

# Consumer product trends

Navigating 2020



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# Executive summary: Rough seas likely ahead

**C**ONSUMER product companies and retailers face a confluence of rapidly evolving technologies, consumer demographic shifts, changing consumer preferences, and economic uncertainty. These dynamics have the potential to undermine not only historical sources of profitable growth but also historical sources of competitive advantage, and render traditional operating models obsolete.

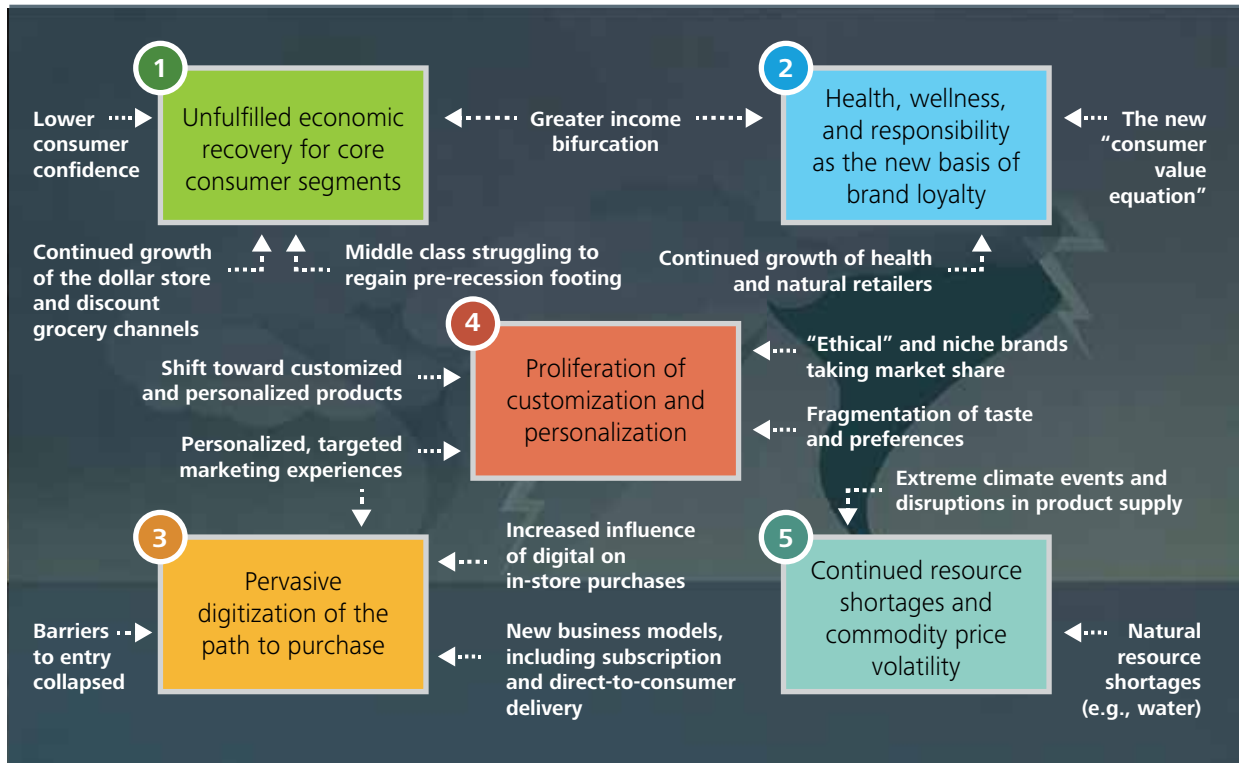
*In this rapidly evolving, low-growth, and margin-compressed environment, clear strategic direction and coordinated efforts are not all that should be pursued. Speed of execution and completeness of action are just as important, if not more important, to consider.*

Because no one knows exactly how marketplace dynamics will eventually play out over the next five years, consumer product companies should be prepared to operate amid uncertainty. Yet preparing for an uncertain future in 2020 is particularly difficult. The undercurrents in play place stress on the consumer product company's traditional sources of competitive advantage—scale, brand loyalty, and retail relationships—and the operating model that many of these companies are built on. Agreeing on strategic actions while not being able to agree on what the consumer product landscape will likely look like in five years is challenging in itself; concurrently moving rapidly with thoroughgoing actions is even more difficult.

The historical profitability of the consumer products industry indicates headwinds impeding performance in a difficult environment. Measured by return on assets (ROA), the consumer product industry's median profitability has trended downward over the past 30 years (from 5.8 percent in 1980 versus 3.7 percent in 2013).<sup>1</sup> While the bottom quartile of consumer product companies has suffered the most (1.9 percent ROA to a negative ROA of -5.6 percent), top performers are also slightly less profitable than they were before: Top-quartile ROA performers' ROA fell from 9.2 percent to 8.1 percent.<sup>2</sup> In other words: Collectively, the industry has lost steam.

Furthermore, the US consumer packaged goods market is unlikely to grow beyond the rate of population growth, and small players may be better positioned to take market share from traditional industry leaders. Perhaps the slowdown in return on assets is partially because many companies are neither bold enough in their plans, nor fast enough in their actions. To help consumer product executives prepare for change and uncertainty, this article presents five potential “undercurrents” that may impact the consumer product industry in 2020—marketplace undercurrents whose exact direction and pace, while still unknown, can be broadly identified today—that companies should keep in mind as they try to chart a clear path to 2020 and beyond.

