

Designing a Growth Strategy in 3-Circles*

Analysis Guide

EIGCA/TORO

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*Revised from an instructional document prepared by Prof. Joe Urbany of the University of Notre Dame's Mendoza College of Business. Used with permission.

Analysis Guide: Growth Strategy in 3 Circles

The Search for Growth - Introduction

Business survival, growth and competitive advantage are about effective **positioning**. Successful positioning requires simultaneously addressing shifting customer desires and demands, new and existing competition, volatile and uncertain economic conditions and your organization's skills, focus, and motivation. I can't say this too strongly: failure to consider the essential elements of strategic positioning means risking future performance and stakeholder disappointment. The 3-Circle Model¹ facilitates speed of understanding and action in strategy development by connecting and integrating the critical aspects of positioning. By creating a set of steps in plain language to address this internal-external integration, the 3-Circle framework helps a management team honestly assess its current and future competitive position. The framework stimulates conversations, motivates critical thinking, and encourages the development of resources and capabilities linked to customer needs as your firm pursues growth.

Positioning is typically either *externally-driven* (i.e., how do you differentiate from competitors in serving customer needs?) or *internally-driven* (how do you assemble unique resources and build capabilities to gain competitive advantage?). These views are rarely considered together, hindering speed and effectiveness of strategy execution. As a result, many firms fall into the traps of developing strategy that fits the market but cannot be executed effectively, or of acquiring unique resources and capabilities that fail to create unique value for customers.

The underlying concepts of the 3-Circle Model are grounded in years of research in corporate strategy, marketing, organizational theory and economics. Equally important, the framework has been successfully applied by managers in a wide variety of large and small organizations. The 3-Circle framework very quickly creates meaning and a language that connects key concepts known to affect firm performance.

The purpose of this guide is to present and explain the steps and provide directions for implementing a growth strategy. It is a step-by-step process that you can use to develop competitive positioning to serve a particular market.

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Overview Description of 3-Circle Analysis

CONTEXT

1. Define the context. What customer segment, company unit, and competitor(s) will be analyzed? Since the context determines the focus of the analysis, these are important (but not necessarily obvious) choices.

OUTSIDE VIEW

2. Customer analysis (customer circle). In this step, you'll delve into customer decision-making, obtaining estimates of the attributes / benefits and importance of their needs as well as their beliefs about your firm and the competition. It consists of a **BEFORE Worksheet** assessment that should capture your "best guesses" about customer value perceptions prior to your going out to talk to customers. The **BEFORE Worksheet** is completed BEFORE you actually talk to customers. An **AFTER Worksheet** of customer choice attributes is the result of talking with past customers and prospects. Comparing these two worksheets almost always produces interesting insights about difference between a manager's perceptions and those of the firm's current and potential customers.

3. Sorting. There are 7 distinct areas of the 3-Circle Model, and step 3 involves identifying into which area each of the attributes identified in Step 2 should be classified.

4. Deep diving. Exploring deeper customer values through laddering or other methods that will be explained. This involves identifying customer values that underlie demand for the attributes in particular areas of the model.

INSIDE VIEW

5. Your Capabilities/ Resources / Assets. In this step, you explicitly identify your organization's capabilities, resources and assets (C/R/As).

6. Competitors' C/R/As. Step 5 is repeated with a focus on competitors.

7. Overlapping Circles (INSIDE view). Here you make an assessment of which capabilities, resources, and assets are common to both your firm and the competition, and which are potentially distinctive.

ANALYSIS

8. Alignment. In this step, you address the most important question in the analysis: Are your points of difference from competition based upon real, distinctive capabilities and thus the basis for a competitive advantage?

9. Dynamics. Here, you consider the dynamics of the model. How has this market changed over time? How is it likely to change in the future?

10. Growth Strategy. Steps 1-9 build into the Step 10 analysis, which is the most critical. Prompted by a series of questions in the "Growth through New Value" matrix, you explore a number of growth avenues, and consider implications for marketing tactics. This is the climactic step – all the other steps build to this one.

Analysis Guide: Growth Strategy in 3 Circles

Step 1: Define the Context

To begin the application of the 3-Circle Model, you must select a particular situation. Note that a 3-circle analysis of any particular market involves the same series of 10 steps (below), but can be very different depending upon the unit of analysis. This unit of analysis is defined on three dimensions: (a) a customer/market segment, (b) your company or division (product/service), and (c) a major competitor. To do the analysis effectively, it is important for you to define the business situation under study very clearly.

The Growth Strategy model has been applied to varied exchange situations including businesses, non-profits, religious institutions, and even individuals. Note that a 3-circle analysis of any of these entities involves the same series of steps (described below), but begins with identification of exchange partners (e.g. customers) and competitors. For a business application, exchange partners would be current and/or potential customers. Competitors are those organizations or individuals who in customers' eyes are substitutes for your service. Customers and competitors are as you would define them traditionally.

It is important for you to narrow down the customer group (market) and competition under study. Begin by selecting a market. A *market* consists of organizations with needs to satisfy, money to spend, and a willingness to spend it. For example, existing golf courses interested in undertaking redesigns might constitute a market. However, this is too broad a context for analysis because within this market there are almost certainly sub-groups or segments, the members of which are similar to each other but as a group they have important differences from others in the market in terms of such things as location, priorities, funds, and decision-making processes. Therefore, it is important to narrow down this market to a strategically important *customer segment*. For example, choose one that represents a large proportion of your business, perhaps one you currently stand the chance of losing, or one that would be new to you but appears attractive, that is a customer segment with whom you would like to acquire new business. In addition, identify *one particular competitor*; the one firm that you feel you currently (or would) compete with most for this segment. Perhaps select a competitor that is the largest or most threatening, or one that is representative of a larger group of important competitors. Clarity in **defining the context in Step 1 is imperative**, making the subsequent analysis much more straightforward and useful. The analysis can later be repeated for different competitors, markets, or customer segments.

Conclude this step with a simple, one-line description of the context. Using this particular format helps to reinforce the purpose of the project. Keep in mind that you're seeking to study *somebody's choice about something*. The one-liner format goes like this:

<p>My goal is to figure out how _____ can grow by creating more value for _____ than _____ does.</p>
--

So, there are 3 blanks. The first one is your company or unit of your company. The second one is the customer or customer segment. The third one is the competitor. So, more specifically, your one-liner context should read like this:

My goal is to figure out how [**I / WE / MY COMPANY ...**]
can grow by creating more value for [**CUSTOMER / CUSTOMER SEGMENT ...**]
than [**MY COMPETITORS ...**] do.

This is the generic form of the project context. A fast food firm might formulate the context like this:

My goal is to figure out how **STARBUCKS** can grow by creating more value for
BREAKFAST CUSTOMERS than does **McDONALD'S AND SIMILAR FIRMS** do.

Applying it to a hypothetical EIGCA member-firm selling services to a customer segment, seeking to gain share on a competitor, the context statement might look like this:

My goal is to figure out how **SMITH DESIGN, Ltd.** can grow by creating more value for
MUNICIPALITIES SEEKING GREEN SPACE than **GREEN SPACE PROVIDERS, Ltd.**
(GSP, Ltd.) AND SIMILAR FIRMS do.

