

Consumer Packaged Goods Practice

How CPG companies can sustain profitable growth in the next normal

After safeguarding their employees and businesses from COVID-19, consumer companies must develop new strategies to find micropockets of growth amid changing consumer preferences and market dynamics.

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The arrival of the COVID-19 pandemic suddenly and completely reshaped the consumer landscape at the start of 2020. At the same time consumer packaged goods (CPG) companies were looking to break out of a decade of inconsistent growth, many saw their expectations of growth replaced by a struggle for survival, while others had to ramp up production to meet never-before-seen spikes in consumer demand. Channels have also been shaken up: for example, e-commerce and omnichannel grocers have benefited greatly to date, while restaurants and food-service companies are facing the specter of bankruptcies and a major overhaul. All companies must now confront the prospect of navigating the worst economic downturn since the Great Depression.

The transition from responding to the pandemic to recovering and navigating the path forward means that executives will have to manage several priorities simultaneously: tracking changing consumer preferences, identifying micropockets of growth to prioritize in future plans, adjusting commercial strategies, and becoming more agile to pursue opportunities. As CPG companies embark on the road to recovery, a consumer-centric, analytics-driven, and comprehensive approach that increases top-line revenues profitably—what we refer to as predictive growth—has never been more critical. Such an approach must start with understanding the contours of the next normal. Companies should then devise an intentional plan to build the commercial capabilities needed to win in the next normal and permanently adopt the agile decision making that got them through the first stages of the pandemic.

Contours of the next normal

In the immediate response to the pandemic, the wave of lockdowns forced consumers to adjust their daily routines and purchasing habits. A critical challenge for CPG companies is to develop comprehensive strategies that are rooted in the needs of the consumer of the future.¹ This process starts with effectively harnessing all the insights,

data sources, and analytics techniques available. Initial McKinsey research into the pandemic's impact explores how consumer behaviors have changed, in many ways permanently, across eight areas (Exhibit 1).

The stickiness of these areas and the degree to which they penetrate a consumer segment will vary by region and market, depending on how the pandemic evolves and how long it takes for consumers to get back to their “normal” ways of life. Similarly, these eight areas' impact on any given consumable category can vary greatly within a market. Further, stickiness will likely depend on the quality of the experience, so the actions that companies take now can have a significant impact in the next normal. However, we believe changes in five areas will have an impact on occasions and influence CPG companies as they plan to achieve the right balance of top-line growth and profitability in the future.

Life at home. During the pandemic, the home has been recast as the new coffee shop, restaurant, gym, and scene of entertainment—leading to an unprecedented increase of in-home activities. Nesting has fueled spending on at-home categories and compelled previously offline individuals to try e-commerce offerings; for example, more than 10 percent of US consumers that had never shopped for groceries online before have started to do so. Globally, people have turned to online sources for entertainment, learning, and communication while exploring contactless and digital alternatives to shopping.

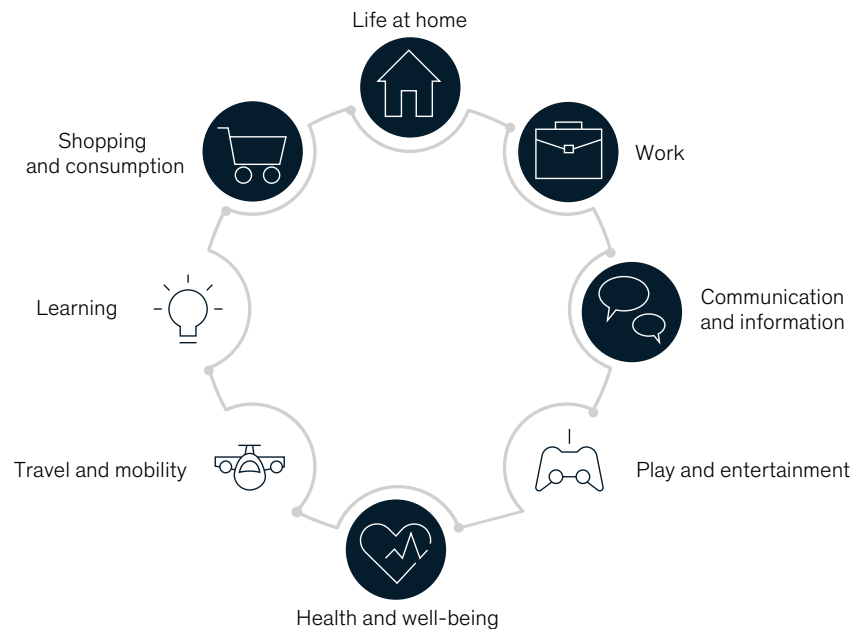
Shopping and consumption. As lockdowns have naturally reduced shopping frequency and consumers spend more thoughtfully during economic uncertainty, consumers have decreased their overall spending and consumption, with the largest impact on discretionary categories such as jewelry and gum. In Europe and the United States, consumer spending is on track to fall by ten to 20 percentage points for the near future. Importantly—driven by convenience, availability, and affordability—almost 20 percent of consumers

