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Improving Marketing Productivity: The 80/20 Principle Revisited

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A small proportion of an organization's marketing units often generates a large proportion of the profits. This 80/20 situation can lead to decreased marketing productivity and constrained profits if not addressed.

A vice-president of marketing in a large industrial-products firm recently reviewed the profit figures for the just-ended fiscal year. His initial reaction was one of great satisfaction, and for good reason. For the sixth consecutive year, total company profits had surpassed management's objectives. After closer examination of the results, however, the executive's euphoria gave way to a feeling of concern: he noticed that the bulk of the firm's profits was concentrated in a small proportion of the organization's products, customers, and sales personnel. As he reflected on the data, he asked the rhetorical question, "Is this disproportionate contribution from a minority of marketing units a fact of life, or can something be done to alter this situation and generate even greater profits for the firm?"

In the above vignette, the executive's company is experiencing the 80/20 principle. The 80/20 principle describes situations where 80 percent of a firm's profits emanate from 20 percent of its customers, salespeople, or products. Although the percentages will vary depending upon the situation, the essence of the principle is that a very small proportion of a firm's marketing units (salespeople, products, or customers) are in fact "super units" providing a large percentage of company profits, and the remaining marketing units actually add very little to (or may even detract from) the firm's profits.

The existence of an 80/20 condition can indeed constrain profits. The rationale for the preceding statement is that not all marketing

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units provide an equal profit contribution. Despite this situation, it is not unusual for companies to provide relatively comparable marketing resource support (advertising, sales promotion, personal selling efforts) to units having dramatically different profit contributions. Thus, a misallocation of resources occurs whereby potentially stronger marketing units (those capable of providing large profit contributions) do not receive their "fair share" of marketing support, and potentially weaker marketing units (those capable of providing little profit contribution) receive a disproportionately large amount of support. The misallocation can lead to reduced profits as marginal marketing units become profit drains rather than profit contributors and potentially strong marketing units are unable to realize their full potential.

Companies experiencing the 80/20 principle may find it rewarding to alter the ratio in an attempt to increase profits. The reason for such efforts is that the development of more super units will generate a larger profit pie. With an increased emphasis being placed on asset utilization in marketing departments, marketing managers are expected to seek out additional opportunities for productivity enhancement.[1] If the 80/20 principle is ubiquitous and, further, is amenable to change, it constitutes a promising arena for marketing management attention.

The 80/20 principle has long been discussed in the marketing literature,[2] but only a few investigations have examined it empirically.[3] In an attempt to determine the extensiveness of the concept, as well as managers' beliefs about it, the authors performed an exploratory study. Sixty-two industrial product and service marketing managers from throughout the United States were surveyed (see Table 1). Forty-four of the sixty-two firms (71 percent) indicated that a small percentage of their salespeople, products, or customers provides a large percentage of company profits. In addition, the managers did not feel an 80/20 condition is immutable. Ninety-three percent believed an 80/20 situation can be changed in such a way as to improve a firm's profitability. In fact, 65 percent of the respondent companies experiencing an 80/20 condition have taken action to address the imbalance; they tend to use four alternative strategies. The objectives of this article are to: describe the four strategies; present three examples of companies that have successfully altered an 80/20 ratio; provide a managerial framework useful in identifying and addressing an 80/20 condition; and discuss the pitfalls in changing an 80/20 situation.

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Table 1. Demographic Characteristics of Respondent Companies

Annual Company Sales	Companies Responding No.	%
Less than $250 million	19	31
$250 to $500 million	13	21
$501 million to $750 million	2	3
$751 million to $1 billion	4	6
More than $1 billion	24	39
Total	62	100%
Company Salespeople		
Less than 50	28	46
50 to 100	7	12
101 to 150	9	16
151 to 200	5	8
More than 200	13	18
Total	62	100%
Customers		
Less than 1,000	19	36
1,001 to 5,000	18	34
5,001 to 10,000	4	7
More than 10,000	12	23
Total[1]	53	100%
Products Sold		
Less than 100	37	65
101 to 200	7	13
201 to 1,000	5	9
More than 1,000	7	13
Total[1]	56	100%

[1] Total does not equal sixty-two because some respondents did not provide the particular demographic information requested