There are many different contexts in which the process has been applied. Although in some of the examples below, the definition of target segment would need sharpening (disguised here for competitive reasons), these are examples of some projects that have been done in the past:

3 CIRCLE CONTEXT EXAMPLES

(Firm, Customer, Competitor)

Ricoh, business customers, IBM
Orbitz, frequent business travelers, Expedia
Harris Bank, high volume business customers, Chase
Harrah's Joliet (Indiana) Casino, high net worth gamblers, Empress Joliet
Nike, Core distance runners, Adidas
Dow Chemical, natural gas processing plants, Huntsman Corp.
American Airlines, frequent leisure travelers, United Airlines
Army, military recruits, Marine Corp
U.S. Air Force Academy, Air Force recruits, College Air Force ROTC
Kick Boxing, personal fitness fanatics, Tae Kwon Do

NEED SEGMENTATION HELP? → SEE APPENDIX A. Segmentation can be a bit tricky, especially if you haven't thought about it before in this type of analysis. If you're struggling a bit here, check out Appendix A. There you'll find an exercise that will help you uncover different customer segments. The exercise is designed to identify 3 segments within a market (though more or fewer may actually exist). For purposes of the analysis, you would select one of these identified segments as the CONTEXT.

Step 2: Customer Analysis

Customer view. This is a major section which guides much of the subsequent analysis. It deals with questions like: What are the key needs of customers in this segment? What attributes / benefits do customers in the segment seek? How do they perceive you and the competitor on these dimensions?

There are a series of sub-steps described below. The primary goal in Step 2 is to learn the positive and negative perceptions that customers have of you and your competitor. But I ask you to do this two ways because in and of itself, important insights can be gained. First, perform a preliminary exercise in which you internally estimate customer perceptions (the BEFORE Worksheet), then second conduct an exercise in which input is obtained directly from customers (the AFTER Worksheet).

2.1 Preliminary Exercise for you – The BEFORE Worksheet. It is important early on for you to think deeply about customer needs and perceptions, beginning with the initial beliefs of you and/or your team. Prior to talking directly with customers, you need to consider what *you* think, even if you don't have a lot of information to start. The steps are guided by the use of part 1 of the 3-Circle work sheet that appears as Figure 1 below. Here's how it goes:

2.1.1. Step into the shoes of your customers. First, in the left hand column of the Figure 1 worksheet, list the top 10 reasons you believe customers in this market segment choose one competitive offering over another. Try to use phrases that customers would use. Make sure you list at least 5, but no more than 10. These "reasons" will often be described as *attributes* or *features* of the service (or service provider) that customers think about before making a decision. For example, desired attributes of hotel rooms (the service) for the market segment business travelers might be roominess, cleanliness, amenities, work area, etc. and desired attributes for hotel chains (service provider) for the same segment might be price, consistent quality across all location, number of locations, ease of making a reservation, presence of a business center, etc. Again, these dimensions more generally are referred to as *reasons* for selecting a provider. In the far right hand column of the worksheet write down the consequence or customer value that explains the corresponding reason. In many cases these seem obvious, but they often provide interesting insights. For example, "roominess" of a hotel room might be desirable because it makes it easier to meet clients in the room or it might make a hotel stay feel more like home.

2.1.2. Importance. Next provide a relative rating of importance for how influential each reason is in your target segment's decision-making. On the worksheet, *estimate the importance of each reason/attribute as Low (L), Moderate (M), or High (H)* for the selected segment. You'll see this is ultimately about prioritizing.

2.1.3. Ratings of company and competitor. Focusing on the customer segment you've chosen, here rate your firm and the selected competitor on all the reasons / attributes that you identified earlier. Do your best to estimate the *ratings that customers would provide*. First, on each attribute, rate *your firm* in column 3 as you believe customers would. Use the following 3-point scale: are you below expectations (a rating of 1), do you meet expectations (2), or do you exceed the customer's expectations (3)? Record your ratings on the worksheet.

Repeat the exercise, this time estimating customer responses for *the competitor* on each attribute (again, 1, 2, or 3).

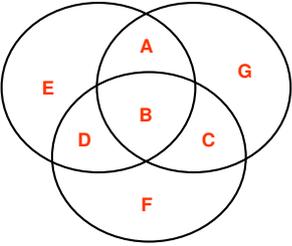
An important point here: Do your best to adopt the view of your customer. Reflect on the needs and values that are likely to be driving their choice of one competitor over another. Do your best to put yourself in the shoes of the customer before estimating their beliefs about you and the competition. You may want to consult with others in your organization or possibly have your management team individually and without consulting with each other produce attribute and importance ratings for the same customer segment and then compare and discuss your results.

Figure 1
WORKSHEET BEFORE TALKING WITH CUSTOMERS/PROSPECTS

(1) = Your “unit,” (2) = chosen customer segment, (3) = competitor unit.

CONTEXT:

My goal is to grow (1) _____ by creating more
 value for (2) _____ than (3) _____ does.

 DATE: PRODUCT / SERVICE: SEGMENT:	CUSTOMER VALUE BASICS			Consequences, Values -- why are these reasons important to customers?
	How important is this attribute/ benefit to customers (L, M, H?)	How do customers rate US on this attribute / benefit? 1= Below 2 = Meets 3=Exceeds	How do customers rate THEM attribute / benefit? 1= Below 2 = Meets 3=Exceeds	
TOP 10 REASONS	Importance	US	THEM	
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				

2.2 Customer Research

Step 2 is ultimately about learning customer perception of your strengths and weaknesses. The sub-steps below provide insight into how preliminary research with customers can be done by having some conversations with current or past customers. The steps involve essentially repeating the steps in section 2.1 above, but this time obtaining information directly from the market to produce the AFTER worksheet.

2.2.1 Sampling. It is possible to interview a few customers and gain a great deal of insight. Clearly, a larger study with a sample representative of the chosen customer segment would provide the most confident assessment for decision-making, but this may be impractical or impossible. The primary mandate is that those who you interview / survey be representative of the customer segment you've selected for analysis. If the segment is small, you can gather data from multiple individuals in the same organization. Just be sure: 1) they are people involved in the choice of suppliers, and 2) that you interview them individually (not as a group).

NOTE: You may have existing data on customer satisfaction or attitude surveys. This kind of data can be a nice input in the project and can substitute for or supplement customer interviews.

2.2.2 Generate a List of Attributes or Reasons for Purchase. You have your own preliminary list of attributes/benefits sought (from the BEFORE Worksheet), but now you want to identify what factors are important to customers in their choices. Logically (and hopefully) there will be considerable overlap between your BEFORE worksheet and the attributes/reasons customers provide. However, important differences in perceptions often emerge. Talk with enough people that you feel confident in the estimates for which you're asked below. Identify the attributes of the product or service that you believe are the very most important in the decision-making and perception of the customer segment that you identified.

Going straight to equities (positive value) and disequities (negative value). An excellent method for having a conversation with customers to determine their decision-making drivers is to ask them why they make the choices they make. In fact, you can identify the primary positive aspects of each firm or choice option (equities), as well as the negatives (disequities) in a few questions. Assuming that you have a customer who recently chose – or in the past has chosen – Firm X over Firm Y, the following questions can be asked:

In seeking	You would ask for Q2 ...
Equity of the chosen option X	... what was the main reason you chose X over Y?
Disequity of the chose option X	... what was the main thing you DID NOT like about X?
Equity of the non-chosen option Y	... what was the main thing you liked about Y?
Disequity of the non-chosen option	... what was the main reason you DID NOT choose Y over X ?

[NOTE: The approach described here was originated by Tom Reynolds, President of SRDA Associates, a long contributor to research on decision-making and one of the early pioneers in research and practice on laddering. Used with permission.]

It is important to get customers to be specific. For example, if they say "quality" in response to the question regarding why they chose X over Y, it is important to follow up with "What do you mean by quality?" or "What are the different dimensions of quality that influenced you?"

One variation of this method is to ask customers to give you an overall rating (from 10 {ideal} to 1 {awful}) for each firm (you and your competitor), say for overall satisfaction or overall value for the money. Then, for each firm, ask your respondent these questions:

Equities: “Why did you rate this firm as high as you did (and not one point lower)? Give all the reasons you can think of.” Make sure the respondent is specific – for example, if they say “quality,” that’s too general. Make sure you drill down on that by asking them to list the different things they mean by quality and then which of those is the most important aspect of quality.

