Category Strategy for Firm Advantage

Abstract

The decision of where to position in a market is crucial to firm success. Most strategy research focuses either on choosing an attractive industry or firm-level differences that lead to sustained advantage. In both approaches, the environment is taken as an exogenous constraint. Overlooked is that firms shape industry sub-markets (market categories) in ways that advantage the firm. In this article, I draw on research in strategy, sociology, and cognitive science to show how firms can use category strategy in competitive positioning. Cognitively, the market categories people use define the playing field for firms, as they partially determine competitive sets and evaluation standards. Sociologically, definitions of market categories are subject to social influence. This means that strategic decisions about how to position on the market affect how market categories are defined and evolve, which firms can (and should) use to achieve long-term value.
When Steve Jobs introduced the iPad in 2010, he proclaimed, “iPad creates and defines an entirely new category of devices.” iPad was not just a small laptop; it would “connect users with their apps and content in a much more intimate, intuitive, and fun way than ever before.”¹ In 2015, Ford CEO Mark Fields announced that Ford was not just an automaker, it was a “mobility company” and would engage in initiatives like autonomous vehicles and ridesharing previously considered at odds with a traditional automaker.² This rhetorical move shifted the scope of what a car company could do, and should do. Salesforce.com founder Mark Beinoff defined the “Software as a Service (SaaS)” market category in the early 2000s, leading to the decline of the once powerful Siebel and the rise of outsourced CRM (Ramadan et al., 2016). These visionary CEOs did not simply locate their firms within existing industries. Part of their strategies were to take positions to define – or redefine – a market category around the strengths of the firm.

Strategy research has long recognized the importance of market positioning (Hambrick and Fredrickson, 2001; Rumelt et al., 1994). Historically, this is conceived as firms’ choices to locate in an exogenously defined, relatively static market. The focus is perhaps strongest in Michael Porter’s work, which emphasizes selecting an industry with favorable market forces (Porter, 1980). Resource-based views look at the other end of the continuum and consider unique firm competencies in taking a position within an industry (Barney, 1991; Teece et al., 1997). But under imperfect competition, many strategic decisions around positioning are at an intermediate level of industry sub-segments (Cool and Schendel, 1987), and determining boundaries for competitive segments is itself a complex cognitive and sociological question (Cattani et al., 2017).

Strategy researchers have not fully considered that firms have agency not only to *choose* their competitive space, but also to *define* it. Taking a market position is not just about matching the firm’s capabilities to the current environment. Firms also have the opportunity to shape market categories in ways that advantage the firm. A crucial aspect of strategic positioning is *category strategy*.

A prominent example is Apple’s turnaround. When Steve Jobs returned to Apple in 1997, it appeared to be succumbing to industry forces outside its control. Apple reversed its trajectory not by outcompeting in the personal computer market category, but by creating, defining, and then dominating new market categories for smartphones and tablets (Yoffie and Baldwin, 2015). Their success was predicated on innovative product development and creative marketing. In conjunction with this, they defined the environment around their strengths. Design, ease of use, compatibility with the ecosystem of products, and signaling a cultural identity became key criteria for purchasing decisions. Apple created an environment such that when analysts or customers thought about a “tablet,” they thought about the iPad.

Categories that comprise an environment are both influential and malleable. Categories determine the kinds of products that already have a line item in a customer’s budget. Category definitions underlie features that are “essentials” versus “nice to haves” in a request-for-proposal (RFP). They are reflected in what industry analysts highlight in their reports. Influencing categories tilts the playing field – and firms vie to tilt it in their direction. When firms search for a market position that confers advantage, they are not limited to selecting existing markets and building capabilities to fit. An important, and underexplored, strategic tactic is to (try and) *change* market categorization so that the environment evolves to favor the firm.
Concepts organize how people think, as abstract representations that reduce an infinite world of information to something tractable (Murphy, 2004). Social categories reflect identities, communities, and consensus about what behaviors are legitimate and appropriate (DiMaggio, 1987; Lamont and Molnar, 2002). People’s cognitive understandings map to social categories that then affect perceptions, evaluations, and performance (Dimaggio, 1997; Hannan et al., 2018).

These insights have implications for strategic decisions in markets. The link between cognitive structures and strategy is most clearly articulated in the sociocognitive research stream, which shows that managerial perceptions determine the formation of competitive reference groups (Porac and Thomas, 1990; Porac et al., 1995), and that market definitions emerge through interplay among producers and consumers (Rosa et al., 1999). Research in organization theory also shows that categories in markets have important effects on outcomes of interest to strategy research: performance of cultural products (Hsu, 2006a; Negro et al., 2010; Kovacs and Hannan, 2015), hiring (Leung, 2014; Leung and Sharkey, 2013), VC investment (Pontikes, 2012), and market responses to firm misconduct (Sharkey, 2014). Together, these studies show that cognitive structures link to market categorization, and that firm positions within market categories have important consequences.