Alternative Strategies

Our investigation of the 80/20 principle has produced four pure strategies for accomplishing a profitable alteration in the ratio: substitution, revitalization, acceleration, and incremental. (Although a firm can employ a combination of the pure strategies, for ease of discussion each of the four strategies will be discussed separately.) A substitution strategy involves replacing the marginal marketing unit with a more promising unit. A revitalization strategy entails improving performance among units that have declined or reached a plateau after performing at a high level. The acceleration strategy is appropriate for units that are relatively new to the organization but in an upward growth mode, units whose progress management is intent on speeding up. The incremental strategy takes the form of adding units that are expected to become high performers.[4]

To increase profitability by altering the 80/20 ratio, a major consid-

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Table 2. Hypothetical Illustrations of Strategies' Impact on Profit Contribution

Marketing Unit	Original Condition: 80/20 Case	Substitution Strategy: 60/20 Case	Revitalization Strategy: 70/20 Case	Incremental Strategy: 60/20 Case	Acceleration Strategy: 70/20 Case
1	$ 420,000	$ 420,000	$ 420,000	$ 420,000	$ 420,000
2	380,000	380,000	380,000	380,000	380,000
3	50,000	50,000	50,000	50,000	50,000
4	40,000	40,000	80,000[3]	40,000	40,000
5	30,000	30,000	80,000[3]	30,000	30,000
6	20,000	20,000	70,000[3]	20,000	20,000
7	20,000	20,000	20,000	20,000	90,000[5]
8	20,000	20,000	20,000	20,000	90,000[5]
9	10,000	300,000[1]	10,000	10,000	10,000
10	10,000	50,000[2]	10,000	10,000	10,000
	$1,000,000	$1,330,000	$1,140,000		$1,140,000
11				300,000[4]	
12				200,000[4]	
13				150,000[4]	
14				100,000[4]	
15				80,000[4]	
				$1,830,000	

[1] Replace marketing unit 9 with a "super unit."

[2] Replace marketing unit 10 with a better performer.

[3] Marketing units 4, 5, and 6 exhibit improved performance due to management efforts to revitalize them.

[4] Marketing units 11 through 15 are added to the original set of marketing units.

[5] Marketing units 7 and 8 exhibit improved performance due to accelerated progress.

eration is the adoption of an analytical mind set. If management is conscious of the opportunity posed by the existence of the 80/20 allocation, it becomes imperative that it think of implementation on a micro as opposed to a macro basis. For example, in the case of the substitution strategy, management must be dedicated to the proposition that in the great majority of instances the selective elimination of a marginal marketing unit affords an opportunity to improve profitability through the addition of a promising unit. Such results, however, cannot be willed or wished. They require serious planning and superior execution. When replacing a salesperson, the recruiting, selection, and training has to be conducted with great care. A "fill-the-slot" attitude will only perpetuate, or possibly even aggravate, the 80/20 condition. Likewise, when a marginal account or product is discontinued, management must be prepared to seize on the opportunity, rather than perceive it as a problem.

In effect, what successful alteration of the 80/20 condition accomplishes is a lesser dependence on the contribution of that 20 percent of the firm's marketing units that are performing in a superior man-

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ner, not through diminished performance from those units, but through improved performance of a portion of the other 80 percent of the marketing units. The result should be the achievement of 70/20, 60/20, or possibly 50/20. Table 2 reveals how the desired results might be secured via employment of each of the four pure strategies. For example, in the case of the substitution strategy, two marginal units were replaced by superior units with the result being an increase of $330,000 in profit contribution and the achievement of a 60/20 ratio. It should be noted that there was no change in the absolute performance registered by the top 20 percent of the units. Similarly, the table depicts the possible impact of the other three strategies on profitability.

Reference should be made to the opportunity for management to simultaneously employ two or more pure strategies within a given 80/20 condition. For example, in a product context, one product could be dropped and replaced by a more promising unit, a relatively new product could be given additional marketing effort in an attempt to accelerate its profitability, a mature product could be subjected to revitalization efforts, and a new product could be added without its being considered a substitute for another product.

A Tale of Three Companies

Three companies that have successfully altered an 80/20 condition are discussed below. These three firms were selected from the sixty-two surveyed because they best demonstrate that a conscientious attempt to change an 80/20 situation can have favorable results.

Company A is an advertising specialties firm. It employs 105 salespeople nationally, has 200,000 accounts, markets a variety of advertising products, and has annual sales of $48 million. Until recently the sales force had not been achieving its projected profit contribution objectives. In an attempt to increase sales-force productivity, management initially examined the performance of each of its personnel. After careful scrutiny of performance data, management opted to use substitution and revitalization strategies to improve its situation. Ten percent of the sales force—the poorest performers—were replaced by more promising individuals (who were then immediately enrolled in an in-house sales training program). In addition, the remaining 90 percent of the sales representatives were put through a refresher sales training course. The end result of Company A's efforts: instead of 80 percent of company profits being generated by only 20 percent of the sales force, 50 percent of the profits are generated by the top 20 percent of the sales force. The overall effect is a much improved profit picture.

