

# A REVENUE MANAGEMENT RESET IN CONSUMER GOODS

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A S THE UNPRECEDENTED consequences of the COVID-19 crisis unfold, one of the few universal certainties for consumer packaged goods (CPG) companies is that their established ways of revenue management will no longer work. Even best-inclass companies—those that have invested heavily in revenue management and achieved strong results over the last few years—will need to recalibrate their underlying assumptions about price elasticity, price sensitivity, and consumer buying patterns to find better ways to deliver value. Rapid changes in consumer and customer demand will require those companies—much like companies in other highly dynamic industries—to reset their revenue management practices in order to survive the coronavirus pandemic and thrive in the future beyond it.

What has changed since the pandemic began gathering strength in January? Consumers around the world are adjusting their behaviors and their willingness to pay as they face job losses and comply with government stay-at-home orders. Channel

landscapes are also changing rapidly, as the necessity of online shopping and the appeal of hard discounters increase. These changes have been markedly different across CPG categories, channels, and markets around the world. Some categories lost important purchase and consumption occasions thanks to the virtual elimination of out-of-home activities, while others—cleaning products, paper goods, over-the-counter medications—saw demand spike to such an extent that retailers couldn't keep their shelves stocked.

Looking forward, certain occasions will grow in importance while others diminish, and these changes may persist even after economies re-open. Companies' responses need to consider how needs and occasions have changed and will continue to evolve in a post-coronavirus world.

The good news is that many CPG companies know where to begin this reset, because they have successfully implemented revenue management practices over the last few years. Some learned to use

artificial intelligence to make sophisticated pricing moves that optimized value across their entire portfolio, rather than optimizing each SKU in isolation. Some companies developed new pack-price architectures to tap into new demand pools, and some undertook structured reviews of their trade and promotion expenditures to understand the ROI for each dollar they spent. The most advanced companies managed to improve in all three of these areas and increased their EBITDA margins by between two and five percentage points.

Their actions proved that revenue management works. But now the CPG companies need to prove it all over again in a new pricing reality, with new baselines, evolving consumer behaviors, and a different balance of power among their customers as channel preferences shift. The sooner they transform their revenue management capabilities and systems, the stronger they will be as the crisis continues to unfold in unforeseeable ways over the next months.

In particular, the reset CPG firms need should focus on three areas: embracing dynamism, delivering the best value to increasingly price-sensitive consumers, and rethinking their pricing across the packprice architecture.

#### **Embracing Dynamism**

The pace of change has accelerated dramatically for CPG companies, and we expect this dynamism—a high level of volatility requiring rapid responses—to continue even after the pandemic is over. That means that the adjustments companies make right now will serve them well in a post-COVID-19 world. Fully embracing dynamism in their way of working will allow them to develop quick, targeted price and promotion responses to demand signals, and also to strengthen partnerships with their most efficient key customers. The need is even greater in emerging markets, because their input cost and exchange rates tend toward volatility.

To accomplish that, companies need, first, a robust, near real-time way to track con-

sumer, customer, and competitor behavior to observe short-term demand shifts. Such a pricing and demand "watchtower" collects and analyzes broad sets of external data sources—such as web traffic patterns, daily retail panel data, online price scrapers, and sanitized credit card data—and incorporates them into easy-to-use, forward-looking dashboards and KPIs.

Second, CPGs will need to adapt both their internal and customer-facing processes to act on real-time information faster and with more flexibility. Adhering to the traditional "waterfall" approach of regular list price reviews, quarterly promotional calendars, and the like will leave a company vulnerable to attacks from more nimble insurgents, both online and in brick-and-mortar.

Third, CPG companies will need to reshape their value-creation activities with key customers in order to cement those partnerships. They should engage with their customers more frequently, while doubling down on pricing and promotion solutions that jointly build category value and yield a win-win for both partners. Finally, they should align their trade investments with shifting customer and channel priorities, even if it means overinvesting in the promising new customers and channels.

## Delivering the Best Value to Consumers

Downturns leave consumers with lower confidence and less money to spend. This combination sharpens their search for the best value, and can reset their expectations even after the downturn subsides. In the post-pandemic environment, a CPG company's portfolio needs to reflect these new realities. The mantra "deliver the best value" might seem obvious and aspirational at first glance, but it has a precise meaning that gives CPG companies three basic options: Larger packages with a lower price per unit; packs at lower price points better aligned with consumer demand; and targeted promotions. Any of these options can offer consumers the right amount of "more for less."

