

Cleaning up

By John Jackson, Susan S. Mann and John Zealley

Demanding consumers, along with profound social and demographic changes, are creating both opportunities and threats for consumer products companies. The top performers have responded by rethinking their business models to emphasize innovation.

There was a time when selling soap powder, shaving cream and disposable diapers was a pretty straightforward and predictable business. Not any longer. The pressures on the demand and supply sides of the consumer packaged goods business are relentless. Even getting ahead through innovation is difficult, since new features and products are copied by competitors in a matter of months.

Yet somehow this “traditional” sector has managed to outperform the S&P 500 for the past five years—and the subset of companies we identify as the high performers in the industry have outperformed the S&P 500 on shareholder returns by a whopping 270 percent. How has this happened? Though a number of factors contribute to success, one thing is certain: The leading companies have redesigned their business models so that innovation permeates everything they do.

Today’s consumers are a demanding bunch. And thanks to the explosion of choice, they have exponentially more products and services to choose from. But they still aren’t satisfied. They expect much more from the brands they buy and use every day, and won’t think twice about trading down to private label if they perceive a better value. Nowadays, consumers judge products along multiple dimensions, including convenience, prestige, sensory appeal and health as well as the traditional standard: how the product functions.

Moreover, profound social and demographic changes are creating both opportunities and threats for consumer products companies. Those that can successfully understand and anticipate these changes and their impact on consumers will thrive and grow new categories and businesses; those that do not will decline as their products and markets continue to mature.

For example, aging consumers who want to look and feel like they did 25 years ago are turning to advanced cosmetic, hair- and skin-care products for help. Increasing numbers of working women with less time but more money for themselves and their families are using innovative products to “buy” their way out of traditionally female household chores. The rise of single-person households and a trend toward delaying marriage and childbearing means traditional assumptions about shoppers are no longer valid.

However, the rewards for insights into “new” shoppers are large. Similarly, the migration of consumers away from traditional channels such as TV and print signals the declining value of mass marketing. But this shift also means the companies that successfully target consumers using the emerging media mix can gain a distinctive source of competitive advantage that cannot be readily copied.

Rising costs—for raw materials and marketing, among other things—are putting pressure on margins. The value-driven retail landscape and the accelerated pace of innovation are leading to large-scale increases in advertising and promotion budgets to drive growth.

Rapid concentration in the retail sector has added to manufacturers’ challenges. Retail giant Wal-Mart is

About the research

We started with a competitor set of the 15 largest publicly held household products and personal care companies in the world, ranked according to annual sales. Eight of the companies analyzed were North American, two were from Germany, two from Japan, one each came from the United Kingdom and France, and one came from both the United Kingdom and the Netherlands.

We then applied the five standard Accenture performance metrics to the competitor set. First and foremost, we looked at longevity, measured as sustained total return to shareholders, experienced over three, five, seven and 10 years. We also evaluated growth, measured by revenue expansion; profitability, measured as the spread between the return on capital and the cost of capital; positioning for the future, represented by the change in market value not explained by current earnings; and consistency, measured by the ability to outperform the industry median on spread growth on a consistent basis.

Because this industry has a fairly long investment-to-returns cycle, we placed greater emphasis on the longevity-of-returns metric. Profitability can come at the cost of underinvesting for future needs, and growth can look good at first, but if a company becomes overextended, its long-term value will be destroyed.

Based on this analysis, there are four high-performing companies in this industry.

High-performance businesses have delivered above-average returns to shareholders in both the long run and the short run.

Total return to shareholders, seven-year TRS (CAGR) vs. five-year TRS (CAGR)



Total shareholder return includes stock appreciation (with splits) plus dividends. Data points are at end of month. Company F was not categorized as a high-performance business because it had poor profitability relative to its peers. SOURCE: COMPUSTAT; 10K; ACCENTURE ANALYSIS

one obvious example. The company is famous for driving down vendors' prices, in part by competing against them with its own, value-priced private-label products (see "Consuming passions," *Outlook*, June 2005). However, many of the best retailers now realize that collaborating with innovative brand manufacturers with deep consumer insights can help drive bottom-line results. Consequently, there has been significant growth in collaboration between retailers and manufacturers. This is because both sectors confront similar challenges from consumers, although product manufacturers must impress consumers at point of purchase and at point of use to drive brand loyalty.

So how have players in the household products and personal care industries, which are part of the consumer packaged goods sector, responded to these challenges and opportunities?

The best retailers now realize that collaborating with innovative brand managers with deep consumer insights can help drive bottom-line results.

The global spread of an affluent middle class, time poor but cash rich, means that a rising number of people are willing to pay significantly more for convenience items like mops that don't require a bucket of water and liquid soap, or pampering products like multi-bladed shaving systems and anti-aging creams—all of which also happen to have higher margins because they are distinctive. Innovative products not only create larger initial sales, they can also help lock in repeat sales through replacement components, thus enhancing loyalty and profit margins. Crucially, innovation has also helped turn relatively expensive consumer

durables (like electric toothbrushes) into grocery items (like Procter & Gamble's Crest SpinBrush).

Yet achieving consistent commercial success in innovation is far from easy in this intensely competitive industry, where more than 33,000 products were launched in 2004 in the United States alone. The majority of new products do not succeed. Worse, perhaps, consumers continue to complain that most of the industry's products look more or less the same.

However, a few companies in this sector—four in total—have risen to address the challenges and the opportunities to become high-performance businesses. Indeed, our research suggests that between April 2000 and April 2005, they generated 73 percent greater total return to shareholders than their peers (see "About the research," page 23). These companies have achieved higher performance by fundamentally rethinking their business models to position innovation as a pervasive capability driving an entire organization, rather than as a discrete strategy or initiative.

