

A photograph of a metal shopping cart filled with various groceries, including bags of chips, a carton of milk, and other packaged goods. The cart is positioned in a supermarket aisle with shelves of products visible in the background. A semi-transparent white box is overlaid on the upper portion of the image, containing the title and authors' names.

Winning in the Gulf region's consumer-goods market

Best practices in customer and channel management

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INTRODUCTION

The six member states of the Gulf Cooperation Council (GCC)¹—Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE)—are home to 45 million people. The resource-rich region controls about 30 percent of the world's oil reserves and about 23 percent of its natural-gas reserves. Although the region's growth has slowed somewhat due to the dramatic drop in oil prices, it continues to outpace that of other emerging economies. Between 2010 and 2014, the GCC's GDP grew by 11 percent a year on average, well above rates seen in developed countries and many emerging markets. And while levels varied widely among member states, GDP per capita in the region grew during this period by 3.5 percent a year.

Consumer-packaged-goods (CPG) manufacturers operating in the GCC are poised to benefit from rising consumer demand. The region is attractive for other reasons as well: governments in the GCC are generally stable and amenable to business interests. More than 60 free economic zones, known as free zones, provide business incentives that include tax exemptions, less onerous regulatory regimes, and modern infrastructure. In some GCC countries, foreign direct investment as a percentage of GDP is higher than inflows seen in China and Brazil and much higher than those in, for instance, Germany and the United States.

But selling CPG products in the region isn't without challenges. For one, CPG manufacturers must do business with *baqalas*, family-owned neighborhood shops that constitute a highly fragmented retail network. Modern retail channels—such as hypermarkets and convenience stores—are growing fast, but *baqalas* still account for a considerable fraction of retail sales. The GCC has strong cultural traditions and a large expatriate population, reaching as high as 82 percent of the population in the UAE. Marketing and sales approaches that succeeded in Western markets, as an example, may fall flat or even be counterproductive.

To better understand how to win in this growing market, we surveyed 13 leading manufacturers operating in the GCC about their practices in customer and channel management. This report summarizes the GCC-specific findings of the 2014 Customer and Channel Management Survey, developed in collaboration with Nielsen.

Survey participants were a mix of food and nonfood manufacturers in Saudi Arabia and the UAE. These two countries, which account for almost three-quarters of the region's economic activity and slightly more than three-quarters of its population, are a reasonable proxy for the trends and challenges in the GCC generally. The survey covered three core areas of customer and channel management: sales strategy, pricing, and trade investment. Using Nielsen's retail measurement of in-market performance, the survey revealed differences between the practices of "winners" and the practices of "others"—winners being companies that achieved higher sales growth than the categories they play in, while also outperforming peers on one or more customer- or channel-management metrics.

¹ Though widely known as the Gulf Cooperation Council (GCC), the official name of the economic and political group established in 1981 is the Cooperation Council of the Arab States of the Gulf.

The survey results show that the most successful CPG companies in the GCC excel along four dimensions. First, they **focus on high-growth channels**:

- Winners are twice as likely as others to develop tailored products and conduct exclusive launch events for hypermarkets, their largest growth channel.
- They are three times more likely to develop effective containment strategies for channel conflict.

Second, winning companies **use data and analytics**:

- They are two to three times more likely to invest in data and advanced analytics.
- They are twice as likely to be satisfied with the quality of their company's data and the usage of that data.
- They are twice as likely to use advanced analytics and trade-promotion-management tools.

Third, winners **engage in next-generation collaboration**:

- They are twice as likely to measure the cost to serve each retail account and use that information as a basis for selecting distribution models and setting prices.
- They are twice as likely to collaborate with key accounts to improve logistics efficiency.

Finally, winning companies **create capability-building organizations**:

- Winners are 30 percent more likely than others to have increased their investments in training and capability building.
- They are more likely to build dedicated centers of excellence for core functions such as pricing and trade investment.

SURVEY OVERVIEW AND METHODOLOGY

This report draws primarily on data collected from the GCC participants in the 2014 Asia Customer and Channel Management Survey, supported by market retail performance from Nielsen. The survey is designed to identify winning practices by linking financial performance and in-market results with self-reported business practices across three performance areas: sales strategy, pricing, and trade investment.

