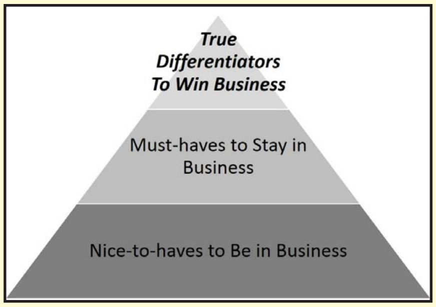
Understanding and Finding Your True Differentiation



In this article, the author explores how the roles of strategy, pricing and marketing have become even more central to ensuring that value propositions remain attractive and that differentiation strategies are sustainable in this very dynamic global market. Stephan M. Liozu is Chief Value Officer of the Thales Group (www.thalesgroup.com). He is also an Adjunct Professor & Research Fellow at the Case Western Research University Weatherhead School of Management. He holds a Ph.D. in Management from Case Western Reserve University (2013), is a Certified Pricing Professional (CPP), a Prosci® certified Change Manager, and a Strategyzer Business Model Innovation Coach. He authored three books, *Dollarizing Differentiation Value* (2016), *The Pricing Journey* (2015) and *Pricing and Human Capital* (2015). He sits on the Advisory Board of LeveragePoint Innovation and of the Professional Pricing Society. He is a Strategic Advisor to 360pi, The Kini Group, and PriceSenz. He can be reached at sliozu@gmail.com.

Business grows more challenging each year. The level of competitive pressure is unprecedented, and the level of disruption in business models has increased exponentially. Over the past ten years, many companies have gone out of business, sold themselves, or undergone radical re-engineering efforts. With no end to competitive intensity in sight, the role of strategy and marketing becomes central to ensuring that value propositions remain attractive and that differentiation strategies are sustainable in this very dynamic world.

Faced with this reality, marketing and strategic teams are designing and deploying business strategies to protect their businesses from price wars and copycat competitors. But these strategies either lack true differentiation power or are swiftly copied by more nimble competitors. Differentiation is hard to find, to crystallize into value propositions, and to maintain over time. It's a complex construct of business strategy that is often misjudged or misrepresented.

The purpose of this paper is to help executives in business, marketing, and pricing understand the key concepts related to differentiation, especially with what we call *true differentiation,* which is at the heart of pricing willingness-to-pay and value-based pricing.

I first propose potential explanations for why differentiation is difficult to gauge. Next, I discuss what differentiation is and how you can identify it in your current business. Finally, I propose a process for managing differentiation and for linking it to your business and pricing strategies.

General Confusion about Differentiation

There is much confusion in the business world about what differentiation is and is not. Being differentiated and being different are not the same. In my experience deploying differentiated business and marketing strategies, I encounter five areas of confusion:

1. *Lack of **understanding** of the concepts of commoditization and differentiation.* It is clear that understanding differentiation requires having taken a strategy and marketing class. Professionals from backgrounds such as IT, finance, accounting, or manufacturing do not necessarily fully understand them.

2. *Lack of **knowledge** of the organization's strengths and weaknesses.* Many professionals are unaware of their strengths and weaknesses, especially outside of go-to-market functions. The lack of competitive knowledge also leads to blurry perceptions of what makes a company unique or better than its competition.

3. *Lack of essential **training** on the company's products and services.* Given cost-cutting programs and an emphasis on cost-consciousness, many firms have cut back on training programs on their products and services. These training workshops are essential to providing deep, detailed product and service advantages. They give people theoretical and practical knowledge of critical functionalities and features.

4. *The power of the **commoditization** mindset.* In organizations facing extreme competitive pricing pressure, the commodity mindset has taken over. There might be very little discussion of differentiation and uniqueness. The focus is on handling commercial and pricing pressure.

5. *Lack of **access** to the markets and customers.* In some industrial markets where semi-finished goods or heavy industrial products are manufactured, teams feel that they are too far from end users and thus do not understand the value that their products and services bring to the ecosystem. They tend to rely on large OEMs or on powerful distributors to get a sense of their differentiation. This is not good.

