



# Commoditization

## Friend or Foe?

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A commodity is a product or service that is mass-produced and has few or no features that distinguish it from other similar products.

The commoditization of products and services involves marketers, retailers, and wholesalers trying to make a profitable exchange of these goods or services with a client or customer.

Opportunity and loss are at stake; the commoditization of a product or category can create either an opportunity to take advantage of or a threat to be faced. Are you ready to welcome your new friend or surpass your competition?

When a new product or category hits the market and is shown to sell, it is “rich” with value for the manufacturer, retailer, and customer. After the product has taken on a marketing profile, through volume and customer acceptance, these same success factors can lead to commoditization. The marketplace seeks new successes all the time. Indeed, the cycle of identifying and exploiting new products and services and bringing them to commodity is incredibly short.

Discount channels exist to bring products and services directly into a commodity position. The field immediately narrows to those that can deliver the commodity to the market at the lowest price.

The speed of commoditization is accelerating, with Big Box retailers spurring it on. Wal-Mart, the world’s biggest retailer, is setting the pace for global growth.

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## Commodity Markets

A marketplace becomes a commodity market when it chooses not to differentiate a product, service, or brand.

If your strategy is to operate within a commodity market, then you must realize that your price will be under constant pressure to be lowered. This reality requires an emphasis on efficiency and an effective logistics plan. Success and volume will create pressure to lower your prices. Too much success in commodities can be damning, but this is the reality of the market.

For suppliers, pressure comes from many fronts, such as from wholesale selling to retail and the retail partner demanding price concessions. As the volume grows, more gross dollars from the program and an improved gross profit rate will become more and more critical to a retail category's results.

If a program is sold to a retailer as branded, she or he might consider duplicating the program under a private label and improve pricing, especially since it is an alternative within the assortment.

As stated, the pressure on commodity price comes from the market and competition. Your product will be 'knocked off' by your competitor and presented to retail as the 'new and improved version' or 'next generation' – always at a lower price than the original. Some retailers put commodity items up for tender and allow competition to bid on your program with the program going to the lowest pricing bidder. Invariably, you will have no choice but to lower your prices if you want to stay in business.

If you are to operate as a commodity specialist, then your selling proposition will depend on price, although price still may not secure the continuity of your program. Price also may limit your return on investment; commodity price is dynamic and

difficult to plan because anyone can mark down the price of similar goods and "meet or beat" your pricing. It goes without saying; the most efficient company with lowest cost to deliver to market will control the market price.

## Wal-Mart

Wal-Mart is the best example of a commodity retailer. It has succeeded through its execution of its strategy of 'everyday low prices' and built a logistics pipeline of 'everyday low cost.' It fine-tuned its technology, developed extremely efficient 'backroom' and logistics support, perfected the retail store model, and engaged suppliers in its strategies. Its early merchandising and marketing accommodated a smooth-running logistics operation, based on a policy of identical merchandise in all stores and stores of the same size.

Wal-Mart tries to continuously eliminate costs from the product and the pipeline. A portion of the savings is passed on to customers through lower retail prices, which directly supports its marketing message of 'rolling back prices.' This is why such continuous pressure on cost prices with suppliers; it is these concessions that drive the strategy. Through this efficient and rigorous marketing of commodities, Wal-Mart has become the biggest retailer in the world.

## How is commodity retailing done?

Does a service, product, category, or business become a commodity by design, evolution, or default? A commodity requires substantial volume, which is generated by customer need, repeatability, strong lifecycle, price elasticity, and adequate and continuous availability of product. A commodity must be convenient to buy, available through multi-channels or bricks-and-mortar stores. The product must inspire confidence in the retailer and the product. Gas and oil, banking, cars, travel, groceries, and foodstuffs, for instance, are all commodities. All were ripe for the Wal-Mart formula.

If Wal-Mart sets the stage for commodity retailing, then how does one operate in a commodity market? Firstly, a company must have the financial, structural, and cultural resources. Successfully managing a commodity business requires relevance, efficiency, and control, in addition to exceptional branding, operations, products, merchandising, sourcing, and logistics.