The larger packages give value-conscious consumers the ability to stock up and take advantage of a lower per-unit price. The smaller packages at an entry-level price point offer a lower out-of-pocket cost for the consumer in absolute terms, even though the price per unit is higher. Such packs are especially important in traditional trade, which predominates in emerging markets and serves rural or less affluent consumers.

A company can also preserve its current package prices but use targeted promotions—through limited time offers—to offer consumers either a lower pack price or the opportunity to stock up. Using the data-driven analyses we have described, they can build more flexible promotion calendars and look actively for partners who want to pursue an everyday-low-price strategy.

A mid-tier snacks company applied these tactics in a country that recently faced an economic downturn. The company's market share had begun to decline as lowend value players grew. To neutralize the threat, the company increased distribution of its own value brands. At the same time, it introduced a new pack-price architecture for its key brands to offer consumers lower price points that still yielded healthy margins, while minimizing the cannibalization of their existing SKUs. This "value" combination helped the company recover its lost market share without jeopardizing margins.

Amid all of these changes, CPG companies still need to protect profitability by striking the right balance between volume and margins for the portfolio, rather than focusing on strict margin thresholds for every SKU. Focusing on metrics for the whole portfolio allows companies the flexibility to deliver better value on a wide range of SKUs—while carefully identifying SKUs that allow higher margins. This balance ensures competitiveness and is predicated on understanding how consumers make choices and how the importance of certain products—and their willingness to pay for them—are evolving in real time. But in the short-term, companies should avoid making any price moves that risk damaging brand perception, such as the appearance of price gouging in categories that are experiencing huge spikes in demand.

### Differentiating Pack-Price Architecture

For the sake of speed and simplicity, CPG companies might be tempted to fall back on one-size-fits-all approaches. But such thinking will not stand up to the new revenue management realities that emerge after the pandemic. Changes in consumption occasions, shopper missions, and buying criteria will create new pockets of demand, and CPGs need capitalize on these opportunities quickly in a time where growth opportunities come at a premium.

The overall objective of a differentiated pack-price architecture is to better meet the unique needs of consumers across the key channels—such as online, grocery, mass, discount, club, and traditional trade. Moving away from uniformity, CPGs need to purposefully "de-average" their assortments, prices, and package architectures and tailor them to customers and their shoppers while taking into account the roles of discounts, promotional spend, and private labels in their portfolios.

This includes a robust online pack-price strategy. Gone are the days when a CPG company's online pricing activity was an appendix of its offline pricing strategy. As consumers gravitate toward online options, by choice or necessity, companies need a holistic revenue management strategy that considers the important differences in online occasions, buying criteria, and willingness to pay.

But all of this does not mean simply increasing SKU count. As retailers adapt to the new reality themselves, they will struggle to maintain full assortments and would rather increase focus on the most productive SKUs. CPGs need to proactively meet this challenge by ruthlessly prioritizing "must have" SKUs on a channel-level and rationalizing their long tail. With typical category assortments running in the hun-

dreds of SKUs, striking the balance between assortment size and productivity is a complex task that needs continual refinement.

WHEN THE PANDEMIC has subsided, we do not expect the new dynamism that it sparked to end. Customers will continue to experiment with new approaches, and the buying patterns and behaviors of consumers will have changed significantly. While we can't know which new habits will stick and which will revert back to previous patterns, the changes that occur will likely be so pervasive that they will radically reshuffle market shares across categories and geographies.

All of this makes it imperative that CPG companies act quickly and decisively right

now. Those that wait too long to prepare take a huge risk. CPG companies have a small window now to reset their revenue management capabilities and systems to reflect the new pricing realities to come.

Traditionally, in a time of crisis, a company would try to stabilize its business before adapting its pricing processes and policies and investing in tools and capabilities. This crisis is much different, because "stability" could remain elusive for a long time. We contend that a CPG company must undertake these steps concurrently, not sequentially. Adapting to the new price reality with the right vigilance and the right supporting advanced analytics may even bring about a new level of stability more quickly.

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