When business teams are not fully educated about and prepared for the differentiation discussion, the procurement teams they face have an easy time breaking apart their weak value propositions. In fact, professional buyers are trained to

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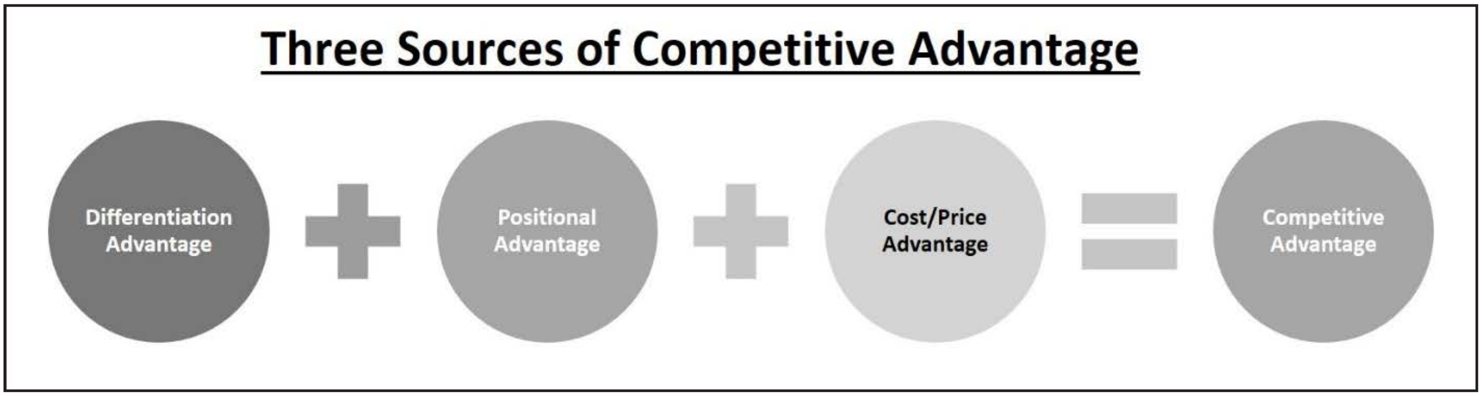
Figure 1



do the following:

1. Break the sales team's **confidence** in their differentiation.

2. Place your business in a **commodity** bucket and focus on price.

3. **Generalize** your positioning: "It's all the same" or "A satellite is just a satellite."

4. **Object** to your intended differentiation and **refuse** to hear about it during value and pricing discussions.

5. Tell you what **stories** they hear about you and competitors in the market.

6. List all your performance **breakdowns**, issues, and areas where your premium is not justified in order to weaken your differentiation.

At the same time, competitors' salesforces are trained in the art of creating confusion in the differentiation position. Their role is to make everything fuzzy, especially if their products or services are performing less well than yours. Often these sales reps will do the following:

1. **Pretend** they offer the best value for money.

2. Tell buyers that they are the **same** as or better than you.

3. Make the differentiation position **fuzzy** or blurry by claiming that they can deliver the same level of performance, even if it isn't true.

4. Offer aggressive discounts to make the buyers hesitate about the performance/premium relationship they might have with your products.

