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# How **consumer goods** companies are coping with complexity

*A recent survey suggests that the rapid pace of change in the industry is leaving some marketers behind.*

**Blair Crawford, Jonathan W. Gordon, and Susan R. Mulder**

**The consumer-packaged-goods industry,** the birthplace of modern brand management, was for many years at the cutting edge of marketing. Recently, however, marketers in the industry have struggled to keep up with unprecedented levels of change—from an explosion in the number of media choices to the growth in size and importance of major retailers such as Wal-Mart Stores.

To understand how consumer goods marketers are coping, we surveyed chief marketing officers and their key subordinates at 20 leading North American consumer goods makers.[1] We asked them about their approaches to managing brands and brand portfolios, the changing media environment, innovation, consumer insights, relationships with retailers, and the relationship between corporate- and division-level marketers.[2] In addition, we reviewed the performance of the manufacturers (and, where possible, business units within them) in areas that matter to marketers, such as market share in product categories, the growth rates of brands

[1] The companies' collective sales represent roughly 50 percent of the US packaged food, personal and household care, nonalcoholic beverages, spirits, and tobacco categories. Examples of key subordinates include managers responsible for brands, innovation, customer insights, and relationships with retailers.

[2] By divisions, we mean units that have their own marketing initiatives and are held accountable for results. Typically, divisions represent brands, categories, or collections of both.

**Article at a glance**

*Consumer goods marketers are struggling to keep up with unprecedented levels of change—from an explosion in the number of media choices to the growth in size and importance of major discount retailers.*

*Recent McKinsey research combined a survey of marketers at 20 leading North American consumer goods companies with a review of their relative market shares, growth rates, and new-product sales, as well as other metrics.*

*Some leaders appear to be coping with today's challenging environment by experimenting with new media, novel approaches to gathering insights about consumers, and more collaborative relationships with retailers, among other things.*

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and brand portfolios relative to category averages, and sales from new products. Together, the results provide clues about the connection between specific marketing practices and marketing performance.[3]

Our findings highlight the prevalence of persistent experimentation among a few leading marketers. In today's uncertain environment, winning companies are experimenting with new media, new approaches for gathering insights about consumers, and more collaborative relationships with major retailers. Central marketing organizations at high-performing packaged-goods companies are more likely to let frontline marketers take chances and to provide information and disseminate best practices created by marketers across the company.

[3] We emphasize the word clues because it is impossible with such analyses to prove causation statistically. For more on the perils of linking high performance with a specific set of steps or operating formulas, see Phil Rosenzweig, "The halo effect, and other managerial delusions," *The McKinsey Quarterly*, 2007 Number 1, pp. 76–85.

## Evaluating performance

Marketing is an inexact science, and identifying cause-and-effect relationships between specific activities and individual metrics is challenging. Therefore, in each area we reviewed we used more than one metric to assess performance. To determine a company's performance in brand management, for example, we looked at the growth rate of its brands versus the growth of the relevant categories in which those brands competed, as well as the market share that its brands held in their core categories. At the same time, some metrics are a function of how well a company performs more than one marketing activity. We therefore used sales growth from new products to analyze a manufacturer's performance in both innovation and the management of consumer insights. Similarly, the growth rate of the revenues of a manufacturer's overall brand portfolio relative to category averages contributed to our assessment of its brand portfolio and the strength of its consumer insights.

In four areas—brand management, brand portfolios, innovation, and consumer insights—we could isolate the top performers and compare their results with those of the remainder of the sample. Achieving strong performance in all four areas was extremely difficult. Nearly half of the divisions we assessed failed to break into the leading group in even a single area. Less than 8 percent were leaders in all four.

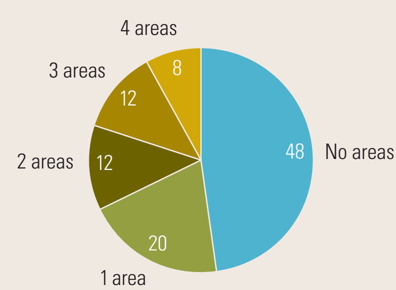
EXHIBIT 1

### Identifying high performers

| Area | Criteria for defining high performance |
|---|---|
| Brand management | • Brands ranked No. 1 or No. 2 in core category by share, **and**<br>• Sales growth in excess of category sales growth from 2002 to 2005 |
| Brand portfolio strategy, spending | • Divisions[1] with portfolio sales growth of at least 1% in excess of category sales growth from 2002 to 2005 |
| Innovation management | • Divisions[1] that achieved sales growth from innovation greater than 2% from 2002 to 2005, **and**<br>• Retained, on average, at least 50% of 1st-year sales per point of distribution in 2nd year after new-product launch |
| Consumer insights management | • Divisions[1] that achieved portfolio sales growth of at least 1% in excess of category sales growth and/or sales growth from innovation greater than 2% from 2002 to 2005, **and**<br>• Received top-quartile cross-functional ratings for consumer insights impact |

**Few companies cracked the code on all dimensions**

% of divisions[1] designated 'high performers' in . . .