Given how influential market categories are, it is not surprising that firms employ category strategy in taking a market position. A firm’s environment is not strictly exogenous: it is composed of competitors and includes the firm itself. Firms do not have ultimate control of category definitions, but they can influence how people think about categories. If successful, their initiatives might aggregate to changes in collective beliefs that favor the firm’s strengths. As the above examples indicate, many firms intuitively employ category strategies (Ramadan et
al., 2016). Scholars have not provided an intellectual framework to guide their actions. This is striking because a number of social science literatures speak to such initiatives. This paper brings together research in strategy, sociology, and cognitive science to develop a theoretical foundation for category strategy. It explores implications for strategic positioning, innovation, and market evolution.

Foundations for Category Strategy: A Tale of Three Disciplines

Strategy: Competitive Groups

Categories are the backdrop for most models of competition. Determining the set of firms that compete is a categorization problem. But for traditional strategy research, categories are parameters that underlie an analysis rather than an important strategic consideration. For example, in models of perfect competition categories are defined by a commodity with an implicit assumption that markets comprise obvious clusters of homogenous, substitutable goods.

Categories feature prominently in Michael Porter’s work where the industry – a category of firms – is the unit of analysis. The focus is to understand forces that underlie competition within the industry in order to evaluate the root causes of long-term profitability (Porter, 1980). This line of research explicitly acknowledges the challenges of defining industry boundaries, but treats it as a practical problem. Industry categories are assumed to be exogenous, discoverable entities that can be uncovered if the framework is correctly applied (Porter, 2008).

Theories of imperfect competition are built on the recognition that most markets do not readily sort into clusters of homogenous goods separated by a “marked gap” (Robinson, 1933, page 17). But much of this research emphasizes firm heterogeneity and overlooks the categorization issue. In the resource-based view, the focus is individual firm characteristics that
underlie competitive advantage (Penrose, 1959; Barney, 1991). Competition is modeled in terms of substitutability between firms, not commonalities among a set of competitors (Peteraf, 1993). Firms achieve competitive advantage when they take a market position where their resources yield profits, if resources are difficult to imitate (Teece et al., 1997). The ascendance of this research stream is testament to the value of considering the unique resources of individual firms. But in avoiding categorization it leaves out additional factors that drive (or impede) firm success. Most evaluation processes are based on comparing a set of similar firms: for example in analyst projections and the consideration sets buyers assemble. If we consider that most markets do not naturally cluster into homogenous groups separated by a gap, this means these is some subjectivity in how these sets are created, which creates an opportunity firms might exploit to gain strategic advantage.

Research on strategic groups directly tackles the question of categories, proposing performance differences for within-industry sets of firms pursuing similar strategies (Caves and Porter, 1977; Cool and Schendel, 1987). In this approach category definition is a primary concern, and scholars quickly faced issues around how to meaningfully group firms in a generalizable, *ex ante* manner to show causal effects (McGee and Thomas, 1986). Unfortunately, such questions remain open as engagement in the topic receded (Cattani et al., 2017). This literature recognized the importance of intermediate level categories in competitive positioning, as industries are a broad classification containing great deal of variance, and competition is not so localized that we can simply restrict attention to one firm. However, scholars did not fully consider the sociological and cognitive underpinnings inherent in strategic group definitions. Without this, they struggled to delineate reliable characteristics upon which strategic groups should be based.
The sociocognitive approach proposes how organizational strategists perceive the market influences who they track as competitors and how they respond (Porac et al., 1989; Porac and Thomas, 1990). This research stream abandons the search for the universal definition of competitive groups in favor of understanding different actors’ mental models (Porac et al., 1995). Acknowledging various perspectives does not mean that there is no common structure to the market, however. Market interactions require that people make sense of each other’s perspectives, and through this competitive categories become coherent (Rosa et al., 1999). Drawing on research from psychology, sociology, and marketing, this approach presents a realistic picture of how strategists within firms define competitive sets. It also highlights that customers’ demand-based understandings of product categories influence producers’ mental models, and thus their definitions of competitive groups. This research does suggest that categories eventually cohere, which is consistent with traditional models of competition. At the same time, it uncovers that competitive sets are socially constructed. Extending these ideas suggests that competitive definitions can be influenced, presenting an opportunity for firms to employ a category strategy.