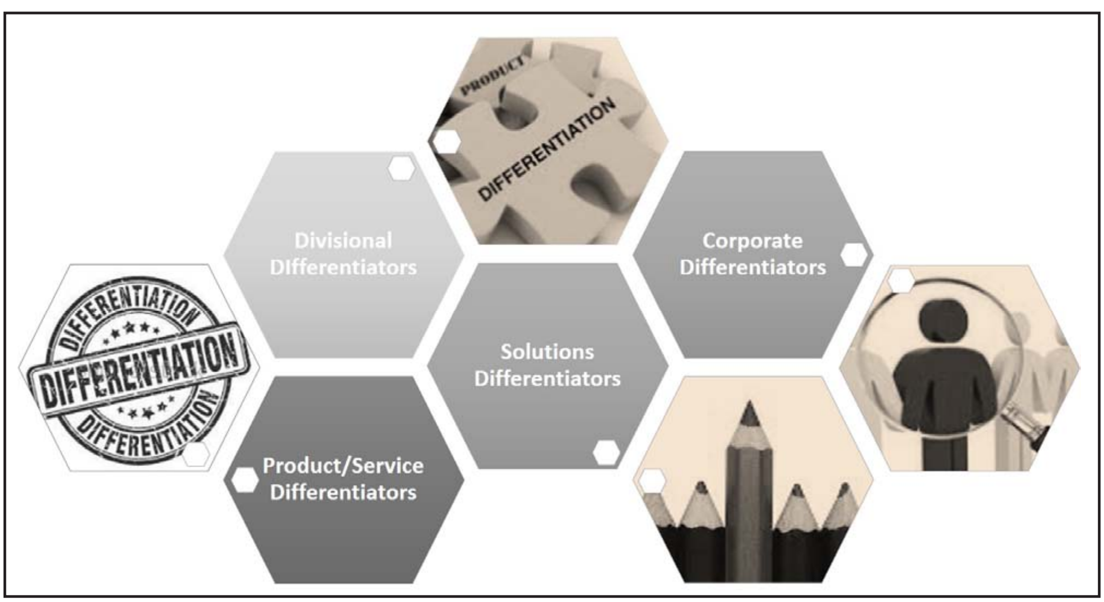
5. Tell their **own stories** about you without backing or evidence.

6. Disrupt value maps by offering **promotions and rebates.**

7. Make short-term **promises** they cannot keep over the long term.

So there is a lot of noise out in the market about who is better, who has differentiation and who does not, and what uniqueness means. It is therefore essential to win the communication battle against buyers and competitors by fully understanding what your differentiators are and by educating your internal organization about these differentiators. But first, it's even more important to train your organization about what differentiation is, where it resides, and how you validate it as true differentiation.

Figure 2: Levels of Differentiation



What Is Differentiation?

In economics and marketing, product differentiation (or simply differentiation) is the process of **distinguishing** *a product or service from others, to make it* **more attractive** to a particular target market. This involves differentiating it from competitors' products as well as a firm's own products. The concept was proposed by Edward Chamberlin in his 1933 "Theory of Monopolistic Competition."

Differentiation is not a new

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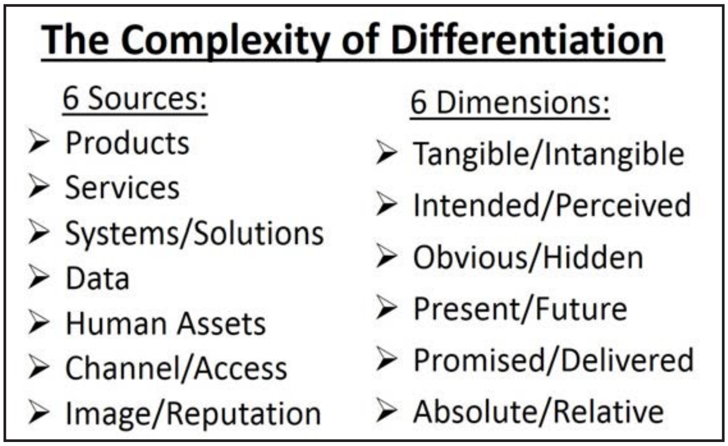
Figure 3



concept. Plenty of papers and books discuss the topic. I highly recommend the work of Michael Porter, Chris Zook, Clayton Christensen, or Peter Drucker, just to cite a few. It's worth refreshing our memory. The concept of differentiation is at the heart of competitive advantage. There are three sources of competitive advantage, shown in Figure 1.

