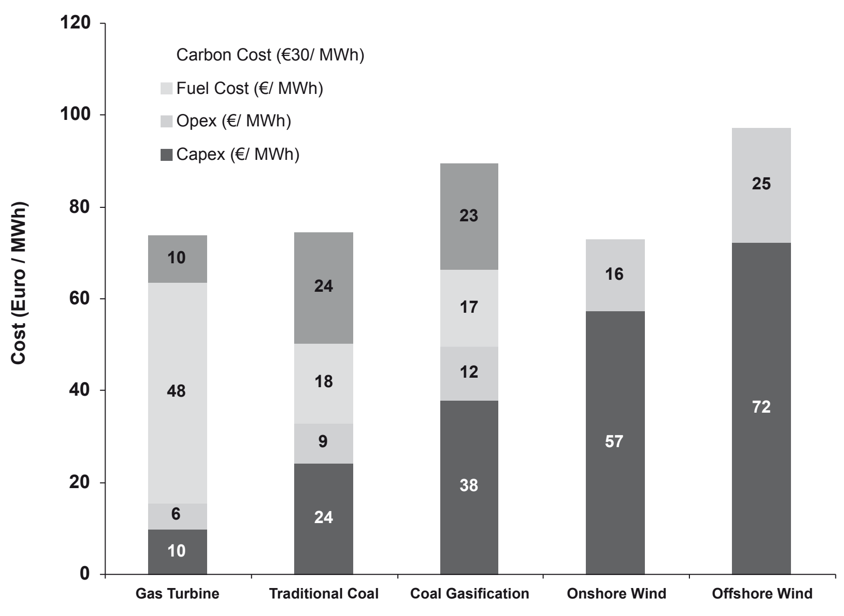
Source: GWEC (2011)

An important option to curb greenhouse gas emissions, while at the same time decreasing energy import dependence, is to use renewable sources of energy such as electricity generated from sun, wind and water (IPCC 2011). Among those technologies, wind energy has

recently experienced the most significant growth and is now the most widely used form of renewable energy worldwide. The global wind energy market has grown with an average 29% p.a. worldwide over the past two decades (**Exhibit 12.2**). Initial growth has been facilitated by favorable energy policies in countries like Denmark, Germany and Spain.

More recently, while still enjoying political support, wind energy is also increasingly becoming one of the most economically competitive forms of power generation (**Exhibit 12.3**). Technological progress has led to larger and more efficient turbines, and the ever-increasing scale of manufacturing facilities has allowed suppliers to reap additional economies of scale. The entry of large incumbent firms from the electrical engineering sector, as well as new entrants from China, have further contributed to cost reductions. On the other hand, traditional sources of power generation have become more expensive due to carbon regulation and fuel price volatility.

Exhibit 12.3 Cost of Generating Electricity from Coal, Gas and Wind Power



Source: EER (2007)

2008 marked yet another record year in the history of the wind energy sector. A total of 27,056 Megawatts (MW) of wind turbines were installed worldwide (see **Table 12.1**).

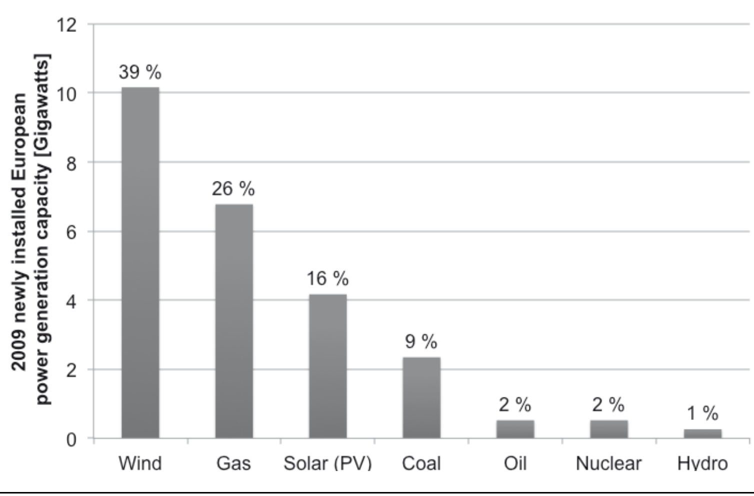
Table 12.1 Global Wind Market 2008 by Country

Country	Cumulative Capacity (MW)	Newly Installed Capacity (MW)	Year-to-Year Growth (2007-2008)
U.S.	25 170	8 358	49.7%
Germany	23 903	1 665	7.5%
Spain	16 754	1 609	10.6%
China	12 210	6 300	106.6%
India	9 645	1 800	22.9%
Italy	3 736	1 010	37.1%
France	3 404	950	38.7%
UK	3 241	836	34.8%
Rest of the World	22 728	4 528	24.9%
Total	120 791	27 056	28.9%

Source: GWEC (2009)

In Europe, in both 2008 and 2009, more wind energy was installed than any other source of electricity, including gas, coal and nuclear power plants (see **Exhibit 12.4**).

Exhibit 12.4 EU New Power Generation Capacity 2009



Source: European Wind Energy Association, Platts (2010)

Whereas politicians and industry associations in several countries adopted rhetoric of 'nuclear renaissance', new nuclear capacity was limited to two reactors under construction in Finland and France in 2009, compared to 10,163 MW of new wind turbines in Europe alone. Internationally, the U.S. and China were the top two countries in terms of newly installed wind turbines with 8,358 MW and 6,300 MW respectively. Germany now ranks second in terms of cumulative installed wind energy capacity (23,903 MW) and gets 8% of its electricity from wind. Denmark continues to be the country with the highest share of wind energy in its national power supply (20%). On windy winter nights, up to 100% of Danish electricity is generated by wind energy. The fluctuating nature of wind resources implies that wind power works best in a portfolio of different electricity sources. For example, countries with large capacities of hydropower storage plants like Switzerland or Austria are well positioned to supply energy-on-demand that complements the production characteristics of wind energy.

