How companies respond to competitors: A McKinsey Global Survey

Management theory suggests that companies facing serious competitive threats should extensively analyze how to fight back. Actual managers, however, say they are satisfied with the results of a less active approach, according to a McKinsey survey. Companies that understand how their competitors really react may be able to gain an edge.

When a competitor strikes—introducing an innovative new product, for example, or slashing prices—management theory suggests that companies should immediately dive into complex analyses of their possible moves and countermoves across the whole competitive landscape, assess these potential responses with sophisticated financial metrics such as net present value (NPV), and promptly mount a response.

The real world is much simpler, according to a McKinsey survey of executives from around the world and from a variety of sectors, including financial services, manufacturing, and high tech.[1] On the whole, as companies determine how to respond to a competitor's moves, they generally assess three or fewer options and don't look forward more than two years. About half don't examine more than one round of countermoves by any competitor. A significant number rely on intuition to determine a response. And companies most frequently respond with whatever counteraction is most obvious in the moment—answering a price cut, for example, with a cut of their own, which often doesn't hit the market until at least one or two sales cycles after the competitor's move.

Even so, most respondents to the survey say they were able to counteract at least some of the reduction in earnings they expected when they found themselves facing a competitor's price change or innovation. Overall, they say they expected earnings to fall by an average of 7 percent, and only 22 percent of respondents felt they could offset at most 25 percent of the expected decline.[2] In addition, a majority would conduct their analysis the same way—or even less exhaustively—if they faced the same situation again.

Knowing that responses to competitive moves are generally straightforward and relatively slow—and that companies are unlikely to change in this respect—gives managers new ways to think about how they might gain competitive advantage from their own moves.

Monitoring the competitive landscape

This survey asked executives how their companies responded to a specific competitive situation: either a significant price change or a significant innovation. Answers about both were strikingly similar in most cases, as were the answers of executives across regions and industries.

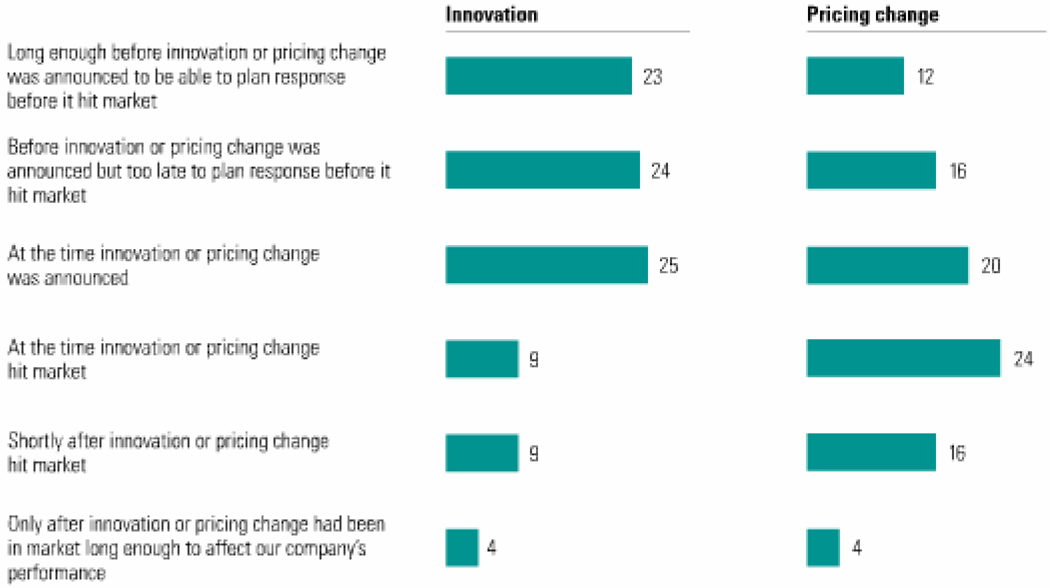
A majority of executives in both groups say their companies found out about the competitive move too late to respond before it hit the market (Exhibit 1). Thirty-four percent of those facing an innovation and 44 percent of those facing a pricing change say they found out about the competitor's move either when it was announced or when it actually hit the market. An additional 20 percent of the respondents facing a pricing change didn't find out until it had been in the marketplace for at least one or two reporting cycles.

