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THE BATTLE FOR BRANDS IN A WORLD OF PRIVATE LABELS

BY PAT CONROY AND ANUPAM NARULA

> ILLUSTRATION BY JOHN UELAND

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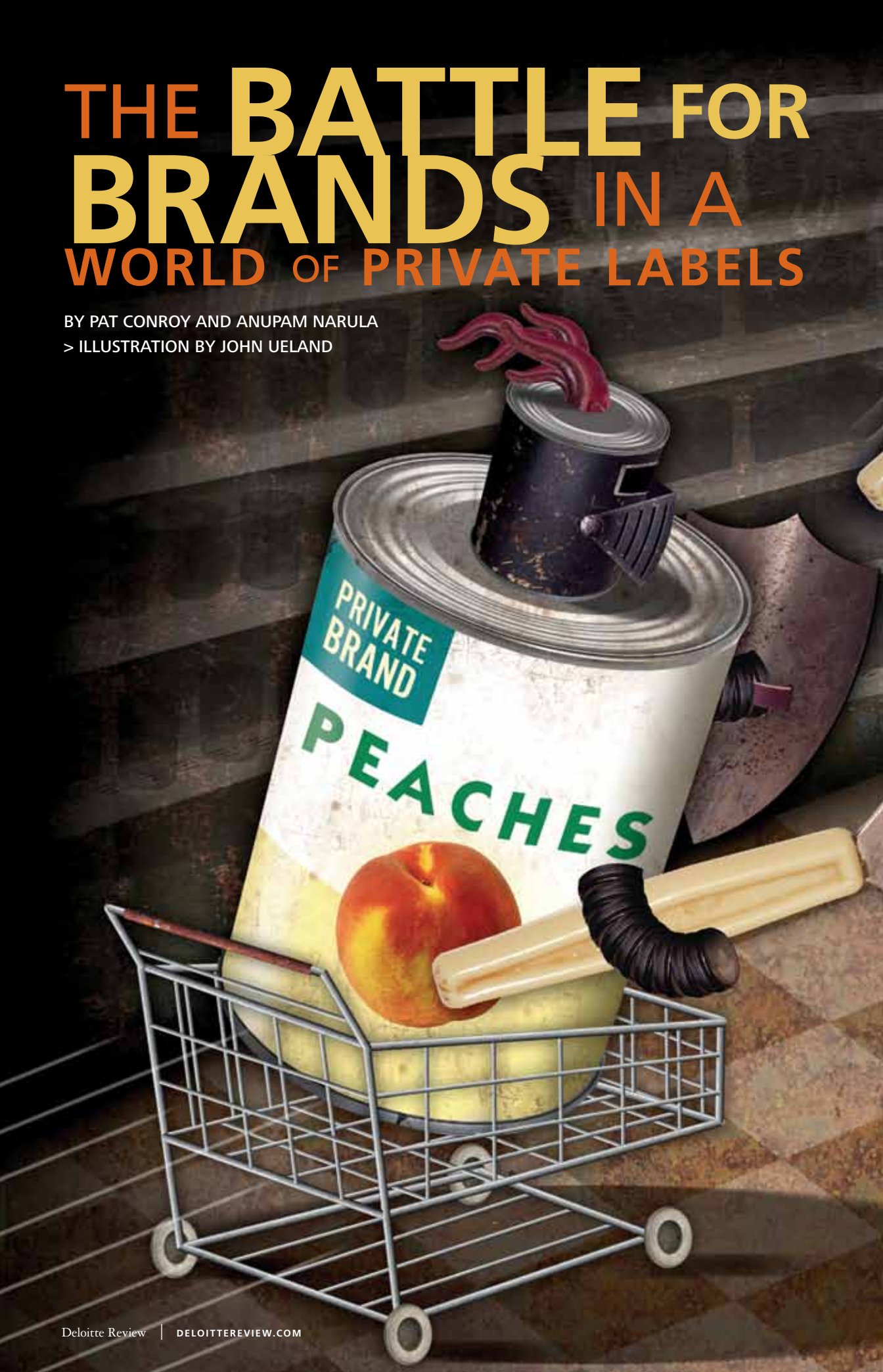