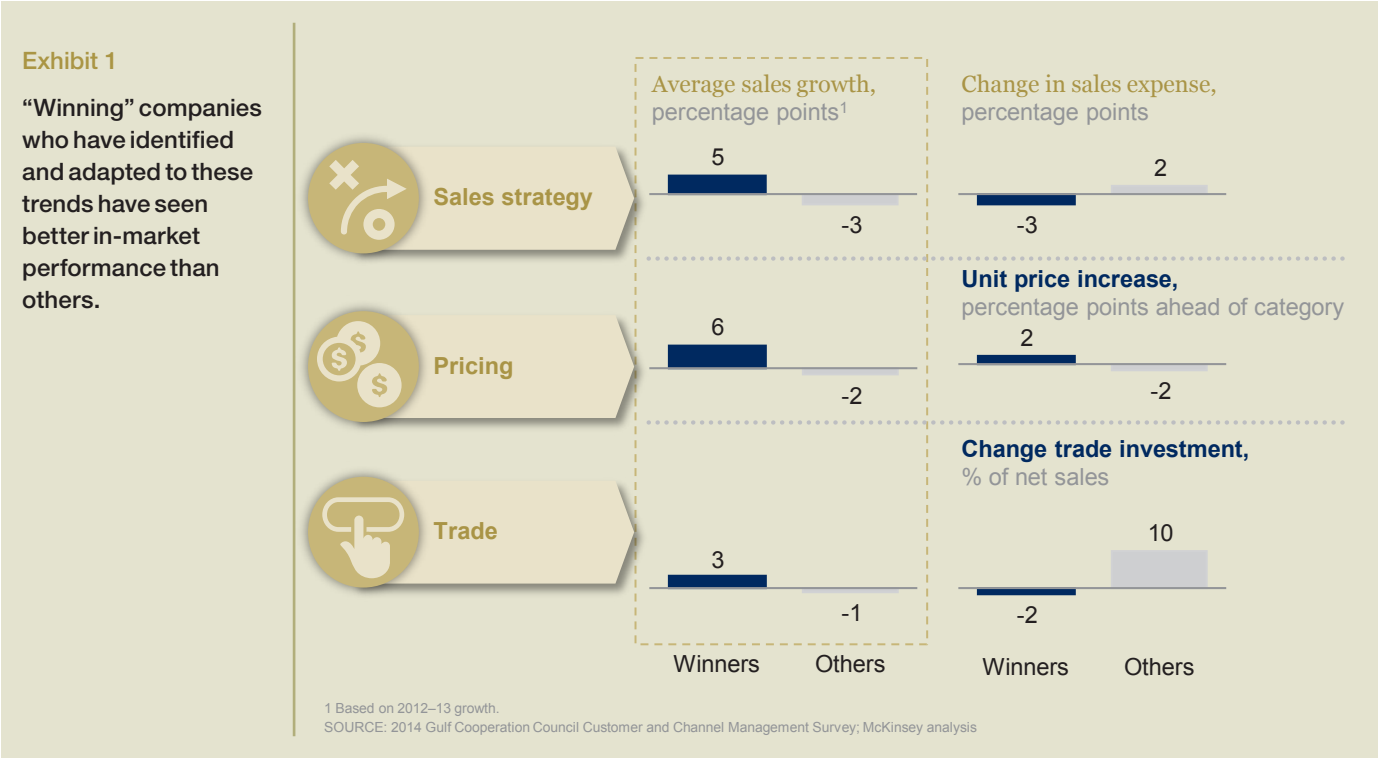
The 2014 survey is the latest in a series that began in 1978, when McKinsey gathered data and performance benchmarks on the sales organizations of leading CPG companies in the United States. Since then, the data have been updated every two to three years. Over time, the survey evolved to include a deeper focus on performance

across a wider range of topics and was augmented with analytics from Nielsen. Its geographic scope also expanded. The 2014 Customer and Channel Management Survey covered almost 200 companies globally, with combined net sales of \$150 billion and trade spend of \$40 billion. Of these, 52 companies were part of the Asia survey, including 13 from Saudi Arabia and the UAE. Together, the 13 companies had a market share of approximately 10 percent in the food and beverages category and approximately 20 percent in the home-care category in 2014.

