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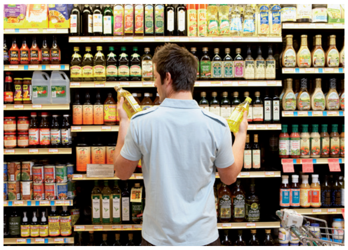
Saving, scrimping, and . . . splurging? New insights into consumer behavior

Consumer Packaged Goods March 2016



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Saving, scrimping, and . . . splurging? New insights into consumer behavior

Our global survey of more than 22,000 consumers highlights recent shifts in buying behaviors, which have important implications for retailers and packaged-goods companies alike.

For many people around the world, the economic downturn isn't a thing of the past but rather a persistent everyday reality. Money remains a constant worry—and fear of yet another downturn looms large, driven by political upheaval and financial-market volatility. More than 50 percent of consumers are afraid they or someone in their household will lose a job in the coming year. More than a quarter are living paycheck to paycheck. No surprise, then, that they are delaying purchases, clipping coupons, and shopping around for the best deals.

That said, many other consumers are enjoying financial stability and maintaining a brighter outlook. More than 30 percent are optimistic about their household's financial future. The majority of consumers in Mainland China and North America aren't worried about job loss. About one-third of shoppers around the world are staying loyal to their favorite brands instead of downgrading to cheaper options, and some are even splurging on certain types of purchases.

These are among the findings of our first-ever global "consumer sentiment" survey, which encompassed more than 22,000 respondents from 26 countries worldwide (see sidebar, "Our survey methodology," page 4). Our aim was to understand how consumers feel about their financial prospects and how these sentiments are affecting their buying behavior. Of course, consumer attitudes and behaviors can differ markedly across markets, and we will present country- and region-specific results in more detail in forthcoming articles.[1] In this article, we summarize broad global trends and high-level insights from the survey. These insights have crucial implications for consumer-goods companies and retailers as they seek to meet consumers' ever-changing needs and preferences. (For more on global consumption growth, see McKinsey Global Institute's *Urban world: Global consumer groups to watch*, forthcoming on McKinsey.com.)

Some are cautious, others are more confident

In general, consumers are making cautious financial decisions. After all, 28 percent of survey respondents said they are finding it harder to make ends meet than they did a year ago, and 26 percent said they live paycheck to paycheck (Exhibit 1). Approximately one-third agreed that their precarious financial situation was causing them to delay purchases and cut back on spending.

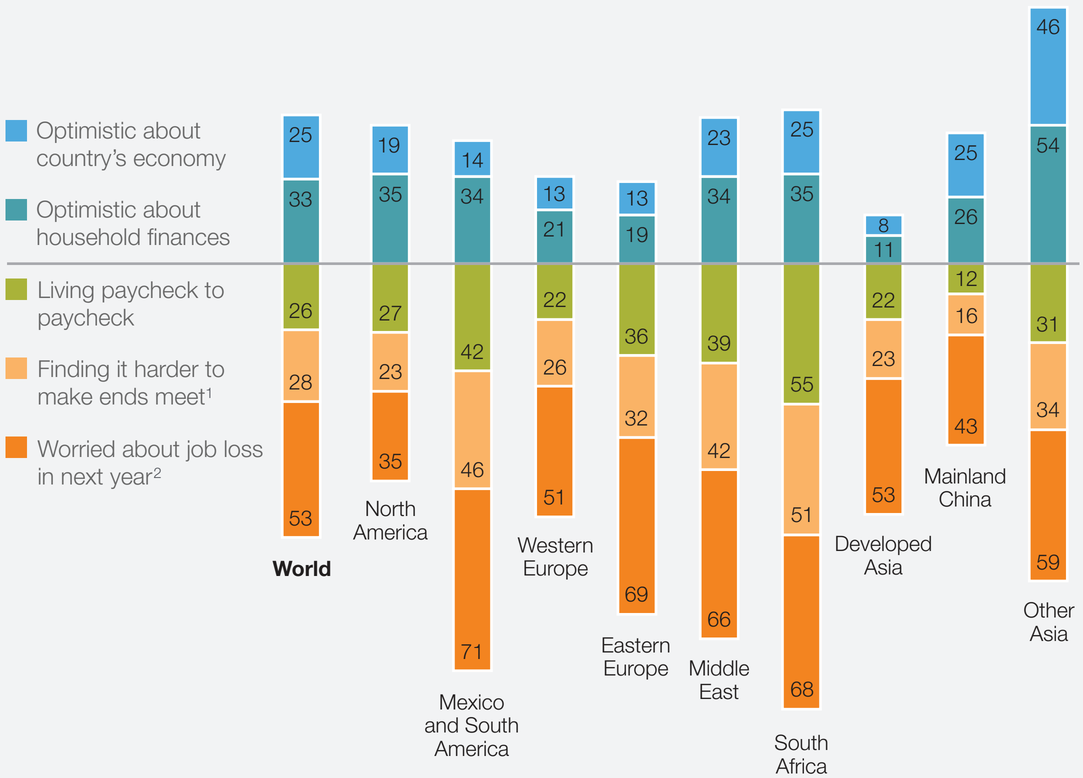
This sense of financial instability was more pervasive in emerging markets than in developed countries. Worries about job loss were particularly acute in Mexico and South America, affecting 71 percent of survey respondents. Most North Americans and Western Europeans, on the other hand, did not feel as pinched—fewer of them said they are delaying purchases or curbing their spending. In North America, 65 percent expressed no concern about losing their job. Consumers in Mainland China also felt more secure in their employment, with 57 percent saying they're not worried about job loss.