Sociology: Categories in Markets

Sociologists have been interested in classification dating at least back to Durkheim ([1912] 2001). Sociologists conceive of categories as socially constructed boundaries that reinforce cultural differences and create hierarchy (DiMaggio, 1987; Lamont and Molnar, 2002). An important contribution of this literature is to recognize that categories do not need to be objectively defined to be experienced as an objective reality. Widespread agreement on social meanings creates reality (Berger and Luckmann, 1967).
A productive line of inquiry applies conceptions of categories from cultural research to categories in markets, studying outcomes of interest to strategy. In this stream, scholars assume markets are heterogeneous and structure is created from actors negotiating boundaries. They study intermediate-level categories that reflect social identities, like healthcare forms or film genres (Ruef, 1999; Hsu and Hannan, 2005). Studies show that an object’s position within a category system affects how it is interpreted and therefore how it is valued.

Initial research adhered closely to the sociological view of categories as social structures that constrain behavior. Studies document penalties for objects located in multiple categories because these positions do not squarely fit with people’s expectations and tastes. For example, films in multiple genres receive lower ratings (Hsu, 2006a) and generalist eBay sellers are less likely to make a sale (Hsu et al., 2009). These effects depend on how the underlying categorical structure is defined. For example, restaurants in multiple distant categories are especially devalued (Kovacs and Hannan, 2015), and wines that span low-contrast categories less so (Negro et al., 2010). Penalties associated with multiple category membership are only found when category systems are institutionalized (Ruef and Patterson, 2009).

Subsequent research questioned the view that category nonconformity is detrimental. A close consideration of the cognitive basis for market categorization suggests there are situations where category nonconformists might flourish. Pontikes (2012) finds that whether category nonconformity is problematic depends on the goals of the evaluating audience. For example, venture capitalists in software – “market makers” who aim to disrupt markets with novel products – favor companies in ambiguous categorical positions. This helps reconcile seemingly opposite findings in the category literature (benefits for category conformity) and innovation literature (benefits to bridging distant areas). The way a firm spans categories is also important.
because anchoring affects how people interpret category combinations. In the carbon nanotechnology industry, venture capitalists were more likely to fund hybrid firms rooted in the “science” category that drew on “technology,” but less likely to invest in “technology” companies that bridged “science” (Wry et al., 2013). People with sophisticated, unpredictable needs that connect many areas value firms that span categories, which explains why such law firms have higher performance (Paolella and Durand, 2016). Hedge funds atypical of a category are more rewarded for strong short-term performance, presumably because strengths are attributed to the unique characteristics of the fund as compared to category trends (Smith, 2011). Cultural “omnivores” value variety or atypicality, and therefore prefer cultural products that span category boundaries (Goldberg et al., 2016).

This literature, together with sociocognitive strategy research, demonstrates that categories affect evaluations. It also shows effects differ in magnitude and even direction depending on people’s mental models. That social categories are based in individual cognition is a foundation of both lines of research (Dimaggio, 1997; Porac and Thomas, 1990), but neither tackles the details of how cognitive processes aggregate to social structures. An assumption from the sociological tradition is that collective cognitive beliefs form institutionalized social structures that become powerful forces of conformity and so can be treated as exogenous to the individual. Findings from the body of research on categories in markets suggest this story does not fully represent how people navigate social categories and their effects. A general theory requires a foundation that links cognition to social categories. It should recognize that different evaluators may use different category systems, that people influence each other’s cognitive understandings, making category evolution endogenous, and that they may do so strategically.
Cognitive Science: Psychological Foundations

As studies increasingly demonstrate effects of categories in markets depend on cognitive underpinnings, scholars are calling for research that better accounts for cognitive bases of market categorization (Vergne and Wry, 2013; Cattani et al., 2017; Durand and Khaire, 2017; Pontikes and Kim, 2017). This is challenging since mental models are difficult to measure and vary over time and across people. But cognitive science provides a rich foundation based on laboratory studies of how people create and are influenced by categorization. (And with recent computational developments, scholars can meaningfully structure large corpora of text to empirically study how such individual cognitive models affect macro outcomes of interest to strategy research).

Research in cognitive science shows human thought relies on concepts and categories. Concepts reduce a world of infinite dimensions to a manageable number of clusters in which category members are treated equivalently. This allows people to quickly make assessments and react to objects they encounter (Mervis and Rosch, 1981). Concepts are so foundational to human thought it is difficult to imagine navigating the world without them (Murphy, 2004).