Figure 1. Rough seas ahead: Five undercurrents in the consumer products industry



Graphic: Deloitte University Press | DUPress.com

### Undercurrent 1: Unfulfilled economic recovery for core consumer segments

The economy will likely continue to stagnate, and may give rise to increased income bifurcation, middling level of consumer confidence, and a struggling middle class.

**The likely consequence:** Core consumer segment(s) will experience minimal income growth at best.

**Challenge to current model:** Channel strategy and product portfolio shift to meet new price points.

### Undercurrent 2: Health, wellness, and responsibility as the new basis of brand loyalty

Emotional ties to national brands will likely decline due to growing consumer discontent with large companies' perceived values,

coupled with increased consumer focus on personal health, the environment, and social impact.

**The likely consequence:** Companies will experience greater pressure to better align offerings and activities with consumer interests and values.

**Challenge to current model:** Tremendous shifts are likely in brand portfolio, innovation strategy and capabilities, and ecosystem partners as companies move toward a health and wellness platform.

### Undercurrent 3: Pervasive digitization of the path to purchase

Concurrently new marketing channels to reach consumers, the convergence of sales and marketing environments, and the growth of disruptive retail models emerge. Traditional brick-and-mortar business models may be dismantled as consumers fully embrace digital.

**The likely consequence:** The lion's share of consumer spend and activity—promotion, search, and procurement—will take place over digital channels.

**Challenge to current model:** Traditional marketing and channel economies of scale dissipate, with many more paths to the consumer and many more convenient options for consumers to make initial and recurring purchases.

### Undercurrent 4: Proliferation of customization and personalization

Consumer spending will likely shift toward customized products and experiences across a broad range of consumer products.

**The likely consequence:** Customization of both the product and the end-to-end shopping experience will be critical to capturing value.

**Challenge to current model:** The value of mass-production economies of scale is undercut by new business models based on customization and delivery of individual units.

### Undercurrent 5: Continued resource shortages and commodity price volatility

The cost and cost volatility of key packaged goods inputs will likely continue to increase.

**The likely consequence:** More frequent shortages of natural resources, including water, will cause more supply chain disruptions.

**Challenge to current model:** Traditional commodity management strategies are increasingly insufficient to guarantee supply, harness innovation, and align with social responsibility.

These potential undercurrents are not mutually exclusive. Rather, companies should consider being prepared to steer a winning course even if two or more of these concurrently occur. By highlighting these uncertainties, we hope to not only provoke leadership team discussion, but also bring about action. Consumer product companies should consider taking steps to guard against being thrown off their chartered course by these undercurrents—or they may find themselves capsized by a future that takes them by surprise.

# Adrift in uncharted territory

**D**ON'T mistake the momentum of a collection of loosely coordinated projects as strategic progress. In this rapidly evolving environment, strategic transformation may require concurrently retooling many aspects of the operating model. No one wants to set sail in a storm with a nearsighted, narrowly focused, and overly optimistic captain at the wheel—and consumer product executives should consider taking care to avoid becoming exactly that.

A confluence of marketplace changes (figure 2) means that, for consumer product companies, the traditional levers for building loyalty are likely becoming less and less effective. Consumer product companies are complex, and nearly every organizational and process area is impacted by these rapidly changing industry dynamics. Brand and product portfolios designed for traditional economies of scale may no longer seem relevant. The shift toward new, as-yet-unproven digital marketing vehicles—by consumers and companies alike—could heighten the need to discover how to develop a better end-to-end consumer experience. The downward trend in profitability for both big and small players suggests

the need to revisit the relevance of traditional R&D and innovation models. Traditional consumer insight collection techniques, analytical models, and decision-making models may not be dynamic and granular enough to rapidly make pricing and trade promotion decisions with more precision. Furthermore, consumers and retailers could demand greater variety and customization in both product offerings and purchase channels.

The rapid pace of change necessitates companies to move quickly and completely in a coordinated way. Many consumer product companies risk being outpaced by these uncertainties because they are merely piloting projects as a proof of concept, and not rapidly moving the entire organization forward. Our hope is to not only provide you with a guidebook to help you set your course, but also to bring about action on these challenges. If changes are not made in the near term to enhance and fully scale up the capabilities of both your organization and your people, you may reach a point where both your ship and your crew will be irrelevant—precluding the possibility of smooth sailing into 2020 and beyond.