Would higher incomes spur consumers everywhere to loosen their purse strings? Somewhat. Consumers said that if their incomes were to rise by 10 percent, they'd spend about one-third of that extra money; the rest would go into savings and

Exhibit 1

Globally, more than half of consumers are worried about job loss; one-third are optimistic about their finances.

Consumer sentiment, 2015, people who "agree" or "strongly agree," %



Note: North America includes Canada and the United States; South America includes Brazil, Colombia, and Peru; Western Europe includes France, Germany, Italy, and the United Kingdom; Eastern Europe includes Poland and Russia; Middle East includes Kuwait, Qatar, Saudi Arabia, Turkey, and the United Arab Emirates; Developed Asia includes Australia, Japan, South Korea, and Taiwan; Other Asia includes India, Indonesia, and Thailand.

[1]Compared with 12 months previously.
[2]Worried that "I or a member of my household" will lose a job in next year.

Source: McKinsey Global Consumer Sentiment Survey, 2016

toward paying off debt. Consumers in Mainland China seem to be the least conservative, saying they'd spend 46 percent of any additional income—more than double the 21 percent that North American consumers said they'd spend.

Among consumers who said they'd spend a portion of their extra income, most—60 percent—would buy everyday necessities such as food and household items. More than half of these respondents said they'd also allocate some of the money toward clothes and vacations. Slightly more than 40 percent would spend some of their money on entertainment and on electronics.

Five truths about today's consumers

The survey responses brought to light not just regional differences in consumer sentiment but

Our survey methodology

The online survey was in the field from September 3 to 27, 2015, and garnered responses from at least 1,000 consumers in each of 21 countries, plus another 1,000 consumers across the Middle East and 250 consumers in Taiwan. Because the survey was administered online, the sample largely reflects the characteristics of the typical online population—younger, urban, and more affluent.

For the purposes of our analysis, we grouped the countries as follows: North America (Canada and the United States), Mexico and South America (Brazil, Colombia, and Peru), Western Europe (France, Germany, Italy, and the United Kingdom), Eastern Europe (Poland and Russia), the Middle East (Kuwait, Qatar, Saudi Arabia, Turkey, and the United Arab Emirates), South Africa, and Asia–Pacific. We further divided Asia–Pacific into three subregions: developed Asia (Australia, Japan, South Korea, and Taiwan), Mainland China, and "other Asia" (India, Indonesia, and Thailand).

The country results are weighted by age based on census data and weighted by income based on panel data. The category-specific results are weighted by purchase incidence. The weighting of region- and country-specific data aligns with the procedures used by the McKinsey Global Institute. In particular, responses to survey questions on consumer confidence are weighted according to the size of the consuming class; responses to questions on consumer behavior are weighted according to both the size and per capita consumption of the consuming class.

also a set of behavioral shifts among consumers worldwide. Some of these shifts are intuitive; others less so. Collectively, they underscore the challenges and opportunities that consumer-focused companies will face in the near term. The following five truths provide a fairly nuanced picture of today's consumers:

1. They proactively search for savings.

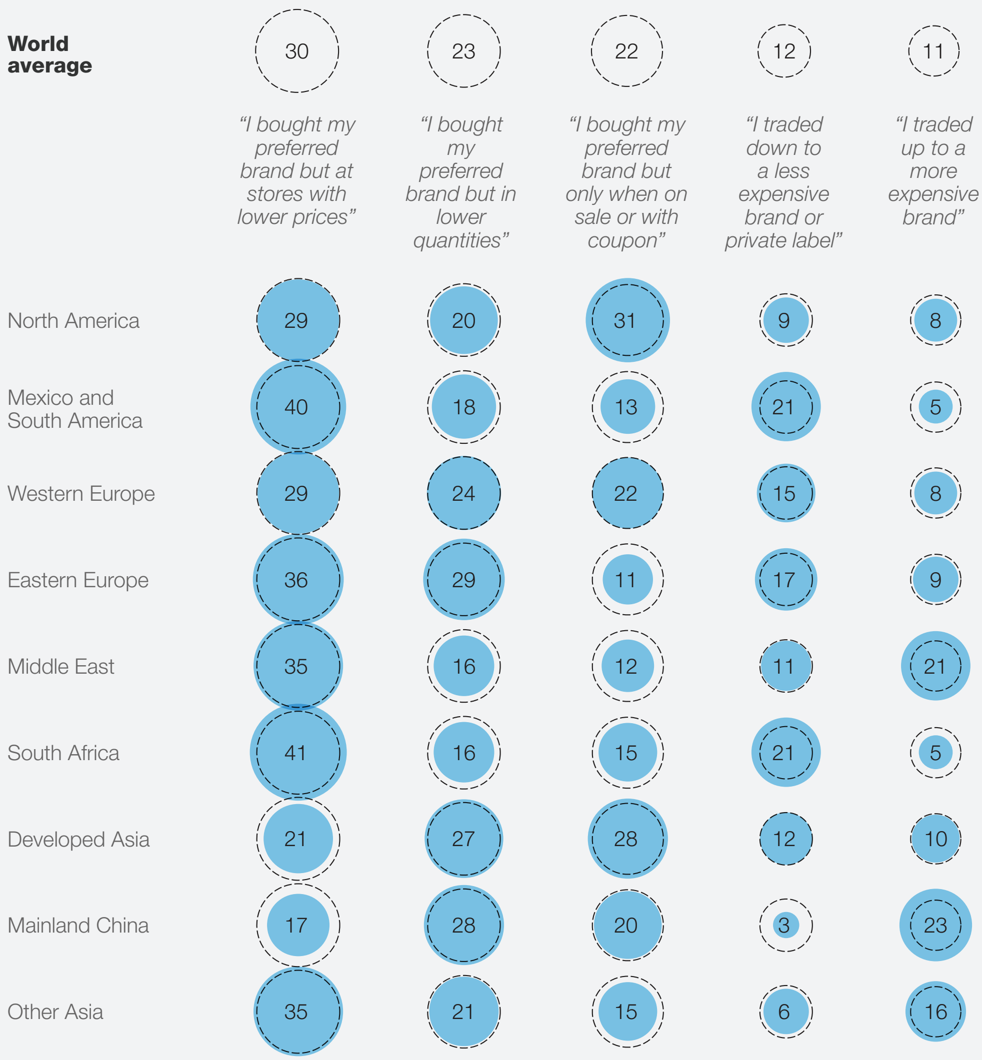
Consumers are reducing their spending in a variety of ways. Forty-four percent agreed that they're "increasingly looking for ways to save money." (In some countries, including Brazil and South Africa, more than 70 percent of respondents agreed with that statement.) In past years, a consumer may have engaged in only one or two belt-tightening behaviors such as comparing prices, seeking out sales and promotions, using coupons or loyalty cards more often, shopping at several stores to find better deals, or buying more products in bulk. Today, frugal consumers go out of their way to do almost all of those things. In addition, many are changing their eating habits—in particular, eating at home instead of eating out, or cooking from scratch more often.

2. They are brand-loyal . . . but only if the price is right.

Fifty-eight percent of survey respondents said they've modified their buying behavior when it comes to their favorite brands. The trend is particularly pronounced in South Africa and Asia, where three out of four consumers said they've changed their buying behavior. Most consumers haven't abandoned their preferred brands but are watching their budgets more closely: shopping around to find retailers that sell these brands at lower prices, buying only with discount coupons, waiting until the brands are on sale, or purchasing in smaller quantities (Exhibit 2).