EXHIBIT 1

A late response

% of respondents[1]

Relative to when this major competitive move hit the market, when did you learn about it?

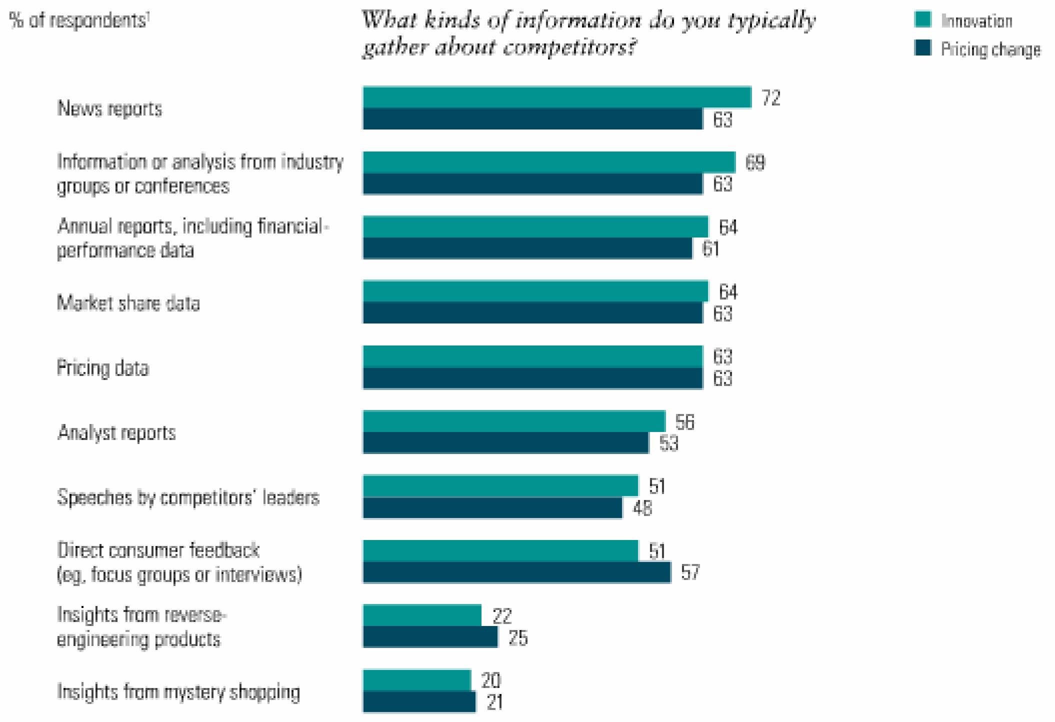


[1]Respondents who answered "don't know" are not shown.

These findings suggest that companies aren't conducting an ongoing, sophisticated analysis of their competitors' potential actions. That view is supported by the executives' responses to questions on how they gather information about what competitors might do. Executives most often say they track information from news reports, industry groups, annual reports, market share data, and pricing data (Exhibit 2). Far fewer respondents obtain information from more complex sources, such as the reverse engineering of products or mystery shopping.