¹“Survey: US consumer sentiment during the coronavirus crisis,” June 26, 2020, McKinsey.com.

Exhibit 1

COVID-19 is transforming every aspect of people's lives.

● Most critical for consumer goods



indicate they have switched from preferred brands and retailers during the pandemic, and about half of those consumers indicate they expect to make these switches permanent.

Health and well-being. Consumer spending has increased in health and hygiene. Health concerns are largest in Brazil, India, Italy, and the United States, suggesting consumers in such markets may prioritize future spend in these and related categories. The higher awareness of personal health has led consumers to embrace brands that they consider safer; some are moving away from products that are manufactured in harder-hit countries and toward perceived healthier options. The United States has seen a tenfold increase in the sales of organic produce and a 130 percent rise in vitamins and supplements. And in Brazil, purchases of fresh food have outpaced groceries overall during the lockdown.

Communication and information. Consumer media consumption has increased considerably, with a

focus on social media, digital channels, and TV and radio. This shifting behavior has led companies to adjust their marketing approach: some have reduced their in-person sampling and testing, more than 40 percent have canceled campaigns, and 65 percent plan to decrease ad spending. Consumers have also been drawn to brands with an active response to the COVID-19 outbreak—especially in emerging markets—elevating the importance of communications that matches the prevailing consumer sentiment.

Work. The economic downturn has resulted in rising unemployment and the disruption of traditional business environments. Companies that were able to transition to remote working have fueled spending on collaboration tools and home office categories. Executives are starting to understand the potential of remote-work arrangements as well as the associated challenges and are seeking to find a sustainable balance. After having experienced the full lockdown, 80 percent of employees surveyed in China preferred

a hybrid model where they can work remotely part of the time. Overall, the higher number of people working from home will result in a shift of occasions.

CPG companies must monitor trends in these areas and be prepared to reexamine and adjust their growth strategies accordingly.

Developing a winning growth formula for the next normal

To win in the next normal, where some degree of the changes to these eight areas of life will stick, CPG companies should follow a three-step predictive growth process: predict, rebound and transform, and sustain (Exhibit 2).

Predict consumer demand

Data and analytics have become more critical than ever to accurately forecast demand across product segments. The pandemic has created significant challenges to what was already a difficult task. Time-series data sets have been disrupted, making it more difficult to identify trends, and we don't yet know the extent of a given trend's stickiness in specific regions, markets, or categories. One-off effects that should be considered include work-from-home arrangements, temporary closures of schools and restaurants, brand switching caused by stockouts, and shifting channel and retail-outlet preferences as shopping occurs closer to home.

Consumer responses to the pandemic have made demand more difficult to gauge accurately. The past is no longer a predictor of future demand. In the initial stages, the spike in purchases of certain categories was caused, in part, by pantry loading in preparation for shortages. So while actual consumption during this time didn't rise, spending toward some foods (such as lunch meat) did increase. Other categories (such as beauty supplies) saw a drop-off because of declining consumer confidence. Through the use of analytics, companies should seek to recognize these patterns and plan for a potential second wave of outbreaks.

We believe CPG companies should rely on three principles when developing more accurate category, brand, and product projections for the next normal:

- *Base analytics on the most up-to-date understanding of consumer behaviors.* As countries gradually transition out of lockdowns, CPG companies will need to develop a robust comprehension of the short- and long-term applicability and impact of changes in consumer behavior. This process is usually best informed by a mix of consumer sentiment research, proprietary category-specific research, online search, and digital engagement data.
- *Harness a wide range of data sources as inputs for fit-for-purpose machine-learning techniques.* The pandemic has forced companies to aggregate and process more data and data sources than

Exhibit 2

Revising and iterating on three predictive growth elements can help refine and clarify scenarios over time.