[1]Units that have their own marketing initiatives and are held accountable for results; typically, divisions represent brands, categories, or combinations of both.

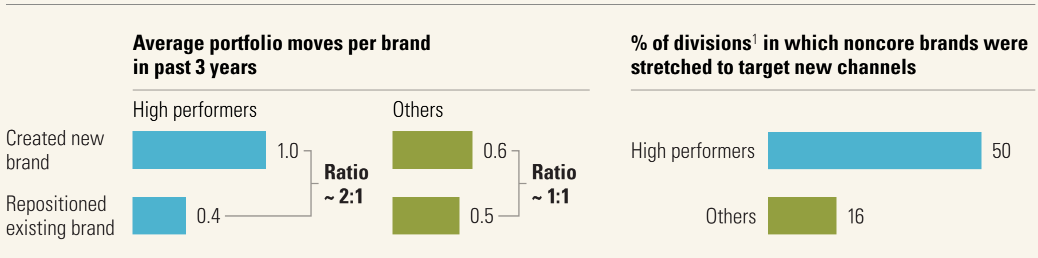
## Managing brands

Aggregate spending levels did not appear to explain the strength or weakness of individual brand portfolios. When we compared the marketing spending as a percentage of sales of the fastest-growing portfolios with the corresponding category averages, we found virtually no difference.[4]

A key area of difference, however, was the frequency of brand creation: high performers were nearly twice as likely as the others to create new brands, presumably because top companies feared overstretching their core ones. These findings help explain why brand proliferation continues to bedevil consumer goods makers: despite the costs, each one-off decision to add a new brand offers the hope of raising sales without cannibalizing existing brands.[5] Concerns about overreaching with core brands may also explain why companies that have high-performing brand portfolios were more likely than the others to use peripheral brands for exploring opportunities in particular distribution channels (such as increasing penetration among discount or specialty retailers).

EXHIBIT 2

**Protective brand proliferation**




[1]Units that have their own marketing initiatives and are held accountable for results; typically, divisions represent brands, categories, or combinations of both.

[4]Marketing spending as a percentage of sales was 7.7 percent for the high performers and 7.6 percent for the others. The average level of sales from a high-performing company's brand portfolio was 5.3 percent higher than the category average; the average level of sales for the others was 2.5 percent below the category average. The average annual sales growth rate for brand portfolios was 6.2 percent for high performers versus –1.6 percent for the others.

[5]For more on coping with brand proliferation, see Stephen J. Carlotti Jr., Mary Ellen Coe, and Jesko Perrey, "Making brand portfolios work," *The McKinsey Quarterly*, 2004 Number 4, pp. 24–35.

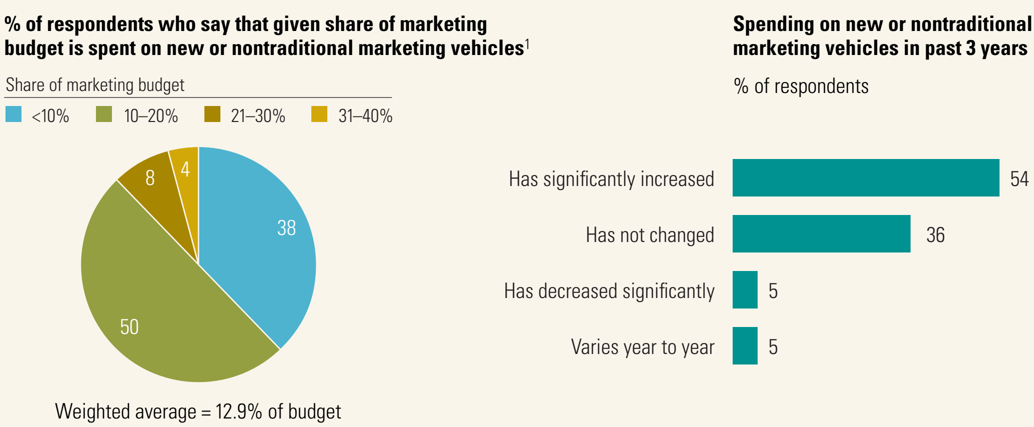
## A changing media landscape

More than 80 percent of the survey respondents say that the declining efficacy of television, radio, and print advertising is pushing them to experiment with new media such as Internet banner ads and paid search, product placements in video games, and cell phones. Further, a significant number of marketers say that their spending on nontraditional media has increased significantly over the past three years.