In Germany alone, the wind energy industry now accounts for over 96,000 direct jobs in wind power companies (BMU 2011), and further development of the renewable energy sector is seen as an important driver of economic growth. The installation of new wind turbines has also contributed significantly to the reduction of greenhouse gases. According to the European Renewable Energy Council, the wind turbines installed in Europe by the end of 2010 avoid the emission of 99 million tons of CO_2 per year – equivalent to taking 50 million cars off the road, or about one quarter of the EU's obligation to reduce greenhouse gases under the Kyoto protocol (EREC 2004).

As this short snapshot shows, the global wind energy industry is a booming sector with an excellent growth outlook. At the same time, while a handful of European countries have achieved a significant penetration of wind energy in their power supply and others like the U.S. and China have started to catch up, the wind industry is still facing strong competition from dominant conventional players. Also, the concentration on a relatively small number of key markets and the strong influence of regulatory drivers implies a number of specific risks and opportunities. The next section provides a glance at market leader Vestas Wind Systems.

12.2 Vestas Wind Systems – A Danish Niche Player's Journey to Global Leadership

1898-1978: The Early Days of Vestas

The roots of Vestas date back to the end of the 19th century, when blacksmith H.S. Hansen opened his first workshop at Lem (Denmark). According to Vestas' history, Smith Hansen had a reputation for creating many ideas and showing fearless initiative, inspiring many of his colleagues at the time to start their own businesses and thus contributing to the emergence of an important center for the blacksmiths' craft at Lem. It was not until thirty years later that H.S. Hansen and his son, Peder Hansen, founded their first industrial company, Dansk Staalvindue Industri, a manufacturer of steel window frames for industrial build-

ings. After World War II, Peder Hansen formed a new company, Vestjysk Stålteknik A/S, which subsequently changed its name to Vestas. With starting capital of DKK 75,000, Vestas moved into the Business-to-Consumers (B2C) market of manufacturing household appliances and kitchens. Over the following 15 years (1945-1960), the company's product range continuously evolved, from appliances to agricultural trailers to intercoolers. In 1960, Vestas' offices and warehouse burnt to the ground and the factory had to be rebuilt. As a consequence, the company faced several years of consolidation, until it identified, in 1968, hydraulic cranes for light lorries as a new promising product area, which proved to be a major export success in a flourishing B2B market. A couple of years later, as the two oil crises of the 1970's hit the transportation industry and lorry crane sales declined, Vestas had to look for yet another growth area.

1979-1985: First Steps in Wind Turbine Manufacturing

Inspired by the second oil crisis in 1978-79, Vestas began to examine the potential of wind turbines as an alternative source of energy. Initially, they chose the Darrieus Turbine design, but after 18 months of experiments, the company decided to focus on a three-blade model, which soon became the dominant design in the wind industry. In 1979, the first wind turbines were delivered to Danish customers. Though being an industrial product, these deliveries were rather taking place in the B2C market, classically with medical doctors or other wealthy individuals enthusiastically investing in independent and environmentally benign power production. Subsequently, the industry experienced its first boom, mainly driven by government incentives in Denmark and the United States, with Vestas definitely also entering a market driven by governmental incentives (B2G market). Vestas started serial production of 55 kW wind turbines in 1980. By 1985, the number of employees increased to 800. It was also in 1985 that Vestas introduced pitch-regulation, a major technological innovation that optimized the energy output of a wind turbine by constantly adjusting the angle of the blades to current wind conditions. By the end of that same year, Vestas had sold 2,500 wind turbines to the US.

1986: Crisis and Turnaround

The strong exposure to the US market turned from blessing into curse for Vestas when at the end of 1985, the California tax credit legislation expired for the first time. As a consequence, Vestas' US market collapsed and, after a rescue plan failed, the entire company filed for bankruptcy in October 1986. This demonstrates that Vestas' characteristic ability to take advantage of growth opportunities wherever they emerged around the globe was not only a high-return, but also a high-risk, strategy. A more cautious approach to the booming California market might have mitigated downside risk, but would also have had limited upside potential if the tax legislation had in fact been extended. Another way of looking at this crisis is that Vestas apparently was better at managing technology risk than it was at managing regulatory risk. No governmental advisory services were then in place at the technology-focused company Vestas. On the positive side, there was a healthy core of the company that allowed for a major restructuring, which finally led to the establishment of a new company called Vestas Wind Systems A/S in 1987. After large parts of the Vestas

Group had been sold off, the new company emerged as a pure wind energy player, managed by the new CEO Johannes Poulsen and with a dedicated team of 60 employees.

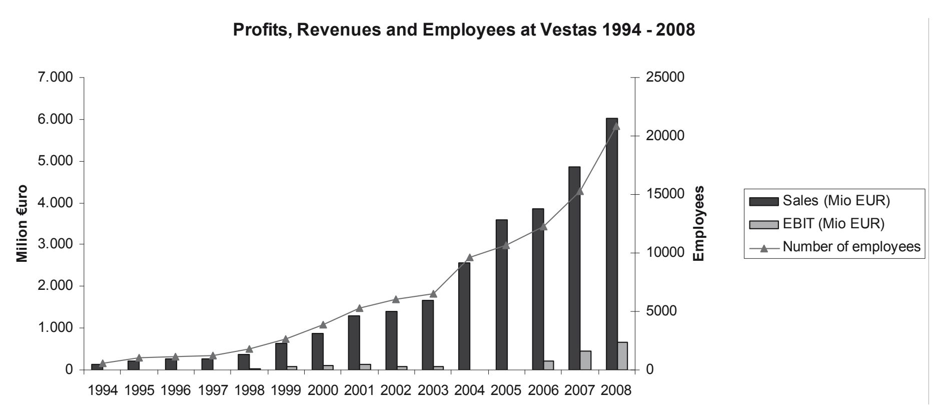
1987-2001: Strong Organic Growth and IPO