Early research relied on similarity as the basis for concept formation (Tversky, 1977). But scholars subsequently acknowledged that similarity is underdetermined and cannot ground cognition (Murphy and Medin, 1985). As philosopher Nelson Goodman asserts, similarity is meaningless without a frame of reference that defines “in what respects” two entities are similar (Goodman, 1972). Addressing this critique, Medin, Goldstone and Gentner (1993) propose

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3 Much of the literature in cognitive science focuses on concepts as mental representations, but uses the terms “concept” and “category” interchangeably. It is useful to distinguish these terms. Following previous work, here concepts refer to mental representations about (which are internal and hard to measure outside of the laboratory), and categories to the set of objects a person considers instances of a concept (which are shared socially and easier to uncover from a historical record) (Hannan et al., 2018).
similarity is not a hard-wired perceptual process but depends on contextual cues, so concepts and categories can only be defined relative to a particular frame.

There is a great deal of evidence that the relationship between similarity and categorization is bidirectional, and categories influence similarity assessments. People are better able to distinguish among speech sounds (which are the same physical distance apart) when the sounds come from different phonetic categories (Liberman et al., 1957). Native speakers of languages with different words for adjacent color categories can more readily distinguish hues across the category boundaries: comparing English speakers to those of Tarahamura, which lacks the distinction between “blue” and “green” (Kay and Kempton, 1984), or Russian, which distinguishes between light blue (“goluboy”) and dark blue (“sinyi”) (Winawer et al., 2007). Effects are found when categories are learned in the laboratory. After training to categorize boxes of different sizes and brightness, subjects were better able to discriminate between squares along dimensions relevant in the training (Goldstone, 1994). Categories even affect perceptions. After categorizing images of morphed faces, within-category similarity increased relative to an uncategorized image but between-category similarity did not, suggesting categorization leads to a representational change in how objects are mentally encoded (Goldstone et al., 2001).

Most cognitive research conceives of categories arising from (context dependent) similarity judgements of observable features: for example distance to a category prototype (Hampton, 1998). But there is also goal-derived categorization, where people create “ad-hoc” categories to aimed at fulfilling a particular objective, for example “things to take from one’s home during a fire” (Barsalou, 1983). Scholars have called for research on categories in markets to consider how this different form of category creation might affect macro-level outcomes (Durand and Paolella, 2013; Pontikes and Kim, 2017). Such flexibility in how people construct
categories opens opportunities for category strategy to influence how people conceive of markets.

This literature provides a cognitive foundation for how categories operate in markets. Findings show that categories must be formed with respect to a context. This has implications for strategy research. It suggests there is not one way to determine a competitive set, and that sociological and cognitive approaches to competitive category formation should be taken seriously. There are also implications for sociology research. People can be easily trained to use different category systems, suggesting institutionalized categories may not be the exogenous constraint envisioned in that literature.

The complexity of cognition does not mean that category effects are random or haphazard. As Medin et al (1993) state, “similarity is changeable and context dependent, but systematically fixed in context,” (p. 272). This applies to concepts and categories. Once context is correctly specified, researchers can uncover influential and predictable effects of categories in markets. To do this, scholars need to properly identify categorical contexts using models that link individual cognition with social categories. Recent work moves in this direction. Hannan et al (2018) develop a Bayesian model of concept formation over a feature space that treats concepts as probability distributions. It starts with the formation of individual concepts, allows them to change in response to social interaction, and then links this process to the emergence and evolution of social categories. Such a model can inform an approach to competitive groups that allows for a systematic analysis while accounting for different perspectives. It also indicates that individual attempts at influencing category meanings can reverberate through a market, suggesting category strategy might be effective.
Category Strategy

The above research shows that (1) positions firms take within market categories affect how they are valued, (2) market actors influence category definitions, and (3) categorization has cognitive effects on how people perceive and evaluate objects. As previous research recognizes, these findings show it is important to account for sociological and cognitive effects when defining a competitive space.

Scholars have not considered how this research sets the stage for category strategy. These literatures suggest an opportunity for firms to strategically influence category definitions and gain advantage. Cognitive research finds categories influence perceptions and evaluations even when subjects learn categories in the laboratory over a relatively short period of time (minutes to hours). Studies are designed this way to enhance internal validity by ruling out whether external knowledge influences results. But it is also informative for category strategy. Given that categories learned over the course of an hour affect how people perceive and compare objects, there is ample potential for information campaigns spearheaded by firms to influence how analysts, investors, and customers conceive market categories and thus evaluate the firm and its competitors.