To ensure the accuracy of the data, the person accountable for each performance area completed the appropriate part of the questionnaire. For instance, heads of sales answered the questions related to sales strategy.

THE VALUE OF WINNING

Winning companies significantly outperformed their peers not only in average sales growth but also in other important customer- and channel-management metrics. For instance, the five companies that emerged as winners in sales strategy grew five percentage points ahead of the category average and eight percentage points ahead of nonwinners (Exhibit 1). At the same time, their selling expenses as a percent of net sales were three percentage points lower than the category average and five percentage points lower than that of nonwinners.



In pricing, the four winning companies in our sample on average saw sales grow six percentage points faster than their category. They were also able to release unit price increases of two percentage points above the category average and four percentage points above the average for nonwinning companies.

And in trade investment, the five winners we identified achieved average sales growth of 3 percentage points above the category, while reducing trade investment, as a percentage of net sales, by 2 percentage points more than the category average and a full 12 percentage points more than the other companies in our survey.

DETAILED FINDINGS IN EACH PERFORMANCE AREA

Sales strategy

When asked to cite the most important change that will affect their business over the next five years, the GCC companies in our survey were unanimous in their response: the growth of modern trade channels at the expense of traditional trade. Across the board, CPG companies recognized hypermarkets as the biggest driver of sales growth in the region. But winners in sales strategy are more deliberate about nurturing their customer relationships in both modern and traditional trade and about building sales capabilities. They adhere to the following best practices:

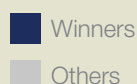
Identify and invest in growth channels. Winners more actively pursue growth in hypermarkets. For example, 60 percent of winners (and only 31 percent of others) said they increased the level of senior-management involvement with hypermarkets (Exhibit 2). Winners were also more likely to develop tailored products and exclusive product launches for hypermarkets.

Exhibit 2

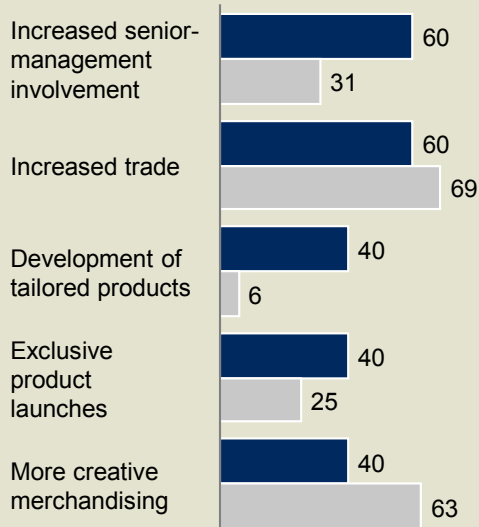
SALES STRATEGY–WINNERS ANALYSIS

Winners are more likely to increase senior-management intervention and product innovation to drive growth in hypermarkets.