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Company B provides insurance for over 6,500 group accounts. It employs approximately one hundred salespeople and has sales of more than $700 million annually. Its twelve product lines are comprised of health, life, disability, and dental insurance accounts—the firm was pondering how to enhance productivity from its product mix. Management utilized an incremental strategy whereby it introduced a new insurance product aimed at the small group-insurance-account market. Three years after product launch, company profits have increased 20 percent, and the historic 80/20 ratio in the product mix has been improved to a 60/20 ratio.

Company C manufactures fabricated steel products. It has over one hundred salespeople, 1,600 products in inventory, and 20,000 accounts. Its annual sales are in excess of $75 million. For several years its sale force had been achieving its overall sales goals, but many of the individual orders were small or unprofitable. To correct this situation, management selected a revitalization strategy. Its strategy was two-fold. First, an educational program was started whereby Company C sales representatives instructed their customers about advantages of buying in large quantitites and about the additional uses of Company C products. And second, quantity discounts were increased substantially to encourage customers to maintain their stock levels and to buy in large quantities. Two-and-one-half years after the implementation of the revitalization strategy, the results are: rather than 80 percent of Company C profits coming from only 20 percent of the customers, 80 percent of the profits come from 50 percent of the customers. The result has been a 30 percent increase in profits.

As is evident from the example above, actions can be taken to profitably alter an 80/20 condition. In the next portion of this article, we provide a framework useful in achieving that end.

Managerial Framework

It is believed that a large majority of organizations experience the 80/20 phenomenon in one or more arenas, including sales personnel, products, and customers. Further, there is reason to believe that the 80/20 condition is amenable to change with the result being enhanced profitability. This situation, combined with the persistent challenge facing management as it attempts to achieve its organizational objectives, strongly suggests that organizations can benefit from a disciplined effort dedicated to uncovering and exploiting opportunities that can alter an 80/20 condition.

An action program can be implemented by any organization interested in improving profitability. The elements of this program are:

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organizational readiness; opportunity candidate inventory; marketing-unit assessment; strategy selection and plan of action; implementation; and evaluation of results. These six steps will now be briefly described.

The first step is organizational readiness. Contrary to our study findings, it has long appeared that too many organizations have adopted a seemingly fatalistic posture concerning the 80/20 condition. They agree it exists, but have little desire to do anything about the situation. Thus, a company intent on improving its profitability should consider not only such traditional approaches as product development, market development, diversification, and market penetration, but also should include an 80/20 alteration as a viable candidate for profit enhancement.

The next step, opportunity candidate inventory, involves the accumulation and display of selected accounting information designed to reveal the existence of the 80/20 condition within product-mix, sales force, and customer categories. An examination is made to determine whether an 80/20 situation exists for product lines or product categories, sales force territories or branch offices, or customer classes.[5] Obtaining the requisite accounting information will require the active cooperation of the accounting department. The inventory should be conducted annually, at a minimum, and focus on profit contribution.[6]

If an 80/20 condition is found within product-mix, sales-force, or customer categories, the next step, marketing-unit assessment, is performed. A marketing-unit assessment entails reviewing each existing product, salesperson, or customer (depending upon which categories are experiencing an 80/20 condition). Each marketing unit within the appropriate category needs to be assessed on two dimensions: current profit performance and profit growth potential. The results should then be displayed within a grid such as that presented in Figure 1. The horizontal dimension represents a continuum concerned with the unit's profit potential, with the vertical dimension portraying the unit's current profit performance. (The strategy recommendations found in the figure will be discussed in the next step of the managerial framework.) Further, it can be noted that the two dimensions are divided into three groups, high, moderate, and low. In the classic 80/20 case, 20 percent of the marketing units will be located in the high-performance sector of the grid. A successful alteration will result in an increase in the proportion of high performing units or the average performance of the remaining 80 percent of the units.