A number of studies show that firms are strategic about taking market positions. Firms enter new markets when they have complementary technologies (Helfat, 1997), especially when they face competitive threats at their existing positions (Mitchell, 1989). Cognitive biases also come into play, when firms enter new markets due to overconfidence from success bias (Barnett and Pontikes, 2008). Research also shows firms take advantage of sociological and cognitive aspects of market categories. In the software industry, firms responded to competition by reframing their offerings in a close category (Pontikes and Kim, 2017). In the tobacco industry,
the emergence of the “light” category provided a strategic opportunity. As the category became taken-for-granted, customers increasingly assumed light cigarettes were healthier (low nicotine/tar) rather than checking product features. Tobacco firms exploited these cognitive defaults, positioning products in the “light” category to appeal to preferences for a healthier option even as they increased levels of tar and nicotine to appeal to customer tastes (Hsu and Grodal, 2015).

Less acknowledged is how positions a firm takes can change the external context. A firm’s environment is composed of other firms, and includes the firm itself. As competitors respond to one another, the environment evolves (Barnett and Hansen, 1996). This can happen when firms position against individual rivals (White, 1981), or because taking a market position changes category definitions. For example, in French cuisine, as chefs increasingly borrowed elements across rival food categories, penalties for borrowing decreased as category boundaries blurred (Rao et al., 2005). Category definitions are partly inferred from characteristics of members, which means firms can shape category meanings by simply claiming membership. This aggregates to a co-evolutionary dynamic, where category meanings evolve as firms develop new technologies and change market positions (Pontikes and Hannan, 2014). Some research suggests that firms take market positions to strategically influence categorization. Firms claim market categories for reasons other than product fit (Pontikes and Barnett, 2015), for example to shape symbolic boundaries (Grodal, 2017) or try to reap rewards from faddish market trends (Pontikes and Barnett, 2017a).

Firms that do not pay attention to shaping market categorization may struggle to gain traction, especially if they are innovative. Pollock and Williams’s (2011) ethnography of technology analyst Gartner documents an incident where a company considered purchasing a
product from a start-up (‘Picolo’) as its customer relationship management (CRM) system. Initially, Picolo was the preferred vendor for many employees. But Gartner was brought into the evaluation, and according to them Picolo was not a true CRM product. To some extent Picolo agreed; they thought their offering was more useful than standard CRM and stated that analysts like Gartner “do not have a category for what [Picolo] are offering…” (p. 202). Gartner simply saw it as a misfit and a “risk.” Picolo had an innovative product, but no category strategy. As a result, they were stuck evaluated against standards that emphasized their weaknesses and ignored their strengths.

Category strategy is an overlooked tactic that firms can use to gain competitive advantage. Many firms intuitively adopt one, and it is starting to be noticed in popular management literature (Ramadan et al., 2016). But the academic community has provided little guidance. Research in strategy, sociology, and cognitive science can provide theoretical (and practical) guidance. Below, I draw on these traditions to develop a framework for category strategy.

Labels

Labels are used to communicate about categories. In most strategy research labels are not subjects of interest. The focus is on firm capabilities and market characteristics, and it is assumed that to enter a market, a firm creates capabilities that fit. But when we consider how we know that a firm has entered a market, or whether we should consider firms with moderately different capabilities as differentiated but in same market, or in different markets, it becomes clear that labels themselves are influential.
Category labels are the simplest way to communicate where a firm is positioned. When a firm claims the label of a well-established category, it triggers assumptions about what its products and practices should be. The more a firm’s capabilities are mismatched from category expectations, the more problems it will encounter – as the example of Picolo demonstrates. In Picolo’s case, there was no category that fully captured the value of its products. But having capabilities perfectly matched to an established category carries risks as well, as typically those market positions are crowded. This is an example of the well-known tension between conforming and differentiating (Deephouse, 1999; Hannan and Freeman, 1977; DiMaggio and Powell, 1983).

Strategically using labels to convey a market position is one tactic firms can use to try and address – or perhaps circumvent – this tension. The example of Ford illustrates this strategy. Ford shifted its underlying capabilities from focusing solely on making cars to also developing other modes of transportation. There are multiple labeling tactics compatible with this move. Ford could have chosen to stay in the “automotive” category and educate the public to change their definition of the category. They could have claimed both the “automotive” and “ridesharing” categories. Instead, they claimed the “mobility” category. Their use of a new label conveyed Ford was undergoing a major shift and building an entirely new market. This tactic of using a new label – category innovation – is employed by firms that want to signal that they are so innovative that they are categorically different from others (Pontikes, 2018). A study of nanotechnology provides another example. Claiming the “nanotechnology” label had little relationship with a firm’s underlying capabilities. Instead, it was driven by whether executives thought the label was ambiguous, if the claim would be credible, and how valuable the label was as a signal (Granqvist et al., 2013).
Research in cognitive science provides insight into why labeling is important to category strategy. Language facilitates categorization. When the same label is applied to two anchor objects, subjects generalize category membership to all objects in between, but generalizations drop off sharply when the anchors are assigned different labels (Landau and Shipley, 2001). The presence of redundant, nonsense labels facilitates category learning (Lupyan et al., 2007). Labels activate a more prototypical category representation (e.g., “dog”) as compared to sounds (e.g., a bark) (Edmiston and Lupyan, 2013). Subjects attribute more stable characteristics over time and context when a character is described with a noun label (“she is a carrot eater”) versus a verbal predicate (“she eats carrots whenever she can”) (Gelman and Heyman, 1999). Subjects judge objects assigned the same category label as more similar, as compared to the same objects assigned different labels or unlabeled (Hannan et al., 2018).