The *cost/price advantage* is straightforward. A firm needs to ensure that it has a cost advantage and solid financial shoulders to sustain this positioning, especially in cases of price wars, as we see in many industries. *Positional advantage* may or may not be intentional, but it's nice to have. This advantage comes from having a preferential position in an industry, including having well-positioned plants, unique access to key decision makers, and high switching costs due to legacy infrastructure; being a sole-source supplier until competitors bring new assets online; and so forth. A decade ago, Dell Computer had a positional advantage, with plants close to suppliers, and a low-cost advantage. Most businesses, however, gain their competitive advantage from their *differentiation advantage,* which refers to the uniqueness and attractiveness of their products, services, and solutions. Differentiation advantage is thus more intentional; it's what makes them win in the market. The key is identifying the sources of differentiation that customers perceive and acknowledge as superior or unique. And that's the tricky part. As Figure 2 shows, differentiation can come from specific products, services, or software. It might come from the integration of systems and solutions. A firm might have no specific product differentiators but some divisional or corporate differentiators. The search for differentiation should be multi-level, and the exploration cannot end with products and services. Let me pause here for a second. Ask yourself this question: What are my firm's corporate and/or divisional differentiators? Most people I work with can't recite a clear and crisp value proposition that includes critical differentiators. Now, it's a real necessity.

The complexity does not end here. There are sources of differentiation and several dimensions to consider. The sources listed in Figure 3 are also straightforward. Business books discussing differentiation encourage professionals to look beyond products to services, software, data, human assets, experience, and channel considerations. This isn't hard to understand. What might get a bit complicated is gathering enough information about your competitors to be able to assess whether your firm is differentiated or not. For this, I highly recommend the use of competitive analysis tools such as performance benchmarks, competency inventories, competitor profile matrices, and value maps.

Let's focus more on the dimensions of differentiation displayed on the right side of Figure 3.

1. Tangible versus intangible. The analysis of differentiation should include both tangible and intangible components of the offer. Intangible elements include brand, experience, ease-of-doing-business-with, trustworthiness, stability, longevity, and more. They might be a big part of the value proposition.

2. Intended versus perceived. Often, we focus too much on what we intend to deliver to customers. Internally, we are convinced that our advantage is real. What really matters in this analysis is what the customer perceives versus our intended advantage. Peter Drucker stated that "*the customer rarely buys what the business thinks it sells him*." My experience in leading differentiation discovery workshops suggests that the internal gaps between intended and perceived differentiation can be huge. Gaps can exist between internal functions of a single organization. Finally, multiple stakeholders within the customer organization might also have different perceptions. This brings me back to the previous statement that we need to manage differentiation

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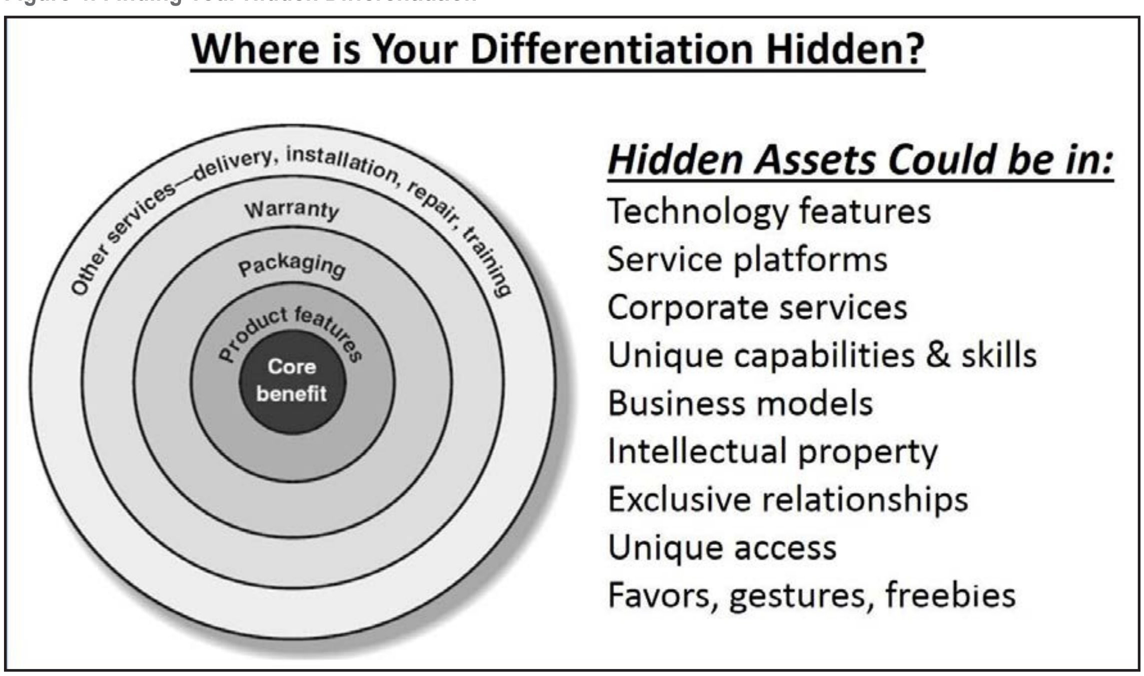
Figure 4: Finding Your Hidden Differentiation



