Market Share as a Performance Measure: A Conceptual Framework

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ABSTRACT
In this article, the author provides an overview of the literature in the market share research and proposes a comprehensive model which can empirically investigate the relationship between market share and profitability. Also, several potential theoretically-driven moderators that may have impact on the MS-Profitability relationship are identified and included in the proposed model. Of the moderators, the author divides them into two different groups: firm-specific and market-specific. The difference between these two groups can also further provide business managers some implications for their practices.

Keywords: Market share, Profitability, Performance Measure

Introduction
Marketing professionals have been feeling the increasing pressure to justify why companies need marketing. “Researchers in marketing have cautioned that the inability of marketing to demonstrate its contribution to firm performance has weakened its standing within firms” (Gao, 2010). Therefore, measures to evaluate the marketing performance have received much more attentions than ever. Among those financial or non-financial measures, market share has been the one which researchers and business managers focus on the most.

The biggest reason why market share got the most attention is that it has been empirically proved that market share can lead to profitability (Buzzell et al., 1975; Kurtz & Rhoades, 1992; Szymanski et al., 1993; Bhattacharya et al., 2021). However, there also have been completely opposite results
found by several researchers (Buzzell et al., 1975; Kurtz & Rhoades, 1992; Prescott et al., 1986; Szymanski et al., 1993; Wernerfelt, 1986). Therefore, in this article, the author provides an overview of the literature in the market share research and proposes a comprehensive model which can empirically investigate the relationship between market share and profitability. Also, several potential theoretically-driven moderators that may have impact on the MS-Profits relationship are identified and included in the proposed model.

**Measurements of marketing performance**

With the advancement of marketing discipline, “scholars have been developing and evaluating schemes for measuring the performance of marketing activities for the past half century (Clark, 2001). Even though research on market performance has been very well established, there is no clear and explicit definition of marketing performance (Gao, 2010). The only agreement that has been reached in the strategic marketing literature is that marketing performance is multidimensional in nature (Gao, 2010). However, there are many different measures that have been utilized in marketing literature and a superior marketing performance may differ between businesses (Vorhies & Morgan, 2003). Basically, some of them are financial-related measures and others are non-financial measure.

According to Gao (2010), within the marketing discipline, there is a general trend of marketing performance measurement. First of all, researchers have begun to use non-financial measures instead of traditional financial measures more frequently in these days. These non-financial measures mentioned here includes market share, customer satisfaction, customer loyalty, and brand equity (Gao, 2010). Secondly, in additional to measuring just the output produced by market activities, more and more practitioners and researchers start to pay attention to measuring the market input, such as marketing audit, marketing implementation, and market orientation. They often can lead to intermediate outcomes such as customer satisfaction, customer loyalty, and brand equity, which in turn lead to financial output (Gao, 2010).

Thirdly, instead of using single measure to evaluate the marketing performance, researchers gradually switch their focus to multiple-dimensional measures. More researchers now agree that marketing performance is multidimensional (Vorhies & Morgan, 2003). Finally, the last trend that has been observed is that the marketing performance is not only measured from the customer’s perspective but also evaluated from the investor’s perspective. In other words, “a new trend has appeared that links marketing performance to firm value, and in particular to shareholder value” (Gao, 2010).

In this new trend, among these non-financial measures that have been used more frequently to evaluate the marketing performance, market share has appeared to be the one that received the most attention (Kurtz & Rhoades, 1992). Also, the market share effect has been proved to be “robust across a wide range of variable definitions, sampling frames, and controls for accounting method variation” (Jacobson, 1988). Therefore, more and more analysts motivate businesses to implement a market share strategy based this evidence (Jacobson, 1988). For example, if a company incorporates the strategic planning orientation into its business goals that will lead them
to the development of measures of marketing productivity which are market share and net income (Mehrotra, 1984).