It soon became apparent that the new Vestas was set to become a unique success story. The years 1987 to 1997 saw a sequence of international expansion, technological innovation and ever larger orders. The company set up subsidiaries in India (1987), Germany (1989), Sweden, and the US (both in 1992), and formed the joint-venture Gamesa Eolica in Spain (1994), where Vestas held 40% of the shares and Gamesa, the parent company, 51%. The Spanish market became a particularly important market in the mid-1990s when big utilities started placing large orders to benefit from government incentives. In terms of technology, Vestas – as did its very first competitors – gradually increased turbine size with every new generation of their product. While the company had entered the wind turbine business with a 55 kW machine back in 1980, it introduced its V39-500 kW turbine in 1990, followed by the V44-600 kW turbine in 1994 and the V66-1.65 MW turbine in 1997. Today, the company offers a V52-800 kW, the V60-800 kW for the Chinese market, the V80-1.6 / 1.8 MW for the US market, the most successful V90-2 MW for the global market, the V90-3 MW for stronger and offshore wind sites, as well as a V100-3 MW and its new V112-3 MW for low wind sites especially in maturing markets.

Most of Vestas' exceptional growth during this period (see **Exhibit 12.5**) was organic, accelerated with only selected acquisitions as in the case of DWT – Danish Wind Technology in 1989 or Costas Computer Technology A/S, a long-standing supplier of software and components for Vestas' wind turbine control systems, which was taken over in 1999. When expanding into new international markets, the company often chose to form a joint-venture together with a well-established partner in the target country, as was the case with Vestas RRB India Ltd. or the joint-venture with Energy System Taranto S.p.a. in Italy. In countries where Vestas felt comfortable that they knew the market, however, they went in with fully owned subsidiaries, as in the cases of the US, Sweden and Germany.

This decade also saw Vestas' first turbine deliveries to a smaller offshore project, involving ten 500 kW turbines in the Baltic sea in 1995. Also in 1995, the company for the first time exceeded 1,000 employees and generated more than 200 mio € of revenues, a 66% growth rate over the previous year (for convenience, all financial figures in this paper have been converted from Danish crowns to euros with the exchange rate of July 2009: 1 DKK = 0.134 EUR). It became increasingly clear that in order to maintain the pace of growth, the company needed additional sources of capital. Two years later, in 1997, the company introduced two new turbine models and consequently posted a slight loss, despite sales growth (in MW) of 24%. Therefore, in early 1998, CEO Johannes Poulsen announced that the time had come to float the company on the Copenhagen Stock Exchange, stating that in his opinion, "there is no doubt that in future environmental factors will play an increasingly large role in any political and probably also any commercial decision" (Press release announcing IPO, March 23, 1998).

Exhibit 12.5 Profits (EBIT), Revenues and Employees at Vestas 1994-2008



Source: Vestas Annual Reports (1994-2008)

Vestas' initial public offering in April 1998 became a big success. The shares were eight times oversubscribed and the company raised 175 million euros of fresh equity capital to finance its future growth, including new international subsidiaries and new fiberglass production and turbine assembly facilities. During the year of its IPO, Vestas increased revenues by 45% and opened production in the newly established Italian joint venture in July 1998. Within its first year, the Italian subsidiary immediately generated revenues of 35 million euros with just 50 employees. 1999 saw the opening of a new blade factory in South-Eastern Denmark, an area of high unemployment that provided good recruiting opportunities for Vestas, as well as the launch of a prototype V80-2.0 MW turbine. 1999 became another record year for Vestas, largely due to exceptional growth in the US market. At the end of 1999, the Production Tax Credit (PTC) expired, an important financial incentive to wind energy generators in the US. Thus, a large number of project developers ordered turbines before the end of the year to take advantage of the incentive. As a result, Vestas increased sales by 66% and more than doubled profits compared to the previous year. In 2000, growth continued, fuelled among other things by the largest order ever for wind turbines, received by Vestas' Spanish joint-venture Gamesa from Energia Hidroeléctrica De Navarra, worth more than 600 million euros.

2001 brought more good news for Vestas, being chosen as the supplier for the first major offshore project in the North Sea (Horns Reef), which meant the largest offshore order to date, worth around 130 million euros. 2001 was also the year with the strongest growth of the global wind energy market in history, increasing by 51% over 2000 levels. In this year, Vestas achieved a market share of 24.1% and was clearly the market leader. However, 2001 can also be seen as a turning point in Vestas' history in several respects. Remarkably on the morning of September 11, 2001, the company announced that 59-year old CEO Johannes Poulsen, who had led the company since it was formed in 1987, had decided to resign from his position at the General Meeting in April 2002.

Also, increasing strategic differences between Vestas and Gamesa led to the sale of Vestas' 40% stake in the joint-venture in December 2001. Retrospectively, Vestas had ultimately helped to grow a major competitor who was now seeking independence. Finally, the outlook for the US market appeared uncertain following another expiration of the PTC. Due to different political priorities in the aftermath of the September 11 terrorist attacks and contentious issues in the proposed US energy bill, PTC extension was eventually delayed until March 2002. The company ended the year 2001 with 5,240 employees, which meant a tripling in the three years since the IPO.

2002-2004: Changing of the Guard and the Merger with NEG Micon

The beginning of the post-Poulsen era at Vestas was challenging in many ways. The start of Svend Sigaard, the former CFO and new CEO, was accompanied by the news that a major competitor had entered the market: General Electric (GE). The large US engineering conglomerate announced in February 2002 that they had acquired the assets of Enron Wind from the bankruptcy proceedings of Enron and formed a new subsidiary, GE Wind. As an established player acknowledging the growth potential in the wind energy market, this news was perceived as a boost to the credibility of the emerging industry. Given GE's influential position in the US, it may also not be fully accidental that legislation extending the PTC was passed only five weeks after they had announced their market entry. Nevertheless, given GE's expertise in the conventional power business, its strong distribution channels in North America, and its financial strength, this clearly became an important new competitive threat for Vestas. In addition, during 2002, Vestas struggled with technical problems on its new flagship V80-2.0 MW turbine and faced delays at the high-profile Horns Reef offshore project, which eventually resulted in cost overruns of 15-17 million euros. Looking positively at this, Vestas had an opportunity to learn important lessons for the emerging growth market of offshore wind parks. In contrast to the previous boom years, 2002 ended with the company's announcement that after the second profit warning in three months, they had to lay off 495 employees – the first downsizing since 1986.