Labels cue categorical thinking and highlight category-consistent characteristics. This is relevant to strategy. Given the same features, a product is differently received depending on the market category position invoked by its label. It mattered that Ford claimed to be a “mobility” company rather than in the “automotive” category, or that Salesforce.com positioned as “SaaS.” This is not to say that a new label is always preferable to an existing market category. Rather, executives need to understand how labels influence cognition and the sociological dynamic of market categories, in addition to their firm’s capabilities, to inform labeling tactics for their category strategy.

Rivals

Category strategy is not the same as brand strategy. Brand refers to the perception people hold of the firm, and ideally distinguishes the firm from competitors. A firm’s category refers to its
competitive position in the market, and necessarily includes rivals. Category strategy is aimed at developing a socially meaningful category, to influence whether people even assemble a consideration set for an offering, who is included in that set, and the standards of evaluation. Categories are not formed around a set of one. Rivals will be included in any evaluation process. A sound category strategy focuses on influencing the category boundary such that the firm is in a favorable position with respect to competitors, not keeping all competitors out of the category.

A tenet of organizational ecology is that close competitors both contribute to category legitimacy and compete. Studies find that when market categories are emerging legitimation is more important, and an additional rival increases survival rates. Once the category is established competitive forces are stronger, and an additional rival decreases survival (Carroll and Hannan, 2000). These studies conceived of markets on a fixed trajectory, but ideas apply even when we relax this assumption and recognize that market categories continually change. Influencing who is included in the competitive set redefines and re-legitimizes categories as industries evolve.

Consider the emergence of the market for craft beer (Carroll and Swaminathan, 2000). On resources alone, craft brewers are quite similar to “big beer,” and one could easily imagine craft beer makers taking a differentiated position within the “beer” market. But craft brewers created a distinct market category around a social identity that emphasized small batch production, independence, and innovation. Craft brewers banded together in associations, participated in beer festivals that excluded national producers, and lobbied for government regulations on who could claim to be part of the market. This increased demand for craft beer at the expense of mass beer, and blocked the ability of mass producers to enter and compete, helping all producers in the category. The emerging market for craft chocolate is using a similar category strategy (Mishra and Pontikes, 2015). Craft chocolate is a small but growing market,
with a few hundred producers in the United States as of 2018 that create high-priced chocolate using ethical sourcing, high quality beans, artisanal production, and creating a curated experience. They are attempting to carve out a unique category around these characteristics that is substantially different from “mass chocolate” as offered by Hershey and Mars. In doing so, most craft chocolate makers have focused on collaboration over competition, sharing information about sourcing (which can allow them to reduce shipping costs) and working together to define standards product quality and sourcing transparency. They are creating institutional structures to support this, through the Fine Chocolate Industry Association and a yearly “Chocolate Maker Summer Camp.”

Often, executives conceive of rivals as competitive. For category strategy, they should also weigh how rivals can help define and expand the market category.

**Analysts**

Analysts, critics, and other mediators play an important role defining markets. The act of issuing a report on a market category validates that the class of goods is a distinct “type” worthy of consideration. The firms they include define the boundaries of the category, and what features they highlight the schema for evaluation (Hsu and Podolny, 2005). Industry media coverage of the “minivan” helped solidify the category as something different from “cars” or “trucks,” with its own evaluation standards (Rosa et al., 1999). Gartner identifies and defines important information technology market categories for its Fortune 1000 client base (Pollock and Williams, 2009). The influence of critics on film and food is well-documented (Rao et al., 2005; Hsu, 2006b).
Management research often casts analysts as neutral third parties, but analysts are also strategic actors (Pontikes and Kim, 2017) that bring their own perspective to the market (Chatterji et al., 2016). Analysts are evaluated on how well they make sense of industry trends and they face their own pressures to differentiate and add value. To be effective, analysts must be in the know of firms’ latest activities. It is obvious that firms benefit from favorable analyst coverage and analysts are wary of attempts to curry favor. A more subtle (and more effective) tactic is to use category strategy, lobbying analysts to cover the firm’s category and define it in a way that is favorable to the firm. This means influencing analysts to use the same labels as the firm, to emphasize functionality that are unique to the firm, and to draw boundaries such that rivals that excel at something different are excluded, perhaps considered to be in a different category. In this way, firms should have a cohesive category strategy that includes labeling, identification of rivals, and analyst communication.

