Marketing Insights for Thought Leaders *Jan/Feb 2003*

The NECG Edge

NECG PREDICTS

Business 2.0 (1/15/03): "When women race to the top." James M. Aitrim (Spencer Stuart) comments on a recent study showing women are less competitive than men. His own internal analysis shows that more women are getting top jobs than just five years ago with "team player" the most important reference.

Edge: A parallel study of young boys and girls would prove that women are naturally better team players than men. We predict that women will continue to get more top jobs as more companies practice what they preach about teamwork.

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Business 2.0 (1/16/03): "Target thinks outside the box wine." In response to Wal-Mart's highly successful launch of its own wine label, Target is replacing cheap wines with middle-market labels priced from $7-410. It even has its own Master Sommelier (Andrea Immer, dean of wine studies at the French Culinary Institute) for credibility.

Edge: This is another example of Target's proven ability to compete with Wal-Mart via clever segmented marketing. However, we predict it will be difficult for Target to continue "one-upping" Wal-Mart in the long-run.

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Time (1/6/03): "It's getting all screwed up." Wine makers are beginning to abandon corks and replace them with screw tops, and it's not the cheap wine you drank in high school.

Edge: Be careful wine industry, most people consume the bottle once open in a very short period, a good screw top could actually lower consumption over time.

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Wall Street Journal (1/14/03): "We test five tooth whiteners, from gel to the dentist chair." P&G, Colgate, Den-Mat, are just a few of the companies deluging the market with products promising us whiter teeth quick, comfortably, and economically.

Edge: While appealing to ones' vanity, a novel product usually garners significant trial. However, repeat purchases are driven by product performance, and these products are not up to the task as they often cause more "drool" than whitening. We predict that brands that add whitening benefits to existing products (i.e., Trident Gum, Arm & Hammer Tooth Paste) at little or no cost to the consumer will win this vanity battle.

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New York Times (1/19/03): "A Sinking Feeling at the Register." Deflationary prices in many consumer goods industries are forcing a new round of cost cutting, further delaying our economic recovery.

Edge: Many companies are trying to gain share at the expense of smaller competitors. We predict, though, that smart marketers will stop trying to buy loyalty among the most price sensitive customers. Instead, they will focus more on growing their share of wallet among their best customers resulting in higher margins.

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New York Times (1/19/03): "Risky turn on Madison Avenue." As more medical device companies are promoting surgically invasive procedures are unnecessary and / or risky.

Edge: We view this attempt to stifle DTC advertising for medican procedures similar to the negative press about prescription drug advertising. We predict that medical procedure advertising will accelerate as the consumer wants to be more aware of these procedures and their options. ■

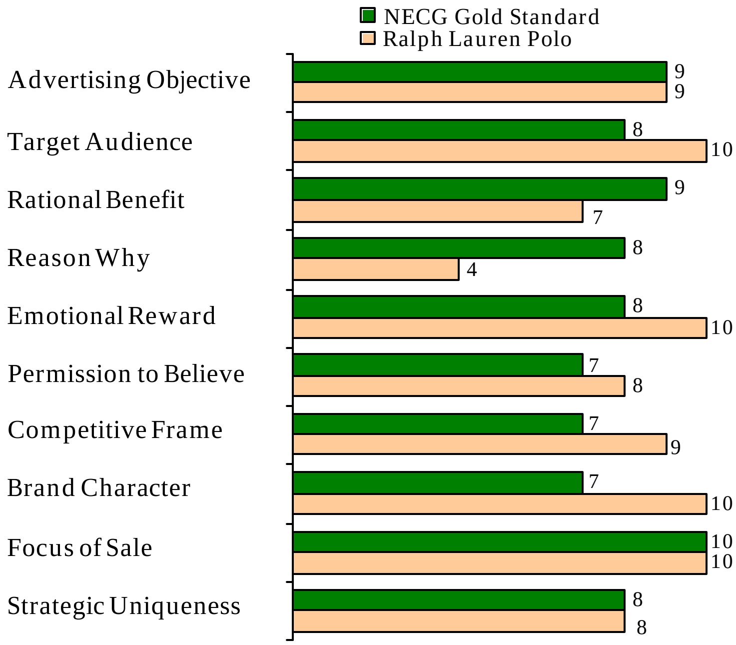
In This Issue

What's Hot, What's Not

Hot!	Not!
Nissan	Mazda
Lizzie McGuire	Britney Spears
Lowe's	Home Depot
LeapFrog	Learning Co.
Hands-Off Spa	Deep Tissue Massage
Grand Theft Auto	NASCAR Thunder