% of respondents¹



Actions to drive growth for hypermarkets



Most critical capabilities to drive growth in hypermarkets²



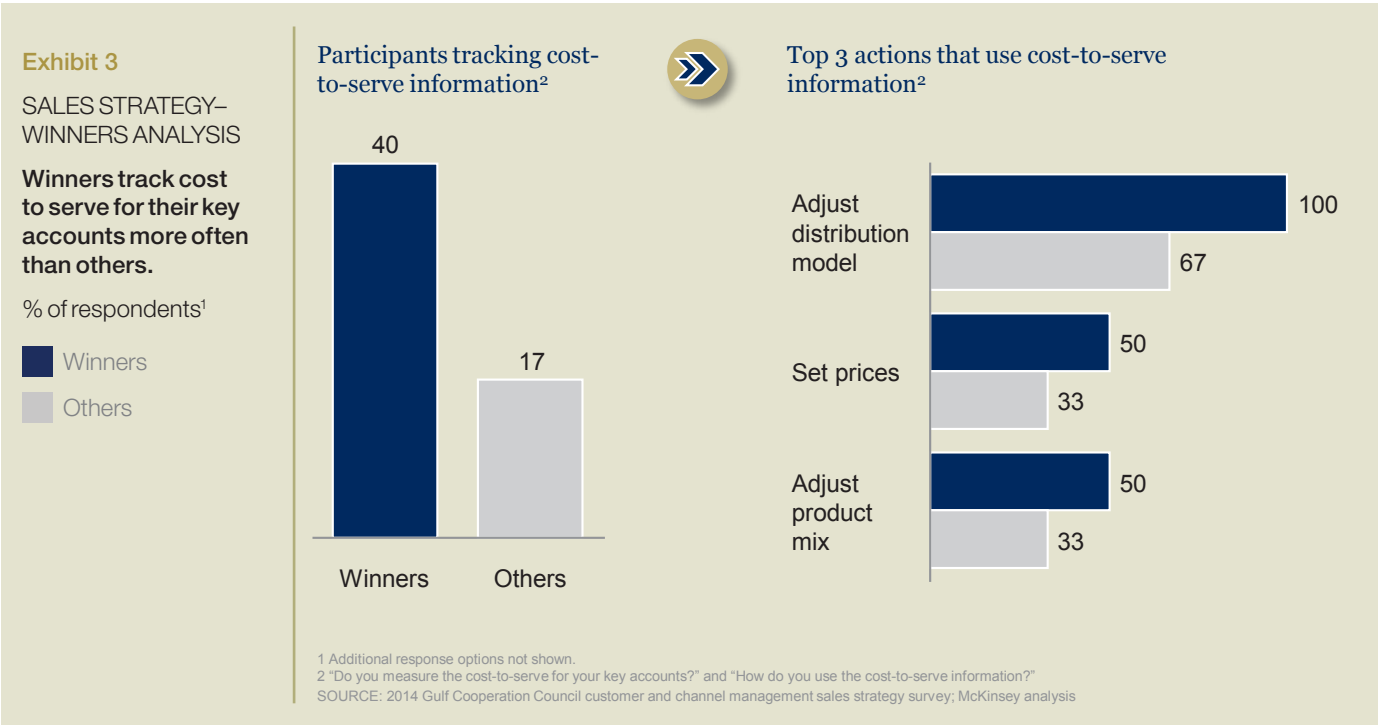
¹ Additional response options not shown.

² "Please select the top 2 capabilities that you believe are most critical to driving growth."

SOURCE: 2014 Gulf Cooperation Council Customer and Channel Management Survey; McKinsey analysis

In addition, all winners said they analyze and manage channel conflict and implement containment strategies, such as ensuring price consistency and simultaneous product distribution across channels. Meanwhile, 42 percent of others said they don't address channel conflict at all.

Review and revise route-to-market strategy. Winners take a more rigorous approach to selecting route-to-market (RTM) models. Eighty percent of winners (and only 22 percent of others) choose their RTM model based on detailed economic factors and guidelines. For instance, 40 percent of winners track cost to serve, and use that information to adjust their distribution models, set prices, and change their product mix (Exhibit 3). By contrast, more than a quarter of the other companies have no clear guidelines at all for RTM selection.



Winners collaborate more with their key accounts, working with them on activities such as improving logistics efficiency, forecasting demand, and developing joint promotions. Also, 60 percent of winners conduct granular reviews of their RTM strategy at least once a year, compared to none of the others. Almost half of others review their strategy only once every two to three years.

This rigor extends to how winners evaluate their distributor network: 80 percent of them review distributor performance once a month, compared with 33 percent of others, and 60 percent of winners—but only 17 percent of others—develop predefined account plans and targets for their distributors. Winners are also more likely to link performance to distributor discounts. Eighty percent of winners have

discount policies and rules that differentiate among distributors based on their performance. It's therefore not surprising that all winners (compared with only half of others) are satisfied with their distributors. Every winning company gave distributors high marks in two critical activities: sharing sales data and market insights, and actively increasing outlet coverage.

Build sales capabilities. At winning companies, salespeople spend most of their time interacting with customers and crafting sales strategies—not doing administrative tasks. At other companies, the opposite is true. Furthermore, all the winners in our survey had increased investment in training. They were also significantly more likely to deploy new tools and technologies, create job-rotational programs internally and externally, and hire outside talent or partner with other companies to boost sales capabilities.

Pricing

Winners in the pricing arena take a disciplined, data-driven approach to setting and adjusting prices. In particular, the four pricing winners do the following:

Set prices strategically. In setting list prices, all the winners examine pricing gaps with the competition, as well as brand equity or brand health. They're also more likely to pay attention to consumer price elasticity (Exhibit 4).