perceptions and systematically communicate differentiation messages internally and externally.

3. Obvious versus hidden. Sometimes advantage is easy to identify and quite visible. It's what I call *obvious differentiation.* Other times, differentiation is hidden, forgotten, and taken for granted. This is often true for groups who've succumbed to the commoditization mindset. *Hidden differentiation* is difficult to find and requires some digging and a dose of open-mindedness.

4. Present versus future. Your current offerings might have differentiation as they stand today. Your innovative offerings have yet to be adopted by your customers. In that case, differentiation is in the future. You're promising your customers a certain level of superior performance versus your competitors. This assumes that you've done all the performance testing needed to show this advantage in the value proposition.

5. Promised versus delivered. What's in the future is therefore not yet delivered. It is promised to customers. In that scenario, you'll need the discipline to demonstrate the advantage versus competitors as delivered. This is often an issue with the quantification of customer value. Customers might trust you once based on your analysis and your promises. In the end, the proof of the pudding is in the eating.

6. Absolute versus relative. Differentiation and value are relative. The era of monopolies is over. Patents are worked around, and disruption is everywhere. It may be that your windows of opportunity, where you're in a unique position or have a strong advantage, are open for just a short period.

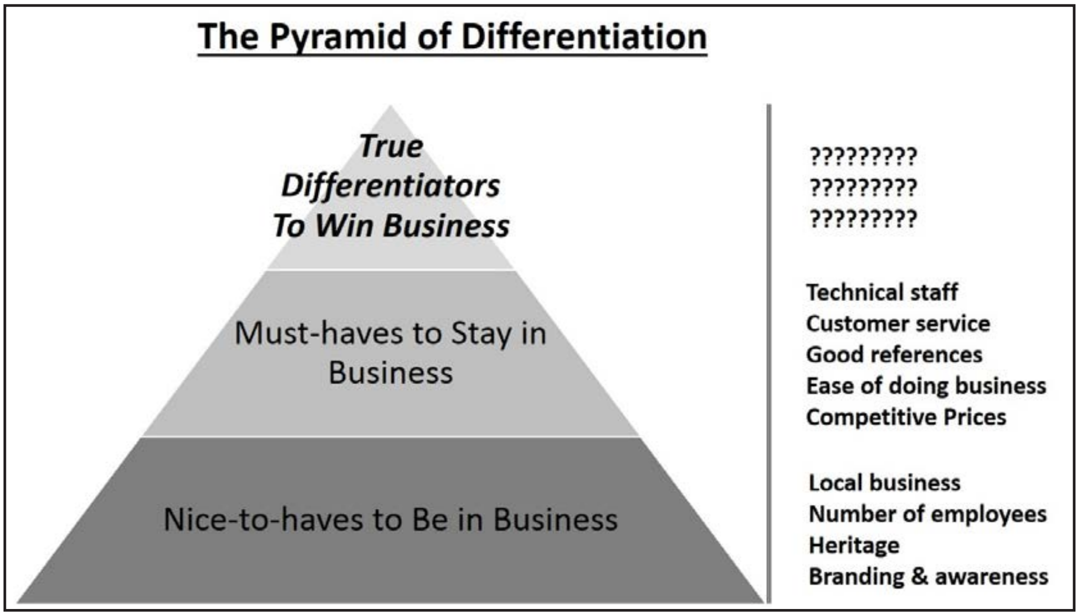
Based on the levels, sources, and dimensions of differentiation, you can understand the discipline required to conduct a thorough analysis of differentiation. I usually recommend a 90-day differentiation blitz that involves a multi-functional team.