**Figure 2. Continuum of marketplace changes and considerations**

	Current environment	Likely future environment	Considerations
Channels	Grocery, mass, and club, with a few emerging formats; relatively homogeneous set of product portfolio offerings across channels	Dozens of formats, all with an element of digital commerce. More precise portfolio deployment by channel due to greater understanding of purchase and consumption occasions	Need for greater variety and customization tailored to channel dynamics
Pricing	Cost-plus pricing	Value-based pricing and dynamic, personalized promotions	Need to understand and shape consumer willingness to pay
Promotions	Weekly promotions based on static annual plan	Hourly promotions based on dynamic customer signals	Need for faster and more granular trade promotion management capabilities
Basis of consumer loyalty	Value	Authenticity and value	Imperative to align offerings with consumers' interests and values as traditional levers for building loyalty become increasingly ineffective
Product portfolio within brand family	Homogeneous	Broad variety	Shift away from traditional, scale-based sources of volume toward scope-based portfolios
Innovation focus	New products, primarily line extensions	Encompasses product offering, business configuration, and customer experience	Innovation should focus not just on products, but also customer experience, channels, delivery, customization, and revenue models
Consumer insights capability	Manual, self-reported, backward-looking	Real-time, forward-looking, predictive	Need to develop new sources of consumer insight and new analytical capabilities
Consumer engagement model	One-way, static push communication	Two-way, dynamic collaborative conversation	Need to discover how to develop an end-to-end consumer experience and ongoing consumer relationship
Brand-building vehicle	Mass advertising	Personalized messaging	Major shift to new, unproven marketing vehicles
Ecosystem	Consolidated set of large retailers, consumer product manufacturers, and traditional suppliers	Retailers and manufacturers coupled with a complex mix of nimble startups and digital technologists; broadening of the ecosystem to players that haven't traditionally been part of the CP landscape	Growth now requires effective external management of relationships, including co-opetition (collaborating with competitors) with a variety of players
Manufacturing	Long runs of limited SKU assortment	Flexible short runs with greater variety/customization	Need to variabilize or reconfigure manufacturing assets
Distribution	Full-truckload shipments of full pallets; majority of volume through traditional channel partners	Full pallets to retailers and eases (individual units) to consumers; sales via subscription and direct-to-consumer	Need to variabilize or reconfigure distribution assets
Suppliers	Transactional partners; focus on commodity acquisition	Integrated partners managing scarce resources. Focus on commodity preservation, agricultural innovation, and social impact	Sourcing shifts from resource procurement to resource preservation
Talent	Stable workforce with a mix of high potentials and solid citizens	High-turnover workforce with reliance on scarce, in-demand skills	Potential need to incorporate non-traditional employees into resource model; need to develop new talent recruitment and retention models

# Preparing for the journey: What might be expected along the way

**T**HROUGH our research and analysis of the current and anticipated future landscape, informed by case studies, executive interviews, prior research, and research conducted specifically for this report (see sidebar, “About this study”) we have identified five “undercurrents”—uncertainties which could move in directions contrary to the normal course of action—that may have the potential to capsize unprepared companies.

## Undercurrent 1: Unfulfilled economic recovery for core consumer segments

*“We used to be able to be successful serving just core consumers in grocers and mass merchandisers, but now we need to be present and deliberate in fragmented consumer segments and more channels.”—Packaged goods sales executive*

Our first uncertainty for 2020 relates to the economic environment in the United States—specifically, whether the continuing recovery uniformly helps consumers at all income levels. If the 2020 economy is sluggish, with greater income bifurcation between the most and least affluent consumers, the middle class may struggle to regain its pre-recession footing, consumer confidence may decline, and income growth may be muted among lower-income and middle-class consumers.<sup>4</sup>

Fewer consumers self-identify as middle class (44 percent in 2014 versus 53 percent in 2008), and more identify as lower class (40 percent in 2014 versus 25 percent in 2008).<sup>5</sup> These dynamics likely shaped the recessionary mind-set we observed in the 2015 American Pantry Study.<sup>6</sup> Fifty-eight percent of surveyed consumers believed that the US economy was currently in a recession in January 2015, and 94 percent said that even if the economy improved, they would remain cautious and keep spending at current levels. This finding is of particular concern to many packaged goods companies, which traditionally target a consumer base composed primarily of lower-income and middle-class consumers.

## Undercurrent 2: Health, wellness, and responsibility as the new basis of brand loyalty

*“To build brands in the future requires more than the basics. You need additional differentiation: good for you, good for the environment, and supporting a shared social cause.”*

—Packaged goods sales executive

*“Health and wellness can clearly differentiate our brands and drive brand loyalty.”—Packaged goods marketing executive*

The second uncertainty envisions a decline in emotional ties to national brands, growing discontent with the perceived values of large

## ABOUT THIS STUDY

The research described in this article is based on 14 case studies conducted between June and December 2014, an executive survey conducted in August–September 2013, consumer surveys conducted in January 2014 and January 2015, and seven executive interviews conducted between July and November 2014.<sup>3</sup> The executive survey polled 205 US executives and senior managers; the consumer surveys, over 4,000 adult US consumers.

Eighty-five of the 205 executives and senior managers surveyed from August–September 2013 worked in retail, consumer product manufacturing, or food and beverage. Of these 85 respondents, 38 percent worked at retail companies, 36 percent at consumer product manufacturing companies, and the remaining 26 percent at food and beverage companies. The remaining 120 executives worked in other consumer-focused industries, including commercial banking, travel, hospitality, automotive, and consumer electronics.

Executive and senior manager respondents' roles and titles reflected a broad range of experience in operations, finance, sales, information technology, marketing, and general management. A majority of the 205 executives and senior managers surveyed (56 percent) worked for companies with annual revenue greater than \$10 billion.

The consumers surveyed in January 2014 and January 2015 were screened to target consumers who did at least half of their household's shopping and food preparation. Most of the consumer respondents (58 percent) were female. Fifty-five percent reported an annual household income of less than \$50,000, 27 percent earned between \$50,000 and \$99,999, and 18 percent earned \$100,000 or more.

The seven executives interviewed had experience in marketing, sales, operations, and/or information technology at consumer product companies. The interviews covered four topics: trends in consumer demographics, behaviors, and attitudes; retailer and channel dynamics in consumer products; the impact of technology on consumer engagement, the shopping process, and business models; and commodity supply management.

In addition to the surveys and interviews described above, this report draws on data from a May 2014 survey of 2,004 consumers surveyed as part of the Deloitte Food Safety Survey. Respondents were screened to target consumers who did at least half of their household's shopping and food preparation. The report also uses information collected by the Deloitte Social Media Study. Conducted in July 2014, the Deloitte Social Media Study analyzed social media posts from the United States on the topics of "food safety" and "health and wellness."

companies, and a shift in consumer focus toward personal health, environmental sustainability, and social impact.