Janet GLANCES AT THE ITEMS IN HER SHOPPING CART AND THEN AT HER GROCERY LIST, REALIZING THAT THIS IS GOING TO BE AN EXPENSIVE TRIP. SHE WONDERS HOW MUCH SHE COULD SAVE BY REPLACING MORE OF HER FAMILY'S PREFERRED NATIONAL BRANDS WITH THE STORE BRANDS. AFTER ALL, NOBODY NOTICED WHEN SHE SWITCHED THE CANNED VEGETABLES, PASTA, AND ICE CREAM. HER DAUGHTERS' BREAKFASTING OBJECTIONS TO STORE BRAND CEREALS SUBSIDED BY THE THIRD MORNING. SIMILARLY, HER HUSBAND RAISED HIS EYEBROWS WHEN SHE BROUGHT HOME STORE BRAND

ketchup, sliced cheese and soft drinks, only to raise them even further when she described the price difference. Nonetheless, the family held the line in the soft drink aisle. "I know times are tough," said her husband, "but surely there's another way to save." Now, Janet only purchases national brand soft drinks during sales or in bulk.

In the next aisle, Janet's neighbor David shuffles by. "What do you think of those store brand paper towels?" she asks.

"It's all from the same tree and costs less. My family can't tell the difference."

"Probably true," says Janet as she adds store brand paper towels to her cart. "I am open to saving a few bucks – it adds up quickly. The feeling that I am paying for advertising when I buy a national brand is tough to stomach in this economy."

"My kids actually prefer the store brand frozen pizza. It's funny because my mother always avoided store brands; if she could see us using these paper towels now …" David shook his head and they both laughed.[1]

THE BATTLE FOR BRAND LOYALTY

Consumers like Janet and David are emblematic of store brands (or private label goods) gaining market share at the expense of national brands. Between 2006 and 2009, market share rose across 74 percent of products in the personal care, household goods and food and beverage categories in the United States, according to Information Resources, Inc.[2] In 2009, store brands represented nearly 18 percent of consumer packaged goods spending and over 23 percent of CPG products sold.[3]

Many consumers increasingly sense a diminishing discrepancy between the quality of national brands and their private label counterparts as retailers sharpen their focus on store brands and garner loyalty, and consumer product companies cede connections to retailers and increasingly knowledgeable customers. Private labels represent 20 percent of grocery store and 18 percent of supercenter sales.[4] Furthermore, store brand products were 31 percent cheaper across product categories than their national brand counterparts.[5] Store brands are not just a recession related phenomenon – U.S. store brand sales continue to grow over the long run despite improving economic conditions.[6]

The following recommendations may help consumer product companies to navigate this changing environment:[7]

- Be a brand that the retailer cannot be.
- Be irreplaceable.
- Shed homogeneity.

- Create a retailer-specific product portfolio.
- Make me-too strategies an onerous path.
- Stop reckless promotions.
- Leave retailers bricked and mortared.

For retailers, the challenge is to anticipate and counter these consumer product company actions.

HOW PRIVATE LABEL GOODS ARE CHANGING

Generics no more

Store brands no longer suffer the stigma of inferior quality among most American consumers. Supporting this notion, *Consumer Reports* compared store brand and national brand products across 29 food categories of which the national brand was the winner in only six. Furthermore, the tested store brands cost 27 percent less on average than the national brands.[8]

Reinforcing this perception of improved quality, grocery and mass merchandise retailers have created multi-tiered store brands in many product categories that include premium products which, in some cases, cost more than their national brand competitors. Furthermore, in a recent survey a whopping 89 percent of participating senior leaders at consumer product companies and retailers think consumers are more open to trying private label products than they were two years ago.

MOUNTING EVIDENCE SUGGESTS THAT NATIONAL BRANDS ARE LOSING THEIR HOLD ON THE CONSUMER. AS A RESULT, CONSUMERS ARE MORE WILLING TO TRY NEW AND DIFFERENT BRANDS AND BELIEVE THEY HAVE MORE CONVENIENT ACCESS TO A WIDER ARRAY OF PRODUCT CHOICES.