Nonetheless, television is still the most widely used vehicle. Although marketers agree that the world is changing, many apparently aren't in a position to abandon the tried-and-true approaches, because the available alternatives lack the scale to fully achieve the marketers' brand priorities. This may explain why more than one-third of all respondents devote less than 10 percent of their marketing budgets to nontraditional media, and fully half of them spend only 10 to 20 percent. Such findings are consistent with our experience, which indicates that while some testing is taking place, marketers should do more. In our view, marketers should be more rigorous both in determining which segments to address with particular tests and in measuring the impact of spending on all types of marketing vehicles.

EXHIBIT 3

**Testing new media**




[1]For example, Internet banner ads and paid search (for a fee, companies can get top listing in Internet search engine results when specific search terms are entered), marketing through video games, cell phones.

## Pursuing innovation

All of the consumer goods companies we surveyed followed one of two innovation approaches also prevalent in many other industries—“bloom” or “prune.” In the bloom approach, companies pass nearly every raw idea into concept testing and gradually weed many out; those using the prune method cut approximately 75 percent of new ideas prior to testing.

We identified high-performing innovators in both camps by examining two metrics: how often a company’s new products retained, in their second year, at least 50 percent of the sales they had earned during their first year and the sales growth rates associated with a company’s new products.[6] Almost all the high performers using the bloom model said that their innovation strategy focused on incremental innovations (defined as line extensions or other minor improvements). These companies let large numbers of raw ideas move into concept testing and brought larger numbers of minor innovations to market than would have been possible with other approaches. Conversely, all of the high performers using the prune model pursued more substantial, or breakthrough, innovations.[7] These companies required a lower number of high-potential product concepts to achieve their growth goals.

The fact that high performers don’t all pursue the same innovation model suggests that either one can be appropriate. The pace of change in consumer tastes and technology, along with the nature of competition in the product categories where a company operates, is likely to influence a manufacturer’s choice of strategy. Whichever strategy a company chooses, our survey suggests that aligning it with the proper innovation model—bloom or prune—is important.

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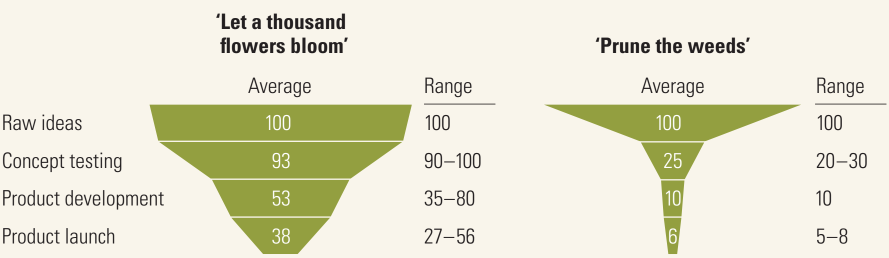
[6] The percentage of new products retaining at least half of their year-one sales during year two was 61 percent for high performers and 11 percent for the others. Sales growth from innovation was 4.2 percent a year for high performers and 0.7 percent for the others.

[7] Breakthrough innovation typically involves truly novel science or technology. For more on the distinction between breakthrough and incremental innovation, see Sharon M. Flanagan and Carl-Martin E. Lindahl, “Driving growth in consumer goods,” *The McKinsey Quarterly*, Web exclusive, October 2006.

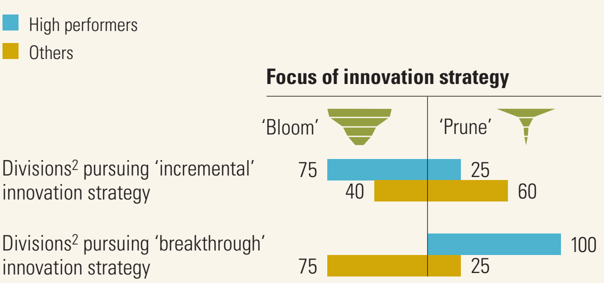
EXHIBIT 4

## Two distinct innovation models

% of raw ideas passing through each stage of innovation process[1]




% of divisions[2] employing innovation model




- Among high performers, incrementally driven innovators consistently employ 'bloom' model (75%), and all breakthrough-driven innovators employ 'prune' model (100%)
- Others don't consistently pick models best suited to their innovation strategy
- Both models can work well if aligned with overall strategy

[1] % of original number of ideas, not of previous step's total.
[2] Units that have their own marketing initiatives and are held accountable for results; typically, divisions represent brands, categories, or combinations of both.