This uncertainty reflects an awakening of consumer consciousness along many dimensions. Almost half of US consumers have stronger preferences for brands and products aligned with the shifting value drivers of health and wellness, safety, corporate citizenship, and transparency, and the data suggest that this preference is not isolated to Millennials and high-income segments.<sup>7</sup> Some consumers are becoming increasingly aware of corporate values and placing more emphasis on the role

of the company within the community. Other consumers are placing greater emphasis on a product's impact on health, the absence of all things artificial in a product, or a product's cradle-to-grave environmental footprint. Still other consumers are focusing on the well-being of their community and on their community's values—which, more and more, include concepts like "green," "local," and "back to nature." Today, a sizable portion of consumers describe themselves as health-conscious shoppers (47 percent). Additionally, 35 percent of consumers described themselves as "ingredient sensitive" in 2015, up from 29 percent in

2010. The majority of consumers (74 percent) are paying close attention to the nutritional content of the foods they purchase and try to avoid preservatives and chemicals. Being able to cater to today's definition of healthy products can potentially help reap rewards in terms of commanding a price premium. For instance, 16 percent of consumers are willing to pay more than a 10 percent premium for healthier versions of products, while 55 percent are willing to pay up to 10 percent more.<sup>8</sup>

In this uncertainty, the basis upon which brand loyalty is formed is weighted toward characteristics beyond product taste, performance, or price. Of course, not every consumer will necessarily embrace personal health, environmental sustainability, and social impact, but a growing portion of consumers is likely to increasingly consider these attributes when making buying decisions. Under this uncertainty, national brands that do not reinvent themselves and reformulate their products along these attributes risk losing brand loyalty. Companies may undergo a major shift in their brand management approaches, their relationships with suppliers and retailers, and their business practices along the entire value chain. For some companies, this may entail reshaping their brand portfolio through innovation, acquisition of new brands, and/or divestiture of traditionally strong brands.

### Undercurrent 3: Pervasive digitization of the path to purchase

*"We can't ignore structural changes in advertising and marketing. Digital marketing is an imperative to be successful. We need to move beyond experimenting with direct-to-consumer storefronts, and develop a working online business model to drive growth."*—Packaged goods marketing executive

Our third uncertainty posits an environment in which consumers completely immerse themselves within a digital world, and the traditional brick-and-mortar business

model becomes less viable—or perhaps even irrelevant.

A decade or more after online shopping became mainstream, e-commerce for consumer packaged goods is finally arriving. While e-commerce is a small proportion of US retail sales (6.4 percent of sales between January and September 2014, according to the Retail Indicators Branch, US Census Bureau), online retail growth is outpacing overall growth. According to the Retail Indicator Branch, e-commerce sales across all retail channels (including non-CPG retail) grew by 18.7 percent annually between 2000 and 2013, while overall sales only grew by an average of 3.2 percent annually.

Growing hand in hand with digital commerce is last-mile delivery of consumer products to the home. A few examples of organizations providing last-mile delivery services are Instacart, FreshDirect, and Peapod. Instacart is a grocery delivery service that provides consumers with a third-party personal shopper that picks up and delivers groceries to them.<sup>9</sup> Instacart shoppers pick up groceries at national retailers, as well as at local retailers, in 16 metro areas across the United States. Other last-mile delivery services are also emerging in the grocery and general retail space.<sup>10</sup> Of note to consumer product companies is that some retailers have reported incremental sales through the online delivery channel.<sup>11</sup>

Preparing for this undercurrent is important: Recent research suggests that many packaged goods companies may be less prepared to capitalize on digital commerce than they should be—or than many consumer product executives would like to be.<sup>12</sup> In a 2013 study comparing consumers' and CPG executives' views on e-commerce, 92 percent of CPG executive respondents agreed with the statement, "The e-commerce channel is a strategic sales channel for CPG companies." Yet only 43 percent of these same executives thought that their company had a clear, well-understood digital commerce strategy, indicating a substantial gap between e-commerce's perceived

importance and consumer product companies' readiness to execute.

## Undercurrent 4: Proliferation of customization and personalization

*“Manufacturing flexibility is vitally important to create products across all price tiers efficiently and profitably.”*—Packaged goods sales executive

The fourth uncertainty is about consumer spending shifting toward customized products across a broad range of “commodity” consumer products.<sup>13</sup> Forty-two percent of consumers are interested in technology to customize products, and 19 percent indicate a willingness to pay a 10 percent price premium to customize or personalize products they purchase.<sup>14</sup> This state of affairs might be particularly challenging for consumer product companies because it runs counter to the dominant packaged goods market approach of offering a few high-volume SKUs through large traditional retailers. In a world where customized products and personalized, targeted marketing experiences win companies market share, technologies like digital commerce, additive manufacturing, and artificial intelligence can give a company an edge by allowing it to create customized product offerings.

