1.5 Growth and evolution

Tool: Ansoff matrix

As you have learned in Subtopic 1.5 (/study/app/y12-business-management-a-sl-may-2024/sid-352-cid-174703/book/the-big-picture-id-36864), many organisations aim to expand, in a traditional sense, by growing revenues and profits. Most of them are interested in developing rather than staying still and, in doing so, they have many possible options.

The potential avenues for growth were classified by Igor Ansoff, a Russian–American mathematician and business strategist. Ansoff grouped the different options for growth into four categories, based upon combinations of two criteria: products and markets. The four options are often depicted in a matrix like the one in **Figure 1**. This is known as the Ansoff matrix. The matrix can be used with both internal and external growth strategies.

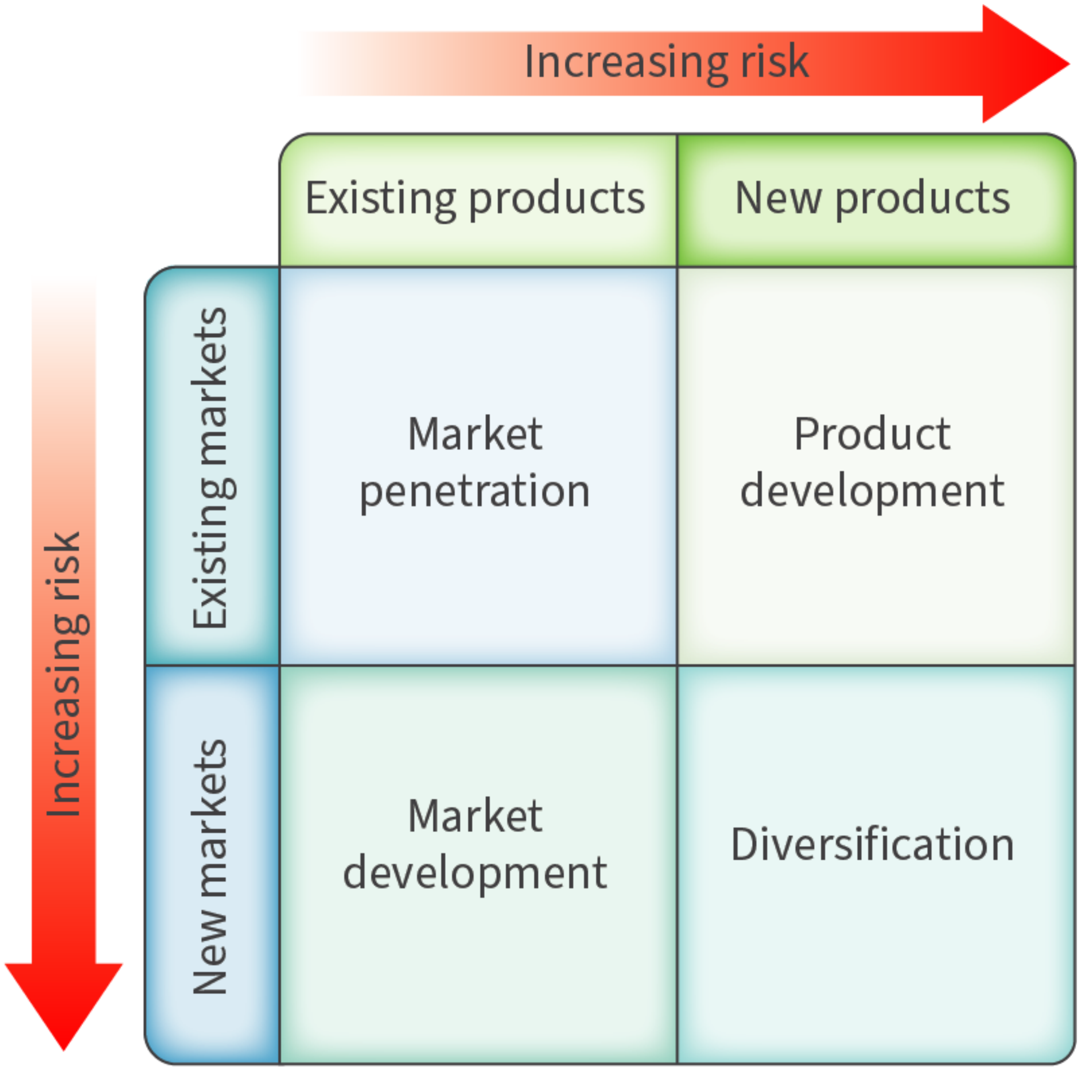

Figure 1. The Ansoff matrix describes potential revenue growth strategies.