Activists

Activists, enthusiasts, or influencers – ordinary people who take an interest in the market – help shape the public perception of a market category. Strategy research has not focused on activists, but the social movements literature provides insights. Activists draw on social values and frame issues to mobilize the public in support of their cause. They disseminate information through networks, create associations, and organize events to promote their perspective (McCarthy and Zald, 1977). These tactics are also effective in the construction of new markets (King and Pearce, 2010). This perhaps is unsurprising for markets linked to traditional social causes, like grass-fed beef and dairy (Weber et al., 2008). But activists can be important in even in markets not clearly connected to prosocial causes.
The craft beer market is a classic example. Homebrewers and beer aficionados were key to expanding this market. They were steeped in dense networks through which information would rapidly flow. They published newsletters, magazines, created a brewers guild and other associations, hosted festivals, met in beer clubs, and socialized at craft beer pubs. To them, craft beer was not just a product, but a way of life, linked to traditionally American ideals like freedom and individualism (Carroll and Swaminathan, 2000). Activists spread information about “imposter” beer that did not adhere to the codes of the craft beer market, and lobbied governments for official regulations on who could be called a craft beer maker. They recruited more people to their movement, and as their ideas became more public, even those who did not fully share their passion were happy to join in the revelry. Activists were critical in promoting and maintain a social definition of “craft beer” that kept mass producers out as demand grew.

When cars were first invented, frequent explosions made the public (justifiably) wary of the new technology. Automobile enthusiasts helped redefine the category through organized certification contests where manufacturers had the opportunity to race their cars. This provided a forum for the public to get used to the new technology, witness improvements over time, and evaluate the technologies that seemed most reliable. These activist-organized races changed the public impression of the category from wild and unpredictable to safe, reliable, and useful (Rao, 2008). Lululemon cultivates relationships with “ambassadors,” fitness leaders in local communities. They give ambassadors complimentary clothes and host classes at their stores, forming a close-knit community of fitness enthusiasts who are exposed to their corporate values. They do not formally require anything in return, but expect that ambassadors will become natural advocates – not only for their products, but also in promoting the athletic lifestyle that will increase demand in the category (Tushman, Page and Ryder, 2010).
Market activists tap their informal social networks and evangelize what interests them. They draw attention to a market category and help define its social meaning by highlighting important features and scouting out inauthentic producers. This can work to a firm’s advantage if views are aligned. But it is a mistake to approach activists to directly promote the firm or product. Most activists are driven by personal curiosity and are not interested in being advertising vehicles, and this would reduce their credibility. The best way to incorporate activists in a category strategy is to create a vision for the market category that both speaks to the firms advantages and resonates with the social values that already motivate the constituency.

**Innovation and Market Evolution**

A core tenet of category strategy is that firms can shape their environments through market positioning. This means category strategy is especially important in times of change, whether driven by factors external to the firm (e.g. new entrants) or the firm itself (e.g. releasing a new product). In this way, category strategy relates to research on innovation and market evolution. Most research in this area focuses on firms developing resources and capabilities, typically in the form of new technologies or routines (Nelson and Winter, 1982). But firms have to position any new development in the market, and for this, category strategy is crucial.

Category strategy for innovation relates to a line of work on that articulates the role of cognition in technological change. In a pioneering paper, Clark (1985) proposes that customer concepts inform technological trajectories. Firms can deliberately influence this by creating a design for a technological innovation that cues cognitive and emotional responses (Rindova and Petkova, 2007). Kaplan and Tripsas (2008) show multiple constituencies develop collective frames around the meaning of new technologies, which can change technological outcomes. A
discourse analysis reveals differences in linguistic presentation that may explain why IBM was more successful than Remington Rand in introducing the computer to the insurance industry (Kahl and Grodal, 2016). These studies show that new technologies are interpreted in different ways depending on cognitive lenses in a market.

A firm’s category strategy (or lack thereof) will affect how an innovative development is received. Studying this requires that we theoretically and empirically decouple a firm’s market category position from the capabilities it develops. Much research on market evolution defines positions in a market based on a firm’s underlying resources. This type of model does not allow for researchers to study category strategy because it presumes market positions are determined by underlying attributes and assumes away the strategic nature of choosing a category. An alternative is to model firms as occupying positions in different planes. For example, a firm can be located in a product or technology space based on features of its product offering, and in category space based on the market category labels it claims. With this model, researchers can ask whether positions in two spaces are aligned, and then study consequences in terms of both firm outcomes and how positions in the two planes co-evolve (Pontikes and Hannan, 2014; Pontikes and Barnett, 2017b; Pontikes, 2018).