In 2003, Vestas introduced its new flagship turbine V-90 3 MW, which made wind power technology even more competitive and still is a standard product in today's market. In order to step up to increasing competition, Vestas and its Danish competitor NEG Micon merged in 2004; this represented a combined world market share of 32%, which was even increased to 34% by the end of the year. In the same year, CEO Svend Sigaard resigned.

2005-2008: The 'Will to Win' leading to record results in turbulent times

In 2005, new CEO Ditlev Engel introduced Vestas' 'Will to Win' strategy with the objective of making wind a competitive source of power on par with oil and gas. Ditlev Engel formerly worked with Danish protective paint producer Hempel A/S, and his journey at Vestas did not start as a walk in the park – high steel prices combined with a weak US dollar squeezed Vestas' margins and started to severely hit its profitability. However, the PTC in the US became effective again and led to Vestas' biggest order intake so far from Horizon Wind Energy in the US. 2006 marked the opening of Vestas' production facilities in Tianjn,

China. Financially, Vestas still lost money primarily due to high repair costs. However, the 'Will to Win' strategy led to a profitable 2007.

Table 12.2 Market Share of Wind Turbine Manufacturers as of 31/12/2009

No	Name	Location	P/S*	Turbine sales in 2009 [MW]	Market share 2009 [%]	Cumulative sales since market entry [MW]	Market share cumul. [%]
1	Vestas	Denmark	P	4766	12.5%	39705	24.8%
2	GE Wind	USA	S	4741	12.4%	22961	14.3%
3	Sinovel	China	P	3510	9.2%	5658	3.5%
4	Enercon	Germany	P	3221	8.5%	19798	12.4%
5	Goldwind	China	P	2727	7.2%	5315	3.3%
6	Gamesa	Spain	P	2546	6.7%	19225	12.0%
7	Dongfang	China	P	2475	6.5%	3765	2.4%
8	Suzlon	India	P	2421	6.4%	9671	6.0%
9	Siemens	Germany	S	2265	5.9%	11213	7.0%
10	Repower	Germany	P	1297	3.4%	4894	3.1%
11	Nordex	Germany	P	1060	2.8%	6105	3.8%
12	United Power	China	P	768	2.0%	792	0.5%
13	Clipper	USA	P	595	1.6%	898	0.6%
14	Mitsubishi	Japan	S	583	1.5%	3252	2.0%
15	Mingyang	China	P	573	1.5%	747	0.5%

* P=Pure Play, S=Subsidiary

Source: BTM Consult (2010)

Vestas' financially best year ever was 2008, when operating profits increased by more than 50% year-on-year to reach 668 million euros, an increase in employment of 5,524 new employees and an EBIT margin of 11.1%. While Vestas was successful in maintaining higher profitability than many of its competitors, including GE Energy, it lost some market share in 2008. Vestas accounted for about 19% of the global wind turbine sales, with the decline

being mainly due to recent entrances and growth of new competitors in China, India and the US. In China, Sinovel and Goldwind accounted for the majority of order intakes and – although exclusively delivering to China – for 9% of global sales (in MW). Indian Suzlon exporting to the world market accounted for another 9% of global MW sales. And GE Wind's aggressive sales strategy in the US as part of its "Ecomagination" program led to a global market share almost on par with wind-focused Vestas (see**Table 12.2**).

Vestas' success in the period 2005-2008 is reflected in a more than six fold increase in its share price, from less than 100 DKK in the beginning of 2005 to an all-time-high of 692 DKK at the end of August 2008, two weeks before the collapse of Lehman Brothers marked a milestone in the global financial crisis (see **Exhibit 12.6**).

Exhibit 12.6 Vestas Share Price 2005 - 2009

Shareprice Data: euroinvestor.com (2011)

12.3 Opportunities and Challenges in Remaining 'No. 1 in Modern Energy'

Ever since it has been exclusively focused on wind energy in 1987, Vestas has been leading the wind turbine manufacturing industry in terms of market share. Being 'No. 1 in Modern Energy', as CEO Ditlev Engel puts it (Engel 2008), has not been an easy task, and remaining so in an increasingly competitive industry will lead to a number of further challenges.

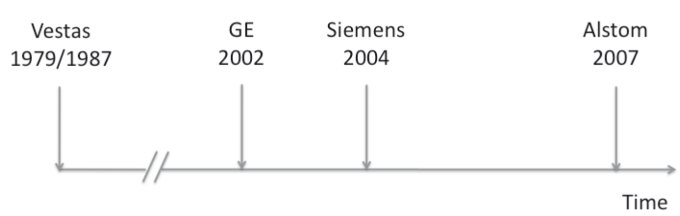
Managing Internal Growth

Not only has Vestas grown from 1,000 to over 20,000 employees in less than 20 years, but it also operates in a market where annual growth rates of 25-30% have been the rule rather than the exception for the same period. Given the favorable outlook for the wind market, the company expects to grow by an annual rate of 33% in the next three years, doubling its turbine output from 5,000 MW in 2007 to 10,000 MW in 2010. “This is more than a gigantic challenge”, says CEO Ditlev Engel, adding that “change is never easy, but when, at the same time, you are talking about developing a new form of energy at global level, it is almost as difficult as it gets.” Even for a company that has an impressive track record of managing internal growth, the dynamics of this industry represent a recurring challenge, but also amazing opportunities.