Exhibit 2 **Consumers are being frugal while staying loyal to their preferred brands.**

Behavioral shifts in the past year among those who changed buying behavior,[1]
2015, weighted average for categories, %



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[1]Multiple answers possible.

Source: McKinsey Global Consumer Sentiment Survey, 2016

3. Once they 'trade down,' they might not go back.

Only 12 percent of consumers reported trading down—that is, buying cheaper brands or private-label products instead of their preferred brands. The most vulnerable categories (those with the highest trade-down rates) were bottled water and household cleaning supplies, perhaps indicating that branded products in these categories haven't differentiated themselves enough and thus don't stand out in the minds of consumers.

Among consumers who traded down, 45 percent opted for private-label products. And most down-traders don't regret their decision; they find they are satisfied with the less-expensive options. Indeed, 69 percent of down-traders in this survey said they intend to stick with the less-expensive options and don't intend to return to the brand they bought previously. However, that satisfaction isn't universal: in India, the Middle East, Poland, South Africa, and Turkey, down-traders said they desire to go back to the more expensive brand they used in the past. This suggests that value brands and private-label products in these countries still have much room to improve with respect to quality. It is perhaps also a testament to the powerful allure of aspirational brands for emerging-market consumers.

4. They are selective splurgers.

Trading down is only part of the story, though. As Exhibit 2 shows, the percentage of consumers who traded down is almost equivalent to the percentage who did the opposite: traded up. Eleven percent of consumers decided to upgrade their purchases in certain categories. In aggregate, the world's consumers appear to be "rebalancing the portfolio"—spending less in categories where they don't favor any particular brand, and spending more in others. Cosmetics and wine had the highest trade-up rates (Exhibit 3), suggesting that higher-end brands in these categories were able to persuade consumers that their products are worth the price premium.

Trade-up rates varied by geographic region and by category. Mainland Chinese consumers had the highest trade-up rate (23 percent) both in Asia and globally.[2] Forty-four percent of Chinese up-traders said they traded up in the cosmetics category.

5. They shop across channels.

Another important change in spending habits has to do with *where* people shop. Consumers claimed to have shifted a considerable fraction of their spending toward online and discount channels. The magnitude of these perceived channel shifts differs by region, with Mainland China leading the online migration: Chinese consumers said they shifted 62 percent of their spending to online pure plays and 55 percent to online grocers.

Implications for consumer companies

In light of these new consumer behaviors, what actions should consumer-goods companies and retailers take? How can they best position themselves for future success? In our view, they would do well to consider the following imperatives, each of which addresses one or more of the behaviors discussed above. Although the specifics and nuances of execution will vary for each market, we believe these imperatives are broadly applicable everywhere.

At every price point, think 'value for money.' With many consumers seeking savings opportunities, brands must give consumers solid reasons to choose their product over lower-priced alternatives. That means emphasizing not just the emotional attributes of a product but its functional benefits as well: reminding and reassuring shoppers about the particular features that make the product worth its price. They need to articulate and communicate a clear value proposition that differentiates them from the competition and that resonates with consumers. Products don't necessarily have to be in the lowest price tier, but any price premium needs to be explicitly linked to well-defined benefits. Consider the success of salon-quality hair-care

Exhibit 3 **Cosmetics, wine, and fresh produce were among the categories with the highest trade-up rates.**

Trade-off rates for selected categories[1] in past year among those who changed buying behavior, 2015, %

Note: North America includes Canada and the United States; South America includes Brazil, Colombia, and Peru; Western Europe includes France, Germany, Italy, and the United Kingdom; Eastern Europe includes Poland and Russia; Middle East includes Kuwait, Qatar, Saudi Arabia, Turkey, and the United Arab Emirates; Developed Asia includes Australia, Japan, South Korea, and Taiwan; Other Asia includes India, Indonesia, and Thailand.

[1]The survey results include trade-off data for more than 20 product categories.

Source: McKinsey Global Consumer Sentiment Survey, 2016 brands in the US market: they've been able to persuade consumers that using their products is a credible substitute for getting their hair done at a beauty salon. Consumers therefore feel they're getting good value for money, even though the salon-quality brand might be twice as expensive as their old shampoo brand.