## Undercurrent 5: Increased resource shortages and commodity price volatility

*“The ad-hoc and relatively uncoordinated commodity strategies of the past have left us*

*underprepared for the higher uncertainty we face.”*—Packaged goods finance executive

The fifth uncertainty posits commodity cost increases and higher cost volatility for key food and beverage inputs. Increased supply disruptions and natural resource shortages, such as water shortages, may put the business economics of consumer product companies under stress. Under this uncertainty, agricultural innovations are likely to emerge that have the potential to change the economics of food and beverage ingredients. There are many drivers fueling this volatility, including rising food demand, constrained food supply, volatile energy costs, and global economic uncertainty. Many of the drivers appear to be enduring, while others appear temporary or episodic in nature. Crop commodities in categories such as food (wheat, corn, rice, soybeans), beverages (coffee, cocoa), and cotton have trended upward over the past decade.<sup>15</sup> The International Monetary Fund (IMF) Food Commodity Index has risen 44 percent over the past decade, and the IMF Beverage Commodity Index has increased 56 percent. These commodity indices represent the price paid by consumer product companies to farmers for crop commodities. Furthermore, many food and beverage companies are increasingly subject to product supply disruption due to extreme climate events. Since 1980, there have been 178 weather and climate disasters in the United States. Disaster events—where overall damages reached or exceeded \$1 billion (including CPI adjustment to 2014)—resulted in a total cost of over \$1 trillion between 1980 and 2014. In 2014 alone, there were eight weather and climate disaster events across the United States.<sup>16</sup>

# Charting the course: Navigating through the storms

**T**O help executives plan and act amid these undercurrents, we have developed five sets of specific steps that may help address each of the five potential uncertainties described on page 5 (figure 2). The risk for many packaged goods companies is that they may be slowly proceeding to address two or three of these areas, and their approaches may be incomplete. The risk for executives is that they may be unknowingly incrementally falling behind such that by 2020 there could be a vast performance gap.

## Navigation aid No. 1: Revisit product portfolio, pricing, promotions, and merchandising

Consumer product companies should consider understanding and targeting lower-income and middle-class consumers' preferences in what they consider affordable in terms of price point and what they consider desirable in terms of channel. One example of how this can be achieved is offered by the food company Kraft. In an effort to display commitment to the lower-income US shopper,<sup>17</sup> Kraft developed products along “good-better-best” price points in many categories to give value-conscious consumers lower-priced access to national brands. For example, it offered tiered pricing in the cheese aisle, offering Velveeta Singles and Kraft Singles for the low- to mid-income consumer while selling Kraft Deli Select cheese slices at a higher price point.

According to Tony Vernon, former CEO of Kraft Foods, “Families in the middle [are] in fear of moving lower. We have an obligation to financially strapped low- and middle-income families that drive America’s grocery sales.”<sup>18</sup>

Kraft has also recognized the steady growth in popularity of dollar stores and drugstores among lower-income consumers as part of their overall grocery shopping routine.<sup>19</sup> The company has partnered with a dollar retailer in a promotional partnership to improve signage around and placement of the Kraft brand, and it has designed products—such as more affordable snack packs—specifically for the dollar and convenience channels.<sup>20</sup>

## Navigation aid No. 2: Align offerings and engagement strategies around consumer interests and values

For many consumers, perceptions of health and wellness seem to be increasingly important influencers of buying decisions at the shelf. Across food and beverage categories, we expect companies to continue acquiring brands perceived as healthier and experimenting with reformulating products with ingredients that are perceived as healthier, such as low-calorie natural sweeteners. For example, SlantShack Jerky makes handcrafted artisanal beef jerky sourced from sustainably raised, grass-fed cattle.<sup>21</sup> Rising consumer interest in protein-rich food has driven increased sales of products

such as jerky and other meat snacks in recent years. SlantShack Jerky allows consumers to “Build-a-Jerky” online.<sup>22</sup> The company initially allowed consumers to select either 100 percent grass-fed or USDA Choice beef.<sup>23</sup> However, the company now offers only 100 percent grass-fed beef, and it includes customization options and subscription options for its products.<sup>24</sup>

### Navigation aid No. 3: Create seamless experiences via technology and collaborations

We expect the importance of digital commerce to be amplified by the rapid pace of technological change. Digital technology has already permeated the path to purchase, as today’s consumers use websites, social media, and mobile apps not only to research products, compare prices, and make purchases, but also to provide feedback to peers and even companies.

Consumer product companies can use digital media to become a part of the consumer’s pre-store planning process by offering features such as online product comparison tools. During in-store shopping, technology can enhance the in-store product experience and deepen the brand conversation to help consumers save time and make better decisions. Technology can also allow consumer product companies to pursue greater collaboration with retailers, shopping-related application providers, and payment companies. And during post-purchase, companies can take advantage of technology to extend the product experience as well as to build a life cycle view of consumers through sophisticated data analysis.

### Navigation aid No. 4: Develop processes and business models to allow for customization and consumer interaction

Savvy companies are already increasingly tapping into consumers for ideas on new products and product variants. Crowdsourcing has emerged as one popular method for doing

this: Several successful campaigns, including PepsiCo’s FritoLay “Do Us a Flavor” campaign, have been built around seeking consumer input by crowdsourcing ideas on social media.<sup>25</sup> In this campaign, consumers suggest new product flavors, and the winning flavors are developed and launched.

Nestlé Purina’s ability to offer customized dog food provides an example of a company embracing both customization and customer interaction. Nestlé Purina observed the intense emotional bond that exists between pets and their owners, with pets often treated as members of the family. Consequently, attitudes toward packaged foods such as an “increasing desire for real food” and “using food as a way to attain and maintain good health” are highly relevant for the pet food category.<sup>26</sup> In March 2014, Nestlé Purina introduced “Just Right by Purina,” a brand that allows US consumers to create a customized blend of dog food online and have it home-delivered.<sup>27</sup> To evaluate the nutritional needs of the pet, Nestlé Purina’s website asks consumers to input details such as breed, gender, age, weight, activity level, and coat condition. The website also considers dietary preferences (for example, inclusion of chicken, lamb, salmon, grains, or soy) and allows consumers to personalize the package with the pet’s name and picture.<sup>28</sup> The website uses automated reminders so that consumers can conveniently reorder the customized blend before they run out of dog food.<sup>29</sup>