Increasing Competition

While Vestas operated in a sellers’ market for more than a decade, large incumbent players have started to enter the field since 2002, making it more important for Vestas to position itself as a preferred provider of wind power solutions. GE, under its ‘ecomagination’ campaign, launched an aggressive campaign to position itself in the green energy market. Not only marketing budgets were increased, but real efforts were put into a transformation of the company’s product portfolio and revenue streams. Between 2005 and 2008, GE increased its eco-efficient portfolio from 17 to 80 products, increased R&D investments for environmental energy solutions from 750 mn to 1.4 bn USD and boosted its revenue with ecomagination products from 10 bn to 17 bn USD (GE, 2008). On the wind turbine product side, GE now positions itself as a premium supplier of grid-friendly wind power solutions, pointing at decades of experience with various energy solutions for stable energy supply. Last but not least, GE’s financial services arm allowed the firm to offer financial solutions to customers seeing wind-financing banks drawing back from insecure markets and requiring larger shares of equity in wind projects.

Exhibit 12.7 Market entry timing of Vestas versus large incumbent firms in global wind energy industry



Source: author’s compilation

While it took GE's close competitors a while to react (see **Exhibit 12.7**), Siemens was the second major entity to enter the field two years later by acquiring Bonus, a Danish manufacturer of wind turbines. Today, the company holds a global market share of 7%. Including other technologies like fuel cells and waste-to-energy plants, the company reported 2008 revenues of 27 bn USD with its environmental portfolio. Like GE, Siemens' strong position in energy financial services gives it an advantage over a pure player like Vestas in times of a credit crunch. The firm's financial services arm is said to have supported major sales contracts in the turbulent 2009 market – amongst others with major Danish utility DONG, signing a framework agreement for 500 Siemens offshore wind turbines for the client's offshore projects in Northern Europe.

Increasing competition is also coming from China, where Goldwind, Sinovel and Dongfang are now among the top 12 producers of wind turbines worldwide, and 35 new manufacturers entered the market in 2008 alone. Vestas continues to be the largest foreign turbine manufacturer in China, with facilities in Beijing and Tianjin, and recent investments in new production facilities in China's wind-rich industry hub Hohhot.

David vs. Goliath – the pros and cons of being a pure player

A much smaller player than Siemens and GE, Vestas had a product portfolio of five Wind Turbine Generators, R&D costs amounted to 170 mn USD and achieved revenue was 8.5 bn USD in 2008. Unlike those larger players, Vestas is not equipped for major lending to its customers, a disadvantage during the financial crisis where banks have become extremely risk-averse and no longer lend up to 75% of a project's cost, despite the proven technology and often guaranteed long-term returns of those projects due to established government policies. With their extensive conventional power technology business and established relationships in B2B markets, GE and Siemens have a far stronger foothold among electric utilities and grid operators than Vestas. This is an important factor in a market where the customer base is increasingly shifting towards larger clients. With a base of several hundred customers, Vestas finds itself still serving a relatively large number of small wind energy project developers, while large utilities such as the world's largest wind power producer Iberdrola, Portuguese EDP, Spanish Acciona Energia and Endesa, Chinese Longyuan, German E.ON, French EDF-EN, US MidAmerican, or Independent Power Producers like US NextEra Energy Resources or Chinese Datang increased their holdings of wind power solutions to now form a group of the 10 largest wind power producers globally (EER, 2009). Some of them started to build up their own development departments or subcompanies. Not least during the financial crisis, utilities with relatively large financial means and modest interest requirements find themselves more capable of finalizing wind projects through increased balance sheet financing with at least 50% equity.

On the other hand, almost like a David among Goliaths (Hockerts and Wüstenhagen 2011), Vestas' focused position and smaller size also have important advantages. When it comes to being an early player in new markets, Vestas has developed unique capabilities in its 20 plus years of being a 100% wind-focused company. It is the most internationally diversified focused wind turbine producer and marketer with global exposure (see **Exhibit 12.8**). Ves-

tas' wind market know-how on practically every wind market in the world remains unmatched. This put Vestas in a good position to profit from global markets wherever they were. When one market became too saturated and price-competition too fierce, Vestas was and is still able to sell where conditions are more favorable. And looking at the global market as a whole, the wind market has probably been one of the most attractive markets in recent economic history with growth-rates comparable to those in the emergence of IT markets.

Exhibit 12.8 Vestas' Global Revenue Distribution

Source: Vestas Annual Report (2008)

On the customer side, more and more utilities and experienced wind park developers are starting to look for new opportunities in emerging markets. While it was hard for some to take their suppliers of wind equipment off to new markets, Vestas is present in almost all markets where turbines have been sold so far either through local offices and production or through local or nearby service staff. Its historic first-mover advantage in many emerging markets especially in Eastern Europe, Asia and Middle East differentiates Vestas from most competitors and puts it into a favorable position as a supplier to increasingly internationalizing customers.

Exhibit 12.9 Vestas' 100% Wind-focused Value Chain

Source: Company Data

Vestas' complete focus on wind power, or 'modern energy' as the company calls it, not only makes it the most experienced player in the field with unmatched know-how about the global wind business, but it also allows it to invest in its business without making compromises. Large incumbent players entering the wind industry, in contrast, may find them-

selves in the midst of internal and external controversy between 'new' and 'old' business, where existing customers push back against a focus on renewables. Jeff Immelt, the CEO of GE, pointed out that introducing the 'Ecomagination' strategy was not easy to do for exactly those reasons: "There were plenty of guys on our energy team who hated this in the beginning because half of their customers were saying they hated it" (Stewart 2006). Immelt explains that he managed to convince the skeptics by outlining the long-term objectives behind Ecomagination and presenting it as making pure business sense: "We just kept talking: 'Here's where we're going. Here's why we think it's good for both of us. And it's going to come someday anyhow, so let's get ahead of it'" (ibid). And although Ecomagination's sales numbers today provide evidence that customers liked the products even more than expected, large players such as GE and Siemens still also serve clients whose core business is in the coal or nuclear business, sometimes perceiving wind as too junior and as an inconvenient form of power production.