EXHIBIT 2

Tracking competitors

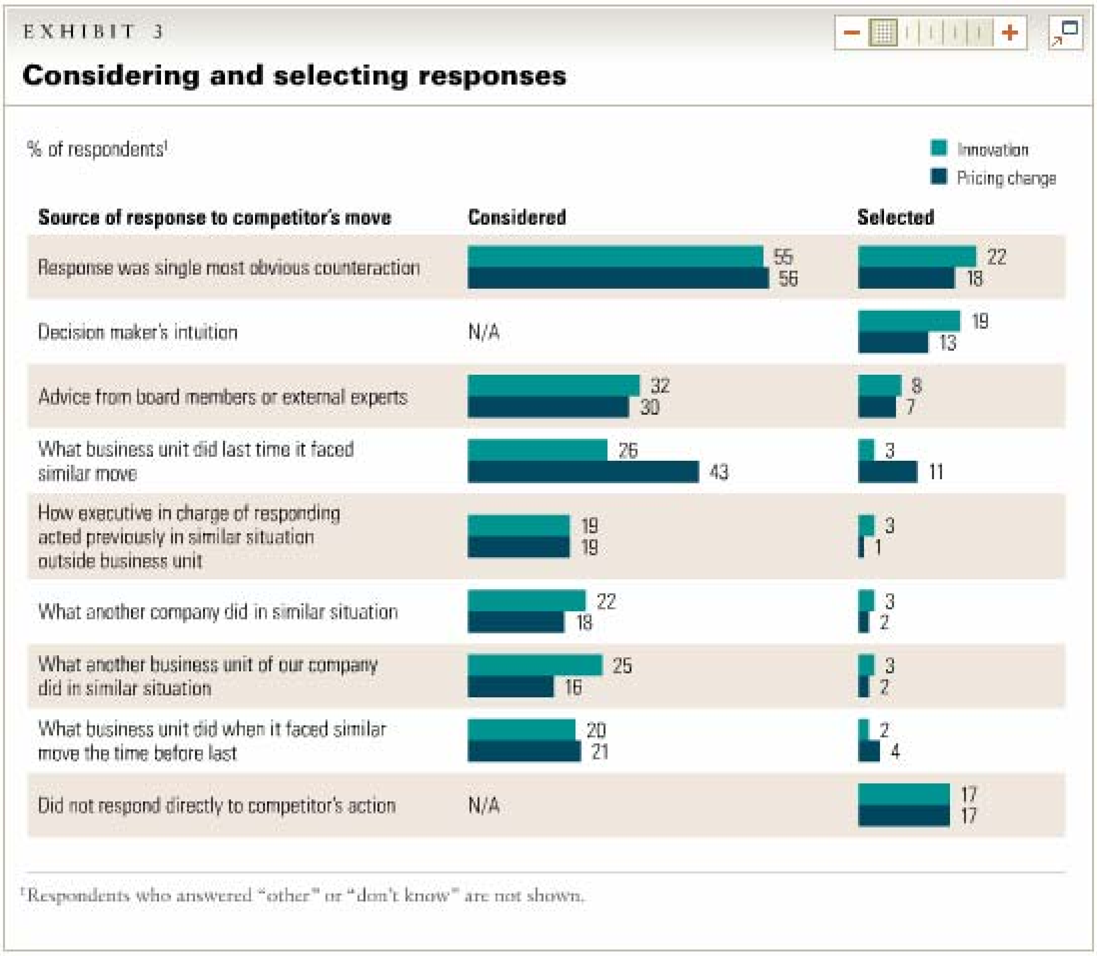


[1]Respondents could select more than 1 answer; those who answered "other," "no typical kind of information," or "don't know" are not shown.

Yet the threat is real. Respondents say the competitive move they were answering questions about had the potential to cause a noticeable reduction in their annual earnings—an average of 7 percent. Among those who answered the questions about innovation, 50 percent say they expected a drop of 6 percent or more, and 9 percent a drop of 21 percent or more. Among respondents facing a price change, 45 percent expected a drop of 6 percent or more, and 6 percent a drop of 21 percent or more.3

Making the obvious move

Despite the potential for serious earnings drops when a competitor introduces a significant price change or innovation, executives say their companies assess surprisingly few options for responding: half, only one or two, and just 11 percent, five or more.4 The most common option assessed—by more than half of the respondents—is the single most obvious counteraction, such as matching a price change or offering an imitative product (Exhibit 3). Other common sources of ideas are what a company did the last time it faced a similar competitive move and advice from board members or external experts.