A sharpened focus on private labels

Retailers, drawn by the prospect of bolstered profits and customer loyalty, are increasingly investing in product portfolios and brand building to capture the most demanding consumers. Many U.S. retailers are following the precedent set in 1998 by Tesco, a European grocer and mass merchandiser that began segmenting

its customers and developing brands that cater to each group. For example, Target, a U.S.-based mass merchandiser, offers a broad portfolio of private labels—Market Pantry, up & up and Archer Farms, for example—each of which caters to a different consumer group.

Increasingly, retailers are taking cues from national brands when managing their portfolios of private labels, including refreshing and homogenizing packaging. They are also applying more advanced marketing strategies and hiring brand managers to complement their buyers and category managers.

Some retailers are also rationalizing the number of traditional national brands they offer, often to make space for store brands.[10] Some people cite the selective return of secondary and tertiary national brands and argue that retailers are overstuffing their shelves with private labels. Others consider the significantly higher market share of store brands in Europe and say that U.S. retailers have a long way to go.

Furthermore, Costco Wholesale Corporation, a U.S.-based warehouse club operator, has blurred the line between national brands and private labels using premium offerings and co-branding strategies with the likes of Starbucks, Quaker Oats and Tyson.[11] Surprisingly, both consumer product and retail executives tend to believe that co-branding between retailers and traditional national brands is a win-win situation.

IN AN INCREASINGLY TRANSPARENT WORLD, THE MOST IMPORTANT AND DISCERNING CONSUMERS—THE ONES WITH STRONG OPINIONS ON WHICH SALTY SNACKS TASTE BEST AND WHICH HOUSEHOLD CLEANERS ARE MOST EFFECTIVE—ARE TWICE AS LIKELY TO HAVE A FAVORABLE IMPRESSION OF STORE BRAND QUALITY.

Losing the consumer connection

Mounting evidence suggests that national brands are losing their hold on the consumer. As a result, consumers are more willing to try new and different brands and believe they have more convenient access to a wider array of product choices.[12]

Storefronts also constitute a significant advantage for retailers relative to their national brand competition. Stores let retailers collect cross-category sales data, determine product placement, and influence on-site consumers. Retailers use point-

of-sale transaction data at a granular level to analyze and understand consumers' preferences between national and store brands, and 94 percent of surveyed senior leaders at consumer product and retail companies agree that retailers can improve the way they use point-of-sale data to promote store brands.[13]

In addition, the reach of traditional advertising is diminishing, and retailers have strengthened their interactions with consumers. While traditional advertising still has its role, many consumers, when asked, believe that it is easy for them to avoid marketing efforts.[14] Retailers have increased their advertising spend, redesigned product displays to create favorable impressions of their products, and printed targeted coupons at checkout.

Transparency

Thanks to the proliferation of digital technology, consumers have become increasingly empowered with comparative information about products. Consumers have easy access to weekly retailer circulars and coupons and a variety of online purchasing and comparison tools such as Amazon reviews, *Consumer Reports*, Frucall.com, and Alice.com. This transparency makes brands less relevant in buying decisions compared to other aspects of the product.[15] As a result, some consumers are trading down to lower-priced products, demonstrating reduced brand loyalty, and increasing their use of private label products across a wide array of product categories.

While transparency is still in the early stages of manifesting itself in the consumer product and retail sectors, the challenge is clear. Brand advocates—discerning consumers who disproportionately spend money on and interact with a favorite brand—are more likely to recommend products, read reviews and offer feedback.[16] So, in an increasingly transparent world, the most important and discerning consumers—the ones with strong opinions on which salty snacks taste best and which household cleaners are most effective—are twice as likely to have a favorable impression of store brand quality.[17]

WILL CONSUMERS RETURN WHEN THE ECONOMY IMPROVES?

The recent recession accelerated consumers' movement toward store brands. While some consumers migrated back to national brands after prior recessions, a majority stayed with the store brand in recent U.S. recoveries.[18] As the economy improves, according to a recent survey, only 22 percent of participating consumer product executives agreed or strongly agreed that a majority of the consumers who switched to store brands in recent years will switch back to national brands.[19] Not surprisingly, participating retail executives are more optimistic about their store brands' ability to stick.