POLO.COM RALPH LAUREN Polo Ralph Lauren Campaign

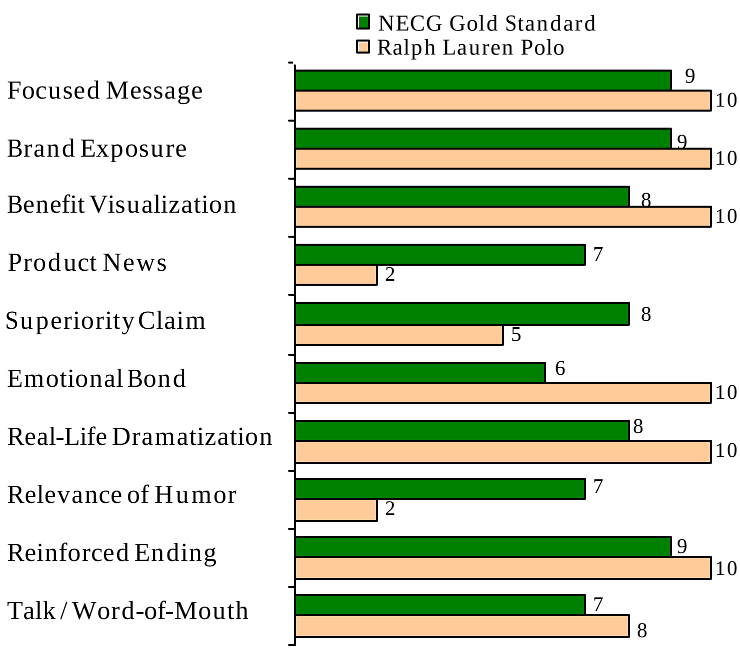
The Polo Ralph Lauren TV campaign is an oddity in the land of fashion which relies primarily on print advertising. The :30 sec commercial features vignettes of young men and women enjoying outdoor sports and activities like horseback riding, football, etc. Emotionally charged, patriotic theme music is heard throughout the spot which culminates with the VO celebrating the glory of Ralph Lauren and inviting people to visit Polo.com. In their first review of a fashion ad, Gary Stibel and Bob Lepre rank the campaign very strongly on many measures, suggesting that fashion and TV can coexist.



STIBEL ON STRATEGY

"What this campaign lacks in rational benefit and reason why, it makes up in emotional reward and brand character. From the music to the talent, this campaign is focused on an aspirational objective of separating Ralph Lauren from the pack of fashion clothiers and elevating it to the unique position of fashion statement of choice for those who are or wish to be among the "beautiful people".

NECG Gold Standard = 81/100
Ralph Lauren Polo = 85/100



LEPRE ON EXECUTION

"Ralph Lauren is the name for sporty, fun, fashion that seems to be always in. This campaign optimizes the "aspirational attainment" positioning that Ralph Lauren strives for. The execution is energizing, upbeat and cleverly blends stills with motion and anthem like music . . . it's just plain fun to watch. I wish it had more product news, but that's a small point for what may be the best fashion oriented spot on TV today. It's an haute couture execution that appeals to you and me."

NECG Gold Standard = 78/100
Ralph Lauren Polo = 77/100

NECG Interviews Michael Delman, General Manager of Advertising about the New Advertising Discipline at Microsoft

On-the-Edge Accomplishments

- Manages Microsoft's $3-4 billion global advertising program
- Has led product and international assignments at Microsoft for 15 years
- Responsible for Microsoft's relationship with McCann Erickson worldwide

NECG: Tell us about Microsoft .NET's new campaign based on 1° of Separation.