Market penetration

The market penetration strategy involves selling more of the same products and services to the same customers, or at least the same types of customers. The market penetration strategy is usually considered the least risky growth strategy as it rarely entails making large investments. In the case of a neighbourhood bakery, for example, market penetration might involve extending hours, changing pricing strategies, or using loyalty cards or other promotion strategies in an attempt to increase sales. However, these strategies may only produce a temporary increase in revenues.

Figure 2. Selling more of the same products to existing customers, for example by lowering prices through a sale, is considered a market penetration strategy.

Credit: JackalPan., Getty Images

In many cases, market penetration does not allow the organisation to grow and develop as fast as it would like. It may be that most potential customers cannot be persuaded to buy more. In the case of bread, for example, a customer purchasing to meet the needs of their family has a limited demand. Or it may be that there are many competitors in the market, so that increasing sales requires winning customers over from other businesses. Many organisations find themselves in circumstances where greater change and risk-taking are required in order to develop. This may involve one of the other three strategies in the Ansoff matrix.

Product development

Product development involves selling new products within the organisation's existing market, often to existing customers. In the example of the bakery, product development might involve selling cakes, sandwiches or beverages to complement the simple baked goods.

Product development usually involves some risk because it requires more investment in time and resources. The bakery will have to experiment with sandwich offerings or various cake recipes to see which ones are popular. Investment in storage and refrigeration equipment may be required. These efforts may distract the owner from the core business of making bread. Efforts to sell new products may fail if managers do not understand customers' needs and expectations.

Figure 3. Selling new products in the same market is considered a product development strategy.

Credit: Luis Alvarez, Getty Images

Market development

Market development involves selling existing products to new customers. In the bakery example, this might involve opening a bakery in a new location and selling the same products in the new shop as the original shop.

Market development is considered riskier than a market penetration strategy. This is because the organisation may not understand the needs of the new customers, so its offerings might not be adapted to the new market.

There are several different types of market development strategies:

- Market development strategies often involve a new geographic market, such as moving to a new neighbourhood, a new town or even a new country.

- Market development can also involve selling the existing product to a new demographic group or target market. For example, Crocs were originally designed for use by boating enthusiasts before they were marketed to a wider range of people.
- Another example of market development is a company that begins selling directly to individual customers and families when the previous model was based on selling only to other businesses. Companies in the personal computer industry grew this way when individuals and families began to purchase computers that had initially been designed for office use.

Figure 4. Selling existing products in a new market is classified as market development.

Credit: Michael H, Getty Images

Exam tip

How to apply the categories in the Ansoff matrix is not as obvious as it might seem. When asked to apply the Ansoff matrix in an exam context, it is therefore important to justify your choice of the classification of different strategies.

It is also helpful to draw the matrix and place the example from the case study in the matrix, as well as to explain it in a paragraph.

Finally, do not forget to consider the risks involved in each strategy as you analyse and evaluate the situation or make recommendations.

Diversification

Finally, diversification involves selling new products in a new market. In the bakery example, this would mean selling new types of baked goods in a new geographic market or to a new target market.

This is considered the riskiest growth strategy, as the business is involved in activities where it may have little knowledge. There is a chance of making costly mistakes.

If the new activity has some similarities with the existing business, it may be considered related diversification. For example, if the baker decides to open a chocolate shop in a new location there may be some similarities to their existing activity. Their expertise in terms of managing a small shop and satisfying customers will be useful in running the new business. If, on the other hand, they decide to sell furniture online, little of their existing expertise will be relevant. This is called unrelated diversification. Therefore, engaging in diversification that is unrelated to the original business is, in most cases, the riskiest growth strategy of all.