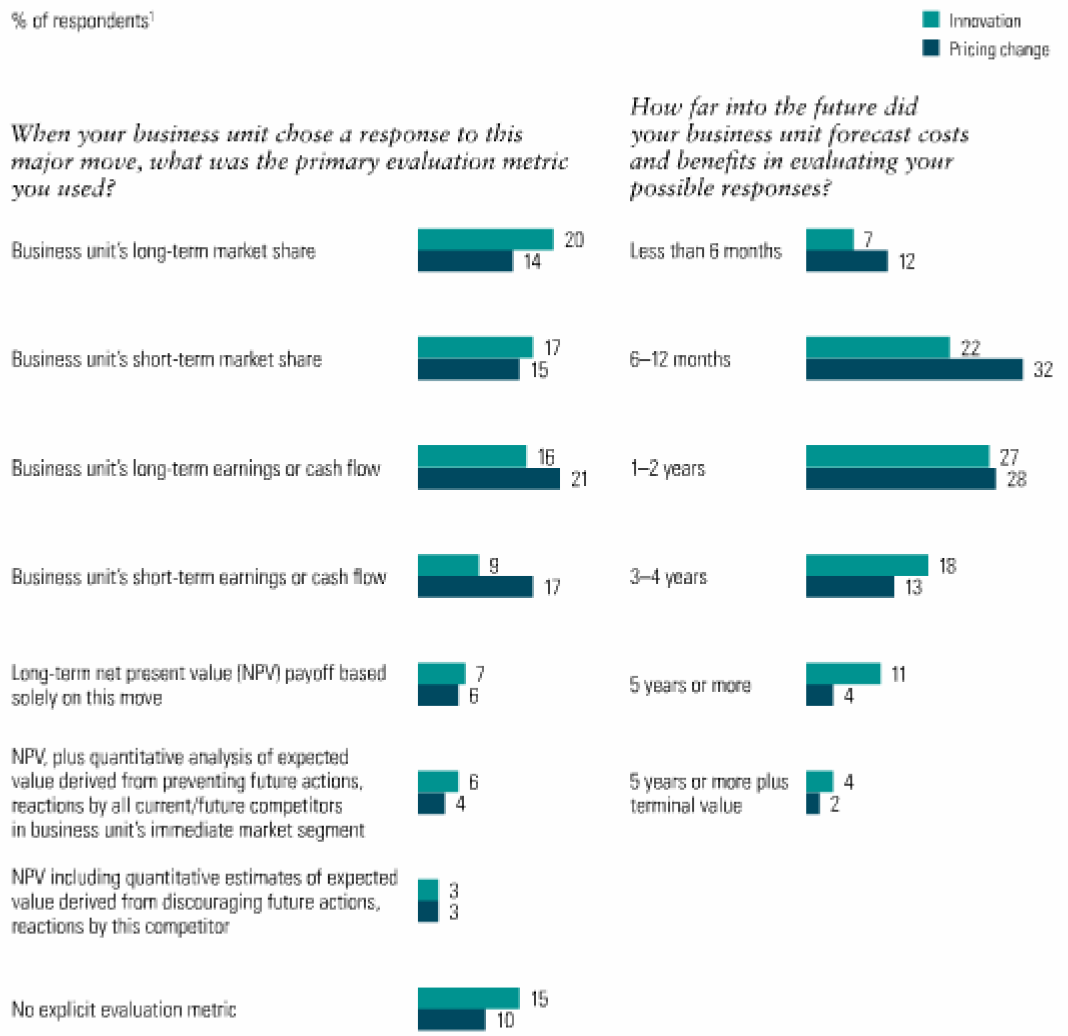


When companies choose a response to a competitor's move, their approach is equally straightforward. The most frequently chosen response comes from the same source as the response most frequently considered: the single most obvious counteraction. For price changes and innovations alike, the other top two responses were making intuition-based decisions and not responding directly at all.

Companies also tend to overlook complex metrics such as NPV when thinking about how to respond in a competitive situation. Instead, they focus on earnings and market share (Exhibit 4). Indeed, they could not rely on NPV over the long term, because most look no more than two years into the future when assessing the potential effects of their response to a competitor's move.

