

Route to a brand's best strategy

New findings challenge the belief that market share alone correlates with profitability. Bain & Company's analysis of 200 brands shows that products at the high end stand to earn considerably more with a smaller share of the overall product category

by **Cyrus Jilla, Nicolas Bloch and Vijay Vishwanath**

Conventional wisdom holds that market share alone determines profitability for branded consumer products. But that masks the full story. Consider what happened to The Gillette Co. after its main competitor Bic introduced low-cost disposable razors sold by the bag in the mid-1970s. Gillette, the global leader in razors, responded with its own razors in bags.

Yet Gillette's brand managers soon realised that even if they maintained a majority share in a value-oriented category, pre-tax operating profit, or return on sales (ROS) would be restricted to only 5-10 per cent. They looked for another road to profitability. Gillette invested more than \$200m in research and development, culminating in the 1989 introduction of its Sensor razor. The Sensor sold at a 25 per cent price premium over its own Atra, which until then had been the highest-priced shaving system on the market and it sold well.

Gillette's innovation convinced consumers to pay a premium for a new set of shaving expectations. Consumers proved willing to spend \$3.75 for a shaving system that required 70-cent replacement cartridges, while there was an option elsewhere

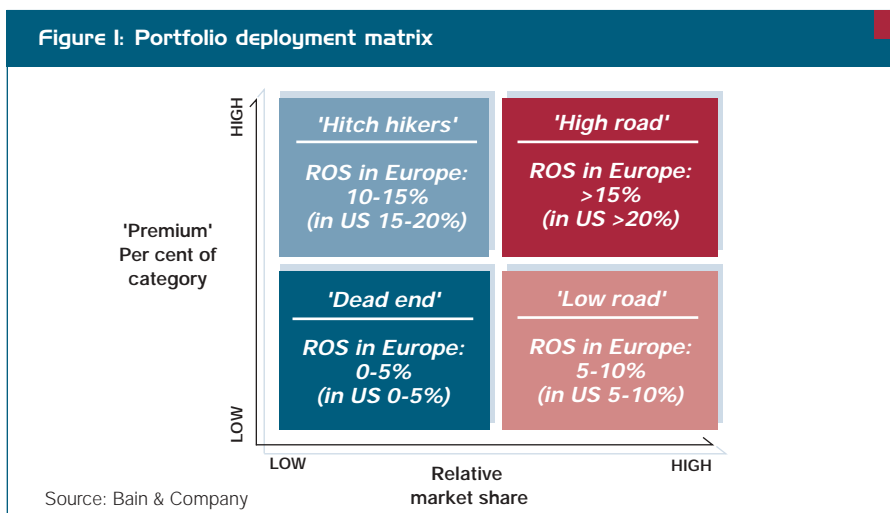
in the market to settle for 40-cent razors. What's more, 15 per cent of Sensor's new sales came from consumers who had bought competitors' disposable razors. The Sensor and its succeeding products returned the razor to a high-end category.

Gillette had decided that making the entire wet-shaving category more premium was more important than just getting back its market share in a category that was becoming a commodity. The lesson is that market share indeed affects profits but market share alone does not strictly correlate with profitability. When Bain & Co. studied the profitability of brands in more than 200 categories of global consumer goods, we found that market share explains only about half of the differences in brands' profitability.

A brand's profit potential is swayed by both market share and the nature of the category in which the brand competes. In Europe, premium brands are those that command at least a 25 per cent to 30 per cent higher price than value brands or private-label counterparts. Premium categories are those in which more than 60 per cent of the volume sold is premium brands.

These findings hold implications for consumer goods organisations and brand managers. They affect not just individual brand strategy, but also brand portfolio strategy, category management, marketing mix, and organisational and investment issues such as R&D, manufacturing capabilities, and even divestitures and acquisitions.

