# Defeating commoditization

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## Just another pretty face

My client's face was stuck somewhere between horror, disbelief, and anger after I said "Over time, all products become commodities, including yours." Then again, most people take bad news poorly.

However, this is a basic fact of life in all industries: left to the competitive strains of a free market, all products will be reduced to a commodity over time. In high tech, it simply happens much more quickly. And in the case of Open Source software, the industry started as a commodity industry and had to find ways of breaking their "for free" image.

Given that commoditization is as inevitable as death and higher taxes, you need to review your strategies on how to deal with this transition . . . without resorting to denial, anger, bargaining, depression and acceptance. Below are a few strategies, and one reversible non-strategy that you can choose from.

## Incremental enhancements

In high tech, the classic response to commoditization is to create small differentiating features in products. This is often called "adding +1 features." Doing so allows a company to avoid dropping prices to attract new business, and adding functionality that in some small way attracts customers or converts.

An ongoing example of this strategy can be found in the Windows personal computer market, where the standard entry-level box sells for $350 and has almost 100 times the horsepower of the navigation computers on the Space Shuttle.

This is a good strategy for high volume markets that are expected to last indefinitely. But it leads to a constant escalation of features, and an equally constant downward pressure on prices and profits.

The oddest thing to happen in high tech has been Linux, which started life as a commodity product. Each commercial distribution grabbed every piece of Open Source software, dumping it onto the CD as a way of creating more value for an inherently commodity product.

## Bundle your cow

Some products, especially software, simply work better with other products. When a product can not usefully be enhanced with more features, or doing so would take too long or cost too much, bundling it with compatible products can create point-of-purchase differentiation.


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This strategy is often adopted in the early stages of commoditization by software vendors, who toss in demo versions of every remotely compatible product on their "strategic partner" list. Often this "shovel-ware" becomes little more than land fill fodder, but it does sway buyers during that vital last moment of comparison shopping.

## Brand your cow

The trickiest strategy, but the best for long term profitability, is to brand you way to success. People – even IT executives who are rumored to be people themselves – have brand preferences. In a market where there is no discernable difference between two products, brand preference will determine which is bought.

There are two problems with this strategy. First, few marketing professionals in high technology really know how to create brand differentiation. They still think that only features sell products. Thus, they are not mentally prepared to find non-technical motivations for creating buying preference.

The second problem is that branding is not a cheap or fast process, and when commoditization happens, most executives are looking for fast solutions that can be done with less budget because the product line is suddenly not as profitable as it once was. If your market is expected to be long lived, you need to create a better brand to keep from becoming unprofitable.

## Cash your cow

One overlooked option is to not do much of anything – to milk your cash cow for everything it is worth while planning your next product or exit strategy. Computer Associates has made a handsome living from buying orphaned technologies, doing little or nothing to improve them, then charging steep maintenance fees while their acquired customers engineered their way out of vendor lock-in.

This strategy is a two-edged sword. The up-side is that it is simple, cheap, and profitable. Hewlett Packard did this with their obsolete HP3000 line for years before announcing they were killing it off (my guess is that in the late stages, it became unprofitable to even maintain the HP3000).

The down side of this strategy is that it leaves a bad taste in the customer's mouth and damages corporate branding. If your long-term goal is to keep and grow your company, then you have to weigh this option carefully, and manage the fall-out if your cash cow gores your customers.

## Morph the core

Some commodity technology products have a central core that is the foundation of the product. On rare occasions, that core technology can be used for a related, or even a completely different product. 3am Labs is an interesting example as they leveraged their core remote PC management technology to create a tool to allow road warriors to use their office-bound PCs while they were away from the office.

Morphing the core has two distinct advantages. The first is that the cost for developing the new


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product goes way down as you have a mature and paid-for foundation on which to build. The second benefit is that you can often find synergies between the old and new products, and even sell the new product to old customers.

One huge downside, however, is technology myopia – a situation whereby your company and your engineers quit looking beyond their safe and familiar point of expertise. The long term effect of this is not too removed from a hermitage – an eventual isolation and stagnation that either causes premature corporate death, or at least the desire for it.

## Just move on

Walking away from a product or a market should be like ending a romantic relationship: bitter-sweet with fond memories, and an active, earnest hunt for your next lover.

There can come a time when the best thing for a company to do is to kill its product and build the next one. When an old product has become a commodity, when the competitors have built a better brand, when price cutting and discounts become the norm . . . in short, when you're in a bad market . . . it may be time to reinvent yourself. This won't be easy or cheap, but it may be your only choice.

## And, a reverse non-strategy – cutting prices

There is one so-called strategy that too many firms employ to their own self destruction – cutting prices. With technology companies, this usually starts innocently enough with deeper than average discounts to "important customers." But it soon becomes the norm with sales and marketing forming a death pact over price cutting to "shut out" the competition. This process accelerates as the primary competitors do the same, and all participating companies spiral down into the abyss.

But if you see this happening, watch the market carefully. There is always one company that either refuses to cut prices or always comes in a few dollars above the competitors. This is a sign of a company that understands the inevitable end of a price war and chooses not to play the game. They will accept temporary lean times, and even spend more on branding and marketing during a price war to create a sense of superior value. These are companies that read Sun Tzu's *Art of War* and took seriously the passage "If you stand by the river long enough, you will see the bodies of your enemies float by."

In this case, the smart marketer will use price cutting as a weapon, not by cutting their prices, but by encouraging their competitors to cut theirs. If you can convince your opponent to commit suicide, then you win the battle. In a commodity market, simply staying alive can be a winning strategy.


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