Disequities: “Why didn’t you rate this firm one point higher? What kept you from giving a higher rating?” (Again, give all the reasons, and drill down if their answer is too general.)

This simple task produces a wealth of information. You’ll get a list of positives and negatives for each firm. You can use this to see if your initial attribute list is missing anything obvious. This method will come into play again below.

Be sure to take notes! You can’t count on your memory for these details.

2.2.3. Quantitative Estimates of Customer Beliefs about Competitors

2.2.3.1. Attribute Ratings. Given an understanding of the attributes / benefits sought by customers through the exercise above, it will be helpful to obtain quantitative estimates of their beliefs about the *competitive brands* as well as the importance they place on each attribute. (Note that some segments consist of so few prospects or customers this broader survey is unnecessary.)

There are many ways to obtain these more detailed ratings from customers. A few thoughts:

OPTION 1: Ask for ratings like you did in the BEFORE Worksheet. Once you’ve got your new or revised list of reasons/attributes based upon a couple of preliminary interviews with actual customers, the simplest thing to ask for are ratings as you did in the BEFORE Worksheet. That is, for each reason/attribute:

- Ask the respondent for a *Low, Medium, or High* rating for importance.
- Ask the respondent to rate your firm (and then the competitor) as *below, meeting, or exceeding* expectations.

OPTION 2: Use your firm’s typical approach or another scaling approach. In the end, the goal is to essentially have a table of customer ratings of both your firm and the competitor, and some sense of importance. The information might be summarized in a table

such as the following for competing hotels for business travelers:

Column A	Column B	Column C	Column D
Attribute	My Firm	Competitor	How important is this attribute in choosing ?
Location	8	7	8
Roominess	8	6	9
Work area	6	9	4
Ease of reserving	10	8	8
Cleanliness	10	9	9
Business Center	10	8	7
Price	6	8	6
etc.			

There are many scaling / measurement options, one of which would be to make these ratings on a 1 to 10 scale where 1 = poor on that attribute and 10 = excellent on that attribute. In addition, you'll want to get a sense of how important each attribute is in making a choice between options, so a 1-10 rating should be obtained for that as well. Note that you sometimes have to press the respondent on scaled importance ratings (i.e., respondent gives every attribute a 9!) or you need to get further clarification, but getting a sense of what's important to decision makers is critical in knowing what gets priority in the 3-circles.

Examine the results of the customer conversations and enter the summarized result in the AFTER worksheet (see below).

Figure 2

WORKSHEET AFTER TALKING WITH CUSTOMERS/PROSPECTS

(2) = Your “unit,” (2) = chosen customer segment, (3) = competitor unit.

CONTEXT:

My goal is to grow (1) _____ by creating more value for (2) _____ than (3) _____ does.

DATE: PRODUCT / SERVICE: SEGMENT:	CUSTOMER VALUE BASICS			Consequences, Values -- why are these reasons important to customers?
	How important is this attribute/ benefit to customers (L, M, H?)	How do customers rate US on this attribute / benefit? 1= Below 2 = Meets 3=Exceeds	How do customers rate THEM attribute / benefit? 1= Below 2 = Meets 3=Exceeds	
TOP 10 REASONS	Importance	US	THEM	
1				
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4				
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7				
8				
9				
10				

Comparing your BEFORE worksheet with your AFTER worksheet may produce some important insights. How well does *your assessment* of choice attributes compare to the *market's*? Did you overlook any important attributes, prioritize them in a different order of importance, or misjudge the market's view of how well your firm or your competitor performs? For some firms reconciling these differences is a great value in itself.

2.2.4. Looking Ahead to Laddering (Step 4)

Step 3 is next, but let's actually look ahead a little bit to Step 4. Step 4 is designed for you to dig deeper through ***laddering*** and find out what these attributes really mean to customers. Anticipating that, you should build a little deeper exploration into your Step 2 interviews, which will help you cover Step 4 more efficiently. In Step 4, I elaborate on the laddering method, but I first wanted to suggest that you may want to integrate laddering into the interviews you're doing with customers here is Step 2.

Overall Rating and Efficiency. Laddering can be a bit challenging at first, but it is very doable. So, you'll be able to figure out laddering, it will just take a little practice. But here's the thing. You'll only have time to ladder on a few attributes so you want to pick them strategically. The ideal would be if you could go home and analyze all your Step 2 data to determine which attributes you'd like to ladder on (usually from Circle Area A's, E's, and G's). Then you go back and talk to your respondents again, this time laddering on the chosen attributes.

However, this may be impractical or even impossible in some cases!

So, here's an option that will be more efficient. It is an elaboration of one of the Step 2 methods above for learning quickly about equities and disequities.

Here's how you do it. To be attractive to a market segment, it helps to know what you're pretty good at (potentially so you can keep improving on that) and what you're not so good at (so you can fix it). Here's how you can quickly identify those two strategically-important attributes and then move right into laddering on them:

In seeking	You would ask then you can jump right into the laddering questions.
MAIN EQUITY: Our main positive value (likely to be an Area A item)	... what was the main positive that led you to rate us as high as you did and not one point lower? For example, you rated us an 8 - what kept you from giving us a 7? (Make sure the reason/attribute is clear and specific...ask for clarification if need be)	Why was that ATTRIBUTE important to you? Why is (answer above) important to you? etc.
MAIN DISEQUITY: Our main negative value (likely to be an Area E or Area C item)	... you rated us a 7 ... what is the main negative that kept you from rating us at least 1 point higher? In other words, what about us kept you from giving us an 8?	Why was that ATTRIBUTE important to you? Why is (answer above) important to you? etc.

Summary of Step 2

So, just to sum up, your most efficient interview would probably have these characteristics:

- (a) ...it is based on an attribute list that comes from your initial brainstorming and discussion with several members of the defined market segment.
- (b) asks respondents how important each attribute is.
- (c) asks respondents to rate each firm (your firm and your competitor) on all the attributes.
- (d) asks for the main equity and the main disequity attributes, and then
- (e) ... ladders on the main equity and main disquity attributes.

You may have other questions (like demographics or other attitudes), but these are the essential ones for the purpose of the project. I'll have more on this notion of "deep diving" in Step 4. But next, you need to sort.

Step 3. Sorting

Now, review the pattern of the reconciled ratings you produced and those obtained from the market. Your job in Step 3 is to identify where these different dimension of value go in the 3-Circle framework. Figure 3 below presents the "outside view" of the 3-Circles. The upper right-hand circle represents *customer needs and values*. The upper left-hand circle represents *customer perception of the value that our company provides*, while the bottom circle represents *customer perception of the competitor's value*. Each of the 7 areas in the framework – indicated by the letters A through G -- has strategic meaning. The task here in Step 3 is to sort the reasons or attributes that you've assessed into different areas.

