MARKETING STRATEGIES IN RECESSIONARY TIMES

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ABSTRACT

Demand for consumer as well as business products keeps falling during recessions, yet, many businesses cut marketing spending, further exacerbating the blow. Recessions repeat, yet, many businesses respond on an ad hoc basis to respond to shrinking sales and profitability during these times. In this paper, we survey the literature and provide a conceptual framework to outline a systematic strategy for tackling recessions. We introduce a concept of "consumer value migration" from premium to value brands as a result of recession. Thus, we recommend adjusting the marketing mix to respond to value migration, and focus on innovation and sustainability, instead of diminishing marketing spending.

INTRODUCTION

Recessions are not new. A review of historical trend of national income suggests a pattern of recessions and recoveries. Despite having past experiences of recessions, a majority of businesses and marketers seem to be struck unprepared or underprepared by the current recession that started in 2007-2008. Lack of recession-preparedness is clear from reports of cutting marketing budgets during recession when, in fact, experts suggest maintaining or even increasing them. [19] reports that nearly 60% of marketers cut marketing spending during the current recession that was allegedly triggered by a burst in housing bubble in 2007 and further exacerbated by a gripping financial crisis of 2008 [2]. Although the timing and duration of these cyclical movements of economic activities is difficult to predict, it is important to ask what the optimal marketing strategy should be when businesses are faced with recessionary cycles. It is common to observe firms to curtail, to their own peril, marketing spending during economic contraction [14]. Considering how recurrent recessions are, academic research on proper marketing strategies in recessions is surprisingly scant in literature. Most of the published literature on recession addresses business strategies in general, without formalizing how marketing frameworks be adapted to address the chaos and shocks engendered by economic downturns (for example, see [9], [25], and [10]). A major theme of these studies run along the question of whether firms should increase or decrease marketing spending [18], advertising [11], and R&D [29] and suggest that cutting spending in downturns is a counter-productive exercise. These studies also suggest that while spending is a visible and important part of strategy, a comprehensive response to recession should involve other areas of marketing mix, such as product design, pricing, and promotion strategies. Furthermore, any specific prescription to alter marketing mix during recession should derive from theoretical or at minimum, conceptual framework. This research surveys the extant literature on recession and attempts to provide a conceptual guideline for deriving strategies to fight economic recession and prepare for recoveries that always follow recessions.

The primary impact of recession that concerns marketers are changes in consumer behavior and the corresponding change they dictate on business strategy. Economic downturns forces profound and often long lasting changes in consumer behavior to which very few firms act in a proactive manner. First, consumers shun luxury brands and sometimes luxury products altogether, and favor value brand during recessions [24]. Market shares of private label consumer goods gain during economic downturns and the

same diminishes during years of prosperity [17], [23]. Second, news of rising unemployment and falling incomes create economic uncertainties and loss of consumer confidence even among consumers who are not directly affected by the recession [8]. Loss of consumer confidence leads to belt tightening in consumer spending, further exacerbating the marketability of various consumer and business products. Another related effect on consumer psychology caused by recession is consumer anxiety that could lead to consumer animosity to brands [12] resulting in aversions to buy branded products. Third, consumers also tend to hold on to their durable goods longer. For example, the average age of cars in the United States grew from about 8 years in the 1990s to over 11 years in the late 2000s [22].

Most businesses resort to desperate and last minute strategies in order to adapt to new realities. Although there are some signs of economic recovery, advertising spending is falling, following cuts in 2008 and 2009 (Advertising Age, August 10, 2009). That will be the first time since great depression that advertising spending has declined for three straight years. With some exceptions, the first reaction by many businesses to a recessionary sales decline is to cut or suspend marketing spending altogether. This raises a pressing question: why do marketers cut spending during recession?

