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Innovation Cloning: The Introduction and Performance of Private Label Innovation Copycats☆

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Abstract

A controversial trend in grocery is the practice by retailers to quickly copy innovative national brands (NBs) launched by manufacturers with their own private label (PL). In a sample of 1,100+ NB pioneers launched in The Netherlands between 2005 and 2009, 11.7% faced a PL copycat by at least one of the seven leading grocery retailers. These copycats obtained an impressive 5.8% category share at the retailer in the year after launch, thereby outperforming the NB pioneers they copy (2.1%) as well as non-copycat PLs launched in the same period (4.4%). Using a two-step selection model, we identify what motivates retailers to copy NB innovations, and what factors drive subsequent copycat performance, thereby taking into account retailers' innovation assortment decisions. As expected, retailers are more likely to copy successful NB innovations, and these copycats indeed perform well in their stores. However, retailers do not only take into account financial considerations. They are especially hesitant to copy heavily promoted NB innovations and those launched by manufacturers with a strong reputation. To enhance copycat performance, retailers should keep prices of the copycat sufficiently below those of the NB pioneer and limit its promotions. Apart from guiding retailers in their copycat decisions, also NB manufacturers can learn from this study how to discourage retailers from imitating their innovations.

Keywords: National brand pioneer; Private label copycat; Innovation; Imitation; Retailing

Introduction

To stay ahead of competition, retailers can offer an innovative assortment that reflects the latest developments in the industry. But developing and introducing a true pioneering innovation that is the *first* product in a given category to offer novel consumer benefits remains an expensive and risky business. Apart from the R&D and marketing costs involved, pioneers also face a high miss-to-hit ratio: between 35% and 45% of products brought to the market fail upon market launch (Cierpicki, Wright, and Sharp 2000). Retailers in particular are further discouraged to engage in own pioneer innovations due to their limited capacity and skills to invest in the broad and diverse set of categories they offer, while the smaller volume generated by private-label (PL) offerings (due to retailer exclusivity) and their very competitive prices leave only small margins on PL innovations to recoup the R&D investments (Steiner 2004). To avoid this, retailers typically wait for national-brand (NB) manufacturers to develop new products and simply decide whether or not to add them to their assortment (Lamey et al. 2018).

But regardless of their adoption decision, retailers may also pursue an imitation strategy and introduce a PL product that contains the innovative feature pioneered by a NB. Kellogg's Special K line of breakfast cereals, for instance, is as famous for its continuous stream of flavor innovations as for its constant battle with retailers copying these new flavors (Culliney 2013). Such an innovation copycat strategy has gained popularity among retailers in the Consumer Packaged Goods (CPG) industry. In this industry, compared to other industries (e.g., the pharmaceutical industry), a low rate of patent and trademark registration is observed by pioneers. Hence, copying innovations (rather than developing them) is an attractive strategy given the lower development costs (because of reverse engineering) and

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more limited risk of product failure. But unlike manufacturers that copy their rivals' innovations to take part in their success, retailers are in a unique position and can also use these PLs strategically to influence NB manufacturers and pressure them into better trade conditions (Steiner 2004). A retailer's role as both a potential distributor of NBs and their innovations, while also offering PL copycats that directly compete with these offerings, makes this case particularly interesting to study.

In the literature, copycats are known as products that resemble visual aspects of mostly leading NBs (e.g., trademark, tradedress, or theme copycats) (Aribarg et al. 2014; Miceli and Pieters 2010; van Horen and Pieters 2012). These studies are primarily concerned with 'trade dress' imitations and the potential harm to -or consumer appreciation of- the imitated brand. However, the present study deals with PL *innovation* copycats in the Dutch CPG industry. Such copycats are introduced by the retailer to mimic the innovative aspect of a NB pioneer, while visual resemblance is not required per se.[1] When a NB pioneer introduces novel consumer benefits over existing offerings in the category on one (or more) of its attributes (e.g., new formulation, new ingredient, new usage, new package design/type,. . .), a PL innovation copycat is defined as a product launched by the retailer that copies this innovative attribute of the NB pioneer introduced earlier on the market.