How Do You Find Differentiation?

Any product or service can be differentiated, even the commodity that seems to differ from competitors' offering only in price... There is no such thing as a commodity. *All goods and services are differentiable. Though the usual presumption is that this is more true of consumer goods than of industrial goods and services, the opposite is the actual case.*

—Theodore Levitt, *Harvard Business Review,* 1980

Figure 5



The most interesting part of the discovery process is beginning to identify the hidden differentiation I mentioned above. I often get pushback from teams when I force them to find nuggets of differentiation after they've complained about the level of industry commoditization. My response to this complaint is that if they had no differentiation whatsoever, they would no longer be in business. Markets have the ability to neutralize and zap weak players.

So, in small groups of professionals, we begin digging through all levels shown in Figure 2, and all sources shown in Figure 3, seeking hidden assets. These nuggets can be anywhere. We explore things that are taken for granted internally and externally and that generate customer value. I bring people back to periods when the firm was well differentiated and successful. We revisit what made them successful back then to identify whether legacy differentiators still exist. We list favors, gestures, and other little things we do for customers and that we take for granted. We ask ourselves whether the competition also does these things. The process of discovering obvious and hidden differentiators is eye-opening for most people, and especially for sales teams, who might be blinded by competition and price pressures. Undergoing such exploration and rediscovery of differentiation is energizing for commercial teams. They take a break from working in the trenches, step back, and revisit what they're good at.

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The next step is to thoroughly inventory differentiators and to classify them as nice-to-haves, must-haves, or true differentiators. This process leads to intense and sometimes heated discussions about what we do and what our competitors do. We begin to realize that we think we have competitive knowledge but

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do not. My answer here is that we cannot manage a business on intuitions and guesses about what competitors do or do not do. So we have to find out. Most firms know the nice-to-haves and the must-haves, as displayed in Figure 5. They don't know their true differentiators, however, or what makes them truly unique versus competitors. And usually, at the end of the process, there are only a handful of true differentiators.

Figure 6: The VRIO Framework

A Differentiation Value Strategy Must Meet the VRIO Criteria

Is it *V*aluable to Customer in Dollars & Cents?
Is it *R*are to Find or Access?
Is it costly to *I*mitate?
Is the firm *O*rganized to exploit it?

SUMMARY OF THE VRIO MODEL

IS IT VALUABLE?	IS IT RARE?	IS IT HARD TO IMITATE?	IS THE FIRM ORGANIZED AROUND IT?	WHAT IS THE RESULT?
NO				COMPETITIVE DISADVANTAGE
YES	NO			COMPETITIVE EQUALITY
YES	YES	NO		SHORT-TERM COMPETITIVE ADVANTAGE
YES	YES	YES	NO	UNUSED COMPETITIVE ADVANTAGE
YES	YES	YES	YES	LONG-TERM COMPETITIVE ADVANTAGE

For this discovery-and-screening process of differentiators to work, we must be candid and have honest discussions about our true advantages and uniqueness. I use the VRIO framework shown in Figure 6 to facilitate these discussions. This framework allows you to conduct a formal screening of your potential differentiators.

Each differentiator is subject to the yes-or-no process or is rated on a scale from 1 to 10 for each question. The *V* stands for *valuable to customers* and links differentiation to the quantification of customer value. We need to select differentiators that bring economic value to customers. *R* refers to *rarity,* which is something that might not be controllable. In some industries, there might be 20 competitors, and in others, only two. One needs to be aware of this and understand the competitive pressure. *I* is for imitability. This element is critical to gauging differentiation. We refer here to technical and nontechnical switching costs that protect a supplier's position. Sometimes a firm has real, sustainable uniqueness. At other times this inimitability might last only a few years or months. The key is to find real areas of advantage in products, services, solutions, corporate dimensions, or intangible assets. Finally is *O,* for organization: a firm has to be good at executing and exploiting its advantage. A prerequisite of value-based strategy is the discipline of execution: Is the firm organized for success in exploiting the differentiation? Do they have the right structure, people, assets, and culture to execute well? In the end, you compile your rating for each differentiator to determine whether you have short- or long-term advantage. The outcome of this rating process might be three or four critical differentiators that can be ready for customer value quantification versus the competition.