Exhibit 4

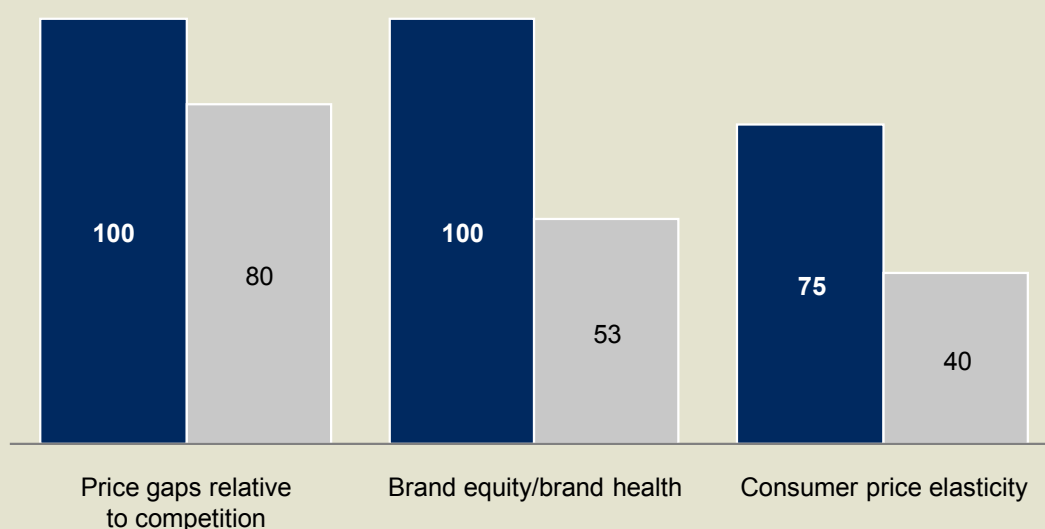
PRICING SURVEY—WINNERS ANALYSIS

Winners consider price gaps and brand equity as the most important factors when setting list prices.

% of respondents¹

■ Winners
■ Others

Top 3 factors considered when setting list prices and suggested everyday shelf prices²



¹ Additional responses not included.

² "What are the factors you consider when setting list prices and suggested everyday shelf prices?"

SOURCE: 2014 Gulf Cooperation Council Customer and Channel Management Survey; McKinsey analysis

Although every company we surveyed had introduced price increases and higher-priced products over the previous two years, winners made other moves as well: half of them reduced their trade funding, compared to almost none of the others, and more than twice as many winners as others upgraded to command higher prices.