MD: I'd like to think of communications at Microsoft as a house. The Microsoft brand positioning is the roof of the house that covers the floors below, and that positioning is - Microsoft enables people and businesses realize their full potential. We just launched a brand campaign broadly in TV and in print.

So, that is the roof of the house. One of the main floors that sits under that roof is the Enterprise Agility campaign, which is our effort targeted towards business. By the way, you're referring to it as the 1° of Separation campaign, but that's just the creative concept. In addition to that, we have other campaigns or floors for Windows, Office, MSN, Xbox, and a whole series of Visual Studio campaigns targeted mainly to developers. So those are the main floors that reach various targets ranging from business decision makers to IT professionals to developers, to gamers, to Internet users. The important thing is the brand really informs everything we do on the floors from a tone, manner, message, look and feel standpoint.

We're a rather unique company in that our customer base is very broad. The challenge is to stay competitive in every category, but also remain true to the brand. Where that becomes really challenging, for example, is in Xbox where you have to have a certain level of action in the games or in MSN, where you have a very entrenched competitor like AOL. We probably have made more progress is shaping the Microsoft brand strategy and having campaigns sit under this architecture in the last 12 months than we have in the last 10 years. It's becoming an important discipline at Microsoft and I think it's all part of being a responsible leader. People expect that consistency from us. The roof is the brand position and what we're gonna talk about mainly today is one of the floors that sit under the roof.

NECG: Are you moving towards a common look and feel across campaigns then?

MD: More and more everyday. Until 2-3 years ago, we had our advertising spread out between a combination of agencies. We have consolidated everything at McCann over the past 24-36 months and that helps a good deal. For example on MSN, where the product name is more prominent than the corporate brand Microsoft, the tone of the ads is still very consistent with realizing potential and responsible leadership. We have evolved to focus more on customer needs than the competition itself, which is different than what we might have done five years ago.

The new round of Enterprise Agility ads that will break in January are also very consistent from a tonality standpoint. The hardest one admittedly is Xbox, which is like Touchtone Pictures for Disney. We haven't quite gone that far to completely un-brand it away from

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Microsoft, but the Xbox brand is more prominent than Microsoft. There are certain things you need to show to be competitive, but we do draw the line and we've actually pulled Xbox ads that we thought were out of the brand character. So, are we totally there in look, tone, and feel? No, but we're a lot further than I've ever seen this company get and I've been involved for the past 15 years.

NECG: What has been the driver of this more disciplined approach to advertising?

MD: It's not just advertising, but a more disciplined approach to how we communicate with customers and applies even to sales calls and consulting services. Steve Ballmer is really the person who's driven the values and vision of the company, but certainly Bill has had a lot of input into it as well.

Since we don't have turnover at the top management level, we have found that it has to come from the top for people to embrace it and once Steve and Bill promote it, people are very willing to follow because they know they're following people who have a long term vested interest.

NECG: Lately, Bill and Steve have been talking about security a lot. How has that affected your communications?

MD: When Bill announced our focus on security, we stopped development of products for a quarter and worked only on security issues. What I try to think about from an advertising standpoint is not getting too far ahead of what we actually deliver. Going back to this Enterprise Agility campaign, it would have been a lot harder to do four or five years ago because we were mainly a desktop company. Now we have very credible enterprise products, which makes it easier to deliver. Same is true with security. We spent a quarter focused on improving the security of our product line and that effort continues every day. So now we can start to talk about it significantly in advertising, especially to IT professionals. We're trying to be responsible and pragmatic about what we say and when we say it so we're not over promising.

NECG: What was the genesis of the Enterprise Agility idea?

MD: Historically, Microsoft was a company that focused on developers. Over time, we branched out to focus on influential end-users, people who generally led companies in a certain technology direction on software usage. The influence model works best when there are a couple million users of a product. When there's hundreds of millions of PC users, the influence model isn't quite as strong at the core.

We realized that what we need is a 3-way dialogue between us, business decision makers & IT professionals so they have a common understanding of Microsoft beyond the desktop where we are well understood. The Enterprise Agility campaign is a result of that effort.

NECG: How did you get to the specific copy execution of 1° of separation?