Predict

What growth goals should we target after COVID-19? What is the full potential across the three growth cylinders considering each company's unique evolution during COVID-19?



Rebound and transform

Which levers should we pull to drive profitable growth in a COVID-19 world? In which sequence? Where and how much should we invest given changing consumer preferences?



Sustain

What operating model changes will be required to sustain profitable growth in the mid- to long-term in a post-pandemic world?

they likely have in the past. By casting a wide net, executives can create an up-to-date snapshot of category, brand, and competitive dynamics. To accurately predict demand, we believe analytic practices should not only track historical sales trends but also stitch together offline and online data with dozens of macroeconomic variables—such as GDP and the consumer price index. Consumer sentiment, social listening, search trends, and category-specific data (for example, products that tie in with movie releases) should augment these data sources. Finally, machine-learning techniques can identify underlying predictors of consumer trends.

- *Translate insights into scenarios that help provide corridors for the unknown.* Since there are still degrees of unknown (for example, the future progression of COVID-19 in a given market or the effectiveness of government stimuli in jump-starting economies), CPGs must navigate multiple scenarios—and

concentrate on the most likely ones as time passes and certainty increases. Companies should use data and analytics to explore a range of scenarios and determine the demand elasticity of specific categories.

To some extent, these three elements should be iterative as frequent revisions will contribute to refined, more precise scenarios over time. A set of scenarios developed in a given month should be regularly updated with new data and insights (Exhibit 3).

Rebound and transform to thrive

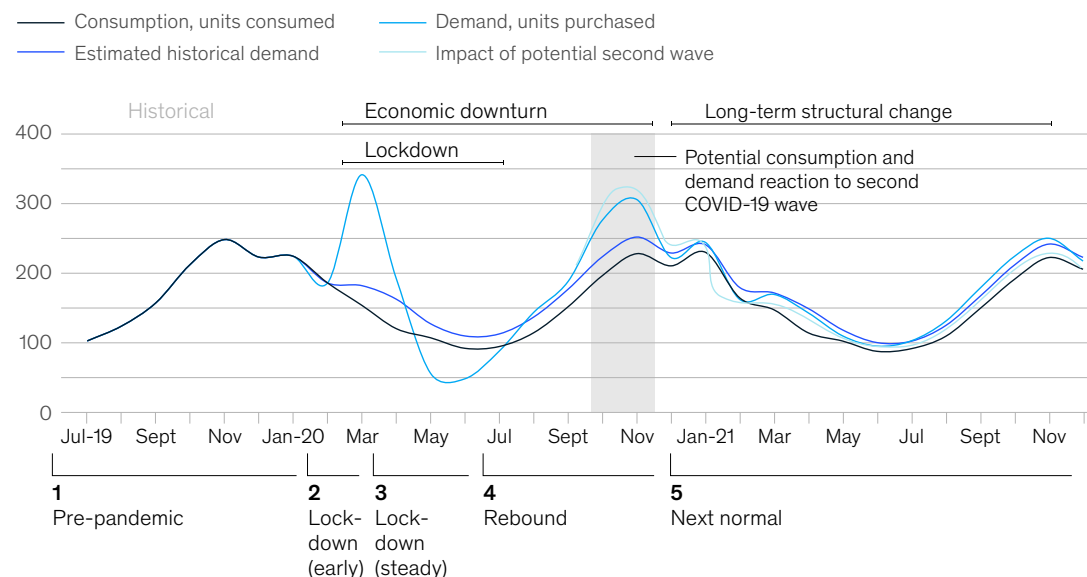
As lockdowns lift and detailed demand forecasts help identify growth opportunities, companies should prioritize rebounding and transforming. Plans to boost organic growth should include four core commercial capability areas: portfolio and innovation strategy, marketing, revenue growth management (RGM), and sales (omnichannel and in-store excellence). Any or all of these areas could apply for

Exhibit 3

Predictive growth can produce a real-time snapshot for a specific brand in a specific market.