Managing risk & opportunity of a 'political climate that has never been better'

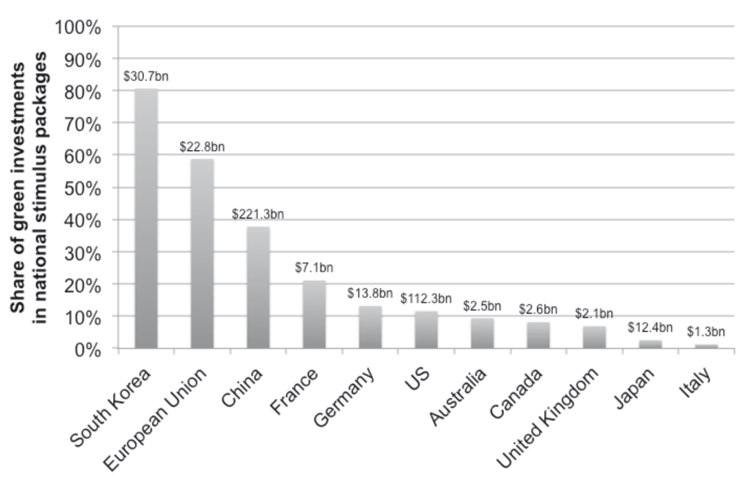
As quoted in the introduction, Vestas CEO Ditlev Engel pointed out at the 2008 earnings presentation in spring 2009 that "the political climate has never been better". Awareness for the environmental, economic and social challenges as a result of global warming, the issue of energy security in the light of scarce resources and increasing demand from emerging countries as well as the quest for identifying opportunities to create 'green jobs' have created significant momentum in the international policy arena that can work to the advantage of renewable energies. Wind energy, as the most mature renewable energy source available (apart from hydropower), is set to benefit. However, as Vestas has experienced several times throughout its history, the flipside of a positive political climate is regulatory risk, which in fact drove the company's predecessor into bankruptcy in 1986. Energy policy can hence be a double-edged sword for Vestas, and the inherent risks require to be well managed.

On the opportunity side, there are a number of positive developments on global, European, national and state levels that Vestas and its peers can benefit from. The United Nations Framework Convention on Climate Change (UNFCCC) aims at significant reductions of greenhouse gases on a global level, and despite the fact that reaching global consensus is no easy task, there is an increasing awareness which will eventually result in stricter regulation of greenhouse gases, shifting the rules of the game in favor of wind energy and other low-carbon energy technologies. At least equally significant are policies on regional and national levels, such as feed-in tariffs for wind energy in several European countries, production tax credits in the US and renewable portfolio standards (RPS) in many US states which mandate utilities to provide a minimum share of renewables.

A more recent opportunity results from attempts by governments to stimulate their ailing economies. Experts like former World Bank Chief Economist Sir Nicholas Stern, now at the London School of Economics, have pointed out that such stimulus packages should be addressed as "green growth", in order to address the financial crisis and the climate crisis simultaneously. As **Exhibit 12.10** illustrates, a number of countries follow that advice, nota-

bly South Korea, the European Union and China, with substantial shares of green investments in their stimulus packages. The graph also demonstrates, however, that many countries seem to set other priorities and invest in areas like building highways and subsidizing the construction sector.

Exhibit 12.10 Share of Environmental Measures in Stimulus Packages of 10 Countries and the EU



Source: HSBC (2009)

An interesting case is represented by the United States, where only about 20% of the stimulus package is dedicated to renewable energy and other green measures, but in the light of the vast size of that package, this still represents a major opportunity. From the perspective of a wind turbine manufacturer, this may be one of the factors to consider in planning its internationalization strategy.

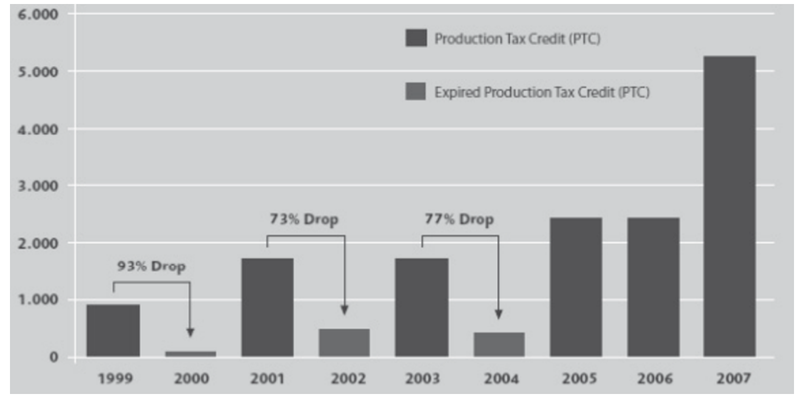
While policy can hence be an important driver for wind energy, it also involved substantial risks. A particular challenge is policy uncertainty. Two kinds of uncertainty are particularly relevant to the wind energy market, namely the price volatility inherent in some types of policies to promote renewable energy, and the risks of stop-and-go policies.

As for price volatility, a notable example is Italy, where power producers in 2008 either had to produce 5% of their energy portfolio by renewable energies or set their requirements off by purchasing green certificates. In Italy alone, certificate prices in 2008 varied by some 46% between 9.5 – 5.4 € cents / certificate in addition to volatile wholesale electricity prices, leaving investors with significant uncertainty about their business case. Although not strict-

ly policy-related, the volatility of oil and gas prices also has an effect on the economic viability of wind energy investments. The strong decrease in oil and gas prices since late 2008 has shifted the balance between conventional power plants and wind turbines. On the other hand, investors may also see the lower volatility of wind power prices as a hedge against fuel price risk. In terms of policies, the so-called feed-in tariff, which was introduced in Germany in 1991 and has been applied in many other countries more recently, has proven to be an effective measure to reduce investment risk. Under this policy scheme, the operator of a wind turbine gets guaranteed returns for a long period of time (usually 20 years). While feed-in tariffs have been criticized for being overly generous to renewable energy producers in some countries, they have clearly been the most effective policy in terms of stimulating renewable energy investment and capacity additions, hence helping governments to reach their renewable energy and climate policy targets.