Even though retailers have a strong incentive to copy innovations, retailers cannot copy -or are not interested in copying- the abundance of innovations launched on the market each year. Instead, they only selectively copy innovations. Kumar and Steenkamp (2007), for instance, state that retailers most regularly imitate innovations that are 'hits'. However, in many instances, retailers decide to copy different NB innovations, suggesting that also other factors drive their imitation behavior. In this study, we aim to address three main research questions: (i) What factors drive or inhibit retailers to copy a certain NB pioneer? (i.e., identifying retailers' underlying motives to copy); (ii) How do these decisions affect subsequent PL copycat performance at the store, if a copy is introduced?; And (iii) how does a retailer's assortment decision with respect to the innovation pioneer change these relations?

To answer these questions, we collected data for 55 CPG categories on all NB innovation pioneers and their PL copycats introduced in the Netherlands between 2005 and 2009, and use a selection model to simultaneously model the retailer's decision to copy the NB innovation, and the subsequent performance of this PL copycat. Our study can guide retailers in their choice what NB innovations to imitate and how to manage them, while it can reduce retailers' risk of having to withdraw a copycat at a later stage.

[1] As such, we also differentiate PL innovation copycats from (illegal) counterfeits which impersonate a brand, and design piracy or 'knockoffs', a situation in which a firm creates a copy of another firm's design and appearance without its logo (Appel, Libai, and Muller 2013; Commuri 2009).

Retailer Motivations to Copy Innovations

Retailers' decision to introduce a PL innovation copycat differs markedly from the launch of an economy, standard, or premium PL tier. The roll-out of these classic PL product lines often encompasses a strategic portfolio decision that involves several categories at the same time (ter Braak, Geyskens, and Dekimpe 2014) while PL copycats target one specific NB in a category. Also, most PLs are introduced as products catering to the price-sensitive segment, but this may be less the case for *innovative* PL copycats where retailers intend to contribute to a distinct (innovative) category and store-quality image (ter Braak, Geyskens, and Dekimpe 2014). These copycats also do not offer anything unique in the category like premium PLs do. Since a PL copycat will incorporate the innovative feature that is pioneered by a NB, it is directly targeted to compete with the NB innovation it copies, and retailers are advised to position it closely to this NB with the same feature(s) (Choi and Coughlan 2006). While there may still be quality differences between both, there is a close match at the horizontal level, creating a fierce lower-priced competitor for the copied NB pioneer. Thus, manufacturers feel especially threatened by a PL copycat of their NB innovations, yet they remain hesitant to act against retailers on which they depend to distribute their offerings and access the consumer market (Collins-Dodd and Zaichkowski 1999). This dual nature of the retailer-manufacturer relationship will be a key factor driving retailers' imitation decisions that will be taken into account in our analysis.

Research Framework

Retailers obviously focus to a considerable extent on the expected economic gains of the PL copycat itself, and, as pointed out by industry experts, when developing new PL products, "*the decision will hinge on the market potential of the private label product in question*" (PlanetRetail 2013, p. 5). But retailers may also introduce innovation copycats (or refrain from doing so) for reasons *other* than their immediate financial rewards. We advance a research framework that includes both *economic* and *other* motives for retailers to introduce (or refrain from introducing) a PL innovation copycat. If considerations other than the direct economic or financial benefits of a PL imitation drive retailers' decisions to launch a PL copycat, the impact on subsequent copycat performance is not straightforward. Hence, we further evaluate the impact of these drivers on copycat performance at the retailer, once introduced. While these factors are expected to directly influence retailers' copycat incentive, their impact may not be independent of the retailer's assortment decision with respect to the original NB pioneer. These relations form the basis of our study and are presented in Fig. 1.

Economic Motives

The likelihood of introducing a new PL depends on the expected outcome following this decision. Higher expected sales *value* (through higher *volumes*, higher *prices*, or both) increases the likelihood that a retailer will introduce an innovation copy-