MD: 1° of separation is just a conceptual idea that will evolve. Our focus is actually more on "connection" than "separation". We are establishing the notion of connecting partners, customers, employees, etc. to create this friction-free environment that lets businesses respond quickly to market changes. That's the core idea behind all executions. 1° is just a creative way to communicate that.

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NECG: How did the campaign perform in testing?

MD: This campaign is very different from launching a new version of Windows. When we launch Windows, we get an amazing lift in awareness and perceptions almost immediately. This requires a more gradual buildup. So far, the results have been promising in pre-post tracking. Obviously, we're seeing more pronounced movement against the IT audience, but there is good progress among business decision makers on "flexibility", which we think is a key metric against the agility promise.

NECG: Launch of the .NET campaign overlaps with one of the worst times in corporate technology spending. How has it moved sales?

MD: You know our sales data is very public and we are making good progress. It is a lot more difficult today than it was 3 or 4 years ago when IT spending was more robust, but there is fairly consistent demand for what we make.

Since .NET really is a core developer concept, what we need is development teams at companies like Volvo and Virgin using the .NET framework. We've seen good progress there. Between 2001-2002 we saw a 25% increase in .NET awareness among IT professionals and a 31% correct branding of .NET to Microsoft. That may seem trivial, but it isn't because there's a lot of confusion in this market with names like Websphere, .NET, J2E, etc. A lot of times people will know the concept, but not really know who it's associated with or what differentiates it.

For a product like Windows, it's not about awareness, it's really about convincing people that the next version is worth the upgrade. For .NET, it's very much about creating awareness and some attribution and comprehension of the concept. We're making progress there too, not just through advertising, but also PR. For example, HP just reaffirmed their commitment to our platform.

NECG: How integrated is this campaign across your marketing mix?

MD: It is much more integrated today than it was 18 months ago. Enterprise Agility started out as an advertising idea and morphed into a full scale marketing program. The marketing programs have done a good job of catching up, so I would say we were probably a "C" 18 months ago and now we are a "B". There is still a lot of potential upside.

NECG: Talk to us a little about your branding.

MD: I think the biggest misconception among people here and on the outside is that we have more brands than we really do. For example, people would say PowerPoint's a brand. I don't agree. I think we fundamentally have 3 big brands and they are Microsoft, Windows and Office.

Going forward, you'll see us putting a lot of weight behind these brands - Microsoft will be the company brand, Windows will be the platform brand, and Office will be a product brand. Most everything we do in the developer space will be under Visual Studio and finally, there will be an IT brand. MSN and Xbox are emerging products as much as brands. I would say we really didn't have a branding architecture until 12 months ago. We had Microsoft and whatever products got a lot of money and market momentum became brands like Windows and Office. Now, it's much more premeditated.

NECG: How is competition responding?

MD: I won't go too much into competition, because we're trying to get away from that and focus more on our customers. I think the best evidence of competitive response is IBM's E-business on Demand work, because it has a lot of the core themes that we've been talking about in our Enterprise Agility campaign for the last 12 to 18 months. ■

NECG Interviews Ian Rowden, EVP and CMO about Sustained Innovation at Callaway Golf Company

On-the-Edge Accomplishments

- ☞ Redefining the Callaway brand portfolio to meet the challenges of a changing competitive golf equipment landscape.
- ☞ Expanding Callaway's global marketing strategy to incorporate new category growth in the apparel and footwear segments.
- ☞ Leading a business category based, product management organization to focus on key business opportunities.

NECG: USA Today voted your Odyssey 2-Ball Putter as one of the best products in 2002? Where did the idea come from?

IR: First of all, the 2-Ball Putter is an extension of the Odyssey putter franchise, which we acquired in 1997. About 2 ½ years ago, we introduced a White Hot feature in that putter, which was in essence an insert made from the same material as the Callaway golf ball cover. So you see, the elements of the 2-Ball Putter have been in place for a while now.

Working on the Odyssey brand, we knew that the biggest issue average golfers have with putting is alignment – both in lining up and staying on line during the putt. Naturally, there has been a lot of work done by this company and others on alignment, but the 2-Ball putter created a solution that is truly unique.