Example output of integrated model across five phases

Estimated consumption and demand curves, units, million



every company, but their mix will vary by context—the timing of the transition to the next normal, geography, product categories, share position, and existing capabilities, among other factors. As part of efforts to achieve profitable growth, executives should evaluate, at a minimum, all four capabilities.

Portfolio and innovation strategy. In the wake of the pandemic, CPGs will need to realign their product portfolios and innovation engines with changing consumer needs; this capability will be more critical than ever in the next normal. Companies too often rely on commoditized data and insights, settle for small moves that don't meaningfully improve the top line, or struggle to scale disruptive innovation sustainably. By contrast, winning companies deploy multiple capabilities, including consumer-back analytics (that is, growth maps or other granular views into consumer behavior) and “right brain” creative thinking early in the portfolio-strategy process. They build new full-stack-innovation operating models that lead from insights to strategy to execution, and they redesign products using a renovation-to-value approach to better meet true consumer needs. Last, leading companies establish integrated-delivery mechanisms such as innovation garages—cross-functional teams empowered to develop disruptive innovations end to end.

With these insights in hand, companies should reassess their portfolios against next-normal trends and rapidly accelerate their innovation pipelines to meet consumer preferences for affordability, health and hygiene, and packaging. Big brands, which once again have momentum, should channel “small brand” test-and-learn capabilities and focus on renovating and innovating bigger platforms. Such moves will enable big brands to respond to evolving consumer needs across new product development, package configuration, and sustainability.

These companies must also look to portfolio simplification and streamlining R&D processes to increase speed to market, cut small projects with low returns on investment, and refocus investment on high-ROI projects—as well as build the organizational muscle to assess their overall

portfolios and core SKUs in each channel on a rolling basis.

Marketing. COVID-19 reset the way consumers view products and brands. In a time of uncertainty, companies that demonstrate both empathy and how their products could provide comfort and security are the ones to excel. Executives also have the opportunity to translate potentially temporary effects (such as pantry loading and brand switching) into more sustainable gains. Accelerating investments in selected areas can create more stickiness. Media consumption has shifted to digital even further than in the preceding decade. Meanwhile, with many companies cutting back on media spending, media rates have plummeted, offering a window to connect with consumers in a moment of captive attention.

Leading CPG companies have looked to data-rich industries that had once raised the bar in areas like contextual personalization and targeting. This new approach moves away from the “mass reach with mass waste” model to embrace personalization across products and messaging in digital platforms such as video on demand. Speaking to customers through their preferred channels and addressing their current needs—with the right tone, language, and brand promise—will be critical to success in the next normal.

Data-driven marketing yields three valuable tools: granular consumer audience creation, which entails developing a 360-degree view of the consumer and identifying relevant target groups with different needs; a content-creation model that enables more personalized (or at least segmented), engaging content to outperform “mass” efforts; and dynamic placement and measurement, which allocates and optimizes spending across channels.

Ongoing cost pressure will compel leading companies to look for opportunities to find efficiencies (for example, reduce nonworking spending and reallocate resources from low-ROI channels) to fuel growth. As CPGs deploy funds back into high-ROI marketing channels in the

next normal, they will require a more-dynamic, hypercustomized approach to provide consumers with the personalized experience they expect.

Revenue growth management. Over the past five to ten years, most CPG companies have built basic capabilities in RGM—the discipline of achieving sustainable, profitable growth through a range of strategies focused on assortment, promotions, trade management, and pricing. More recently, companies that have generated outsized impact from RGM have done so by supplementing basic and tactical capabilities with a long-term strategic focus; scaling capabilities across markets, divisions, and categories; and relying more heavily on data and advanced analytics.

The best companies in a post-COVID-19 world will continue these efforts while also elevating RGM to adapt in several ways.² To take the right action, CPG companies will need to rapidly understand changes in consumer preferences, such as trading down on products and brands, and the implications of these changes on assortment by channel and corresponding price architecture. In addition, adapting quickly to changing shopping occasions and missions requires a reassessment of promotion strategy. And the pandemic's impact on the channel and retail landscape will necessitate adjustments to assortment and trade-management practices.