The immediate answer is the obvious one: because they feel the immediate need to defend profitability in the short run [33] and cost-cutting is an easy way to achieve this relatively quickly. With credit market tightening, borrowing is simply not an option for many firms. However, lack of funds simply fails to answer why marketing becomes the first to go on the chopping block when times are tough. At a fundamental level, two things are at work here. First, many businesses fail to prepare adequately for business cycles and perhaps underestimate the duration or severity of recessions. However, the current recession proved that assumption of quick recovery wrong, as the downturn still drags on, even though the recession officially ended as defined by two consecutive quarters of negative growth in the real Gross Domestic Product (GDP) [27]. However, a new definition of recession identifies it as significant declines in real GDP, spread across the economy, and lasting for a few months [20]. Given that none of us have the crystal ball and economists won't call a bottom until well after the recession ended (for example, the National Bureau of Economic Research declared in July 2003 that the previous recession ended in November 2001—a lag time of 19 months!). Second, marketers themselves have to share a large part of the blame for not being the priority in the organization. Showing the value of marketing in terms of return on investment is the key. Although businesses should re-evaluate their entire business models during recessionary periods, including operations, human resources, purchasing, and marketing, this paper focuses on the marketing strategies that can minimize the impact and make the most of a recessionary period.

LITERATURE REVIEW

Surprisingly, very little is written on recession's impact on consumer behavior or marketing mix in the mainstream academic marketing literature. One of the early articles on recession in marketing literature notes conspicuous absence of studies relating business cycles and marketing [5]. The scarcity of research continued through most of the past recessions since the 1970s, and only during the last recession of 2007, we are observing attention from researchers to this important phenomenon. Nevertheless, the discussion of recession and marketing relationship is rather more common in popular business press and practitioner oriented outlets than academic journals. Many past studies document the impact of recession on various aspects of consumer behavior. [3] outlined some general changes in consumer behavior that is attributed to the ongoing recession. They report that 18% of consumers of packaged goods bought store brand or other value oriented brands in the past two years and a majority of

these consumers report positive experience with their purchases after switching to lower priced products [3, p. 1]. [17] found that sales of private labels gain over brands are pro-cyclical, i.e. private label gains in recession while some gains are claimed to be permanent. [14] identifies three broader trends in consumer behavior during recession. First, they tend to flock to cheaper brands of substitutes for consumer goods. Second, consumers are likely to postpone purchases of consumer durables such as automobiles, household appliances, and furniture. Third, a cut back in shopping trips and increased reliance on meals prepared at home and free entertainment from Internet [14, p. 188]. On a more theoretical level, [12] articulates the concept of consumer animosity, caused by economic hardships, that negatively affects purchase intention. Consumer confidence is also claimed to play a strong role in influencing consumers purchase intention [16], especially in consumer durable goods. However, this relationship is moderated by in-store promotion, particularly for frequently purchased consumer goods some of which are purchased on impulses.

The effect of recession is better documented in the advertising literature. Most studies reported that companies curtail advertising expenditure during recession despite the professionals' recommendation to the contrary [11]. [13] found that companies that increased advertising spending during the 1991 recession generated 25% higher sales growth in the five years period following the recession. [31] conducted a comprehensive study of 41 studies on the sensitivity of advertising spending to economic cycles and found that in multiple countries advertising spending is very elastic to changes in Gross Domestic Product (GDP). For example, a one percent change in GDP is associated with 1.4 percent change in advertising expenses. The implication is that advertising spending overshoots economic cycles which exacerbate the negative impact of recession. The results are mixed for other types of expenditures. [18] report that while R&D spending increase during recession pays off in terms of profits and stock returns, advertising actually fails to produce such results, especially in business-to-business goods and services firms. It is not clear if the direction of results will hold for business to consumer firms. [25] identified marketing pro-activity, i.e. acceptance of recessions by firms as opportunities, is amply rewarded both during and after recessions. The foregoing discussion suggests than there is no single best strategy that will fit well with all firms in all industries and that more research is needed to establish the various caveats of a given strategy.