“Just Right by Purina” launched across the United States in October 2014, after an initial testing phase that began in March 2014. According to Brian Lester, director of Marketing for Just Right by Purina: “So far, people have responded well to it . . . As you look at the many other categories that consumers are in, there are more and more customized features that are being offered every day.”<sup>30</sup> The company is currently working to enhance the product’s personalization possibilities (for example, package sizes, flavors) and ordering features (for example, automatic replenishment); it is also testing a similar solution for cat food.<sup>31</sup>

## Navigation aid No. 5: View commodity decisions with resource preservation and social impact in mind

Forward-looking companies are thinking about not only the economic bottom line as they make commodity sourcing and procurement (for example, vertical integration) decisions, but also about their double (social) and triple (environmental) bottom lines as well. In particular, they are moving away from a “resource procurement” approach to sourcing to a “resource preservation” approach, which means thinking about each resource used and ways to develop or replenish future supply. For instance, a focus on resource preservation can mean partnering with local farmers to deploy improved farming techniques, or it can mean supporting conservation projects such as water-related initiatives.

PepsiCo’s commodity procurement strategy provides an example of how a company can reframe commodity sourcing from a resource procurement decision to a resource preservation decision. The resource in question is water. For the World Economic Forum community, water crises ranked as the third-highest concern among 31 global risks in 2014.<sup>32</sup> According to the Global Agenda Council on Water Security, “[P]oor water quality or shortages are often blamed on business operations even when businesses comply fully with regulatory requirements.”<sup>33</sup> Beverage companies have faced accusations that their operations are depleting groundwater on several occasions and in several countries over the years.<sup>34</sup>

PepsiCo, recognizing the importance of water scarcity as a business risk, established several specific goals around water stewardship in 2007. For instance, in 2012, the company met its goal to improve operational water use efficiency by more than 20 percent per unit of production over 2006 levels. The company has

also, through various partnerships on projects aimed at water conservation, distribution, purification, and hygiene, provided access to safe water to more than 3 million people; it is now working to provide safe water access to 6 million people by the end of 2015.<sup>35</sup> PepsiCo’s focus is on achieving a “positive water balance” in its operations, especially in water-distressed areas. In India, for instance, the company achieved such a balance in 2010 and 2011; in 2011, PepsiCo restored 14.7 billion liters to the environment in India, more than the 6.3 billion liters of water that it used in its Indian operations.<sup>36</sup>

As the worldwide population grows, there has been increasing interest in food and agricultural innovation. One way to address commodity price volatility, higher commodity costs, and resource shortage is the application of food technology. Venture capitalists and other investor groups have been increasingly investing in start-ups that focus on new ways of developing food, often seeking to produce healthy food more sustainably and efficiently. For example, Vinod Khosla of Khosla Ventures has invested in Hampton Creek, which develops products with plant-based proteins, such as egg-free Just Mayo.<sup>37</sup> Food technology start-ups are important to investors like Khosla because “we must invest in humane foods that avoid the industrial food chain, like Hampton Creek, which can achieve five times greater improvement in efficiency through innovation without compromising taste.”<sup>38</sup>

Together, these undercurrents and navigation aids may require new ways of working and a higher level of enterprise-wise coordination. It means considering moving from reactive, beyond responsive, to an intuitive enterprise that is continually sensing and shaping markets to redefine the frontiers.<sup>39</sup> In many cases, consumer product executives know what to do, but their speed of execution and completeness of action may be insufficient (see figure 3).



**Figure 3. Speed of execution and completeness of action may be insufficient in the face of the five undercurrents**

Undercurrent	Recommendations (potential strategic actions)	Awareness*	Speed of execution*	Completeness of actions*
Unfulfilled economic recovery for core consumer segments	<ol style="list-style-type: none"> <li>1. Rethink and reset the product portfolio to meet low-income, middle-class, and affluent consumers where they are, not where you wish they were</li> <li>2. Use shelf-back pricing, promotions, and merchandising as a strategic lever to meet increasingly divergent consumer price-point needs</li> </ol>	High	Medium	Low
Health, wellness, and responsibility as the new basis of brand loyalty	<ol style="list-style-type: none"> <li>1. Develop, extend, or elevate brands using both product and non-product innovation to emphasize health, wellness, and responsibility</li> <li>2. Engage consumers on their terms (using digital, social, and mobile) to rebuild trust and loyalty</li> <li>3. Build a forward-looking predictive insights capability to reduce blind spots and identify long-term market and consumer shifts</li> </ol>	High	Low	Low
Pervasive digitization of the path to purchase and last-mile delivery	<ol style="list-style-type: none"> <li>1. Craft a seamless multichannel consumer experience across traditional and emerging channels, embracing the digitally enhanced path to purchase</li> <li>2. Form partnerships to expand presence, capability, and reach in the new technology-enabled consumer products ecosystem</li> </ol>	High	Medium	Low
Proliferation of customization and personalization	<ol style="list-style-type: none"> <li>1. Create an innovation engine that allows for the creation of customized products, using consumer experiences and direct consumer feedback as inputs</li> <li>2. Reconfigure sales, marketing, and distribution to profitably deliver a greater variety of lower-volume SKUs to customers and consumers</li> </ol>	Medium	Low	Low
Increased resource shortages and commodity price volatility	<ol style="list-style-type: none"> <li>1. Lock in local supply sources of strategic commodities to de-risk operations and form local ecosystems</li> <li>2. Extend commodity sourcing from resource procurement to resource preservation and responsibility</li> <li>3. Invest in food, agricultural, and resource innovation to change the economics of packaged goods ingredients</li> </ol>	Low	Low	Low

Note: Awareness, speed of execution, and completeness of actions are based on Deloitte experiences and observations across the consumer packaged goods industry.