## Gathering consumer insights

For most consumer goods companies, the consumer insights function is a relatively small and isolated group that concentrates on research (through techniques such as focus groups) and analysis.[8] Evaluating this function's performance is extremely difficult, since a strong understanding of consumers confers benefits on everything from new-product development to advertising campaigns. In light of this, we used three criteria to isolate high performers: strong growth in revenues from a company's overall brand portfolio, growth from new products, and high levels of satisfaction among marketers with the quality of the work of the consumer insights function.[9] We recognize that adding self-reported satisfaction metrics to the equation is an imperfect approach—are individuals doing well because they are satisfied or satisfied because they are doing well?—and therefore are cautious in our conclusions about the behavior of low versus high performers. Our findings include the following observations:

- Marketers at the companies identified as high performers were somewhat more likely than the others to perceive insights as central to their culture, working approach, and strategy and to believe that their consumer insights group collaborated effectively across the organization.

- To gather insights, high performers tend to invest more in nontraditional approaches, such as the use of "cool hunters" charged with identifying new trends in the field or "buzz" networks that attempt to generate enthusiasm—online or in person—for a product.

- At high-performing companies, the most senior people in the consumer insights group average 11 years of experience—almost three times as much as their counterparts in other companies.

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[8] For more on the customer insights function, see John E. Forsyth, Nicolo' Galante, and Todd Guild, "Capitalizing on customer insights," *The McKinsey Quarterly*, 2006 Number 3, pp. 42–53.

[9] Portfolio sales growth in excess of the category average was 1.8 percent for high performers and –0.9 percent for others; average sales growth from innovation was 3.8 percent for high performers versus 1.6 percent for others; and satisfaction levels with the quality of work produced by the consumer insights function (on a scale of 1 to 5) was 4.5 for high performers and 3.6 for others.

EXHIBIT 5

## Nontraditional research

**Use of nontraditional research approach,** % of divisions[1] using given approach 'somewhat' or 'extremely' often

| | High performers | Others | Definitions for insights techniques |
|---|---|---|---|
| Ethnography | 100 | 33 | Research based on observations of behavior (eg, watching use of products in home, observing consumers' in-store behavior) |
| Web-based consumer panels | 80 | 67 | Consumers who provide data online, either through social-networking Web sites or consumer polls |
| 'Cool hunters' | 40 | 20 | People who observe cultural trends, social behavior among the general public and identify emerging trends in marketplace |
| 'Buzz' networks | 40 | 0 | New twist on word-of-mouth marketing, eg, consumer clubs, online forums; initially used to create buzz around products, now valued for consumer insights |
| Natural-language programming/linguistics | 20 | 13 | Primarily consists of mining blogs for consumer feedback; can be rich in insights, but false or unreliable information difficult to avoid |
| Marketing gurus | 20 | 7 | Customer insights experts, often sought out for boutique-type consulting expertise |

**Average tenure of senior personnel in consumer insights organization,** number of years

| | Tenure in current role | Tenure in other part of consumer insights organization | Total |
|---|---|---|---|
| High performers | 9 | 2 | 11 |
| Others | 2 | 2 | 4 |

[1]Units that have their own marketing initiatives and are held accountable for results; typically, divisions represent brands, categories, or combinations of both.

## Collaborating with retailers

Another priority for many packaged-goods marketers is learning how to influence consumers more effectively at the point of sale. These efforts, also known "shopper marketing," have become more important and feasible in recent years as big-box retailers such as Costco, Target, and Wal-Mart have represented an ever-growing share of manufacturers' sales and as transaction-level data have become more readily available and easily processed. Measuring the performance of shopper-marketing programs at any level other than the single-store one is extremely challenging, so we did not attempt to establish metrics to distinguish low from high performers.

Nevertheless, it's clear from both our survey results and our experience that achieving the full potential of shopper-marketing programs requires consumer goods companies to balance powerful competing forces: nearly all (96 percent) of the marketers we surveyed say that their objective with such programs is stealing share from competitors. Retailers, of course, are most concerned with increasing overall sales.

Another common challenge for consumer goods companies, in our experience, is determining the impact of shopper-marketing efforts. Marketers find it extremely challenging to forecast and track the impact of these efforts on performance indicators such as brand profitability and brand equity. Indeed, more than half of all respondents simply don't evaluate shopper-marketing programs prior to execution.[10]

Interestingly, companies with high-performing brand portfolios are somewhat more likely than the others to partner with retailers in key discount, grocery, and drug channels and to conduct experiments such as pilots or in-store simulations. It's unclear from our research whether more effective shopper marketing contributed to the strong performance of a product or if rapid growth created the resources to support more in-store marketing efforts. In our experience, the former is more often the case.

