**How markets grow. The factors associated with category expansion.**

**Short Abstract**

We advance knowledge of category growth in developed markets, identifying the factors under manufacturer control that are consistently associated with change in category sales level. The analysis is based on scanner data from four developed markets, 20 packaged goods categories, over 6-8 years. We find that of all factors, change in price per volume has the strongest association with change in category sales, followed by change in the number of SKUs. The intensity of price promotions in the category has no relationship with category sales increase. Category maturity, in terms of relative quarterly penetration, is an important defining condition; below 50%, category sales grow through volume increases. Above that threshold, growth is driven by increases in price, but we find that introducing new SKUs is a common method for manufacturers to increase price per unit at maturity. Brand premiumisation therefore holds the key to growth in equilibrium markets.

***Keywords:*** *Category Growth****,*** *Premiumisation,**Category Maturity*

***Track:***

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**Introduction**

Businesses around the world face a growth imperative, and marketers are being asked loudly to deliver that growth. In developed markets, one way brands might deliver growth is through category expansion (Yoon et al., 2017). Expansion from maturity has been the subject of very little empirical investigation but, if successful, it benefits all actors in the marketing channels, with the highest rewards reserved for the brand leader. Therefore, to advance category growth knowledge this study investigates factors in manufacturers’ control in developed markets and asks which are most associated with category sales dynamics and under what conditions.

**Background**

Most FMCG brands compete in equilibrium markets where supply side (manufacturers) and demand side (broadly, retailers) face a ceiling on category purchase volume and persistent, zero-sum competition. To outsiders, such markets are “unattractive”: to incumbents an increasingly pressing objective is category expansion. Although this remains an area of interest for manufacturers and retailers, understanding the expansion drivers continues to be a challenge in academic research. Prior studies have suggested that categories grow through manufacturer or industry-specific factors (Putsis Jr, 1998) under manufacturers’ control or influence; or through macroeconomic factors beyond manufacture control or influence (Storey, 2003). However, it has failed to consider these factors in tandem, or to use standardized measures to benchmark category performance (Dhar et al., 2000). Thus our aim is first to identify the factors a manufacturer can influence, and then investigate which are most commonly associated with category sales dynamics, through many observations under the differentiated conditions of country, size, type, market maturity and time.

Factors linked to category performance have been identified asproduct assortment, shelf-space assignments, price promotion, pricing decisions ,(Soberman and Gatignon, 2005) and innovation strategy (Chimhundu et al., 2010, Quelch and Kenny, 1994). We now review notable studies which looked at one or two above factors in relation to category expansion. Nijs *et al.* (2001) conducted a large-scale study of marketing mix interventions in Dutch supermarkets. They concluded that the category expansion effect of price promotions was virtually nil, but demonstrated that introducing new products successfully resulted in permanent category demand increases. Vertical line extensions do not however expand category demand (Quelch and Kenny, 1994), but as Soberman & Gatignon (2005) suggest, horizontal product innovation can lead to market expansion by drawing new buyers from other categories, or by trading up existing buyers. These innovations provide additional benefits, for which consumers may be prepared to pay more - premiumisation. The most elegant may also encourage more frequent purchase, for example by reducing pack size.

In summary, the literature has broadly linked three possible factors in manufacturers’ control to category sales growth: (1) The level of discounting; (2) Average price per volume; (3) Assortment, including an innovation factor: more SKUs should lead to category expansion if they include horizontal extensions. Considering the conditions of country, category type and market maturity we asked: *which factors in manufacturer control are most associated with category expansion in dollar sales?*

**Method**

To address this, the study examined scanner data from the US, Germany, France and the UK, extracting quarterly data for over 20 categories and numerous sub-categories, spanning 4-8 years. The variables collected were: % of category on promotion in any given quarter; # of SKUs; # of *new* SKUs; average price/volume. We classified categories as mature (50+% quarterly penetration) or non-mature. Our analysis then involved two steps. First we compared a quarter in one year with the corresponding quarter in a subsequent year to see how changes in dollar sales were related to change in pricing; promotion; and the number of SKUs, thus adjusting for seasonality. In the second step, we deconstructed category value sales into volume and price changes, and the relationship between SKU and category growth.

**Results & Discussion**

We find that, across four countries and 20 categories, price per volume has the most consistent positive correlation with category value sales (*r* =0.28). This is followed by the number of SKU’s (*r* =0.19). The change in the intensity of price promotions has on average no association with change in category sales (*r* =0.04). The results were generally consistent across all markets, but strongest in the US, with correlation between changes in price per volume and category sales being 0.48. In Germany, the number SKUs had the highest positive relationship with changes in category sales, follow by changes in price.

Table 1: Summary of correlations between changes in quarterly category sales and change factors.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **Avg. price/ vol** | **% sold deal** | **# SKUs** | **Mkt Growth** |
| Germany | 0.15 | 0.02 | 0.33 | 1 |
| France | 0.20 | 0.11 | 0 | 6 |
| UK | 0.34 | 0.11 | 0.15 | 6 |
| US | 0.42 | -0.1 | 0.28 | 2 |
| **Average** | **0.28** | **0.04** | **0.19** | **4** |

Next, we deconstructed the category growth into volume and price growth for categories at different levels of maturity. We find that for less mature categories, growth comes mainly from increases in volume, aided by price increases and more SKUs launched. In more mature categories, growth relies on getting prices up, with volume being relatively stable. Finally, we find that in mature sub-categories new SKUs are introduced at a price on average 30% higher than the existing SKUs. This is only 10% higher for non-mature categories, implying that new SKUs are being used to increase category value and grow category sales.

**Implications for Theory & Practice**

Our findings provide important implications for companies wanting to grow within their portfolios of categories and brands. Our main finding is that category growth strategy depends on category maturity. In more mature categories, the main growth strategy is premiumisation. Premiumisation occurs more frequently, diffuses more quickly and achieves higher price premiums from highly commoditised mature categories because it more easily gains the support of retailers and manufacturers {REF}. In less mature categories, growth comes from more buyers buying more often, which is reflected in increases in volume. In such categories, the focus should be on capturing as many new category buyers as possible and building the category within individual shopper’s repertoires. In more mature categories, the focus should be on getting category prices up. Our research suggests that new SKUS are a way to do this, with new SKUs in mature categories being able to demand on average 30% higher prices.

The research has several limitations, which give direction for future study. First, we have considered only a limited number of categories and countries, all developed markets. In order to strengthen empirical generalisations the research should be extended to a higher number of conditions, including emerging markets. We also consider only a limited number of factors. Future research should identify and consider more factors, for example the level of category advertising, which could lead to category expansion.

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