Figure 3
Outside View of the 3 Circles

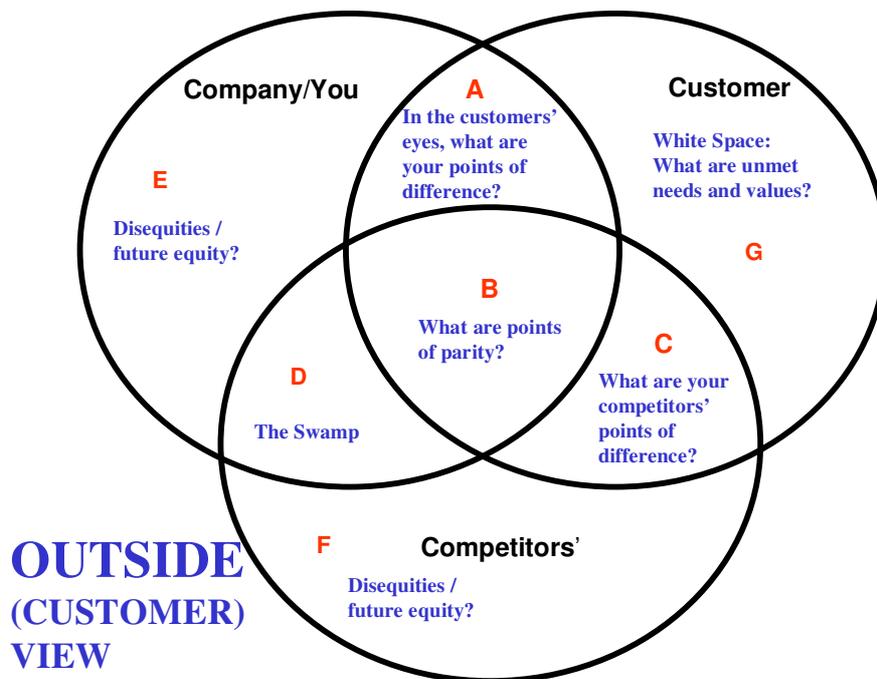


Table 2 below provides some simple sorting rules based upon a comparison of your rating or evaluation (by customers) vs. the competitor, qualified by attribute importance. The goal here is to make judgments about the value you're providing customers relative to the competition. Judgment of value is broken down by attribute or reason. Each individual attribute is sorted into Areas A through F based upon the relative ratings given by customers (first column) qualified by your assessment of attribute importance. Area G is a somewhat unique area on which I'll elaborate later, as it often is not represented in research about customer perceptions of firms on existing attributes. So, on what **important dimensions are you perceived to provide greater value (area A)? On what dimensions are you perceived to be similar to competitors (area B)? On what important dimensions is the competitor perceived to provide greater value (area C)?**

Table 2
Sorting Rules

Customer's Assessment of You vs. Competitor	Attribute importance	Area into which Attribute/ Reason would be sorted
Better than competitor	High	Area A
Same as competitor	Moderate – high	Area B
Worse than competitor	High	Area C
Poor, competitor equally poor	Any level	Area D
Poor, competitor better	Any level	Area E
Competitor is poor, we're better	Any level	Area F

Areas A, B, C. Is your Area A small (bad) or large (good) compared to the competitor's Area C? How large is Area B, relative to A and C for this market? If B is large, perceived substantive differences may not exist.

Areas D, E, F. Now consider the area of the customer circle that does *not* overlap with your circle nor the competitor's circle and that is *unique* to each firm (Areas E, F) or are perhaps *common* to each firm (Area D). If your scores are sub-par relative to customer standards and inferior to the competitor – an Area E problem -- this represents (depending upon attribute importance), either reasons the competitor is likely to win business from you, an unawareness problem, or attributes that are not valued highly and are candidates for reduction or removal. Area D – christened the “swamp” by a previous frustrated client who readily identified with the concept -- captures value that is being created by both firms that is not desired by the customer. Area F is the equivalent of Area E but from the perspective of the competitor.

Area G. This “white space” captures unmet customer needs. The free market rewards firms anticipating and responding to important needs more effectively than others. While the internal language of business tends to be around offerings – i.e., what we produce -- the most profitable value comes by thinking from the view of *customer problems, needs, and values*. These are the real reasons why customers purchase those offerings. When Radio Shack says “don't just buy stuff – do stuff,” the explicit message is that we know you buy products, but what is really important is what you get from buying and using those products.

Area G might be considered “potential features,” an ongoing area in which you might search for new value-creation opportunities. The ideas that may appear in Area G can be identified a variety of ways. Studying customer complaints is the most common and direct. Yet customers can not always put their finger on what ails them. Instead, inferences must often be made from more general conversations about understanding larger problems / concerns the customer has, and research that dig beneath the surface to understanding customer needs and values, for example observing customers and the circumstances surrounding their consumption of the product.

In fact, the *laddering* method is another approach to uncovering deeper needs and values. This is the basis for Step 4.

Step 4. Deeper Diving

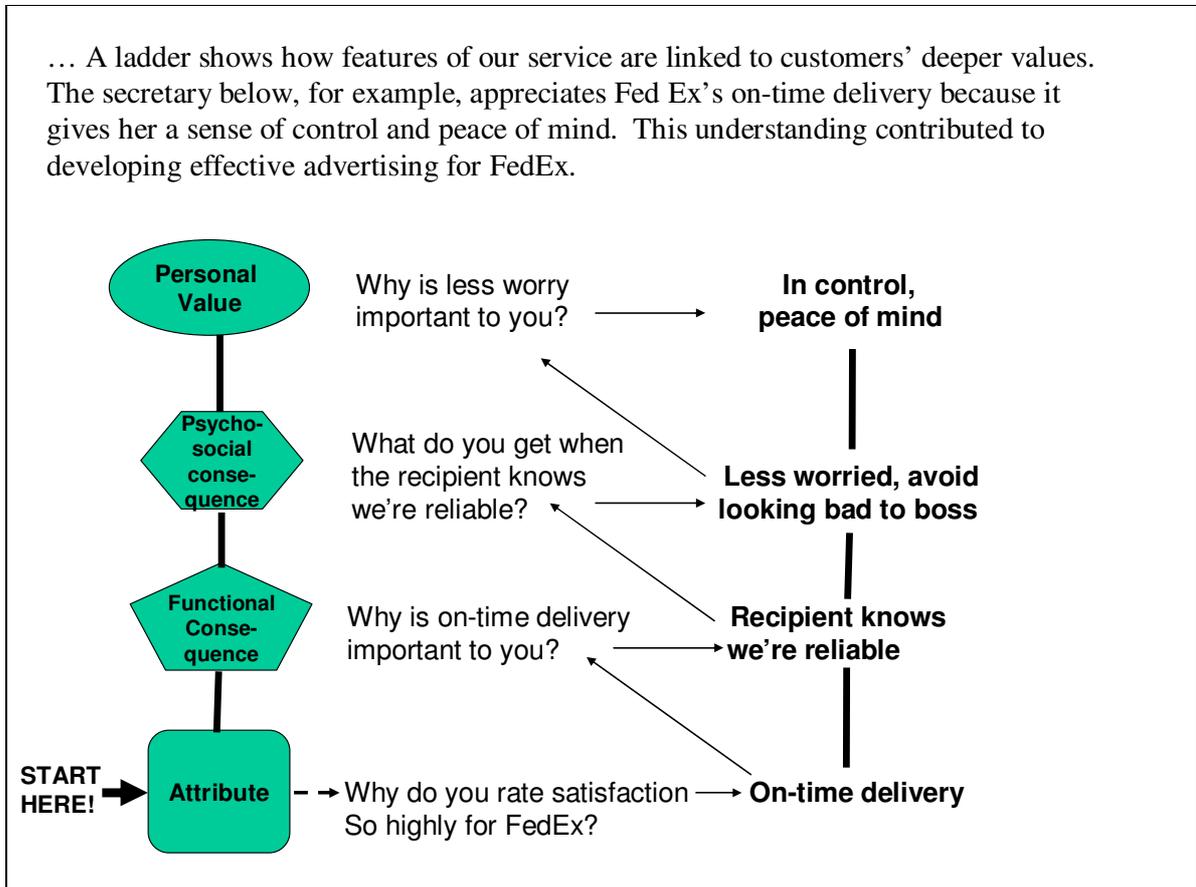
There are two goals here of what I will call “deeper diving.” The first is to truly understand **why** the attributes you identified in the steps above are important to customers. Understanding those deeper drivers of decision-making can help uncover growth opportunities because there are often many ways (beyond the current attribute set) to address needs defined at this broader level. The second, though, is to explore **growth opportunity** in unmet needs.