To begin with, the findings suggest new criteria against which consumer product firms can manage their portfolios. The approach, which we call 'High Road/Low Road', requires asking, first, is the category premium or value? And second, is the brand's market share high or low relative to competitors? For any given brand, there are four possible gradations. Each has its own strategic imperatives and each carries a range of expected returns that enables



companies to calibrate performance. (See Figure 1: Portfolio Deployment Matrix) This is a useful exercise to truly identify under-performing and outperforming brands.

High road/Low road brand strategies

In shorthand, the varying strategic options for each brand can be expressed as follows:

- **High road** Protect and grow the high end through innovation after innovation.
- **Low road** Grow volume relentlessly by focusing on operational efficiencies to reduce costs faster than prices. Only then, with a substantial leadership position, consider moving the category premium.
- **Hitchhiker** Target niche segments to profit from premium prices set by high road players, but avoid competing on price, which could commoditise the category.
- **Dead End** Rigorously rethink participation in the category, retreat to a premium niche, or exit entirely.

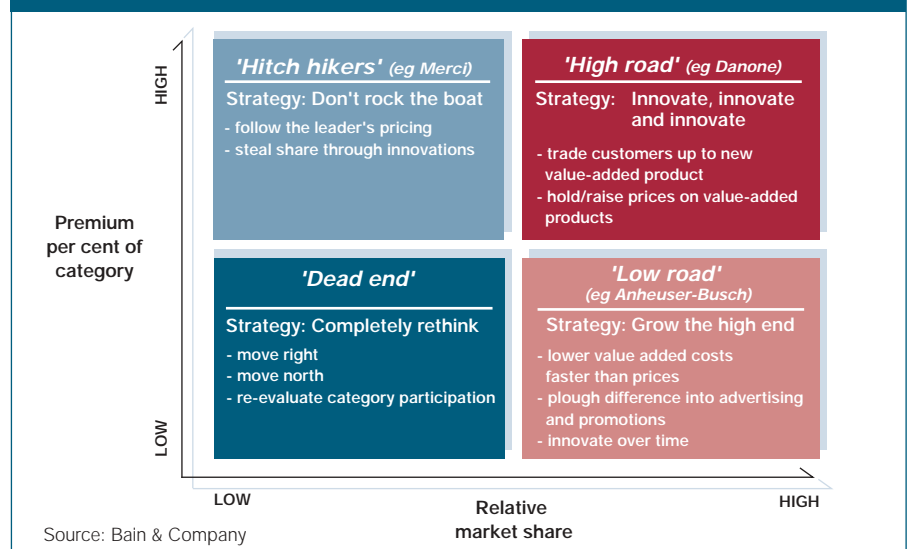
The shorthand rule for consumer products firms, no matter what quadrant, is that a company must pay attention to the nature of its category, not just market share. Let's examine how each quadrant works:

High road

As the Gillette example shows, the way to beat back commoditisation is through frequent and meaningful innovation. Gillette has transformed the safety razor into an increasingly high-value device. Its new M3Power not only features battery-powered vibration or 'micro-pulsation' and new edge technology for a closer shave, it dispenses vitamin E and aloe to help heal skin. Since the MP3 launch in 2004, the product has helped Gillette slightly increase its share in the global blade market.

Similarly, Groupe Danone, the French food maker, has continually upgraded its yogurt products' 'premiumness', lifting an entire category in the process. Historically, the majority of its product was plain and fruit-flavored yogurt, simply packaged. Today, that percentage has shrunk dramatically, market by market. In the US, for example, simple yogurts have dropped from 80 per cent of the firm's output to less than 5 per cent. In the interim, Danone has introduced a host of new yogurt products, including its health-centred Actimel and Activia brands in Europe. In France, the company's share rose from 35 per cent in 1999 to 37 per cent in 2004. Meanwhile, the volume of premium product in the French category rose from 52 per cent to 72 per cent and the

Figure 2: Winning brand strategies



average price premium moved up from 37 per cent to 68 per cent. But the Danone and Gillette experience also underscores another hard and fast rule: taking a value category to the high road is only possible if you're already a clear leader in the category.