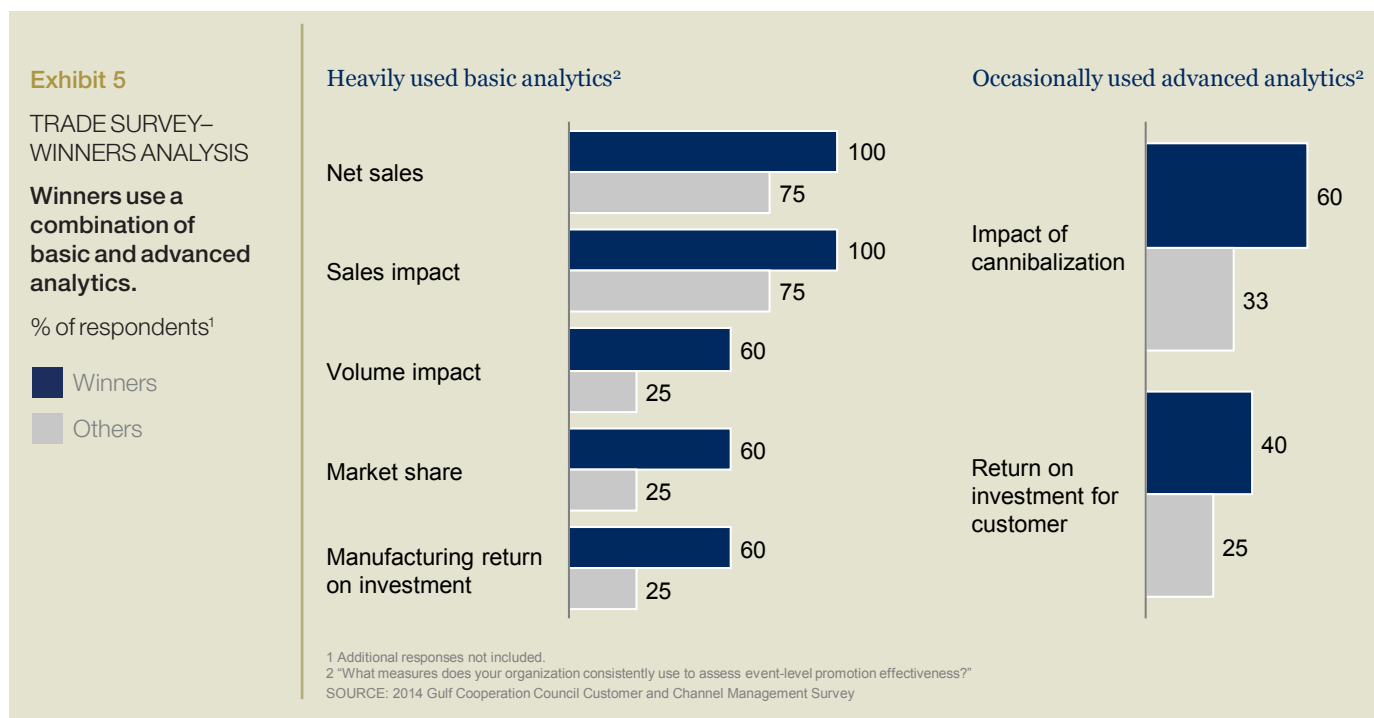
Winners review price levels more frequently. Half of winning companies, compared with only 27 percent of others, track prices at least quarterly. They examine more granular data: for instance, to review or approve proposed price changes, 75 percent of winners (and only 20 percent of others) develop margin guidelines by category, brand, and SKU. Winners tend to change prices less frequently and by smaller increments, but they offer temporary discounts and promotional incentives on their top brands monthly or weekly, whereas others offer them only quarterly or semiannually. Winners' price changes were consistently effective, yielding increases in revenue and profit margin.

Establish a pricing organization equipped with advanced tools. All winners had created pricing centers of excellence, either at the corporate or business-unit level. In addition, data and analytics are more widely used in the pricing organizations of winners than of others. While most respondents said they have ready access to data, 75 percent of winners (and only 20 percent of others) said the quality of the data is good or excellent. All winners are satisfied with their company's usage of this data. Winners are also more likely to develop their own price diagnostic and optimization tools.

Trade investment

In trade investment, just like in pricing, success factors include close attention to metrics, use of analytics, and dedicated centers of excellence. Winners in trade investment do the following:

Analyze the impact of promotions and make adjustments. Almost all companies in our GCC survey review their trade performance regularly. Winners, however, are more likely to eliminate promotions linked to a specific account and replan their remaining promotions without changing the level of funding. Similarly, winners examine a wider range of performance indicators (Exhibit 5).



All winners—and none of the others—have at least three tiers in their bracket pricing structure. Also, 80 percent of winners reported promotional compliance of at least 70 percent, compared to 36 percent of the others, and 60 percent of winners (but less than half of others) said their returns on trade had increased over the previous two years.

Invest in a dedicated trade organization and technology. While all CPG companies in our sample had created trade centers of excellence, winners uniformly had these centers dedicated to individual business units, while about a fifth of the others created corporate-level centers. Winners were also more likely to be developing or using trade-promotion-management and optimization tools.