CONCEPTUAL FRAMEWORK

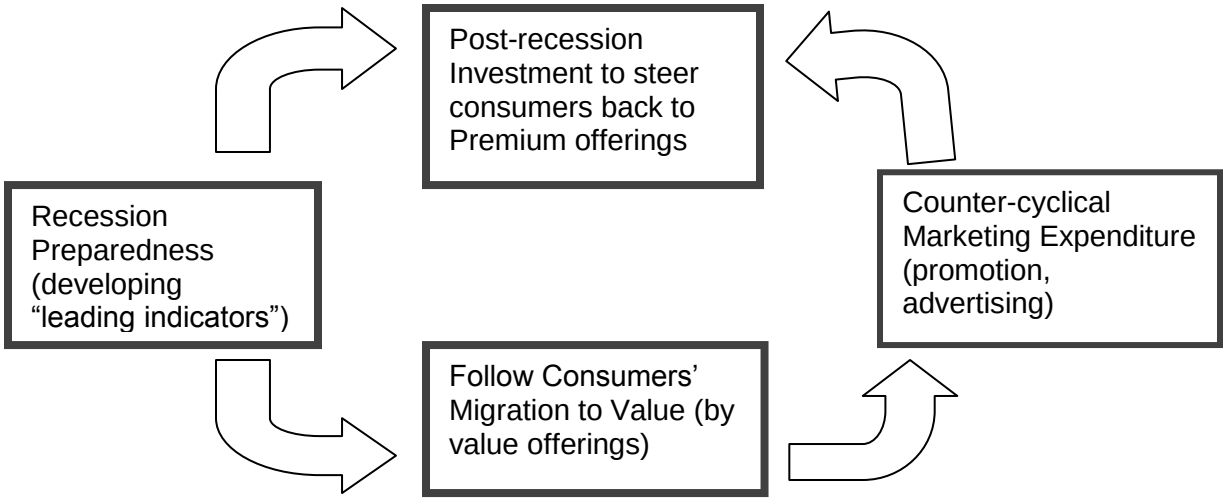
The main mechanism through which a recession impacts consumer and household buying decision is the wealth effect [4] which indicates how much consumption spending is reduced (increased) as a result of a decrease (increase) in asset value. Asset value incorporates a more comprehensive measure of buying power, compared to just personal disposable income. For instance, appreciation in the value of real estate, equities, and other assets might induce consumers to spend more whereas the converse is true for a decrease in asset value. Furthermore, consumers' desire for value is heightened during recession as they are forced to do more with less [6]. It is best to view the consumer behavior during recession as a set of migrations. Consumers may curtail expenses on some types of products, but many products enjoy thriving sales during recessions. For example, faced with tighter budgets, consumers spend on electronic gadgets and get entertainment at home instead of going out [32]. Consumers also migrate to different distribution channels. Specifically, discount stores gain customers while premium stores lose clientele. Figure 1 shows that the stock price of Dollar General, a discount retail store, outperformed that of Wal-Mart by a factor of 5 over the period 2009 to 2011. Purchases of durable goods such as automobiles may suffer in recession but consumers can't avoid maintenance of such products. Thus, during recessionary times, the value migrates from products to services. As a matter of fact, report shows that average age of cars in the US is on the rise for the last several years [22].

Figure 1: Stock Price of Dollar General Stores Outperformed that of Wal-Mart (2009-2012)

Recession Preparedness

Perhaps the best defense against bad times is to minimize the surprise element. The textbook definition of a recession is falling Gross Domestic Product for two or more consecutive quarters. That makes it hard to even detect one that lasts for 10 months or less. The National Bureau of Economic Research (NBER) looks at more indicators other than just the GDP such as unemployment and industrial production index. As mentioned before, even NBER does not identify a recession until well after it happened. So where does that leave ordinary businesses? Well, they should not despair. As a matter of fact, businesses should be able to anticipate recession sooner than the economists who work with secondary data that are typically pretty outdated. It should not be too difficult to observe leading indicators of sales, such as advance reservations in airlines, as a tool to predict economic downturns. If businesses know their sales trend pretty well, any aberration should raise a flag. Sometimes the economy may be fine, but industries within the economy go through dramatic changes. For example, the dot.com burst of the late 90s pretty much left the other sector unscathed.