However, even with the market share measurement, there are several definitions and estimates that have been used. These different estimates of the market share effect have been argued to cause the result of differences in finding the relationship between market share and profitability (Szymanski et al., 1993). According to Buzzell and Gale (1987), there are three different estimates of market share effect: absolute market share, market-share rank, and relative market share. Absolute market share means how a business unit’s sales relate to the total sales of its served market while companies use market share ranks to rank themselves and competitors in the whole served market (Buzzell & Gale, 1987). In addition, relative market share compares a company’s absolute share relative to the single/three largest competitor (Buzzell & Gale, 1987).

### Market share as a performance measure

#### What is market share?

Based on the issues that we have discussed above, we all know that a proper definition of market share is a very important step to begin conducting research in this area. Since the major objective of this article is to provide an overview of market share research and to investigate whether market share can be a good performance measure of marketing, we obtain a strategic marketing definition of market share from the American Marketing Association website. It defines market share as “the proportion of the total quantity or dollar sales in a market that is held by each of the competitors. The market can be defined as broadly as the industry, or all substitutes, or as narrowly as a specific market segment. The choice of market depends on which level gives the best insight into competitive position”. This more competitor-oriented definition reflects its strategic purpose.

#### Why does market share prevail?

As mentioned before, market share has been seen as the most influential measure to evaluate the marketing performance (Clark, 2001). According to the research conducted by the Profit Impact of Market Strategies (PIMS) project and the Boston Consulting Group, companies which have focused on gaining market share can enjoy the economies of scale and long-term profitability (Clark, 2001). Therefore, market share seems to be the main emphasis for a lot companies and also generally seems to dominate market concentration measures in explaining companies’ profitability (Kurtz & Rhoades, 1992).

In addition, since the major goal for a company, regardless of which performance measures it uses, is to be profitable, previous research has indicated that companies with higher market shares are able to enjoy higher rates of return on invested capital (Schwalbach, 1991). Therefore, this is the major reason why market share has received so much attention from businesses. However, several studies published in the Journal of Marketing (e.g. Cook, 1985; Rego et al, 2013; Edeling & Alexander 2018) and other academic journals have questioned the validity and generalizability of the market share-profitability relationship. The discussion about this underlying relationship has focused on inconsistencies in the magnitude, the statistical significance, and the direction of this
relationship reported across studies and across models within the same study (Szymanski et al., 1993). In the following section, the market share-profitability relationship is discussed from both of its supporters’ and critiques’ perspectives.

The market share-profitability relationship

Market share-profitability relationship

The role of market share in positively being associated with firm performance has received increasing attention in the marketing discipline since 1970 (Kurtz & Rhoades, 1992). The nature of the relationship between market share and business profitability has intrigued researchers, consultants and managers for years (Prescott et al., 1986). In 1975, Buzzell et al. published an article called “Market Share—A Key to Profitability”, saying that from an ongoing study of 57 companies, they reveal a positive link between ROI and market share (Buzzell et al., 1975). This is a very important article in the market share research. From then, many researchers began to be devoted themselves to this particular research stream.

As Buzzell et al. (1975) mentioned in their article, “it is now widely recognized that one of the main determinants of business profitability is market share”. They believe that companies with a higher share of the markets are considerably more profitable than their smaller-share rivals under most circumstances (Buzzell et al., 1975). Market share is also thought to be able to reflect the current competitive position for a company. Therefore, companies with high market shares are believed to satisfy customers' needs better and enjoy a competitive advantage against their smaller-share competitors (Schwalbach, 1991).

In addition, in Kurtz and Rhoades’s (1992) analysis based on a sample of 10,690 banks operating in 2165 different geographic markets during 1986, they find that “a statistically strong relationship between market share and profit rates”. They also show that there is no indication of a distinct break or critical level of market share, but increased market shares yield gains in profit rates at a decreasing rate (Kurtz & Rhoades, 1992).

Since so many researchers have demonstrated the positive relationship between market share and profitability, there must be some underlying reasons that cause this positive association (Katsikeas et al., 2016; Bhattacharya et al., 2021) One possible reason leading market share to profitability is that customers use market share as a signal of product quality (Jacobson, 1988). A brand widely accepted by existing customers provides information to potential customers that it is superior in quality to lower share brands (Smallwood & Conlisk, 1979). Therefore, high market share products give customers great confidence that low share products are unable to offer. As a result, high share products can enjoy higher prices and receive return premiums relative to low share products (Jacobson, 1988).