Low road

When a brand competes in a value category and has a high relative market share, we call this a low-road brand. For better or worse, many European brands compete in this category. The winning strategy here can be summarised as 'bigger is better'. That is, it doesn't suffice just to be number one or two to thrive in a value category. Winning brands must have at least two or three times the market share of their nearest competitor. Low-road leaders therefore focus on several inter-related tactics to maximise the benefits of scale: they eliminate costs and complexity throughout the system; they devise ways to win at the store level through trade and promotional activities; they manage distribution tightly, and relentlessly use price to knock out the competition.

US brewer Anheuser-Busch is a classic example of a company that mastered low-road leadership before embarking on the high road. Thirty years ago it dug a wide trench of cost advantage by innovative beer packaging, shifting from traditional bottles to cans that stack more efficiently in trucks and increase gallons of beer delivered per run. This single innovation lowered costs across AB's value chain. It extended the brewer's distribution radius, which justified building larger breweries with better economies of scale and vertically inte-

grating into low-price, high-quality can production. The total system savings let the brewer beat competitors on price and plough more cash into advertising and promotion. Moreover, it changed the game in beer to one of national scale, which AB was uniquely positioned to win.

Hitchhiker

The rule to follow in this quadrant is 'live and let live'. Players here have learned to target niche segments to profit from the premium prices set by high road players. The game here is all about stealing share through innovations and acquiring other niche players. But it's not about price competition, which almost invariably leads the entire category downward. One coffee brand in Germany learned this the hard way when it undercut the leader, only to see the entire market move downscale. That also happened with Procter & Gamble's US coffee brand, Folger's, which took a long time to recover. A good example of maintaining a 'tagalong' pricing strategy can be seen in the market for pralines chocolates. In this category, Germany's Merci brand has maintained high margins by sheltering under Italian chocolatier Ferrero's Mon Cheri, Raffaello, and Rocher brands. Successful hitchhiker brands typically either attract a base of loyal users or lead in a sub-segment of the market.

Dead end

This quadrant is home to follower brands in a value category, which makes it difficult to find growth and make decent returns. This is an important category under pressure

across Europe, as pricing and volume growth have flattened in the face of declining population growth and the incursions of private-label players and hard discounters.

Consumer product firms in this position are often tempted to spend more on promotion and trade incentives with retailers to try to revive sales, or to increase advertising in a saturated media environment. But these efforts frequently fall short. Instead, executives should confront some hard questions: Should they retreat into a premium niche, a strategy of shrinking to grow later? Should they begin manufacturing private-label products for retailers themselves? Or, should they exit the category by selling to a scale player to whom the business is worth more? Firms that focus on just one of these strategies do best, whereas those that attempt to do some of each can become schizophrenic as they try to manage the complexity of two completely different business models and organisations. (See Figure 2)

Europe's complex market reality

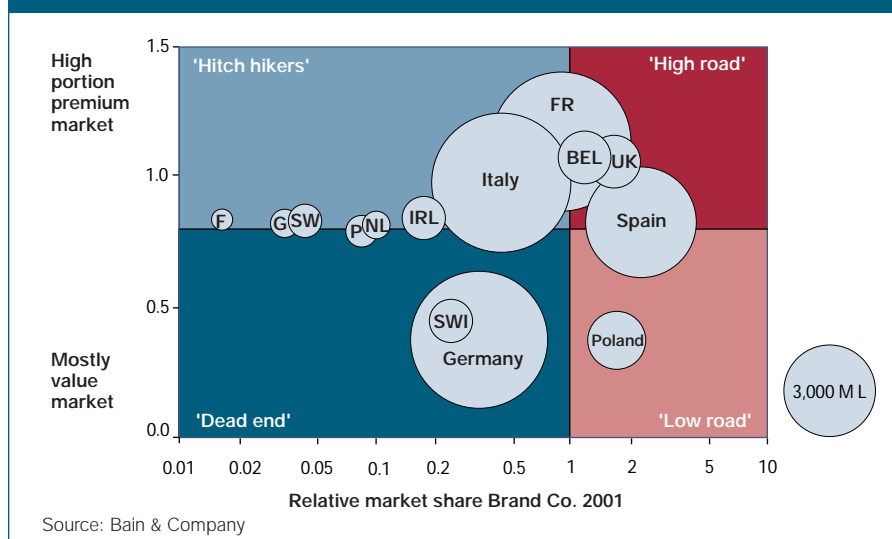
Without a doubt, every company would prefer to be in a high-road position like Gillette or Danone. But most important, companies need to understand their starting position. With that knowledge, firms in all quadrants can develop strategies to grow market share and profitability.