Figure 2: Conceptual Framework for Marketing Strategies during and After a Recession.



Mean Reversion

How to spot a trouble brewing in your business? There is a simple concept called "mean reversion" which states that any trend has a really long term fundamental trend. Persistent deviation from this trend is unsustainable. There are some problems with the mean reversion principle to be used as a practical tool. For example, it may not tell you the exact time when action is needed if data deviates from the long term trend. Further, how "long" is the long time can be left to interpretation? Nevertheless, the mean reversion and frequent comparison to a long term (usually 15 to 30 years) can provide strategic directions.

Following Consumers Migration to Value during Recessions

Recessions not only cause loss of income but also anxiety and consumer animosity [12] on the part of consumers who are not directly affected by recession. When times are sour, even the most loyal customer will tend to defect with the drop of a hat. The key here is to remind value in staying with you (your brand, company). If necessary, modify products that will add value and make comparison shopping difficult. Product differentiation is more important than ever. Resist the temptation of cutting price first without cutting costs—cutting price may hurt the brand image. Abercrombie and Fitch has been resisting price cuts so far in a brutal retail market since WW II. What you need to do is focus on your profitable customers first and provide value by either product modifications or improved customer service or both.

Counter-cyclical Marketing Spending

A recession should be viewed as an opportunity to build market share against weak competitors, invest to reap benefits from recovery approaching ahead, and improve marketing efficiency [21], [25]. History offers many examples of success stories from contrarian practice of boosting marketing spending during recession. In the 1920s, Post cereal tightened budgets during the great depression, whereas Kellogg doubled advertising and introduced Rice Krispies, a value product. Within a decade, Kellogg became the dominant firm in the category and experienced a 30% profit growth [30].

Competitive Advantage

Recessions provide excellent opportunities to steal market share from competitors who are hurting more than you are. Prior research has advocated expanding sales force [7], [15], and [21] in order to gain market share. Investing in marketing communications will help gain share of voice (SOV) first, which in turn will lead to increased share of market (SOM). Advertising can move to the Web or more targeted source, instead of TV or mass targeted media. You can also use current customers as marketers. Vonage internet telephony runs a promotion that pays your when you refer a friend who signs up. You may even take advantage of the situation to acquire a competitor.

Innovation and Sustainability

Necessity is the mother of invention. If recession in tough on businesses, it should provide a motivation for figuring out ways that you would not have thought about when times are good [1]. That seldom is the case. Marketers should spend more time thinking outside the box. Innovation during recessionary times is motivated by the new paradigm of sustainability in marketing in the sense of "Mindful Consumption" [26]. For instance, while consumers are using their durable goods longer, a lot of consumers are also engaged in sharing their durable products, such as sharing automobiles [26, p. 31]. Starbucks hold monthly open forums meetings with employees to figure out new ways of doing business. Great companies do this as a routine practice, but employees usually have more times during downturn. Thus, getting them involved more during recession can pay huge dividends later.

CONCLUSION

A review of extant literature shows that the widespread recommendation from academics and practitioners is to maintain or increase marketing spending during recession. They advise so based on the observation that recessions provide opportunities to gain new customers, prepare for a rebound in economic activity, and they help focus on the marketing efficiencies of existing programs. Despite its ferocity, this recession will be over before long. With smart marketing strategies, businesses can survive the recession with stride and get ready for the rebound. Each recession is different because they occur in different times when the underlying circumstances are different. Not everything is negative in this recession. Today, people are smarter, have more technology at their disposal and prices of many technologies are falling. It is also highly recommended to think about how falling prices in a seemingly unrelated industry can help you boost sales. For example, prices of solar photo voltaic panels are falling. Retailers may go solar and reduce energy costs. Environmentally conscious shoppers may patronize outfits with solar installations. There is no better time to be innovative than when you are in a recession.

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