As expected, private labels perform countercyclically to business cycles in the U.S. and Europe. During recessions, store brand sales tend to increase more rapidly; however, they remain stable or contract slightly in good times.[20] However, as the economy improves, the migration back to national brands lags and is less than the initial gain. In the long run, given the promising track record of store brand performance, a continuation of this trend would be unsurprising.

All of this begs an important question for consumer product companies: how can they compete effectively against store brands? Seven principles may help national brands in their efforts to bolster their competitiveness in the face of mounting pressures from private labels.

1. **Be a brand that the retailer cannot be.**

National brands should develop attributes that positively influence consumer buying behavior and are difficult for retailers to replicate. Leadership in exclusivity, product safety, social causes, innovation and sustainability can help build distinctive advantages that translate into competitive advantages over retailers and other national brands. Consumer product and retail executives see innovation and exclusivity as brand associations that consumers value most besides price and product performance.[21]

For each of its products, a national brand should assess the value, brand and relationship equity and decide which of these attributes will be difficult to replicate.[22] By aligning with widely appreciated social causes, a national brand may be able to foster brand and relationship equity. Targeted marketing efforts, using a mix of both new and traditional media, can also help communicate values and attributes to consumers.

For example, Procter & Gamble has specific strategies pertaining to social responsibility, operations and sustainable product innovation. Since July 2007, P&G's policy of developing and marketing sustainable innovations and products has generated sales of $13.1 billion.[23] P&G also facilitates donations for the causes it supports. P&G donates one dose of vaccine for each pack of Pampers that is purchased as part of the "One Pack=One Vaccine" campaign.[24]

2. **Be irreplaceable.**

Consumer product companies should create destination brands, which share several characteristics. First, they are products that consumers often expect to see at the store and will change shopping patterns to find and purchase. Second, replacing destination brands with substitutes leaves customers disappointed. As a result, if customers do not find the product at a store, they will rarely settle for another brand. Third, they are products that offer high value to the consumer, regardless of how their price points compare to the rest of the product category. Fourth, these

are products that help build loyalty. For retailers, these products help build store loyalty whether or not they are exclusive to the retailer. For consumer product companies, these products have a loyal consumer following that looks across channels for the product. Finally, destination products use claims, certifications and supporting data that are difficult to replicate.

Consumer product and retail managers, when surveyed, believe that 71 percent of consumers will switch stores if their preferred brand is no longer available at a retailer, and 62 percent of consumers make special trips to retailers just to purchase their favorite store brand.[25]

Consumer product companies can learn from retailers like Trader Joe's – a growing specialty grocery store in the United States held by a trust of one of the founders of the German grocer ALDI. Trader Joe's appeals to both value-seeking and health-conscious consumers with a unique product portfolio, some 80 percent of which comprise private labels and, in some cases, destination brands in their own right.[26]

3. Shed homogeneity.

National brands might identify regional or local variations in tastes and preferences and use them to create products. While for national brands a movement toward local variants runs counter to conventional wisdom related to economies of scale, local variants provide an opportunity to appeal to consumers in a more focused way than homogenous store brands.[27] In a recent survey, a majority of the participating retail managers agreed that national brands would increase market share if they create local variations that appeal to consumers in targeted locations.[28] Interestingly, participating consumer product managers showed less support for this notion when compared to retail managers, suggesting they may be missing an opportunity.

CONSUMER PRODUCT AND RETAIL MANAGERS, WHEN SURVEYED, BELIEVE THAT 71 PERCENT OF CONSUMERS WILL SWITCH STORES IF THEIR PREFERRED BRAND IS NO LONGER AVAILABLE AT A RETAILER, AND 62 PERCENT OF CONSUMERS MAKE SPECIAL TRIPS TO RETAILERS JUST TO PURCHASE THEIR FAVORITE STORE BRAND.

National brands can also look to deliver personalized customer experiences to compete against homogeneous store brands. For example, Mars, Inc. offers M&M chocolate candies with personalized colors, text and logos.