When it was first created, we all looked at it and went, "Wow, that looks a little strange". You soon forgot how it looked once you putted with it because it genuinely helped keep the ball on line for the average golfer.

Therefore, what you have today is a wonderful alignment aid incorporated with the technology that we'd already built in Odyssey under a very strong brand name. The net result is the largest selling putter in the industry. Today, one in every three putters sold in the US is a 2-Ball putter and one in every two putters sold is an Odyssey putter.

NECG: Did it cannibalize the base though?

IR: Amazingly, it didn't! Odyssey brand, without the 2-Ball introduction, is also trading and tracking above last year on both units and revenues. And of course, we've seen substantial share growth – Odyssey now has over 52% share of the putter business in the US and we've grown 10 share points in a year.

NECG: You always knew alignment was a problem for golfers. What led to the idea of putting cross-sections of 2 balls on the putter? Was it a brainstorming session? Was it a lot of analysis, a combination?

IR: It was a combination of all those things. This company is very entrepreneurial and invests more money in R&D than any of our competitors. We have built a very substantial competitive advantage based on innovation.

The innovation process here is both structured and informal, and that's the way we like to run it. We've have very talented people and strong processes in place, we work many, many years in advance, we have a good consumer marketplace apparatus that feeds learning into the process and we have an informal element to the design and invention process.

In the particular case of 2-Ball putter, we used a design patent based on a concept from golf instructor Dave Pelz who had done a lot of work in this area.

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NECG: How does innovation differ in developing products for pros vs. average players?

IR: We are absolutely dedicated here to the average player. Philosophically, this company was born on the idea of creating golf equipment that makes the game more enjoyable for average players.

What we know about the average player is that they don't necessarily want to shoot a low score (although they would like that) or cross milestones like lowering handicap from 18 to 10. What they want is to hit more great shots. If you're a golfer you'll understand what I mean. It's the shot after which you say, "Wow, that was really good, if I could only have more of those."

Ely Callaway's vision was to create products that help the average golfer get more great experiences. We think it's an added bonus that professional golfers will also play with our golf equipment.

We do recognize that pros, from a marketing standpoint, are heavy influencers of purchase in the business. So, we utilize many pro golfers on staff, whether it be an Arnold Palmer or a Johnny Miller or a Charles Howell, to test our equipment and give us valuable feedback.

We also share the same equipment when it's further along the development process with the average golfer and make sure that what we're creating is a Callaway product. As you know, Callaway products are unique in their look and feel, particularly our irons. We were the company that essentially created oversized titanium drivers and the brand Big Bertha is really important in that process.

So, all those things play into how the development process works for us. Some products have a development cycle of a couple of years, some have a development cycle of multiple years, depending not only on the design, but the type of materials required to create them.

NECG: How do you organize for innovation?

IR: We are organized by category, so the heads of our wood drivers, iron drivers, putters, and golf balls all report to me. They operate as the lead point for product management and marketing and work under a matrix organization structure to ensure that we've got lifecycles that line up with purchase cycles for products. We think of them as separate businesses because the competitive base is different across categories and geographies. Remember, we do business in 68 countries around the world, so there's a lot of metrics that we think about.

NECG: Is the Odyssey brand fairly independent then?

IR: Yes. We treat Odyssey as a unique brand and never market it as Odyssey from Callaway. It's my belief that the Odyssey brand is strong enough to stand on its own two feet. It has certainly shown that, and, ultimately we will want to bring other brands to compete with Odyssey.

NECG: With a constant stream of innovation, how do you manage branding?

IR: We realized 3 years ago that we had perhaps oversupplied brands in the presentation of our product. At one stage we had the Callaway Big Bertha Hawkeye VFT driver. It's very hard to get all of that on the soul of the driver and have the consumer remember it. So, we started a brand rationalization process.

We have three very recognizable brands in Callaway, Big Bertha and Odyssey. We have also developed strong product franchises in Steelhead and ERC for irons and hot drivers respectively. Going forward, we're looking to rationalize some of that thinking and show some more logic between categories.

NECG: What does that mean for new product names?