MANAGEMENT AGENDA FOR CPG COMPANIES

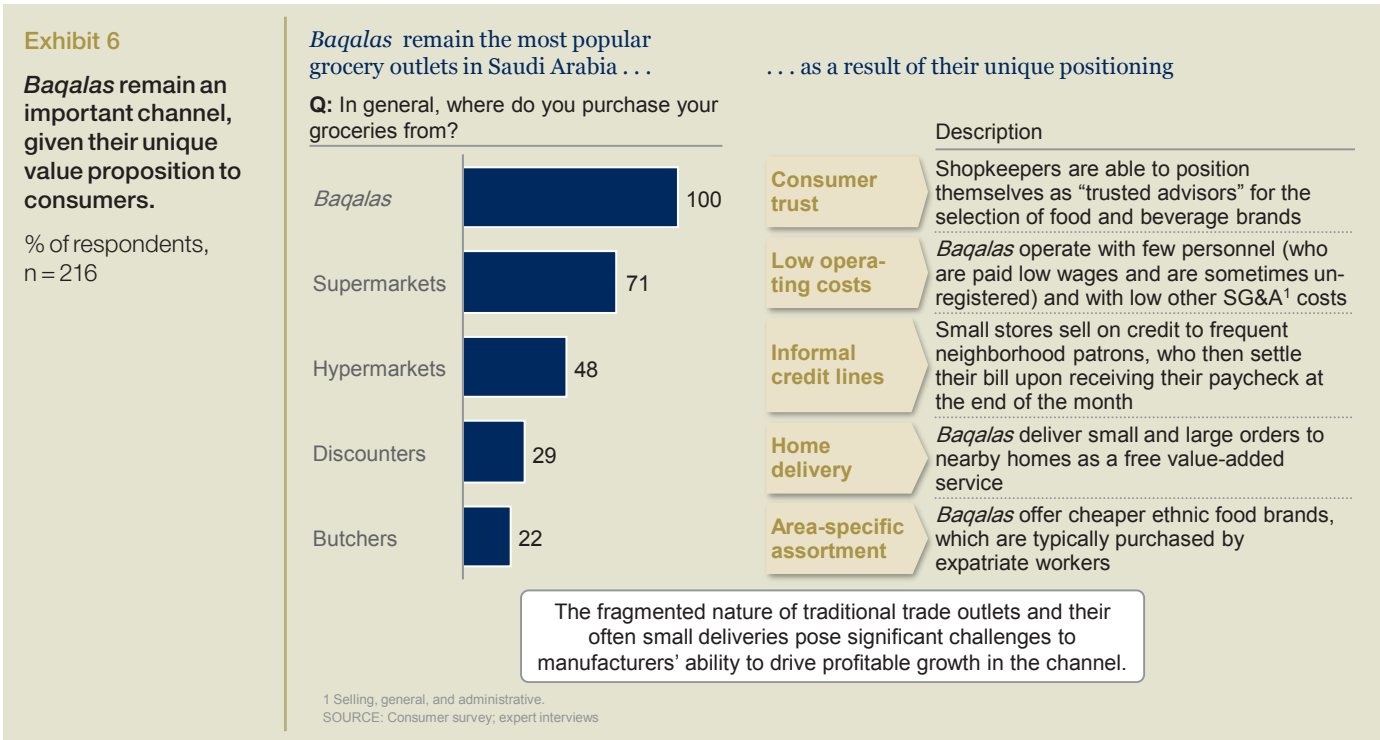
The Customer and Channel Management Survey highlighted six management priorities—three strategic measures and three enablers—for CPG companies operating in the Gulf countries. While these themes are applicable throughout the GCC, companies should recognize that the region doesn't consist of homogeneous countries; specific initiatives to address these themes must take national differences into account. (For example, regulatory changes and new labor laws could alter Saudi Arabia's retail environment dramatically. The same is not true in the UAE, a more mature market.)

1. Give modern trade channels precedence. Modern channels—particularly hypermarkets and convenience stores—will be the primary growth drivers in the GCC. Modern trade already accounts for the majority of sales in both the UAE (82 percent) and Saudi Arabia (58 percent).

Particularly in Saudi Arabia, easily the GCC’s largest market, regulatory changes are expected to accelerate the growth of modern trade outlets. For example, tougher labor laws for migrant workers have reportedly led to the closing of 5 to 10 percent of the country’s *baqalas*, since the *baqalas* couldn’t afford to replace their low-cost staff of migrant workers with Saudi nationals.

The growth of modern trade requires CPG companies to shift from a transactional to a collaborative and customer-centric approach to key accounts—ideally, characterized by multiyear efforts in joint business planning and innovation. This requires sophisticated segmentation that differentiates service levels based on value, improved analytics to plan and optimize trade expenditures, and tailored assortment and merchandising programs that match customer priorities. In addition, CPG companies must monitor in-store execution, optimize their supply chains to improve service levels while lowering cost to serve, and create dedicated multifunctional selling teams to cater to the biggest accounts.