In the placement process, management will be expected to place each unit within the grid. The current profit data should be easy to

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Figure 1. Marketing Assessment Grid and Recommended Strategies

Current Profit Performance	Profit Potential: High	Moderate	Low
High	No change	No change	No change
Moderate	Acceleration (preferred) Revitalization (alternate)	Revitalization (preferred) No change (alternate)	No change
Low	Acceleration	Revitalization (preferred) Substitution (alternate)	Substitution

secure from the accounting department. The potential assessment, however, constitutes a most challenging task for management and should be engaged in with great care since its determination will have a substantial impact on the strategy selection, as will be revealed below.

The next step in the process is that of selecting an appropriate strategy for each marketing unit, followed by determining a specific plan of action for the unit in question. Concerning the strategy selection, the placement of the unit within the grid is of salient importance. Figure 1 suggests the strategies appropriate for units positioned in the various cells. Both preferred and alternate strategies, where relevant, are provided. After all units have been placed in the marketing-assessment grid, management can then select strategies to alter an 80/20 condition.

It should be noted that the incremental strategy is not included in the above market-assessment grid. This strategy constitutes a special case where the firm is embarking on a growth path via market development, product development, market penetration, or some combination of these. The incremental strategy is oriented toward adding nonexisting (new) units. Extreme care needs to be exercised when selecting new units. Only those units having a high potential for profit attainment should be considered.

Following the strategy selection, it will be necessary to formulate a plan of action for each unit. To some extent, batching may be advis-

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able, but care should be taken to avoid too high a degree of commonality in the formulation of the unit plans. The old adage "different strokes for different folks" is something to keep in mind when devising plans. For example, one salesperson's revitalization may take a substantially different form than another's, depending on experience, personality, and territorial considerations.

The implementation of the 80/20 alteration efforts will require a marketing-management perspective given the variety of functions involved, such as recruiting, training, product management, pricing, advertising, inventory control, and shipping. It seems imperative that attempts to alter the 80/20 condition be given a high priority so that top management will ensure that the effort is conducted in a quality manner.

As with all strategic efforts, the results will need to be carefully monitored so as to permit an evaluation of the program's efficacy, control of the effort, and input for needed revisions. Of particular concern should be the recognition of the dynamic quality of the relationship between the appropriate strategy to be applied and the current state of the individual unit vis-à-vis current and potential performance.

Words of Caution

When changing an 80/20 condition, managers must be mindful that such an alteration is not without attendant pitfalls or costs. At least five potential pitfalls can be identified. First, there is an opportunity cost of management time. To alter an 80/20 ratio, management must devote time, energy, and effort. If such efforts do not lead to an improved ratio, management has lost precious time that it may have spent on more successful endeavors.

Second, an attempt at changing an 80/20 ratio runs counter to the notion of management by exception. The thrust of management by exception is dedicated to focusing on a limited number of marketing units, generally problem and superior performers. When trying to alter an 80/20 condition, a subset of the remaining units will also be given special attention. The extra attention will probably necessitate either a reallocation of management time or the adding of more managers. Either result will lead to increased costs. Consequently the resulting cost increase must be compared to the expected incremental revenue to determine whether a change in the 80/20 is warranted.

Third, management may move too expeditiously in hopes of correcting an 80/20 condition in the short run. Such action, however, may only aggravate the situation at the expense of long-run success. For example, product development time may be shortened with the

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result being premature product launch and an increase in the likelihood of product failure. Or a sales-force compensation plan may be changed too rapidly, leading to a negative impact on salespeople's morale and performance.

Fourth, all four strategies (substitution, revitalization, acceleration, and incremental) involve substantial expenditures or investments. Thus, altering an 80/20 ratio can be expensive and may be a problem for a cash-short company.

And fifth, when altering an 80/20 situation, there is a high likelihood that there will be increased discrimination among product, salesperson, or customer units. Some marketing units will likely receive special attention at the expense of others. As a result, some intra-organizational (product managers or sales department personnel) or extra-organizational (customers) members may be alienated and become disaffected by the attempts at altering the 80/20 ratio.

Given these pitfalls, when determining whether to alter an 80/20 situation, management should weigh the benefits of a successful change with the attendant costs of the change.

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4. Although a firm could employ a pure "removal" strategy where marketing units are deleted but not replaced, such action is most likely only a short-run strategy. Therefore, we exclude the removal strategy from our discussion.

5. For an excellent discussion about how to categorize products, salespeople, or customers into various groups so as to perform a profitability analysis, see D. W. Jackson, Jr. and L. L. Ostrom, "Grouping Segments for Profitability Analyses," *MSU Business Topics,* vol. 28 (Spring 1980), pp. 39-44.

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