EXHIBIT 4

Evaluating competitive moves

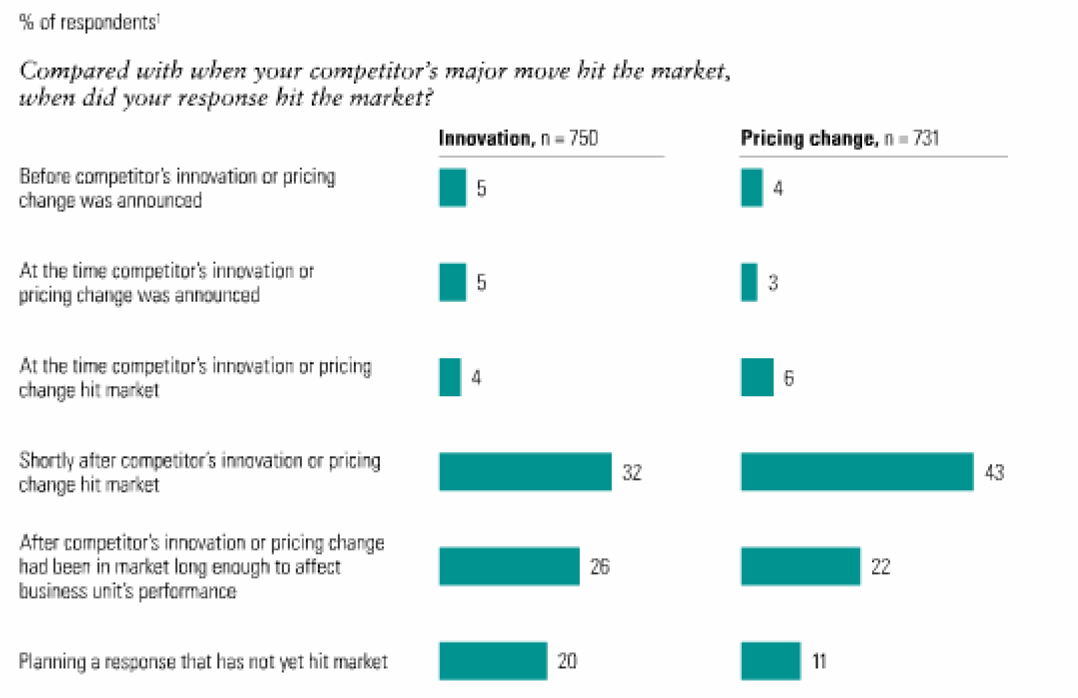


[1]Respondents who answered "other" or "don't know" are not shown.

Although executives usually don't spend time on an exhaustive analysis of the options for responding to a competitor's move, any response tends to be rather slow (Exhibit 5). Indeed, 20 percent of those facing an innovation and 11 percent of those facing a price change say they are still planning a response.5 Companies in the high-tech and telecom sectors are, on the whole, faster to respond.

EXHIBIT 5

Slow response



[1]Respondents who answered "don't know" are not shown; this question was not asked of respondents who selected "We did not respond directly to the competitor's action" in a previous question.