Deeper Values. Whatever attributes you categorized into Areas A and C above are what you believe to be the critical drivers of why customers choose you or choose your competitor. In step 4 the goal is to discover the values underlying the attributes sought by customers. To begin, identify the *most important attribute* in Area A. Then “ladder” on it. Laddering is root cause analysis, except that it focuses on customer decision-making. It involves asking “why” or “what do we get” several times:

- 4.1. Ask yourself (or management team): “Why is this attribute *important* to this customer segment?” (Alternatively, ask: “What does the customer really get from this attribute?”). Write down the answer.
- 4.2 Then ask: “Why is the *benefit* identified in 4.1 important to customers?” (or, “What do they get from it ...?”)
- 4.3 Next, ask: “Why is the answer I just gave in 4.2 important to customers?”

After 3 or 4 “whys?” you’ll begin to delve into the deeper needs or values that customers have that drive their decision-making. In Figure 3 below, I present an example from a study that was done for Federal Express. The study focused on administrative assistants in business organizations, who are key decision-makers in selecting express mail services. It was identified that “on-time delivery” was frequently mentioned as a positive equity (something the firm does well) for Federal Express. The questions and answers below reveal the values underlying this attribute’s importance. The action starts at the lower left (then follow the arrows up).

Figure 4
Laddering Exercise for Federal Express



The research above led to significant change in FedEx advertising. Earlier campaigns had humorously demonstrated the consequences of using the “other guy.” A new campaign was developed around FedEx’s technology / tracking capability. While similarly humorous, the new campaign showed boss and secretary together getting a great sense of relief and control as they learn about FedEx’s satellite communication system.

Laddering on different attributes/reasons can lead to a new understanding of why the value you currently create for customers (Areas A, B) is important to them. Laddering on areas of disequity or dissatisfaction (E or D) can provide insight into needs that have gone unmet – i.e., that essentially reside in the white space, Area G.

Laddering is something of an art, requiring careful listening. It also has some subtle aspects not discussed here. Yet, effectively applied, it provides critical insight into the core values behind customer decision-making. The point is, don’t be afraid to ask “WHY?” That is where growth opportunities exist!

THE INSIDE VIEW

Step 5. Capabilities/ Resources / Assets

Make a list of your organization's capabilities, resources and assets. Organize a listing of capabilities from weak to strong for yourself or your organization. Identify those capabilities that are core to your organization's desired market position. Also, identify those capabilities, resources and assets that are latent or under-utilized. What do you think the company is really good at? What are the capabilities that can be improved?

A key aspect of the evaluation is that you base this analysis not just on your guesses and/or estimations but also on evidence gathered. It is often effective to interview key staff within the organization and/or your previous customers or suppliers to see if your perceptions are correct. Through a series of such interviews it is possible to obtain some consensus about your firm's capabilities and resources. Secondary research (trade publications, conference topics and sessions) on the market in which you compete can also be useful in determining what capabilities, resources and assets are considered essential. Appendix B in this paper provides an overview of different types of capabilities and questions to ask in this analysis. The appendix is based upon the work of several prominent researchers and consultants.

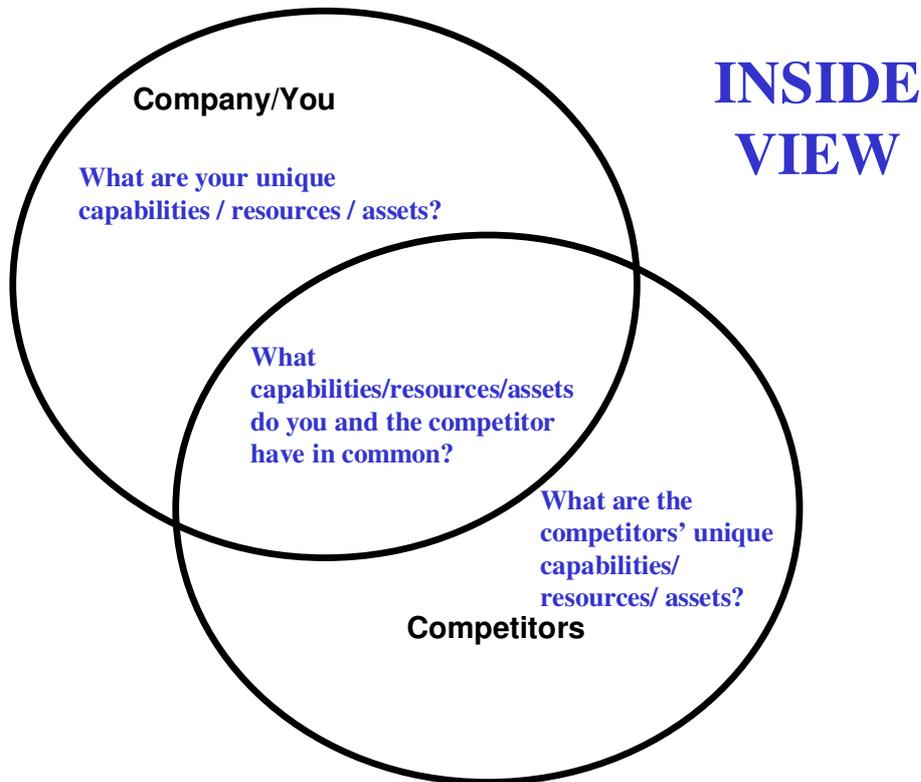
Step 6. Competitors' Capabilities/ Resources / Assets

In this step, the same kind of analysis as Step 5 is undertaken, but instead with a focus on competitors. Competitive analysis is a more difficult undertaking, though, and even can present ethical challenges. I recommend a very conservative approach, which means you only use information that is publicly available. Certainly it is appropriate to interview managers from firms that have gone head-to-head with the competitor as well as clients who rejected the competitor's proposals.

Step 7. Overlapping Circles (INSIDE view)

Make an assessment of which of the capabilities, resources, and assets that your firm and the competition have in common. In addition identify as best you can which capabilities, resources, and assets are unique to each firm. This is labeled the "inside" view because these capabilities, resources, and assets essentially represent the factors behind each firm's ability to generate customer value. Figure 5 illustrates the overlapping circles that support this analysis. Overlapping these internal circles provides three different sets of capabilities.

Figure 5
Inside View



The center, overlapping area includes common capabilities, resources and assets. These may or may not create value for customers, but both organizations share these attributes and as a result, though they may be necessary, they are probably not a source of distinctiveness.

In the non-overlapping portions of the circles, you find capabilities unique to each firm (and correspondingly, the absence of capabilities the other firm has). These attributes have the potential of giving your organization distinctiveness and differentiation from your competitor.

Step 8. Alignment

Here is one of the most important questions to ask: Are our points of difference based upon **substantive capability**? To explore this, make a picture linking up the capabilities that you listed in Step 5 to the points of parity and your own points of difference identified in Steps 2 and 3. Are the perceived points of difference for your organization based upon real capabilities? How about the

competitors? Has either of you truly built a capability that will sustain a distinctive position in the market? Consider the other two, as yet undefined areas of the model. What do they mean for you and / or your competitor?

The most significant point here is to identify whether what you believe to be your key sources of competitive advantage for this market segment are grounded on solid capabilities and resources. If no, new capability development can be a source of solidifying competitive advantage.

Here, you can also separate between existing points of difference, and future or aspirational points of difference. What are the goals? Can you meet them with existing capabilities? Do you need to develop new capabilities?

Step 9. Dynamics

Consider the dynamics of the model and your application. How has this market changed over time? How might it change in the future? Do you see the circles shifting? Changing size? What are the likely patterns of change?

There are two types of dynamics. First, business attributes that were once innovative and distinguishing (area A) become points of parity (area B) and then may go to the swamp and become candidates for elimination (area D). Second, the circles shift over time, as in the case of new golf course construction.