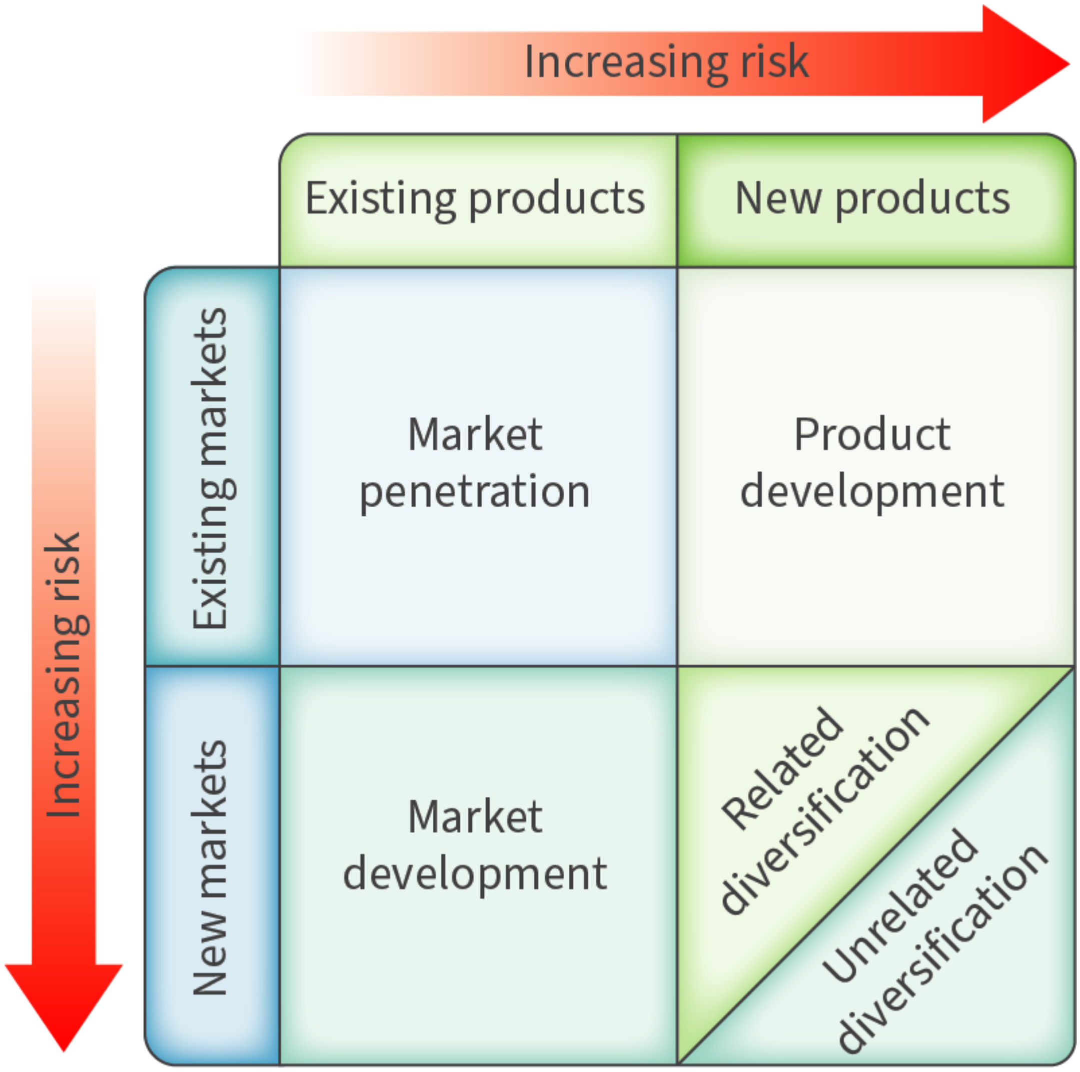

Figure 5. The Ansoff matrix showing the different diversification strategies.

Activity

Learner profile: Knowledgeable
Approaches to learning: Thinking skills (critical thinking, transfer)

Read the following situations and identify how each activity would be positioned in the Ansoff matrix.

	Market penetration	**Product development**	**Market development**	**Diver**
Zara is launching a new line of T-shirts to its current markets.				
Sony is launching a sale with a 5% reduction in price on the PS5.				
Tata Motors is selling its Nexo EV in a new market in South Africa.				

Kog

	Market penetration	Product development	Market development	Diver
Danone is engaging in a joint venture with a dairy company in Mexico, to produce a new line of desserts.				