Note that the same analysis might have to include negative differentiation as well (see Figure 7). It is essential not only to find real and true positive differentiators but also to focus on areas where competitors might be better than us. I've never worked with a business or a division that lacked negative differentiators. I would of course not recommend that these negative drivers be volunteered to customers during value proposition discussions. However, it's a good idea to be prepared for customer objections during business negotiations.

Figure 7: Positive and Negative Differentiation

Positive Differentiation:
Advantage that is generated by your unique differentiators
(efficiency, durability, incremental margin gains, etc.)

Negative Differentiation:
Disadvantage that is unique to your differentiated offering
(training, testing, ramp-up costs, technical support, etc.)

You can do this work across your go-to-market functional staff with two or three differentiation workshops over 90 days. Cross-functionality is essential to avoid internal perception gaps. Between workshops, you might have validation points internally and externally. The outcome is a list of critical differentiators that can feed the marketing and pricing processes.

Make Differentiation a Critical Part of the Marketing Process

Because competition never stops moving, you must manage the analysis of existing differentiation dynamically and make it part of the marketing process. You should revisit your differentiated value propositions once a year as part of the marketing planning cycle or the budgeting process. I propose the process shown in Figure 8. It begins with a 90-day internal process to identify true differentiators and align internal stakeholders.

Once this is done, the differentiators need to be validated through customer research (qualitative interviews or quantitative surveys). Based on customer feedback, the process is revisited and all differentiators are prioritized and packaged for communication. Finally, all relevant go-to-market teams should receive training on critical differentiators in the form of team meetings, lunch-and-learn events, webinars, and formal product training, and so forth. The marketing function then becomes the "guardians of differentiation." Through ongoing customer feedback, customer satisfaction reports, win/loss analysis, and social media analysis, they keep their fingers on the pulse of the perceptions of differentiation over time. I recommend that once a year, they test the level of differentiation for products, services, and other offerings. It never ends. Competition is fluid and dynamic: you might be differentiated one day and commoditized 90 days later. This paper obviously focused on differentiation of existing offerings. The same should be done for innovative offerings through a robust front end of an innovation and customer-insight approach.

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Concluding Thoughts

Finding existing true perceived differentiation is hard. It requires competitive knowledge, deep internal understanding of strengths and weaknesses, and cross-functional teamwork. It also requires to get to what the customer truly thinks is our differentiation. But it's worth the effort to be able to list critical differentiators and to share them internally and externally. These true differentiators can be used in communication campaigns, in marketing programs, in customer value quantification exercises, and in customer negotiations. They become the heart of a systematic value-messaging campaign to regain control of the marketing noise out there and to influence customer perceptions. If you don't do the work, someone else will do it for you, and it might not be pleasant. You have to be in control of the market's and the customers' differentiation perceptions to ensure that intended differentiation is the same as perceived differentiation. That takes time and effort. It takes the hard work of cross-functional teams to dynamically revisit differentiation each year. It takes the commitment of a leadership team to challenge the status-quo and to self-disrupt. But it's the heart of marketing and, eventually, value-based pricing.

Figure 8

The Priorities with Differentiation

1) **Understand** your true differentiation internally.
2) **Align** all internal stakeholders around this understanding.
3) **Validate** true differentiation with customers and prospects by:
   - Conducting internal assessment on how customers perceive you.
   - Conducting informal customer interviews about the elements of differentiation.
   - Analyzing won/lost deals with prospects & existing accounts.
4) **Modulate** internal perceptions of differentiation and adjust the value communication & messaging.
5) **Train** all commercial folks on the perceived dimensions of value and differentiation.
6) **Start over** and never accept the status quo.