Step 10. Assessing a Segment and Finding Growth Opportunities

Given your understanding of the areas associated with the 3-Circle Model, you are now prepared to evaluate the segment analyzed and find areas for growth. These are the major objectives of the model. In light of your analysis, is the segment selected for analysis viable? Can you meet the needs of these customers better than the competition?

Next, what are the implications for “growing” you or your organization? Where do you see the most significant growth opportunities occurring for your organization? What are the implications of expanding or developing new capability?

The key here is that growth ideas are defined with a central focus on *customer value*, defined as a ratio of customer benefits to customer costs (broadly defined):

$$\text{Customer value} = \frac{\text{Customer Benefits}}{\text{Customer Costs}}$$

The conceptual notion here, well-established in practice, is that we increase the probability that customers will choose our offering if we increase the value of it relative to the competition. Increasing value comes from increasing customer benefits, reducing customer costs, or both.

In Steps 1 through 9 of this process, you have worked hard to identify and categorize how customers in the chosen market segment judge value, how your firm stacks up to the competition, how your capabilities are currently aligned to deliver value, and how value is likely to be changing over time. Figure 6 on the next page leverages those insights and pushes you now to think through five key growth strategy questions in a structured way. In summary terms, the five growth strategy questions made explicit in the 3-Circle model are:

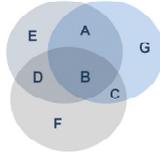
1. How do you identify, build, and defend differentiation that's meaningful to customers? (Area A)
2. How do you fix, or get rid of disequities that customers do not value or are unaware of? (Areas D, E, F)
3. Are there hidden strengths or capabilities you have that can be brought to bear to enhance customer value? (Area E)
4. Should you neutralize competitors' differentiation? If so, how? (Areas C, F)
5. How can you identify totally new growth ideas around customers' unmet needs? (Area G)

These 5 questions can be applied in brainstorming about the attributes as categorized in the first column of the Figure 6 worksheet. The next four columns, prompt questions about how those growth strategies might be pursued. **Value numerator** ideas seek to enhance customer benefits, either through building/leveraging existing capability or better communicating about existing benefits. **Value denominator** ideas seek to reduce customer costs, either by eliminating non-value-adding activity or by improving efficiency.

Figure 6

Growth Worksheet

EXISTING / NEWLY PROPOSED CUST. ATTRIB.	VALUE NUMERATOR IDEAS		VALUE DENOMINATOR IDEAS	
	Build / Leverage Capability & Value	Better Communicate Capability & Value	Eliminate Non-Value	Create Value more Efficiently
A				
B				
C				
D				
E				
F				
G				



CUSTOMER VALUE =

$$\frac{\text{Customer Benefits}}{\text{Customer Costs}}$$

↓

GROW CUSTOMER VALUE BY:

- LEVERAGING EXISTING CAPABILITIES
- BUILDING NEW CAPABILITIES
- BETTER COMMUNICATING CAPABILITY / VALUE
- ELIMINATING NON-VALUE-ADDING STUFF
- EXECUTING MORE EFFICIENTLY

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The matrix above provides insight into potential growth opportunities from a broader strategic perspective. Table 3 below provides some questions that help prompt thinking and brainstorming around the Figure 6 worksheet.

Table 3
Growth Questions

Model Area	Value Numerator: Increasing Customer Benefits	Value Denominator: Lowering Customer Cost
Area A – Our PODs	A1) Are customers REALLY aware of / knowledgeable about our Area A? How do we improve awareness? A2) How do we defend and build Area A? ... etc.	(A3) Can we focus on our numerator ← questions while simultaneously pulling out cost? (D2, E3 below)
Area B – The industry’s POPs or “expected product”	(B1) Are there Area B attributes that we can push to new levels? e.g., shift from Area B to Area A? That is, can we create new points-of-difference from Area B ?	(B2) Are there points of parity that can be delivered at acceptable levels but in less expensive ways?
Area C – Competitors’ PODs	(C1) Should we seek to neutralize competitors’ advantages? If so, how? (C2) To what degree do the competitor’s advantages reflect true superiority for them or the fact that we’re lagging?	(C3) Can we figure out how to provide the same value as competitors, but at a lower cost?
Area D – Joint disequities, or potential equities	(D1) Which attributes/benefits being provided could be more influential if they were better known or delivered more effectively? ... etc.	(D2) Which attributes /benefits does our industry take for granted that could be eliminated? (D3) Which attributes / benefit should be reduced to below industry standards?
Area E – Our disequities, or potential equities	(E1) Which attributes / benefits need to be fixed quickly? (i.e., areas on which the value we are creating is not perceived by customers as effectively meeting their needs)	(E2) Is there value here that we are trying to deliver that the customer simply doesn’t want? How do we remove it and the costs surrounding it?
Area F – Competitor’s disequities, or potential equities	(F1) Which attributes / benefits / capabilities represent “sleeping giants” for the competitor – sources of potentially new customer value not currently being leveraged	
Area G – White Space	(G1) Which attributes / benefits can be created that the industry has never offered?	(G2) Can we radically redefine capabilities or value network for the industry to lower costs?

Tactical Decisions. Once decisions are made about growth at a *strategic* level, there are more tactical choices to be made about how such decisions are to be executed in the marketing program. As such, it is important in this final step to consider as well the marketing program choices that would accompany the growth strategy. (There are some applications for which this is less relevant, but try to be as clear as you can about your growth strategy.) So, what are the implications of your growth strategy for the marketing program?:

Product / service: what innovation / development is required? How will existing offerings be affected? What new capabilities need to be developed?

Distribution: Are there implications for customers gaining access to your service? Is there growth opportunity in taking on more roles in making your offering accessible? Are there new relationships to be built?

Promotion: What promotion vehicles will be most effective in communicating your message? What should your message be?

Price: Will pricing need to change, either permanently or temporarily, to adapt the value proposition? What are the economics of such changes?

Notice that the tactics are step 10, *only after the strategic analyses*. Too often, in their eagerness to put something “concrete” in front of potential customers, managers misdirect their effort and resources by not formulating a strategy first. Tactics are critical. But tactics before (or without) strategy in a dynamic and highly competitive environment are more likely to keep a manager busy than to produce a profit or a future.

Conclusion

The 3-Circle Model provides a frame of reference for assessing market segments and understanding and developing growth strategy. As Figure 7 below suggests, the goal is to develop points of difference or distinctive positioning (Area A) that are aligned with existing or developing skills and assets.

One of the strengths of the 3-Circle Model is that it can be applied today. Managers are able to develop rudimentary analyses that will be beneficial to them in understanding the sources of commoditization, asking the right questions of customers, and brainstorming on points of differentiation and potential growth ideas. One consultant who has used the framework summarized the application in the following way:

“... there was a high degree of excitement and acceptance of the framework and the output. The framework provided a tool that enabled an objective discussion on a topic that is often emotionally charged within consulting firms – namely what makes them unique and why clients would continue to retain them for services given a plethora of options in the market... The framework provides a relatively rapid process to hone in on sources of competitive advantage and to determine if current strategy is on point or whether it requires a course change.”

The larger objective of the framework is to put the insights in the hands of those leading growth for organizations, to empower fast insights and strategy development. These are becoming standard tools for competing in a dynamic, quickly-moving marketplace.