Meijer, a regional U.S. grocery and mass merchandiser, uses localization to compete against national consumer product and store brands from larger retailers. Meijer created a portfolio of premium Gold line products that are positioned as regional specialties that have a "distinctive history, heritage, or story" often tied to a specific region. Products like Michigan Apple Cheesecake, for example, have a unique story to tell about the origin of the ingredients or recipe.[29]

4. **Create retailer-specific product portfolios that surround private labels.**

As retailers develop multi-tiered product portfolios tailored to their consumers, national brands can develop a retailer-specific strategy to compete against low-end, mid-range and premium products, which could include manufacturing private label goods. Retailers increasingly deploy thoroughly researched store strategies for their private label brands. Such strategies sometimes result in SKU rationalization that predominantly impacts second tier national brands.[30] National brands that survive rationalization will be pitted against a bevy of private label products. From a price-sensitivity perspective, removing secondary national brands helps private labels and hurts primary national brands.[31]

"IN THE BATTLE FOR THE CUSTOMER, STORE BRANDS ARE WINNING. UNLESS MANUFACTURERS CAN CREATE A CLEAR REASON IN THE CONSUMER'S MIND THAT THE BRAND IS MORE IMPORTANT THAN THE STORE WHEN MAKING THEIR CHOICES, THE MANUFACTURERS ARE BOUND TO LOSE MARGIN TO THE STORE. DISCOUNTS DO NOT DO THIS. COHERENT BRANDING STRATEGIES DO."

National brands can develop granular, heterogeneous strategies that address threats from competing retailers. Their owners need to identify their cost and quality constraints before developing competitive strategies. At the low end, national brands can create differentiated fighter brands or manufacture private labels. A mid-range product strategy could require constant product innovation, packaging changes, price positioning and targeted promotions. In order to compete in the premium market, national brands could focus on well-communicated product

performance claims driven by innovation and positive brand associations.[32]

5. Make me-too strategies an onerous path for retailers.

"Me-too" private label products with similar look and perceived quality as the national brand allow for easy side-by-side comparisons at the store. All too often, retailers are able to take national brand products to third party manufacturers, or even the branded company, and develop a private label version with similar packaging. While consumer product and retail executives tend to believe that consumer brand companies frequently refresh their packaging and products to compromise "me-too" store brands, in a recent survey, a majority of participating consumer product executives agreed that retailers are able to quickly create "me-too" store brand products after the launch of national brands.[33]

Would your brand be able to stand the test of a retailer promotion to buy the national brand and get the store brand for free? National brands that tend to pass this private label trial test have a number of characteristics. First, they have an aggressive cadence for product innovation, including frequently refreshed packaging and product obsolescence that requires retailers and private label manufacturers to continue to invest. Second, they maintain a pipeline of new product launches using unique R&D and supply chain capabilities. Third, they protect and defend the broad range of intellectual property associated with their brands, including litigation against private label manufacturers on product claims.

6. Stop reckless promotions.

Many consumers are savvy when it comes to promoting branded goods. Excessive promotions train the consumer to wait for deals and can shift the focus from product attributes to prices. Consequently, national brands should pull back price-related promotions that can decrease consumers' reference price points. When developing a promotions strategy, consumer product companies should more actively consider non-price-related promotions. In a recent survey, most participating consumer product and retail executives agreed that consumers have become more price sensitive in the last two years due to national brand promotions.[34] While short-term promotions can increase sales, they can damage brand equity in the long term and narrow the premium between national brands and private labels. According to Professors Leonard Lodish and Carl Mela, brands were less able to command a pricing premium, and private label products gained market share, between 2003 and 2005. Their analysis shows that some of this deterioration is self-inflicted by short-term promotion strategies where brand managers over invest in price promotions at the expense of advertising, product development and distribution strategy.[35]

Furthermore, Mela states that: "In the battle for the customer, store brands are winning. Unless manufacturers can create a clear reason in the consumer's mind

that the brand is more important than the store when making their choices, the manufacturers are bound to lose margin to the store. Discounts do not do this. Coherent branding strategies do."[36]

Promotions during a recession require a balancing act. While overpromotion potentially damages brand equity, a lack of promotional activity could take an established brand out of consideration. With genuinely new products, short-term promotions to generate trial have the potential to generate long-term repeat purchases.