# All hands on deck now

**A** NUMBER of organizations have already made strides in preparing for and addressing these major changes in the consumer product landscape. However, even these companies should realize that a good compass—that is, setting a clear direction—is necessary but not sufficient. Given the multitude

and potential magnitude of these projected marketplace changes, speed is equally critical. The shifts are occurring quickly: We observe many environmental factors today that increase not only the probability of change, but also the speed at which we may see each of the undercurrents come to fruition.

**Figure 4. Factors suggesting rapid change**

Undercurrent	Drivers	Confidence	Time horizon
Unfulfilled economic recovery for core consumer segments	<ul style="list-style-type: none"> <li>The job market and income prospects among lower-income and middle-class consumers remain depressed, with low labor market participation rates, high unemployment rates, and low annual household income growth.</li> <li>The continued growth of the dollar store and discount grocery channels is being fueled by cost-conscious lower-income and middle-class consumers.</li> <li>Traditional packaged goods companies are continuing to target a primarily lower-income and middle-class consumer base.</li> </ul>	Medium	1 to 3 years
Health, wellness, and responsibility as the new basis of brand loyalty	<ul style="list-style-type: none"> <li>Consumers are becoming increasingly skeptical of large companies' values, and they link parent company values with individual brands within the portfolio.</li> <li>Consumers increasingly look at the lifetime impact products have on them, their family, and their community.</li> <li>Store brands and niche brands are taking market share from traditional national brands based on health, environmental, and social impact attributes.</li> <li>The continued growth of health and natural retailers is taking share from traditional grocery channels.</li> <li>Packaged food is increasingly viewed as a mechanism to promote nutrition as part of a healthy lifestyle. Traditional retailers are increasingly including health care outlets.</li> </ul>	High	3 to 5 years
Digitization of shopping and pervasive last-mile delivery	<ul style="list-style-type: none"> <li>Viable last-mile services in urban, suburban, and rural areas offering delivery at lower price points are proliferating.</li> <li>Competitors are emerging with new business models, including subscription and direct-to-consumer delivery.</li> <li>Consumers are growing more trusting of companies with their personal data, and they are embracing the value of context-driven marketing and recommendations.</li> <li>Consumers are using new, convenient payment options (for example, mobile payments) that enable the promotion or delivery of value-added services based on purchase history and location.</li> </ul>	High	1 to 3 years
Proliferation of product customization and personalization	<ul style="list-style-type: none"> <li>Consumers are expecting more variety, and are increasingly willing to pay more for customized products.</li> <li>Preferences and tastes are fragmenting due to diversity along several demographic attributes (for example, ethnicity/race, age, income).</li> <li>Competitors are emerging with new business models that embrace product customization.</li> <li>Advances in manufacturing technologies (such as flexible manufacturing, additive manufacturing, and 3D printing) are enabling customization at lower costs.</li> </ul>	Medium	3 to 5 years
Commodity price volatility and resource shortages	<ul style="list-style-type: none"> <li>Companies are becoming more exposed to risks driven by extreme climate events or disruptions in product supply.</li> <li>The availability of and access to clean water has become a greater constraint globally.</li> <li>Companies struggle to maintain margins when input costs increase, and product costs are highly influenced by commodity prices.</li> <li>Companies are seeking more vertical integration, including locking in local supply sources within countries and regions.</li> <li>Consumers are increasingly concerned about products' supply chain impact and environmental footprint.</li> </ul>	Medium	3 to 5 years

Note: Confidence and time horizon are based on Deloitte experiences and observations across the consumer packaged goods industry.

# Parting thoughts

**J**UST as sailors can't infallibly predict the weather, no one knows for certain what the future holds. But, as any good sailor knows, forethought and preparation are critical to a safe and successful journey. *In this rapidly evolving, low-growth, and margin-compressed environment, clear strategic direction and*

*coordinated efforts are not all that should be pursued. Speed of execution and completeness of action are just as important, if not more important, to consider.* Decisive action along the lines we have discussed could be key to helping your organization meet the challenges it may face in the journey to 2020 and beyond.

# Appendix A:

## The executive and senior manager perspective on consumer trends

**W**E surveyed 205 executives and senior managers in consumer-facing industries to ask: “What are the five most important areas where you would like to know more about US consumer behaviors and attitudes?” Across all surveyed industries, brand loyalty (47 percent) topped the list, followed by consumer willingness to pay higher prices (41 percent). The impact of the current economic situation on the consumer (38 percent), the impact of social influence on loyalty (37 percent), and the impact of technology on shopping and the changing digital landscape (37 percent) round out the top areas.<sup>40</sup>

When comparing the responses of consumer product, food and beverage, and retail executives and senior managers, we observed many significant trends (see figure 5). Note: The remaining 120 executives worked in other consumer-focused industries including commercial banking, travel, hospitality, automotive, and consumer electronics. First, driving greater brand loyalty is very important to each of the three groups of executives—revealing the ongoing tension between both consumer product brands and retailers.