**Empirical Studies**

Designing empirical studies of category strategy requires data on market category positions that capture the mental models of relevant evaluators. Historically, it has been challenging to capture this information on a large scale, and so much previous strategy research on categories were in-depth, hand coded analyses of discourse for a small sample of firms. Advances in computational text analytics presents opportunities to conduct industry-wide studies of category strategy.
Machine learning algorithms can process free text to create structured data that capture the mental maps that underlie descriptions of firms and markets. Researchers have begun to use these methods to capture fine grained market positions and cognitive schemas: using press releases (Pontikes, 2012), texts of patents (Kaplan and Vakili, 2015), critics reviews (Hsu, 2006a), online user reviews (Kovács and Hannan, 2010; Kovács and Sharkey, 2014), and online job postings (Leung and Sharkey, 2013). As methods continue to improve, and as data become more available, researchers will be able to study how category strategy is implemented in various situations, and how it is received by different constituencies who bring their own perspectives to the market.

**Conclusion**

Whether a firm’s capabilities match its environment is critical to its success. Traditional strategy research approaches this topic in terms of firms finding a position that matches their capabilities, or evolving capabilities for environmental changes. Overlooked is a third option: *category strategy*. Firms are not limited to adapting their capabilities to an unfavorable environment. With category strategy, they can try to shape market categories so that environmental forces evolve in their favor. Many firms intuitively employ category strategy – some prominent examples include Ford, Apple, Google, Netflix, Uber, and IKEA. The ultimate goal is to define and then dominate a category.

There is a rich intellectual foundation for category strategy that spans disciplines: strategy, sociology, and cognitive science. Strategy research shows the importance of a firm’s market position, and that there are a number of ways to approach defining a competitive space. The sociology literature emphasizes that categories are socially constructed through interactions
among market actors, and that these become “social facts” and treated as reality. Cognitive science provides a psychological basis for why market categories are important, as they influence how people perceive and assess objects. Cognitive studies help reconcile the apparent contradiction that categories guide behavior even though they are malleable. People’s similarity judgements are coherent within a context, but change depending on their frame of reference, and new categories are readily learned.

These research streams suggest that category strategy can be quite powerful. Once market category definitions are accepted, they are the lens through which people assess a firm. And the firm has some agency to influence how categories are defined. With category strategy, firms can try to define the rules of the game. They do not have the ultimate say: having a category strategy does not mean the strategy will be successful, and there is always the chance that another firm will be able to capitalize on it. But implementing a well-crafted category increases a firm’s chances of success.

A category strategy is aimed at creating social meaning around a market category. The goal is for the category to become a “social fact” – easily recognized, acknowledged as important, and already in a potential customer’s budget. The evaluation standards should favor the firm’s strengths, and the boundaries defined such that the rivals have a comparable product. For example, a financial services firm may be strong in customer relationships and choosing individual stocks for a customized portfolio, but will suffer in an evaluation process if a customer’s top priority is to invest in a managed mutual fund.

Foundational research suggests four important aspects in designing category strategy: choosing a label, identifying rivals, influencing analysts, and connecting with activists. Labels are the way people communicate about categories. They facilitate processes of categorization.
The simple act of choosing the same or different label as a competitor influences others to see the firms as more similar or more different. Claiming the label of an established market can lead others to update their category definition in favor of the firm (but it can also backfire if the existing definition is a strong default). Rivals help create the social meaning for a category. Defining a category is not the same as creating a brand: a category refers to a set of firms (or products). Firms should consider what rivals form the best backdrop to showcase the firm’s strengths. Then category strategy should include organizing industry associations, conferences, or festivals with the chosen group of competitors and excluding others, to define the category boundary. This is especially important if there is another adjacent market where competitive forces are not favorable.

In many industries, there are trusted intermediaries, like analysts, who influence how people conceive of market categories. Firms should make sure analysts are on board with their preferred framework. Analysts have their own objectives, which usually include being the first to spot a trend. Communicating the firm’s perspective on the newest market categories might be helpful to the analyst – and might influence them to take the firm’s perspective. Lastly, activists are not just relevant to social movements. Many domains have activists – influencers, evangelists, or enthusiasts – who become genuinely excited about a new category and talk up its virtues. Activists are difficult to directly control, but they are useful in category strategy if firms take the right approach. Finding an authentic message and a constituency where the message resonates are crucial to leveraging activists for category strategy.
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