7. Leave retailers bricked and mortared.

While consumer product companies are actively experimenting with direct-to-consumer options, they have taken a slower approach to online sales than retailers, perhaps because of potential conflicts with existing channels. In a recent survey, participating retail executives, compared to the participating consumer product executives, tended to be more bullish on recent advances in mobile digital technology that allow product and price comparisons.[37] Moreover, these retail executives are more likely to expect significant sales growth from both the retailer's online presence and the consumer product company's direct-to-consumer efforts. Not only can direct-to-consumer be a path for core products, but it can also be a home for niche product variants that the retailers do not stock. Retailer SKU rationalization presents an opportunity for national brands to shift some consumers to their online channel for lower-volume SKUs.

Across the shopping lifecycle—research, selection, purchase, receipt, use and return—consumer product companies, online-only retailers, multi-channel retailers, and third-party comparison tools each strive to play a role. While physical or multi-channel retailers may be preferred at some points of the shopping experience, consumer product companies should try to play a primary and secondary role at each step because consumers have differing shopping preferences across product categories.

For research, selection and purchase, a variety of emerging and established online comparison and purchasing tools allow consumers to compare product performance and price across branded and private label goods. Consumer product companies should consider how they can become a venue for comparisons, like Progressive Casualty Insurance Company's online automobile insurance quotes that include competitor rates. In cases where the branded products rank favorably, they should be directed to an online or store option.

For repeat purchases, consumer product companies should consider how they can provide automated replenishment, like Gillette's online store that allows consumers to order recurring replacement of razorblades. Furthermore, consumer product companies' online presence can offer always-in-stock service.

BACK TO JANET

Janet's daughters helped her unload the groceries: the ice cream, sliced cheese and then the canned vegetables, pasta and cereal.

While the mix of store brands among her groceries and household products had increased, she would always use the laundry detergent her mother used; clean clothes have that smell she had come to expect, and other laundry detergents just don't clean as well. Likewise with the dishwashing detergent, which she prefers to the store brands because she uses less and she appreciates the company's contributions to charities. Similarly, national brand juice boxes still reassure her that she's providing quality for her children and avoid lunchtime stigma associated with not having a familiar brand in her daughters' lunch boxes. The price difference between private label peanut butter and national brands was less than a dime, so she stuck with the national brand. Most of her remaining purchases were store brands. She doesn't miss the national brands in those product categories as much as she likes saving money.

Janet's husband came home with an I-just-got-promoted smile. A bigger paycheck was a significant help after a couple of tough years. She will continue to compare products from national and store brands, but she will ultimately strike a judicious balance between quality and price.

CONSUMER PRODUCT COMPANIES SHOULD CONSIDER HOW THEY CAN BECOME A VENUE FOR COMPARISONS, LIKE PROGRESSIVE CASUALTY INSURANCE COMPANY'S ONLINE AUTOMOBILE INSURANCE QUOTES THAT INCLUDE COMPETITOR RATES.

ARE YOU READY FOR BATTLE IN A WORLD OF PRIVATE LABEL GOODS?

While, in a recent survey, participating retail and consumer product executives indicated that they expect the market share of store brands to increase in the next two years, we believe national branded goods still have an opportunity to maintain and gain market share.[38] To compete in a world of private label goods, developing clearly differentiated national brands, creating unique products, and renouncing reckless promotions are table stakes. Furthermore, national brands should develop a product portfolio that reflects each retailer's consumer base, that

includes localized products and reflects quickly cadenced improvements to packaging and product performance. Finally, national brands should revisit and accelerate the pace of their direct-to-consumer efforts.

Underlying each of these suggested strategies is the need to address the diminishing disparity between national and store brands through a renewed focus on differentiation.

Pat Conroy *is vice chairman and U.S. Consumer Products Leader, Deloitte LLP.*

Anupam Narula *is a senior research manager with Deloitte Research, Deloitte Services LP*

Endnotes

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