Besides that, Buzzell & Gale (1987) demonstrate four reasons why market share is profitable: economies of scale, risk aversion by consumers, market power, and a common underlying factor. First, when companies have higher market shares, which means they can achieve economies of scale to reduce costs. The role of market share in reducing costs, rather than in creating market power, that generates the association between share and profit (Jacobson, 1988). Secondly, when
companies become the market leaders, risk-averse consumers may keep buying their products because they don’t want to take risks (Buzzell & Gale, 1987). Thirdly, when high-share companies earn the market power, they are able to bargain more effectively because of their sizes. Lastly, Buzzell & Gale (1987) state that without any complicated explanations the reason why market share leads to profitability is just because they reflect the same underlying factors, such as product quality.

**Why market share may not be profitable?**

Even though there has been evidence showing that higher market share can lead to better profitability, emphasis on market share as a performance measure has also proved to be problematic by several researchers (Clark, 2001) and also to have some limitations (VanderWerf & Mahon, 1997). So, these inconsistent findings make us wonder whether this positive relationship does exist or can possibly be just a dust. Therefore, the dilemma both practitioners and researchers encounter is that the pursuit of market share as a goal may be appropriate only if a strong, positive relationship exists (Prescott et al., 1986). However, if the relationship is weak, or if the positive relationship is just an illusion, then the pursuit of market share as a goal may be wrong and even can damage companies’ long term survival (Prescott et al., 1986).

Several authors have also suggested that if market share is an asset, then competing for gaining market share may be just dramatic enough to reduce companies’ long-term returns to zero (Montgomery & Wernerfelt, 1991). Therefore, following this logic, several empirical studies found that small share companies can still be as equally profitable as large-share firms (Schwalbach, 1991). Woo (1981) and Woo and Cooper (1981, 1982) also demonstrated the same results, saying that some low-share companies still have high profitability. It was particularly established that “high-performing low-share businesses were located within environments characterized by stability, high value-added products, and a large number of competitors” (Woo & Cooper, 1981).

Based on those different empirical evidences proved by many different researchers, we can see that there are mixed findings and results regarding the relationship between market share and profitability. Therefore, there may be some potential factors to moderate the market share-profitability relationship. In the following section, by reviewing research literature, we are proposing several possible moderators as well as propositions based the respective moderators.

**Potential moderators**

*Product Quality*

The first factor that can possibly influence the relationship between market share and profitability is the product quality. As Jacobson (1988) mentions, “market share will not the comparative advantage when there is little uncertainty about product attributes or when customers rely on other indicators of product quality”. This means that companies can gain the competitive advantage through winning market share only when customers can be sure about their products’ quality if they value this attribute very much. Furthermore, based on Szymanski et al. (1993), they find that
different definitions of quality as conformance versus superior performance can be affecting the relationship between quality and market share and further influence the relationship with profitability.

However, Porter (1980) raises a completely opposite view. He indicates that a high quality image often requires a perception of exclusivity that is incompatible with high market share. Increases in share may diminish the feeling of exclusivity that enhances a quality perception (Porter, 1980). Also, a strategy of superior quality could lower customer sensitivity to price so that higher prices could be charged without a proportionate decline in sales (Buzzell & Gale, 1987). According to those arguments, we propose the first proposition for our conceptual model.

Proposition 1: Product quality moderates the positive relationship between market share and profitability.

Industrial concentration
By definition, if the industrial concentration is higher, it means there are fewer competitors in the market and the combined market share of all competing companies will be shared by fewer firms in a more concentrated industry than in a less concentrated industry (Szymanski et al., 1993). Therefore, a positive relationship can be expected under such circumstance. Also, high concentration results in joint profit maximization behavior (Kurtz & Rhoades, 1992) and then the relationship is also expected to be positive. However, there is a high possibility that the largest company in the market will stop maximizing growth well before monopolization (Wernerfelt, 1986). So, if the industry gets too concentrated (i.e. close to monopoly), the relationship between market share and profitability can be harmed and even becomes negative. Hence, the second proposition regarding industrial concentration is stated as below.