IR: More simple names. For example, our latest driver is simply called Great Big Bertha II.

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NECG: Has innovation grown the category?

IR: You know, the golf industry has a number of inhibiting factors. From a business standpoint, it's oversupplied with manufacturers. The game itself is difficult, time-consuming and expensive. The net result is that in the last decade there's been no growth in the golf business and in the golf game. As many people leave the game each year as come to the game.

So, what we look at now are avid core golfers and try to own their equipment needs. Don't get me wrong, we do look at people who come and go from the game like children, women, seniors, etc. and think about how to design equipment that can make it easier for these people to enjoy the game. However, we manage it all around the core business.

So, from an innovation standpoint, we look at creating products that are great successors to our current products, we look at market trends, we look at consumer feedback, we look at new technologies available to us, etc.

NECG: How do you manage evolutionary vs. revolutionary innovation?

IR: We realize that we have to not only evolve our equipment, but from time to time, we have to come up with something revolutionary like the 2-Ball putter. It's the key to our business going forward. I'll use an example - we've gone from an X-12 iron to X-14 to now X-16. These irons are somewhat evolutionary in that they take a Steelhead concept, but have new technology, look and feel in them.

We also need breakthroughs to infuse our business with more excitement. There's no particular pattern to it except that we work a process that's multiple years in advance and we try and feed in as many things as we can into the invention element of the process.

NECG: What keeps you ahead of the game?

IR: This will sound trite, but Ely Callaway always said as long as we're focused on making golf equipment that is demonstrably superior and pleasingly different, we will always have an edge. I mentioned earlier that golf is all about great shots that bring people back. We want to create more of these shots. We try to manage that philosophy and that culture against having to sit down with analysts every quarter and explain our earnings.

NECG: Even Wal-Mart sells golf clubs now. How does the changing retail landscape affect your innovation efforts?

IR: This is another key issue for us. I mentioned earlier that I think this business is oversupplied with golf manufacturers. It's also oversupplied with retailers. On-course pro shops are fragmented and provide a diverse range of services. Off-course specialty retailers like Golf Galaxy are relatively new to the business. The combination of an oversupply in retailers and manufacturers, and desire to grow market share in a business that's stagnant has lead to a market share war along with price erosion in our business, which is not healthy.

Not only is there price erosion, but also margin erosion, and when that starts to happen, it puts a lot of pressure on both innovation and your ability to bring new materials and new thinking through the value chain. One of our key business strategies is to figure how to stabilize the pricing mechanism in the industry. To do that, you need a strong brand, discipline and frankly, a strong heart.

NECG: Have niche manufacturers like Orlimar gotten to scale where they're also posing a threat?

IR: No, I wouldn't say they're becoming a threat, they are something that typifies the kind of cottage industry aspect of the golf business. In this business, anyone can come up with an idea and convince some golfer that they can play better.

You can get some traction, but it's very difficult to sustain. Normally what happens is the second, third and fourth generation of these products are very difficult to find, so these people seem to come and go, but they do come and go, and we have to always keep an eye on them. ■

What Price is Right

In a recent pricing survey conducted by the Professional Pricing Society, over half of the respondents said their primary pricing issue is “competitors who price poorly and commoditize their marketplace”. Furthermore, 40% of these respondents also indicated that “customer haggling” has “driven standard pricing out of control”.

Given this situation, how does a manufacturer determine the right pricing strategy? What Price is Right?

New England Consulting Group’s research shows that the #1 driver of pricing decisions at most companies is how the industry / competitors typically price. Increasingly, this approach is not sufficient to make optimal pricing decisions because while it may make you more competitive, it also levels the playing field and makes you less profitable.

Today, pricing is the most evolved function within marketing and it would serve every marketer well to understand new and emerging principles of pricing. Below, NECG offers a simple, but powerful framework to conduct a pricing audit and evaluate your current pricing strategy against potential alternatives.

Pricing is what “powers” the value in your business model. So, the next time your natural instinct is to say, “This is how pricing has always worked in our industry”, consider examples like Dell, Wal-Mart, IBM, Capital One, American Airlines, Ikea, Marlboro, BMW, and Marriott. These companies / brands have changed the pricing playing field in their industries for the optimal combination of competitive advantage and profitability.