A wholesale company must now be able to contend with outsourcing of retail responsibilities to suppliers. These responsibilities can include the following:

- Market research and analysis
- Market and brand share analysis
- Retail sell-through analysis and forecasting
- Category trend analysis
- Consumer studies and insight analysis
- Trend management
- New and emerging market and category analysis
- Vendor managed inventories with GMROI responsibility.

Companies in both retail and wholesale must think of themselves as 'holistic brand managers' to respond to commoditization.

## Differentiation

If your business was not built for commodity or if you want to ensure your product and brand doesn't morph into a commodity, then you must differentiate your product. This means distinguishing your product and brand in a meaningful and obvious way that will allow you to command a premium and also control distribution and your brand's future. Taking this route won't preclude you from other commodity work; in fact, it can allow for downstream efficiencies through shared delivery and procurement stages.

Before developing a product or brand, consider:

- (a) who it is that will pay for the differentiation, and
- (b) the size of the market for the product or brand.

Market segmentation work must be informed by behavioural and/or attitudinal assessments, as well as any traditional demographic research. To achieve a market-focused, sustainable, and profitable product or category requires a complete immersion in a branding strategy. The brand must stand on its own if there's to be decent return on investment and enhanced brand equity.

Differentiation is the key. This differentiation must be within a reasonable price range of commodity. The enhanced or differentiated attributes must be compelling enough to make customers feel they "have to buy it." This means a series of characteristics and benefits that come together to make the branding strategy and product positioning a success.

While the price must be realistic, the product must be perceived to be different from the mainstream. Customers must satisfy themselves as to their purchasing decision or to others who may question the purchase. Qualities such as prestige and image are intangible and present the opportunity for added profit.

Breadth of selection is not an exclusive differentiating factor, especially when businesses are prepared to open up their warehouses as part of their market offering. Toys 'R' Us is an example of a category with breadth of selection as a unique selling proposition. Yet, it wasn't long before Wal-Mart expanded its toy sections and took away the uniqueness that was Toys 'R' Us' only competitive advantage.

Service is another point of differentiation. Service, depending on the business and the commodity, can be achieved at critical or all customer "touch points." The interactions must be valued by the customer and not seen as intrusive. After-sales service, particularly in the automobile industry, is one such critical touch point.

Service convenience and speed are also ways to differentiate oneself from the commodity expert. Again, the goal with differentiation is to attempt to claim ground that the competition cannot easily duplicate. Service is something you can easily and quickly copy; be sure to do it first and to keep raising the bar.

Product innovation, along with “quickest to market” can differentiate a brand and set one apart from others in the market. This differentiation, targeted at a specific customer segment (who obviously like the product and the association with the brand), works best in fashion and style-sensitive categories. One must lead with innovation season after season to maintain ground.

Differentiation of a brand can apply to a store as much as a product. One of the main reasons department stores have been in trouble is because they tried to carry everything but stood for nothing – at least in customers’ minds. Wal-Mart, on the other hand, has a clear differentiation – ‘low prices everyday.’ Target has its ‘mass with class’ proposition, which is well executed and successful.

When you own it, say it, deliver it, and reinforce it at every opportunity. This reinforces your point of differentiation and allows you to control the ground you’re staking out.

Points of differentiation can be both tangible and intangible; tangible in that the customer can see it, use it, or measure it; and intangible in that the customer feels it, perceives it, or believes it. Either way, you must be able to measure the attributes you’ve decided to make your beachhead for differentiation. You must be able to measure how these attributes are advancing, protecting, or maintaining your brand.

## Future Outlook

The answer to ‘Commoditization: friend or foe?’ can be found in the branding model. A holistic branding approach is key to the survival of a commodity, just as strong differentiation is to protect oneself from a commodity.

Brands need to be revitalized, repositioned, and always relevant to the market. The “rebound” or “resurrection” of old brands speaks to the power of brands and the equity they hold. The challenge for retail and wholesale is to decide what you are: a commodity or differentiated? Committing to one or the other is half the battle.

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