Second, retailers seemed more focused on technology-related areas, such as social influence and digital marketing, than the consumer product respondents were. As a result, the latter could be overlooking the potential of technology. Third, understanding consumer preferences was considered more important by consumer product and food and beverage executives than by retailers. Fourth, consumer product manufacturers and retailers were more interested in better understanding retail channel preferences than were food and beverage executives, revealing areas where consumer product companies can help retailers with their consumer and cross-channel experience. And finally, economic impact was the most important to consumer product manufacturers of the three groups. While some differences in perspective are to be expected among these groups of executives, these differences reveal potential blind spots. For example, packaged goods executives seem to be lagging retailer executives in technology, and retailers may not be fully appreciating the impact of the changes in consumer preferences and demographics.

**Figure 5. Executive and senior management perspective on the top five areas on consumer behaviors and attitudes that they would like to know more about**

<b>Consumer product manufacturing executives</b> (n = 31)	<b>Food and beverage executives</b> (n = 22)	<b>Retail executives</b> (n = 32)
<ol style="list-style-type: none"> <li>1. Brand loyalty (What makes consumers loyal and why?) (55%)</li> <li>2. When and where are consumers willing to pay a higher price? (45%)</li> <li>3. Retail channel preferences and how they are evolving (39%)</li> <li>4. Impact of social influence on loyalty (39%)</li> <li>5. The impact of the current economic situation on the consumer (35%)</li> </ol>	<ol style="list-style-type: none"> <li>1. When and where are consumers willing to pay a higher price? (55%)</li> <li>2. The role and importance of traditional advertising (45%)</li> <li>3. Brand loyalty (What makes consumers loyal and why?) (45%)</li> <li>4. Importance of health and wellness to consumers (41%)</li> <li>5. Demographic differences between generations (41%)</li> </ol>	<ol style="list-style-type: none"> <li>1. Brand loyalty (What makes consumers loyal and why?) (53%)</li> <li>2. How to build loyalty with the changing technology landscape (41%)</li> <li>3. The impact of social influence on loyalty (41%)</li> <li>4. The impact of technology on shopping and the changing digital landscape (41%)</li> <li>5. Digital marketing ROI (34%) <i>tied with</i> Retail channel preferences and how they are evolving (34%)</li> </ol>

Legend for color coding:

Brand loyalty

Consumer preferences

The impact of the economy on consumers

All things technology

Retail channel preferences

Source: Deloitte Executive survey for insight on the consumer (n = 85), September 2013.

# Appendix B: Expanded definition of food and product safety

**C**ONSUMERS have expanded the definition of food and product safety to include attributes typically associated with health and wellness.<sup>41</sup> Elisabeth Hagen, senior advisor on food safety, Deloitte & Touche LLP (former undersecretary for food safety at the US Department of Agriculture), recently presented findings from consumer and social media listening research on food safety. When it comes to food safety and food companies, a majority of consumers were concerned about aspects such as safe packaging (75 percent) and accurate labeling (66 percent).<sup>42</sup> Not surprisingly, a substantial consumer segment also associated characteristics such as natural (33 percent) and organic (31 percent) with food safety. The consumer segments that were more likely to associate natural and organic with food safety include individuals or households with allergies, families with children, and 21–29-year-olds. A substantial majority of consumers were very concerned about what they are buying and eating, as well as where their food is coming from. For example, for 87 percent of consumers, clear labeling was a very important purchase driver for a given food product. Furthermore, almost 70 percent were more likely to buy brands that were actively communicating their commitment to food safety in a broader sense. Also, 50 percent of consumers were willing to pay more for a brand if it

communicates its commitment and efforts to improve food safety. And a majority wanted to learn more about ingredients, production processes, and where the food comes from.

Additionally, recent social media listening research indicated that when consumers talk about food safety in the United States, only 14 percent of the discussion is about basic food safety, while the rest is about a broader set of topics, such as health and wellness.<sup>43</sup> Within the health and wellness and food safety discussions, a significant number of posts were about transparency (8 million posts) and sustainability (2 million posts). Through social media listening, key issues identified within transparency were genetically modified foods (49 percent of total discussions), clear labeling in general (22 percent), and greater transparency about food additives (21 percent). Moreover, in our analysis of sample brands across industries on positive versus neutral versus negative sentiments for brands, the general discussions about brands across industries was 90 percent positive or neutral and only 10 percent negative. However, when it comes to food brands on the topic of food safety, almost 34 percent of the discussion was negative. The analysis of social media conversations further highlights the importance of the expanded definition of food safety to consumers as well as sheer negativity around it when it comes to food brands.

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# Acknowledgements

The authors would like to thank **Glenn Goldman** (Deloitte Consulting LLP), **Jacob Bruun-Jensen** (Deloitte Consulting LLP) and **Bernardo Silva** (Deloitte Consulting LLP) for their significant contributions to the research and writing. We would also like to acknowledge the contributions of **Eva Dreger** (Deloitte Consulting LLP), **Julie Finn** (Deloitte Services LP), **Susan K. Hogan** (Deloitte Services LP), **Aijaz Hussain** (Deloitte Support Services India Pvt. Ltd), **Michael Jeschke** (Deloitte Consulting LLP), **Shweta Joshi** (Deloitte Support Services India Pvt. Ltd), **Junko Kaji** (Deloitte Services LP), **Erin Kruse** (Deloitte Consulting LLP), **Robert Libbey** (Deloitte Services LP), **Jarrod Phipps** (Deloitte Consulting LLP), **Anup Raju** (Deloitte Support Services India Pvt. Ltd), **Aditi Rao** (Deloitte Support Services India Pvt. Ltd), **Jack Ringquist** (Deloitte Consulting LLP), **Ben Stiller** (Deloitte Consulting LLP), **Alok Ranjan** (Deloitte Support Services India Pvt. Ltd), and **Neelakantan Subramanian** (Deloitte Support Services India Pvt. Ltd).





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