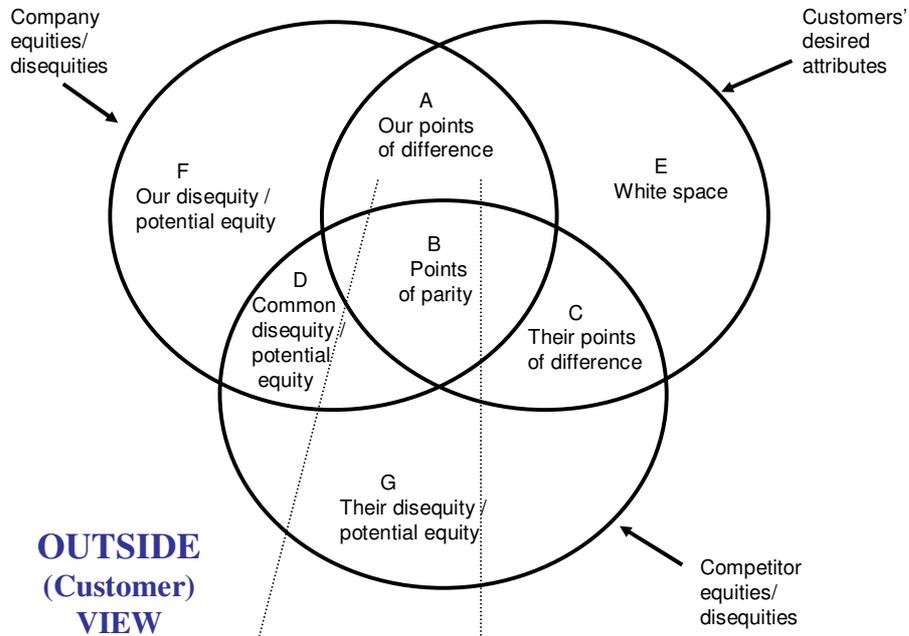
Many of the important implications revolve around *conversations* that firms have simply never had before. The following are examples:

- (a) Identifying what customers actually want or need, both on the surface and deeper drivers of the benefits sought.

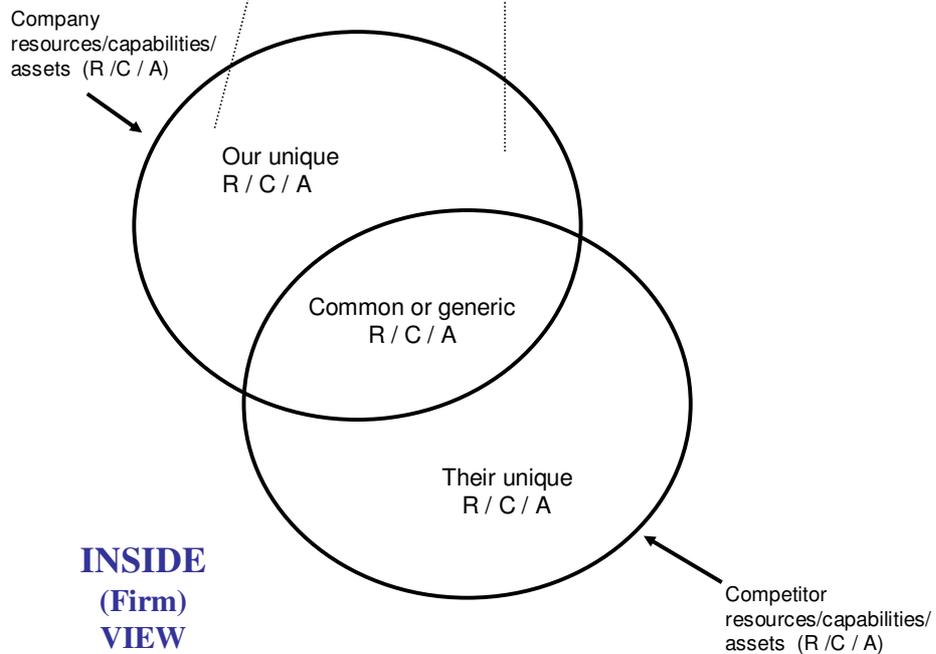
- (b) Linking customer needs to competitive position; a unique sequence of strategic thinking that begins with customer values and ends with being attractively different from competitors.
- (c) Identifying what customers *don't need* or value.
- (d) Linking company capability and focus to customer needs and resulting competitive position.
- (e) Recognizing the “white space,” the often under-appreciated notion that there are *almost always* unmet needs to be explored in any market that provide opportunities for value creation.
- (f) The dynamics of value; how both changes in competitive offerings and evolving customer knowledge and preferences change the size and intersections of the circles over time.

Figure 7
Full 3-Circle Model, Outside and Inside Views

Panel 1: Outside View



Panel 2: Inside View



FOLLOWING THE ANALYSIS, SHOULD YOU PURSUE THE SEGMENT:

Now, in terms of deciding upon a focus ... Think through the relative importance of the segment to you / your firm... how big is it ... how much do you expect it to grow? How much access do you have to the segment? How much competition will you face for the segment? Of course, these are all speculative questions aided by the 3-circle analysis. One way of making the choice more objective is to develop pro forma (or projected) financial statements based on the conclusions about the market segment, your firm and the competition, including an Income Statement with projections of income and expenses of the type shown below.

XYZ Corporation
Income Statement
For the year ended Dec. 31, 2008

Revenue		\$1,000,000
Cost of goods		
Beginning inventory	\$40,000	
Net purchases	150,000	
Cost of goods available for sale	190,000	
Less: ending inventory	(50,000)	
Cost of goods sold		(\$140,000)
Gross margin		860,000
Expenses		
Selling expenses	\$150,000	
General and administrative expenses	200,000	
Total operating expenses		(\$350,000)
Income from operations		\$510,000
Other revenue		
Interest	\$1,000	
Dividends	500	
Gain from sale of equipment	10,000	
		\$11,500
		\$521,500
Other expenses		
Interest		(\$21,500)
Income before taxes and extraordinary items		\$500,000
Income tax expense		(\$165,000)
Income before extraordinary items		\$335,000
Extra ordinary items		(\$35,000)
Net Income		\$300,000

APPENDIX A:

Worksheet for Market Segmentation

The Segmentation Primer Worksheet

It may be helpful to work through segmentation in a bit more detail as you are working through Step 1. You may be looking at a context in which you've never thought of "market segments" before. So, here is a structured way of looking at it.

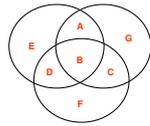
REASONS. An important way to think about market segments is to consider how those segments *differ* in terms of the *importance of different purchase reasons*. [For some organizations price is the most important choice criterion, for example. In contrast, others are willing to pay a higher price for uniqueness.]

So, it's all about REASONS ... the basis or causes for behavior.

Use the exercise that follows to explore the reasons for customer choice in the market you're looking to study.

The 3-Circle Worksheet and Exercise 1. The primary task is for you to think through the reasons why customers choose one competitive firm over another in your selected category.

DATE:	SEGMENT DESCRIPTIONS		
COMPANY: PRODUCT / SERVICE:			
TOP 10 REASONS	Segment 1	Segment 2	Segment 3
1			
2			
3			
4			
5			
Etc.			

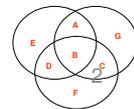


PART 2:
segments?

PART 3:
importance
of reasons?

PART 1:
what reasons?

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The requirement to start is that you've defined the product or service category you'd like to focus on. Then there are 3 three parts to **EXERCISE 1** (Note: the last slide in this file is a blank worksheet for you to use.)

PART 1: Step into the shoes of the customers. List the top reasons (at least 5, no more than 10) that buyers in this market choose one competitive offering over another. Ask yourself, "What are the chief reasons for competitive choice?" Try to use phrases that customers would use. Make sure you list at least 5, but no more than 10.