Pricing Program Spectrum

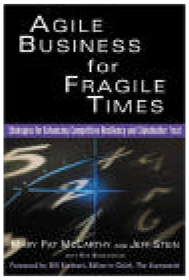
Value Based

Pricing Sophistication

Cost Based

Types of Pricing Programs	Objective	Description
Disruptive Pricing	• Change the basis of competition	• Often marketers who enter an industry with a different business model and cost structure, e.g., Dell, Lexus
Solutions Based Pricing	• Price / acquisition cost based on total value of solution	• Used in many markets where customers are buying a composite of benefits beyond just equipment, e.g., IBM
Added-Value Pricing	• Value product performance superiority, services, delivery, etc. in pricing	• Often used in complex equipment businesses where the manufacturer can capture an added-value in its prices, e.g., Motorola
Continuity Based Pricing	• Price based on volume / loyalty	• Prices based on historical / projected volume and exclusivity
Promotion Driven Pricing	• Price based on temporary discounts, specials, rebates, etc.	• Typically used in competitive markets such as hard goods sold through wholesalers to spike demand, or introduce new products
Cost-Plus Pricing	• Target a specific margin above cost	• Utilities use cost plus with the margin regulated
Experience Curve Pricing	• Price based on stage on experience curve	• Often used in highly competitive manufacturing industries where a large scale producer can take advantage of its position on the experience curve

This article was written by John Ruf, Partner at NECG. Feel free to e-mail him your comments at jjr@thenecg.com



Agile Business for Fragile Times

-- Mary Pat McCarthy and Jeff Stein

Amazon Ranking	NECG Edge Ranking
☆☆☆☆☆	☆☆☆☆

The book, awkwardly subtitled "Strategies for Enhancing Competitive Resiliency and Stakeholder Trust," provides ideas to overcome challenges and identify opportunities, in a recession. It also suggests that companies invest now to be ahead of their competition when the economy rebounds.

It recommends four basic philosophies to excel during and after a recession:

- Base every decision on the needs and wants of customers. Evolve to a customer-centric organization that looks for value creation throughout the enterprise.
- Use communications to create strategic advantage. Turn up the volume of internal and external communications, recognizing their role as a trust builder.
- Don't hibernate during a downturn. Never take the eye off revenue growth.
- Performance cultures need constant monitoring. Vision is good, but execution is the bottom line.
- Strategies must align with market uncertainty. Agile businesses need to observe, react, and factor market changes into continual cost and growth refinement strategies.

Evidence of Agility

The authors define agile businesses as those that can think "out-of-the-box" and can change focus quickly to grow. But, they don't believe in silver bullets, although great execution can look like a silver bullet. They constantly plan for profitable growth regardless of the economic environment, tempered, though, by aligning with cost-reduction plans. Their success is based on innovation and constant streamlining of operations, while establishing a flexible cost structure.

Conventional Wisdom

The authors challenge other conventional thinking that if supported better would have made this book even more provocative.

They question "first mover advantage" because the risks often outweigh the long-term opportunity. They believe you have to execute better, not just be first. To them, market share implies of a false logic because not all customers are equal. The focus must be profitability.

They warn against over-dependence on segmentation. They contend that if you can't match a product's application to a segment's need for that application, you shouldn't be direct marketing. The key to success is "need," not speed (to market).

Transformation Strategies

They believe that agile companies are always searching for opportunities to change their value proposition to more profitably serve their customers. They discuss opportunities for value creation by changing their business models to adapt to changing customer needs. They look for value in intangible assets ranging from brands to patents to distribution systems to customer databases to intellectual property.

Finally, they believe that value should be more transparent. The thought is that everyone inside and outside the organization should have a clear understanding of the value of the company. Recent corporate scandals and bankruptcies have proven the need to build trust in the company's value.

NECG

The authors have presented an intelligent case for the "agile" company as the new success model, regardless of the economic cycle we are in. However, their arguments are weakened by a lack of actual case histories to support their case. To some extent, we all have to imagine what companies best fit the "agile" definition. ■