Invest in advanced revenue-growth-management (RGM) capabilities. Through investments in cutting-edge RGM solutions and analytical talent, leading companies arrive at data-driven answers to critical questions such as: What role does each brand and each SKU play in the assortment? How, if at all, does that role differ by channel and by geographic region? Which promotions are most effective and why? Based on these insights, companies then devise granular strategies for their brands, portfolio, pricing, and promotions—and refine these strategies for each channel, customer segment, and geographic region.[3] For instance, advanced RGM analytics helped a European consumer-goods company pinpoint which SKUs were selling well in which retail formats, and which SKUs it should either add or omit from the assortment based on consumer preferences. The changes to its retailer-specific assortments and planograms yielded a double-digit sales improvement in a low-growth category.[4]

Be crystal clear about who your target consumer is. Instead of trying to appeal to the generic "consumer," companies should define whom exactly they are targeting. The most sophisticated companies gain a thorough understanding of the various consumer segments and microsegments, and the factors that drive buying behavior in each: What attributes does each microsegment value the most in a specific product? What will they pay for and what don't they care about? How often do they purchase a product? How much do they spend on the category per year? Delving into these questions requires gathering data from multiple sources (including point-of-sale transactions, consumer research, and social media) and harnessing the power of advanced analytics. Companies can then develop tailored value propositions for each of their target segments.

Bifurcate your portfolio; avoid getting 'stuck in the middle.' As consumers either trade up or trade down, companies whose portfolios consist primarily of mid-tier products might have little to offer. Such companies could consider stretching their brands upward, downward, or in both directions—developing a premium offering to attract up-traders, or a compelling low-priced offering aimed at down-traders and mass consumers. In these product-development efforts, a design-to-value approach—as well as skillful management of portfolio complexity—will be essential to achieving profitable growth.[5] A beverage manufacturer, pursuing growth in China, established a "price ladder" to encourage trading up within its brands. The company launched a series of progressively more expensive offerings, from value to core to premium and finally to super premium. It also consistently raised the price ceiling through innovation—for instance, introducing an "artisanal" beverage that came in a sleek container with a distinct shape, color, and design. That product sold at five times the retail price of the brand's core offering. The result of this clear pricing hierarchy: double-digit increases in net revenue and significant market-share expansion.

Ensure product availability and pricing consistency across channels. With consumers shopping across channels in search of convenience and deals, a comprehensive channel strategy—one that maximizes reach and minimizes channel conflict—is crucial. The strategy should include investments in the highest-growth channels; partnerships with winning online players, discount formats, and club stores; and the development of a robust digital play, which entails not only creating digital assets but also building a strong presence on the websites and mobile apps of leading multichannel retailers.

Importantly, as manufacturers sell their products across multiple channels, they must ensure that their prices for identical SKUs are consistent across channels—or else they risk losing the consumer's trust. As for channel conflicts, companies must identify and quantify these conflicts, then design and implement containment strategies (for example, differentiated packaging for each channel or coordinated promotional calendars) that they monitor and refine on a regular basis.

■ ■ ■

Consumers are becoming ever more conscientious and more deliberate in their buying decisions. This is certainly a challenge for consumer companies—but it also opens up new opportunities for brands and products that can be responsive to consumers' evolving needs and preferences. Indeed, tomorrow's winning companies will be those that move quickly and assertively to understand, anticipate, and respond to changes in consumer behavior. ■

[1] Separate articles on consumer sentiment in Brazil, South Africa, and the United States will be available in spring 2016 on McKinsey.com.

[2] For more on the consumer market in Mainland China, see Yougang Chen, Fang Gong, and Daniel Zipser, "Here comes the modern Chinese consumer," March 2016, McKinsey.com; and *Urban world: Global consumer groups to watch*, McKinsey Global Institute, forthcoming on McKinsey.com.

[3] Peter Breuer, Brian Elliott, and Stefan Rickert, "The power of advanced analytics in revenue management," *Perspectives on retail and consumer goods*, Winter 2013/14, McKinsey.com.

[4] Peter Breuer, Jessica Moulton, and Robert Turtle, "Applying advanced analytics in consumer companies," May 2013, McKinsey.com.

[5] For more on design to value, see Søren Fritzen, Heiko Nick, and Jan Wüllenweber, "Capturing the full potential of design to value," *Perspectives on retail and consumer goods*, Winter 2013/14, McKinsey.com.

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