At many CPG companies, RGM functions and capabilities are currently ill suited to achieve the expected outcomes for several reasons. The companies' processes are often too bogged down by overall corporate-planning processes, the skill sets of RGM team members are not sufficient to accommodate rapid updates, and organizations lack access to sufficient data. CPG companies must begin addressing and potentially transforming now. Without urgent action, they risk losing share to competitors with RGM capabilities that are nimbler and more advanced.

Holistic omnichannel sales strategy. CPG sales models have been under pressure over the past

five years as a result of retailer consolidation, the emergence of buying groups, and a continued shift to omnichannel and value channels. In the next normal, sales employees will have to embrace more frequent and agile decision making and increased omnichannel partnerships to respond to potentially permanent shifts in shopping and consumption (such as increased digital usage and new retailer and brand preferences). We believe the CPG sales model needs to fundamentally transform.

Sales leaders will determine how to serve an increasingly differentiated market. Doing so will require them to develop a granular view of omnichannel growth priorities and identify opportunities in outlets, micro markets, or consumer segments. These opportunities can't be assessed in isolation; instead, executives must take into account their organization's competitive differentiators. Variances in channel and customer profitability mean that sales leaders will need to make trade-offs: companies using a portfolio approach can capture the most valuable pockets of growth while balancing margins on lower-growth accounts.

The pandemic accelerated the shift to online channels by three to four years, so omnichannel must now function as way to engage with consumers broadly. Depending on the organization's starting point, CPG sales leaders might focus on forging more omnichannel partnerships, creating clear channel strategies, and improving e-category management. At the same time, they should be developing new capabilities—performance marketing, customer journeys, and direct-to-consumer supply chain management—that can be shared with other functions in the organization.

Across key account management, we expect the new, agile ways of working developed during the early stages of the pandemic to become the next normal. The quick adoption of digital processes and agile decision making led to a faster commercial cadence and reduced planning—from quarters to weeks. Frequent ad hoc sharing of insights and category reviews will offer a way to jointly create

²Simon Land, Sheldon Lyn, Ryan Murphy, Pieter Reynders, and Joel Saa-Seoane, "Revenue growth management in the COVID-19 crisis," May 15, 2020, McKinsey.com.

value and respond to rapidly changing consumer trends and shopper behaviors. In the medium to long term, we see winning sales leaders developing additional mechanisms to tailor customer engagement based on individual characteristics; for example, joint business planning could evolve to focus on deep, long-term joint value creation with a few selected partners while transitioning to B2B online portals for all other customers.

Last, for in-store sales excellence, leaders will digitize and automate route to market (RTM) and their direct sales force to super-charge activation at the point of sale. Companies will need to adapt their service models to changing retail restrictions. For example, route-to-market models have incorporated more contactless modes, which often proved more cost effective. The use of B2B platforms for distributors and end customers will become an integral part of the value proposition, and competition with digital disruptors and aggregators will intensify.

Companies should seek to dynamically define the RTM model for each customer segment, basing the frequency and mode of service on the growth potential and ROI. They can then redeploy sales efforts from underperforming segments to other value-added activities and adjust over time to accommodate for changes in demand and possible disruptions.

Sustain performance with agile new models

COVID-19 forced CPG companies to accelerate the pace of operations because their very survival depended on moving quickly. Decisions that used to require months of deliberations were made in

just weeks or days. Executives, having seen what's possible, have no reason to go back. An agile operating model will change the ways of working to achieve better outcomes more rapidly. Agility and a test-and-learn philosophy can sustain the organizational strengths that emerged during the pandemic and enable CPG companies to respond to evolving consumer needs in real time.

For instance, agile war rooms that use data to target consumer segments on a microlevel can contribute significantly to growth. Even companies with advanced marketing functions have increased revenues by shifting to agile marketing. Organizations are now experimenting with similar agile teams to go after opportunities for joint business planning that could yield double-digit growth from the companies' most strategic customers. Across commercial functions, the response center that was formed to lead the pandemic response should evolve to become the new model to deliver growth and instill obsessive performance tracking as the new way of working.

When everything changes, business as usual isn't an option. In times of crisis, companies can gain a robust competitive advantage with a razor-sharp focus on identifying pockets of growth. CPG companies that were preparing for incremental growth this year are now focused on navigating toward the best position in the next normal. Predictive growth, fueled by data and analytics, can give them the insights and tools they need and help transform core commercial capabilities to excel.

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