The Momentum Effect

CEOs dream of delivering efficient and sustainable growth – growth that would put serious distance between them and their competitors. Unfortunately, the way most large corporations generate growth is so expensive and inefficient that for most firms, meaningful, market-beating growth has remained just that – a dream. Until now.

Jean-Claude Larréché, the Alfred H. Heineken Chaired Professor of Marketing at INSEAD, spoke with *INSEAD Knowledge* and shared the results of his ten-year research project into what he calls “The Momentum Effect” a phenomenon that can lead to efficient self-sustaining growth.

His three-pronged approach combines empirical analysis of the performance of Fortune 1000 firms over a twenty-year period, clinical research into more than 150 companies to identify the key drivers of growth, and computerised simulations to test the impact of small improvements in those key drivers. All of which converge on the concept of momentum.

“All of our research showed that when certain conditions were in place, some firms delivered dramatically superior growth using relatively fewer resources,” Larréché says. “We use the word ‘momentum’ to describe the way that some products don’t need to be pushed as hard as others and yet still deliver superior results because they have a momentum of their own."

Larréché and his team studied the advertising-to-sales ratios of Fortune 1000 firms over a twenty-year period (1995-2004) and tracked whether changes in those ratios had any impact on revenues, profits and market capitalisation.

On a first reading, the results are counter-intuitive. "We discovered that the companies that delivered the highest growth in market capitalisation – growth which outstripped that of the Dow Jones Index by 80 per cent – were the firms that *decreased* their relative marketing spend over the period. This is exactly the opposite of what most people would expect." In his book Larréché calls these firms the "Pioneers". Despite cutting their relative marketing-to-sales ratio by 7 per cent, compared to their bigger spending competitors, the Pioneers massively outperformed the market.

He is quick to point out that this doesn't show that firms should cut their marketing budget and expect to deliver superior growth. On the contrary. "The Pioneers," he says, "actually increased the amount they spent in absolute terms, but their marketing efficiency was so high that the growth that it produced allowed them to decrease the percentage of their revenues that went to cover the marketing spend."

So why is some marketing spend so much more efficient than others? "Because it is smarter. The reason companies spend so much on marketing is because they are impatient," he says. "It is much faster, and a lot easier, to spend money than to use brains to solve the problems."

At the heart of the momentum effect, he says, is the realisation that "the only form of sustainable efficient growth is customer-based growth." When faced with a growth challenge, Larréché argues, it is essential to take the time to understand the underlying issues, rather than just keep pouring money in to push sales. "Firms first need to divert resources away from downstream marketing (communication and promotion) and turn towards upstream marketing – acquiring customer insights that will lead to superior offerings that generate real customer traction. Once this is done, and the offer is improved, *then* investments can be renewed in downstream marketing to deliver a new momentum for efficient growth."

His book offers an eight-step process for systematically producing customer-based growth through what he calls a "momentum strategy." This, he says, is a strategy that delivers growth "not only in *quantity* – that is to say the firm’s revenues grow faster than those of its competitors – but more importantly in *quality*, by which I mean that it is so efficient that profits as well as revenues increase and so the growth is sustainable.”

He cites Microsoft as a company that had momentum and lost it. Larréché says that from the very start Bill Gates was a “customer-focused leader with great insights into the needs of personal computer users.”

He says Microsoft remains an excellent company with a lot of resources, many good people and products. But he says somewhere along the line, Microsoft turned its focus from customers to products.

“Microsoft is typical of many companies that give so much importance to self-defined product quality andignore customers’ feelings,” he says. “Obviously Microsoft invests a lot in the quality of products, they invest a lot in the tangible part of the offer, but they miss totally the emotional part. It is insights into the emotional drivers of customer behaviour that produce the most powerful offers.”

Compare that with the Wii. Nintendo’s simple but powerful insights into the fun of combining physical movement with relatively simple computer games designed to make those taking part more emotionally engaged – summed up in the line “Wii would like to play” – are behind the powerful momentum the product has enjoyed since its launch.

Larréché relates a story about getting participants at a seminar to play with a Wii as a means of demonstrating the power of insights into human emotions when it comes to designing the sort of offers that produce momentum. “The Wii is a great illustration of many of the elements of the momentum process presented in the book,” he says, “but there are many others. The thing that unites them all is that they produce genuine customer-based growth, the only growth that is both efficient and sustainable.”

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