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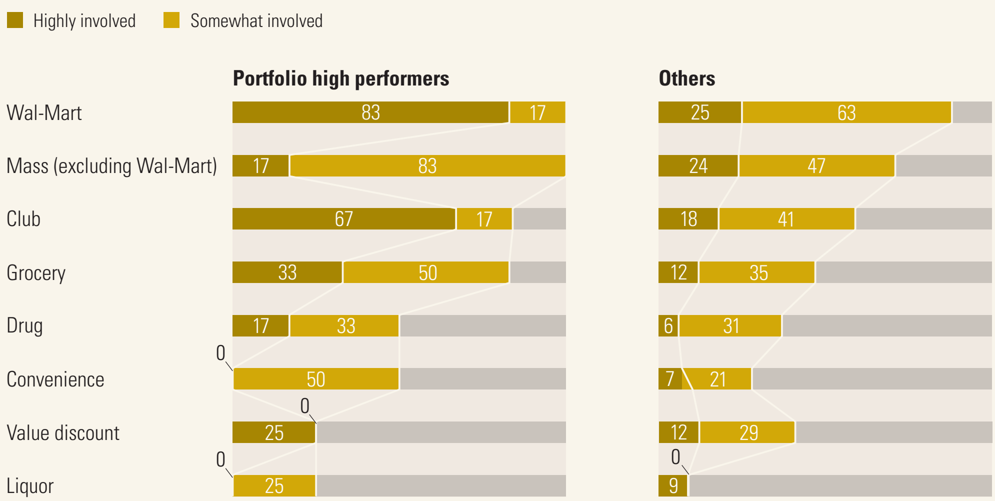
[10] For a case study on using simulation tools to forecast the potential impact of shopper-marketing programs, see Jim Brennan and Scott Liles, "Using technology to improve in-store marketing," *The McKinsey Quarterly*, Web exclusive, April 2007.

EXHIBIT 6

## Partnering with retailers

Extent of involvement with retailers in developing shopper-marketing programs, % of divisions[1] selling in each channel




[1]Units that have their own marketing initiatives and are held accountable for results; typically, divisions represent brands, categories, or combinations of both.

## Achieving organizational balance

More than 80 percent of the consumer goods companies we surveyed have corporate-marketing organizations in addition to marketing groups aligned with individual divisions. Effectively delineating roles and responsibilities between the corporate- and division-level marketing functions is important at any time and becomes critical in an environment where marketers are continually experimenting with new techniques. Marketers in charge of categories, products, or brands need the freedom to take risks as they try to expand the boundaries of traditional approaches. At the same time, however, it's vital for companies to make sure that marketers don't overspend—or cloud the meaning of core brands—while pursuing fragmented consumer segments, new-media opportunities, or evolving channel options.

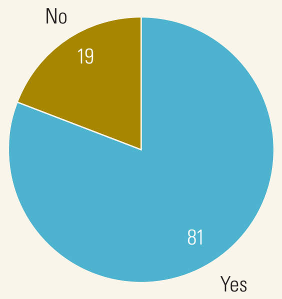
To be sure, the right organizational model depends on factors that vary by company—things such as geographic scope and the number of categories in which a company competes. It is therefore unrealistic to assign a one-size-fits-all metric to differentiate high-performing organizations from other ones. In our experience, striking a healthy balance between corporate- and division-level marketers and clearly defining their respective responsibilities can contribute to strong performance within business units. We therefore compared the organizational experiences of respondents in companies that have high-performing brand portfolios with the experiences of respondents in the other companies.

Companies whose brand portfolios perform strongly tend to place more responsibility for marketing strategy and execution in the hands of division-level marketers. For these companies, corporate marketing serves primarily as a center of excellence that disseminates information and best practices to line marketers. The other companies' corporate-marketing organizations report spending more time providing marketing services (for instance, managing relationships with advertising agencies), as well as getting heavily involved with global brand and innovation management. These tasks can sometimes be profitably performed closer to the front line.

EXHIBIT 7

## A center of excellence

**% of companies that have corporate-marketing group**




**Primary role of corporate marketing, %** of respondents[1]

| | High performers | Others |
|---|---|---|
| Act as center of excellence to disseminate information and best practices to line marketers | 50 | 17 |
| Manage global brands, innovation | 0 | 42 |
| Provide marketing services for company | 25 | 33 |

[1]Figures do not sum to 100%, because respondents who cite other roles are not shown.

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