PART 2: Identify 3 of your current segments. Now think about different types of customers ... *however you currently segment them.* ... although there may be many different types of customers, limit yourself to 3 customer groups or segments for the moment. Try to envision these different types of customers and provide a brief description of them in the boxes above the columns labeled Segment 1, Segment 2, and Segment 3. There are three ways to describe segments. One is to use *physical descriptors* (for businesses, examples include location, size, specialty, etc.). Second is *purchase behaviors* [e.g, frequency of purchase, decision-making group or process, experience, etc.). Third is the *needs or motives* for purchasing (e.g., maintain members, attract new members, minimize the cost,

protect the environment, etc.). The value of these descriptors for meaningful segmentation are: Needs or Motives first, followed by Purchase Behavior, and finally Physical Descriptors. Unfortunately, the ease of identifying them is the exact opposite order.

PART 3: Explore the Reasons. Different types of customers buy for different reasons – so in PART 3 go through your list of reasons and indicate the reasons for purchase that are most important to the 3 segments you identified. It's easiest to do this by providing a relative rating of importance for each segment on how influential each reason is in their decision to choose one competitive option over another. Are there segments that purchase the product / service for different reasons? If the answer is "yes" (and if you skipped Part 2 of this exercise), now consider whether these segments differ in terms of other characteristics ... for example, physical descriptors.

So, in the columns underneath the labels Segment 1, Segment 2, and Segment 3, rate the importance of each reason to that segment. The easiest way to do this is to use a scale of Low, Medium, and High importance. Alternatively, you could get a little more sophisticated and use a 1 to 10 scale where 1 means "very unimportant" and 10 means "very important," but it's usually easier to use L, M, and H.

If again, you're not sure about what segments might exist, use the first column to just indicate how important each of the reasons are in customers' decision-making. Then ask yourself: do all customers place the SAME level of importance on each reason or attribute? The answer is almost certainly NO! If you do believe there are some differences, then go through each reason/attribute and consider if there are different segments which might place a different emphasis on that attribute. Walk through all the reasons/attributes and see if you can come up with at least 3 different segments.

Note that two organizations examining the same market could (and often do) identify the segments in that market differently. There are typically so many Needs, Purchase Behaviors, and Physical Descriptors to choose from that different analysts will produce different conclusions. You should try to focus on the most important reasons customers in the market use in making decisions.

EXERCISE 2 – LADDERING ON YOUR REASONS

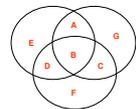
EXERCISE 2. The logic of laddering.

Exercise 2 is about digging deeper on the reasons you identified earlier.

Exercise 2

TOP 10 REASONS	Segment 1	Segment 2	Segment 3	Needs / Values
1				
2				
3				
4				
5				
Etec.				

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GOAL: The goal here is to explore the deeper values that underlie reasons people buy. This can help you think further about both what segments might exist and which segment you'd like to focus on ... sometimes you get new insights about what's important to customers (and to which customers) when you do the exercise below.

For Exercise 2, I'd like you to drill down on the most important "reasons" for the segment that you've chosen for the analysis. You should choose more than 2 reasons to ladder on, but not more than 5. But instead of doing this on your own, it may be helpful to interview someone who is a customer or could perhaps play the role of the customer (in fact, you could have someone interview YOU!).

If you are an interviewer, you should follow the logic of laddering. For each of the most important "reasons" your interviewee has identified, you need to ask questions in sequence, which are contingent upon the answer given to the previous question:

Note that the initial attribute or reason has already been identified --→ Answer 1: attribute
 Why is (Answer 1: attribute) important to you? -----→ Answer 2: functional consequence
 Why is (Answer 2: functional consequence) important to you? -→ Answer 3: psychosocial
 consequence

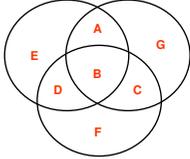
Why is (Answer 3: psychosocial consequence) important to you ? -→ Answer 4: Personal value

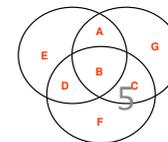
The interviewer should write down the answers on a piece of paper and you can subsequently transfer them to the column to the far right of your work sheet labeled “Needs / Values.”

Note that there are a fairly small number of core needs and values that may emerge at the top of the ladder; values like *Accomplishment, Belonging, Self-fulfillment, Self-esteem, Family, Satisfaction, Security, Control ...* Somewhere within our decisions about products and services, you’ll find these needs / values as important influences. However, it is not necessary to taking laddering to this extreme. Identifying psychological consequence is often enough to develop satisfying products and services.

The key in this exercise is to think through whether there are customer segments that seem to be really focused on particular values that may be different from other segments.

The full worksheet appears on the following page.

DATE:  COMPANY: PRODUCT / SERVICE:	SEGMENT DESCRIPTIONS			Needs/values
TOP 10 REASONS	Segment 1	Segment 2	Segment 3	
1				
2				
3				
4				
5				
6.				
7.				
8.				
9.				
10.				



APPENDIX B: Addendum on Firm Capabilities

B.1. Company resources, capabilities

a. Resources. It's essential to understand both the unique and common resources that you have relative to the competition. Resources can be defined on a number of dimensions:

Resource Category	Description	Key indicators
Financial Resources	+Borrowing capacity and +Internal funds generation (determine investment capacity)	+Debt/equity ratio +Credit rating
Physical Resources	+Size, location, technical sophistication, flexibility of plant and equipment +Location and alternative uses for land and buildings +Reserves of raw materials (all of these constrain production possibilities and determine the potential for cost and quality advantage)	+Resale values of fixed assets +Vintage of capital equipment +Scale of plants +Alternative uses of fixed assets
Human Resources	+Training and expertise of employees +Adaptability of employees +Commitment and loyalty	+Qualifications of employees: Educational Technical Professional +Pay rates relative to industry average
Technological resources	+Proprietary technology (patents, copyrights, trade secrets) +Expertise in its application +Resources for innovation (research facilities, technical and scientific employees)	+number of patents +Revenue from patent licenses +R&D staff as a percentage of total employees
Reputation (see section 5.3.4 below)	+Reputation with customers +Brand associations +Reputation with suppliers +Reputation with shareholders	+Brand awareness / recognition +Price-premium over competing brands +Customer retention (% repeat buyers) +Product performance (objective)

NOTE: Rigsby and Greco (2003), p. 54

B.2. Capabilities defined (Day 1994):

skill and accumulated knowledge (enable the activities of the business process to be carried out)

(i) **Inside-Out Process Capabilities** (activated by market requirements, competitive challenges, and external opportunities):

- Financial management
- Cost control
- Technology/management information development
- Manufacturing capabilities
- Production design capabilities
- Human resource management (recruiting, training, motivating employees)
- Marketing capabilities
- Sales and distribution capabilities

(ii) **Outside-In Process Capabilities** (connect the Inside-Out processes to the external environment):

- **Market sensing:** research and insight about customer and channel member needs, and competitors' activities, accessible memory
- **Customer linking:** collaborative relationships and coordination with customers, communication and problem-solving, joint production, MIS links, mutual commitments to improving quality
- **Channel bonding:** similarly, collaborative relationships and coordination.
- **Technology monitoring:** staying abreast of technology developments as they apply to other key process

(iii) **Spanning Capabilities** (needed to link the inside-out and outside-in capabilities together):

- Customer order fulfillment
- Pricing
- Purchasing
- Customer Service Delivery
- New Product/Service Development
- Strategy Development

NOTE: each of these types of capabilities provides a potential basis for creating *distinctive capabilities*. So what do I mean by that?

(iv) **Generic Capabilities:** capabilities that all firms in the industry have for basic customer value-creation. Essentially, generic capabilities are those required to produce the value captured in the industry's points of parity.

(v) **Distinctive Capabilities (Day 1994)**: capabilities on which the firm bases its competitive advantage. There are 3 criteria on which to evaluate whether a capability might be considered distinctive.

- +contribute disproportionately to customer value
- +cannot be readily matched by competitors
- +robust and can be used in different ways to speed the firm's adaptation to environmental change

REFERENCES AVAILABLE ON REQUEST