2. Change the management approach to traditional channels. *Baqalas* and other traditional channels will remain important in the GCC for many years. After all, they offer advantages that are difficult for big chains to match: *baqalas* serve as trusted local advisers, have low operating costs, extend informal credit lines, make home deliveries, and offer area-specific assortments (for instance, they carry ethnic brands that appeal to expatriates) (Exhibit 6).



But many CPG companies take a one-size-fits-all approach to the traditional trade. Instead, they should develop a simple segmentation of retailers based on historical sales, growth potential, and cost to serve. They should prioritize outlets strategically, developing a compelling value proposition and a differentiated service level for each segment. And, just as important, they should continually refine the segmentation over time as their capabilities improve.

3. Explore online channels to set the stage for future growth. E-commerce isn't currently a priority for CPG companies in the GCC. Online sales in the region are hampered by a general distrust in online payment systems and a lack of government support. In 2014, online sales accounted for less than 2 percent of total retail sales in the UAE and less than 1 percent in Saudi Arabia. Understandably, CPG companies in the region view the Internet as an advertising medium rather than a sales channel. Indeed, a recent McKinsey survey found that 76 percent of consumers in the UAE and 60 percent in Saudi Arabia conduct online research before making purchases.

That said, forward-looking CPG companies are actively exploring e-commerce in anticipation of strong online growth. In the UAE, for instance, e-commerce is projected to account for 6 percent of retail sales by 2019.

Over the past two years, e-commerce company Souq.com has been working with CPG players to build an online growth strategy for categories such as baby care and personal care. Their joint plans encompass assortment planning, design of exclusive SKUs, customer activation, co-marketing, and data sharing. Souq.com's sales of CPG products are growing at a rapid pace, with most categories exceeding 100 percent year-on-year growth.

4. Revamp collaboration models with distributors. In Saudi Arabia, almost half the companies we surveyed are dissatisfied with their distributors, and in the UAE about a third reported dissatisfaction. Companies rated distributors poorly in two critical areas: in-store execution and delivery efficiency and quality. Yet none of them plan to switch to other distributors. Among the reasons they cited for sticking with the status quo are regulatory obstacles (which are slowly changing to accommodate direct-to-retailer distribution), fear that switching to new distributors would be too disruptive or too costly, a lack of alternatives, and contracts that can't be broken.

Best-in-class distributor management requires CPG companies to excel in a number of practices, including gaining transparency into distributor economics, engaging in ongoing performance dialogues linked to pay-for-performance terms, and collaborating on account planning and business development.

5. Invest in data analytics. CPG manufacturers in the GCC have barely begun to use advanced analytics and other technologies: almost two-thirds of survey respondents said they don't have a customer-relationship-management system,

and about three-quarters don't use advanced analytics. Even among winners, 60 percent are neither using nor developing tools to manage or optimize their trade-promotion investments.

The few companies that do invest in analytics reap considerable benefits. A CPG company developed econometric models to answer questions such as: What drove growth last week? What's the likely impact of a specific promotion under these conditions? What's our true return on investment? The company built an intuitive interface for its salespeople, enabling them to make fact-based decisions in their daily work. The impact: efficiency gains of 5 to 10 percent on trade budgets, as well as a more streamlined process for annual promotion planning and trade resource allocation.

6. Focus on finding and attracting talent. The GCC faces a talent shortage for a range of highly skilled positions. One survey suggests that a third of the companies in Saudi Arabia face talent shortages in engineering, project management, and technical roles. The situation in the UAE is similar.

About three-quarters of the companies in our study are addressing this challenge by increasing investments in training, and a similar proportion hire external talent. Other measures, such as job rotation programs and new incentives for sales staff, are less common.

* * *

The member states of the GCC represent a promising growth market for CPG manufacturers. As our survey results show, most companies have barely scratched the surface with respect to what they can do in the region—the potential for improvement in sales strategy, pricing, and trade investment remains immense. By implementing best practices in customer and channel management, companies can see their business flourish in this intriguing and complex part of the world.

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