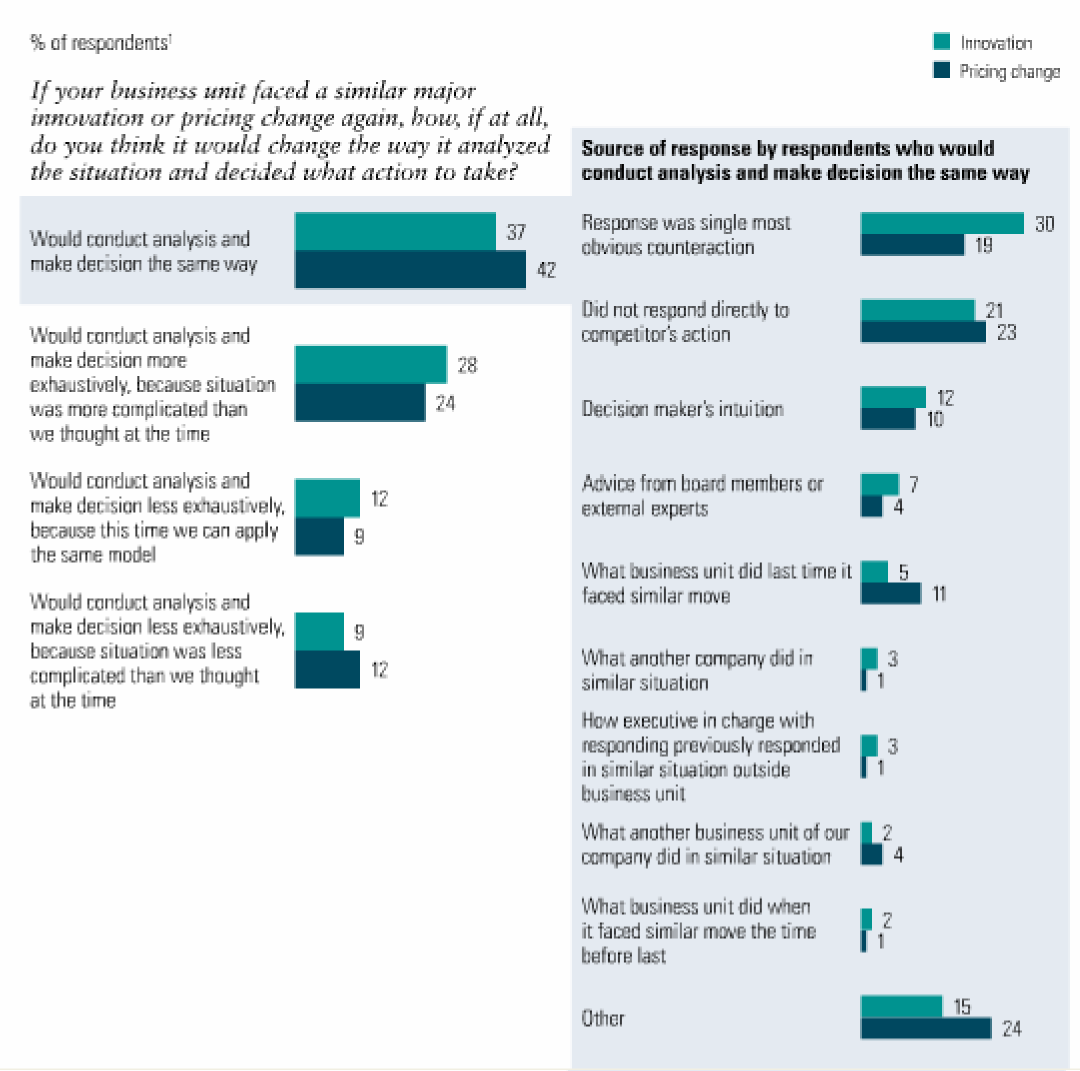
Not changing their ways

Although companies are not pursuing a notably exhaustive or sophisticated competitive analysis, executives indicate that they are pleased, overall, with the results they obtain. First, respondents report, on average, an actual drop in earnings of 5 percent—better than the 7 percent they expected when they learned about the competitive move. In addition, some 15 percent of the respondents who expected earnings to fall by 21 percent or more saw no effect on earnings or even higher earnings. Among those who expected an earnings reduction of 11 to 20 percent, half saw a drop of no more than 10 percent.

Further, around 40 percent of all respondents—and almost half of all the C-level executives—say that if they faced the same situation again, they would conduct their analysis in the same way (Exhibit 6). An additional 20 percent of all executives say they would conduct their analysis less exhaustively, for various reasons. Among executives responding to innovation, those who say they would act in the same way are more likely than others to say either that their response was the obvious counteraction or that they didn't respond; they were a bit less likely to rely on intuition.

EXHIBIT 6

The next time



[1]Respondents who answered "don't know" are not shown.

Management theory says the first concern of companies facing a significant competitive move is to protect their position or to try turning the situation to their advantage. However, only a quarter of executives facing a price change say they intended their responses to deny their competitors any benefit. Only 7 percent say they intended their responses to damage their competitors' earnings—a proportion that rises to 13 percent among respondents from the developed countries of Asia.6 Among executives facing an innovation, only 11 percent say they hoped to deny their competitors any benefit from it. Seven percent report an intention to damage their competitors' earnings; only a negligible number of respondents from the developed countries in Asia gave that response, perhaps indicating that they see themselves as less able to compete on innovation than on price or just that price competition is more acceptable to them. Regardless of the nature of the competitive move, executives in the high-tech and telecom sectors are the likeliest to say that their response to it was intended to damage their competitor's earnings.

Companies that can take into account when their competitors are likely—or unlikely—to react strongly to a competitive move and what the competitors' responses are likely to be can give themselves a competitive advantage as they plan strategy.

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