Proposition 2: Industrial concentration can moderate the positive relationship between market share and profitability.

Market growth rate
High-growth markets are generally viewed as relatively more attractive by businesses because of the high margins and growing demand that characterize them (Szymanski et al., 1993). As a result, more and more companies will be willing to try to enter this market due to the possible good profitability. As more companies enter the market, the number of competing firms in the market will increase. In addition, those high-growth markets can also be associated with high marketing costs, very tight cash flow strategy, needing more investment inputs to be able to stay in the game, increasing productivity, and high levels of buyer spending. By taking those increased profit margins and sales along with the reduced costs into account, the firm profitability seems to be increased (Buzzell & Gale, 1987).

Besides that, Clark (2001) suggests that market share an unrefined measure and it should be used with caution. It is best used as a check on sales growth figures. “Company sales growth should be placed in the context of industry sales growth: the prognosis for firms growing faster than their industry (rising unit share) differs from the prognosis for those growing slower than their industry
(falling unit share)” (Clark, 2001). Therefore, we can conclude that market growth rate is very crucial for the firm growth and its relative market share. So, profitability and market growth rate should be positively related and it makes the relationship between market share and profitability. Based on these findings, here is our third proposition.

**Proposition 3:** Market growth rate positively moderates the relationship between market share and profitability.

**Variations among industries/Customers**

As Buzzell et al. (1975) state in their article that “market share is more important for infrequently purchased products than for frequently purchased ones”. Since infrequently purchased products are usually the ones that are more durable and also require larger capital investment and costs. Therefore, even though the product quality is superior and the market is rapidly growing, potential customers for infrequently purchased products often need more comprehensive evaluation before they buy (Buzzell et al., 1975; Clark, 2001). On the other hand, “frequently purchased products are generally low unit-value items such as foods or industrial supplies. The risk in buying from a lesser-known, small-share supplier is lower in most cases, so a purchaser can feel free to shop around” (Buzzell et al., 1975).

The second issue under variations among industries mentioned by Buzzell et al. (1975) is that “market share is more important to businesses when buyers are "fragmented" rather than concentrated”. Different from the concentrated industry, concentrated customers tend to have more purchasing power than fragmented ones. Therefore, that gives high-share companies to gain more profits from fragmented customers (Buzzell et al., 1975; Clark, 2001). Hence, according to these arguments, here is our fourth proposition:

**Proposition 4:** Variations among industries/customers can moderate the relationship between market share and profitability.

**Product prices**

From the economic perspective, it suggests that for rational and informed consumers, price and quantity sold (which can proxy for market share) would be inversely related (Szymanski et al., 1993). Positive price-quantity relationships can exist when higher prices are proxies for higher quality or confer greater prestige onto owners of the good (Monroe & Krishnan, 1984). In addition, high market share businesses could charge higher prices without losing sales when high market share endows a business with greater market power (Montgomery, 1985). Therefore, our fifth proposition can be stated as following.

**Proposition 5:** Product prices can positively moderate the relationship between market share and profitability.

**The conceptual model**

Based on the five propositions stated above, we are proposing a conceptual research model. These 5 moderators are divided into two different groups. One of them is firm-specific moderator,
containing product quality and product prices and another is market-specific group which consists of industry concentration, market growth rate, and variations among industries and customers. The model is in Figure 1.

Figure 1.
The model of market share and profitability

Conclusion
In sum, companies’ market share can still be positively associated with firm profitability if the potential moderators, product quality, product prices, industry concentration, market growth rate, and variations among industries/customers, are included. To those business managers, in our final conceptual model, since moderators are divided to firm-specific and market-specific groups, there can be some potential managerial implications from this. Therefore, for future research, it is very important that this conceptual model proposed in this article can be empirically investigated. There have been so many mixed findings in this particular area. The empirical results from testing this model can hopefully provide more conclusive findings.

References


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