In Europe, this means getting to grips with a market reality far more complex and challenging than in the more homogenous open US markets. There are major differences. The same categories can behave very differently in different countries, and market fragmentation means that achieving scale is more difficult. Moreover, the level of expected return in each quadrant is about five percentage points lower in Europe than in the US. Finally, the growing strength of private-label brands and hard discounters make business much more challenging for brands in the dead-end category.

A multi-country portfolio strategy therefore starts by charting categories by country. (See Figure 3) For instance, bottled water is a value category (or 'low road') in Poland, but is more premium in France.

In most of the world, even companies in a dead-end position can retrench to profitable niche plays. But the pressure toward 'value' categories has been building in Europe. This reflects the growth of hard discount retailers like Germany's Aldi and Lidl, which sell private-label goods, and it reflects the private-label counterstrategies of other, higher-end retailers, like Carrefour. How should consumer products firms respond?

Figure 3: Brand Co's water portfolio by country



Moving around the matrix

Each category dictates a distinct strategy with related metrics, organisation and people. This means that a common strategy - for example, attempting to pursue only high-road opportunities - will not succeed. Some of the greatest dangers consumer products firms face in Europe involve trying too hard to get out of the box they are in.

Such can be the case for companies with brands in value categories that ambitiously seek to take the whole category premium. Sometimes referred to as the 'Starbucks effect' in the US, this happens when a company creates a step-function change in market innovation and perception. In Starbucks' case, this came from an outsider creating a wholly new coffee-drinking occasion and experience, leading to growth and pushing the packaged goods coffee category in the US more premium.

A second example is the UK's Walkers Crisps, which used innovation in packaging to segment its offering and drive growth in a very mature value category. Today, Walkers, owned by PepsiCo, leads savoury snacks in the UK, with half of the market. To drive upward, Walkers used innovations in packets that lock in flavor with a patented foil design; it created premium-priced 'posh crisps' and rolled out smart advertising featuring a top comedian and football players.

When such feats are carried out from inside, they are nearly always accomplished by a leader with a leading market share, as was true for Gillette, Danone and Walkers. It's tempting to imagine one's company engineering a marketing coup like Absolut

vodka's, which catalysed its low-road category to move to the high road. But such feats can take decades and are thus rare. Indeed, we have found the only quick and easy category move is downward.

Managing the brand portfolio

What does this say about growth prospects? First, that there is no correlation between being in a premium or a value category and unit sales growth. Rather, each quadrant offers a unique growth opportunity that calls for a tailored strategy to adjust marketing spend, research and development based on the category's profit potential. Brand owners with portfolios that span multiple countries and categories can use the High Road/Low Road as a framework to allocate resources differentially across the most promising businesses and stop spending it on dead ends. However, there is a correlation between understanding your positioning - and whether your category is shifting south or north - and profitable growth.

Whether you're selling yogurt or mobile phones, picking the right strategic direction begins with an understanding of what road you are travelling. In the end, the High-road/Low-road matrix emerges as a dynamic instrument of corporate strategy that calls for regular and systematic review.

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