The other kind of policy uncertainty is related to stop-and-go policies. Unfortunately, policies in many countries have been subject to frequent changes, the prime example being the US where tax incentives for wind energy have gone through cycles of being introduced, expired, re-introduced, and so forth. This has led to a boom-bust-cycle in wind energy investment, and therefore industry associations and environmental groups are lobbying for a longer-term perspective. The fact that one of the largest companies in the US, GE, is also on the side of potential beneficiaries of such an increased policy certainty has probably not reduced the chances of getting this into place.

Exhibit 12.11 New Installation of Wind Power Capacity in MW during Years with and without Production Tax Creditst



Source: AWEA (2009)

12.4 Outlook

With more than 80% of the world's economy currently depending on non-renewable sources of energy, the need to cut carbon emissions by 80% by 2050, and wind energy being one of the most cost-competitive sources of clean energy today, there is little doubt that the wind turbine industry is set for a continuation of its tremendous growth path for decades to come. The recent market entry of large manufacturing firms like GE, Siemens, Alstom and Areva, the increasing exposure of incumbent energy utilities like EDP, E.On, Vattenfall, EDF and Endesa, but also the entry of financial services firms like Allianz, Goldman Sachs and Blackstone into this sector indicates that wind energy has made a lot of progress on its way from a niche to a mainstream market. From humble beginnings in the 1980s, Vestas has consistently grown with the industry over more than two decades and is still the market leader. The competitive challenges facing the company are substantial, but so are the market opportunities. The future will tell how big of a slice of the pie Vestas will continue to be able to claim for itself. Given its strong internationalization capabilities, its consistent focus on profitability and its track record of managing internal growth, the company seems well positioned to ride the wave of opportunity. As CEO Ditlev Engel puts it: "Taking the lead demands that we have the courage to change and adapt while things are going well. (…) After all, it is most fun to stand on top of the winner's podium. And quite honestly, why in the world should Vestas not stay there?"

Student Assignments

David vs. Goliath – the pros and cons of being a pure player

1. Consider the situation when GE entered the wind industry in 2002 as the first large incumbent player: What were the main opportunities and challenges arising for Vestas, and for the wind turbine industry as a whole?
2. As you saw from **Exhibit 12.7**, some of the large incumbent players took much more time to enter the wind energy industry than others. What might explain these differences in market entry timing?
3. What are the pros and cons of being a pure wind energy player at the current stage of industry development? How could Vestas make best use of its advantages, and how could it hedge against its disadvantages as a pure player? How does the financial crisis influence your assessment?

Business-to-Government (B2G) – managing policy risk (and opportunity)

1. How has energy policy influenced Vestas' corporate strategy in the different stages of its history from 1985 to today?
2. What are the differences between the 1986 crisis and the company's current position? What are some commonalities?
3. Global climate policy, economic stimulus packages and national renewable energy legislation are three examples of policies that Vestas could benefit from in the near future. How could the company – either on its own, or together with other players in the industry – try to influence adoption of such policies? Which of these options would you recommend the company to prioritize?

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Authors

Björn Ambos is professor of International Management and director of the MSc in International Management/CEMS at WU Vienna. He holds an MA in business administration and a PhD in international management from the University of Hamburg. His research interests revolve around innovation, strategy and management of technology driven multinational firms. His works have appeared in International Business Review, International Journal of Technology Management, Journal of International Management, Journal of World Business, Strategic Management Journal, Long Range Planning, Management International Review, and Research Policy. He teaches strategy and international management to MSc/PhD and executives.

András Bauer is professor of marketing, and department head at Corvinus University of Budapest. His research is tied to distributor fairness and market development, and he has published several books and articles. Professor Bauer had been visiting faculty at multiple universities, including HEC and UC Berkeley. Dr. Bauer's consulting activities include marketing strategy and distribution solutions at local and global companies, including Sara Lee, Philip Morris, Merck, Bayer and T-Mobile. He is a member and former chair of the CEMS Marketing Interfaculty Group.

Renaud Cogels is recently retired as executive vice president of Delhaize Group, a Belgian food supermarket retailer with a strong presence in the United States, several European countries and Indonesia. After having being CEO of Delhaize Belgium and CEO of Delhaize Europe, he was recently CEO of Southern European and Asian Operations. He has a lot of interest for the development of private labels of the group. He has a master's in economics from the University of Louvain, Belgium.

Josep Franch is an associate professor in Marketing at ESADE Business School in Barcelona (Spain), where he is also the director of the MSc programs in management and the academic director for the CEMS Master in International Management. Expert in international and global marketing, Professor Franch has taught in over 12 countries and has been a consultant for multinational and global companies including Novartis, Sony and Xerox. He is an expert on the case study method and has won several case-writing awards.

Mihály Gálik has been a full professor of media economics and media regulation at Corvinus University of Budapest since 1996. He is a graduate of the Karl Marx University of Economic Sciences, Budapest (1968) and holds a PhD degree in economics (1989). He is author of books and articles in the field of media economics and media regulation. He has been co-coordinating numerous research projects on the media in Hungary for the last twenty-five years and has been involved in a couple of international media research projects, as well. He has been a non-executive member of the board at Magyar Telekom Telecommunications Plc, the market leader telecommunications company in Hungary, since 2006.

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Verena Gruber is a research associate at the Institute for International Marketing Management at WU, Vienna University of Economics and Business, where she also finished her master's degree. She worked for the Austian embassy in London and the United Nations in Bangkok before returning to university. Verena has been consulting for multinational companies like Nielsen and Red Bull and has presented her research at numerous conferences.

Matthew Allen Hawkins is a teaching assistant at ESADE Business School in Barcelona (Spain), where he is pursuing a PhD in management sciences. His research is focused on brand extensions and internationalization. He holds bachelor degrees in marketing and political science and has previous experience as a researcher for a consulting firm in Washington, DC.

Dóra Horváth is associate professor at Corvinus University of Budapest, Institute of Marketing and Media, head of the Department of Media, Marketing Communication and Telecommunication. Her areas of research include product design and innovation, diffusion of new technology in personal communication, co-creation, projective research techniques, and postmodern approaches of marketing. Her areas of education involve: strategic and creative planning of marketing communication, design management, advertising management, and direct marketing. Dóra has participated in several CEMS block seminar programs, and is a member of the Design and Innovation CEMS Interfaculty Group.

Alexander Jakubanecs is a Research Fellow at the Institute for Research in Economics and Business Administration (SNF) in Bergen, Norway. He received his Ph.D. from the Norwegian School of Economics and Business Administration. Alexander has been a Visiting Scholar at the Stern School of Business, New York University. He has published outlets such as Journal of East-West Business and Advances in Consumer Research. His main research interests include international marketing, brand management and cross-cultural psychology. Dr. Jakubanecs has served as a consultant to Norwegian and Scandinavian companies such as Orkla International, Heinz Nordic and TINE SA.

Petr Král is senior lecturer at University of Economics, Prague. As deputy head for corporate cooperation at the Department of International Business he is responsible for tutoring business and research projects with leading companies (i.e. L´Oréal, Škoda, 3M). He teaches international marketing and international marketing communications not only in Prague but also as a visiting professor at other universities in Europe (i.e. WU Vienna, IAE Lyon). His research concentrates mainly on marketing in Central and Eastern Europe.

Tore Kristensen is professor of strategic design at Copenhagen Business School in Copenhagen (Denmark). He has been associated with the CEMS doctorate committee and taught at several CEMS schools. He is an expert in the alliances between marketing and design and his work also includes experiments in consumers' experiences, valuation and transformation by design. He works with several Danish companies, mainly in the cultural sector.

Raphaëlle Lambert-Pandraud is a professor of marketing at ESCP Europe in Paris. Following business studies at ESCP, she worked as a senior product manager at L'Oréal in Great

Britain. She then earned a PhD at HEC, Paris, on “the influence of aging in the choice process: the example of brand repeat purchase.” She has published in international academic reviews such as the Journal of Marketing and Marketing Letters. She participated in the Invitational Choice Symposium in 2004 in Estes Park, Colorado and in 2007 at Wharton University. Raphaëlle centers her research on the influence of age on consumer information search and brand choice.

Jan Niklas Meise completed his PhD at the Institute of Retail Management at the University of St.Gallen. His research focused on consumer reactions towards information provision concerning product history and production transparency. Prior to that, he studied marketing and banking & finance at the European Business School, Oestrich-Winkel in Germany.

Yves Morel is CEO of Bazile Telecom, a French mobile virtual network operator dedicated to seniors' specific needs. Yves Morel cofounded Bazile Telecom in 2005. Before that, he held various senior management positions in France and in the US. Over the last five years, Yves Morel has explored the challenges of marketing and selling services to senior people. Yves Morel holds a M.Sc. degree from HEC Paris (1989) and a degree in accounting and finance from Aix-Marseille (1991).

Thomas Rudolph is director of the Institute of Retail Management at the University of St.Gallen and holds the Gottlieb-Duttweiler Chair of International Retail Management. His research focus and applied fields are consumer behavior, strategic retail management and multi-channel management. He has published various books and scientific articles.

Bodo B. Schlegelmilch is dean of the WU Executive Academy and chair of the Institute for International Marketing Management at WU Vienna University of Economics and Business in Austria. Earlier in his career, he also held professorships in the US and the UK, and worked for Deutsche Bank and Procter & Gamble in Germany. Professor Schlegelmilch has taught on six continents and has run executive education programs for major multinationals. His research focuses on global marketing management and strategy.

Isabelle Schuiling is professor at the Louvain School of Management of the Université Catholique de Louvain, Belgium. Prior to her academic career, she worked for 12 years at Procter and Gamble where she was Marketing Director Europe and member of the management committee of Procter & Gamble Belgium. She is specialized in brand management and international marketing. She holds a PhD from the Université Catholique de Louvain and an MBA from the University of Chicago.

Magne Supphellen is Professor in Marketing at NHH Norwegian School of Economics, where he teaches and does research in the areas of brand management and consumer behavior. He research has appeared in journals such as the Journal of Consumer Psychology, Journal of Economic Psychology, Psychology & Marketing, and Public Opinion Quarterly. He has chaired a number of international research projects and been a consultant for multinational companies including Statoil, Schibsted, Yara, GE Moneybank, and the Norwegian Seafood Export Council.

Sigurd Villads Troye is Professor in Marketing at NHH, Norwegian School of Economics, in Bergen Norway and holds a Ph.D from University of Illinois at Urbana/Champaign. His research interests include consumer behavior, coproduction/prosumption, tourism and issues in the intersection between methodology and philosophy of science. He has published books on marketing, services marketing and philosophy of science and has published articles in journals such as Economic Psychology, Journal of the Academy of Marketing Science, Multivariate Behavior Research and Structural Equation Modeling.

Rolf Wüstenhagen is the Good Energies Professor for Management of Renewable Energies and the director of the Institute for Economy and the Environment at the University of St.Gallen. He teaches on Master’s, PhD and executive education levels in Europe, North America and Asia, and has been a member of the CEMS faculty group Business and the Environment since 2004. His research focuses on decision-making under uncertainty of energy investors and consumers and has been published in leading international journals. Prior to embarking on an academic career, he retired from one of the leading European energy venture capital funds.