Innovation alone, however, is insufficient to ensure high performance in this industry. It has to be the right kind of innovation. And that hinges on five other competencies shared by all our high performers.

First among them is **strategic positioning**, the ability to exploit distinctive and relevant positions in the market. To achieve this, high performers constantly and fundamentally question where to invest for growth, when to "harvest" mature markets or products, and when to acquire or dispose of product and market positions. (For more on market focus and position, see "The right place, the right time," page 42.)

The ability to execute these positioning decisions is vital. For example, Avon Products has invested in beauty boutiques for its Chinese sales reps as a way to establish an important foothold in China, which has not allowed door-to-door selling since 1998.

Meanwhile, today's Avon reps are also just as likely to be Russian or Brazilian as American or British.

Establishing effective strategic positioning relates directly to another of the high performers' most significant core capabilities, **customer centricity**. High-performance businesses in this sector are exceptionally good at understanding their target consumers: who they are, where they are, how they use the companies' products, and what they really want and need. If necessary, they'll even reconstruct the company around the consumer. UK-based Reckitt Benckiser, for example, put its innovation center for insect sprays in Australia because that's where some of the world's nastiest bugs are found and where demand for the stuff that kills them is exceptionally high. (For an interview with Reckitt Benckiser CEO Bart Becht, see page 36.)

High performers, indeed, practically live with their consumers. While their marketing functions tend to be globally organized, they establish highly focused, intimate, in-country customer organizations that allow them to keep track of changing consumer tastes within particular market segments. Procter & Gamble involves consumers directly in its product development efforts—witness its recent TV ad campaign, soliciting consumers to pick the next flavor for Crest Whitening Expressions.

These industry leaders are also getting a better understanding of the value

of their advertising and promotion investments. For example, in December 2004, P&G announced its investment in Arbitron and VNU's Project Apollo, which would create a model measuring the impact of media exposure and consumer consumption in the industry. Traditionally, the absence of such information has held back progress in innovation and marketing; after all, it is hard to be happy with your return on innovation if you don't know what it is.

Traditionally, R&D has been more focused on technology, but many of today's breakthroughs are coming from the design side. P&G brand teams include top designers who rethink how consumers actually experience products. The company's Pampers Kandoo baby wipes, for instance, are designed for toddlers to use by themselves, a direct response to the observation that growing children want to be independent. Similarly, Olay Daily Facials give women a spa-like indulgence at home, and Swiffer mops and dusters make household cleaning faster and easier for today's busy men and women.

The development and commercial evolution of high performers' product portfolios is driven by insights from multiple sources, including real-time interaction with customers. And those insights have allowed high performers to beat out competitors still reliant on traditional data models that do not provide a real understanding of consumers or of competitors whose portfolios remain too broad. Indeed, by narrowing their brand portfolios to concentrate on specific categories, and then continually reviewing and improving them, high performers create a "virtuous circle" that enables them to boost spending on future product promotion and innovation.



Clorox: Changing the game

With only \$4 billion in annual global sales, The Clorox Company isn't exactly a giant among household and consumer product manufacturers. Indeed, back in the early 1980s, pundits were predicting that its "mature and boring" bleach business would prompt Clorox to sell out entirely to German company Henkel, which had taken a hefty stake.

Liquid bleach is still the Oakland, California-based concern's biggest product, accounting for more than \$400 million of its revenues. But Clorox has also launched some of the most successful product innovations on the market, innovations that have boosted its sales and helped double its market valuation in five years. (It actually bought out its German partner last year.)

However, Clorox is not your grandmother's bleach; now it is embedded in an astonishing array of products, from bleach pens to cleaning wipes and disposable cleaning tools. The company has accomplished this by applying consumer insight to the process of product innovation—two of the core capabilities demonstrated by high performers in this industry (see story). The \$223 million that Clorox has invested in R&D over the past three years has paid off big time.

Clorox uses the term *gamechanger* to describe its most significant product innovations. Its Glad Press 'n Seal wrap, for instance, successfully addresses two of consumers' biggest complaints about plastic wrap—that it's awkward to use and it doesn't cling properly. Similarly, Glad ForceFlex trash bags boast a unique diamond texture that stretches to prevent punctures and rips from sharp or heavy objects like empty pizza boxes. Now Clorox has applied the same insights to tackle the chore people seem to hate most—cleaning the bathroom.

It recently introduced the BathWand, an ergonomic tool with a 23-inch handle that you can use without having to bend or stretch. The wand comes with disposable cleaning pads, pre-loaded with—what else?—concentrated Clorox cleaner, which lab tests show works better than the leading bathroom cleaner. The starter kit has a suggested retail price of \$9.99—pretty steep compared with a bottle of bleach—but since consumers will pay plenty for such convenience, Clorox is clearly on to yet another winner.

The Clorox Company calls its most significant product innovations *gamechangers* (see case studies)—and changing the game is exactly what it and these other successful innovators do. High performers know that consumers want more than solutions. Finding fresh and valuable variations of familiar products is what they look forward to. And the high performers in this sector excel at delivering "delightful" consumer experiences—often in the most unlikely places. Clorox's ToiletWand has disposable Clorox-embedded heads, which are thrown away—along with the germs—after use. According to the Schneider/Stagnito Most Memorable New Products Survey, the ToiletWand was among the top 10 new products introduced in 2004, in terms of both consumer awareness and purchases.

What's more, high performers don't confine their innovation to inside their four walls. To deliver the complete consumer experience and reduce the costs of innovation,

they will pursue **collaboration and partnerships** with a diverse network, including retailers, suppliers, scientists, appliance manufacturers and even competitors. The November 2002 alliance between staunch competitors Clorox and P&G, for example, combined the strength of Clorox's Glad brand name with P&G's powerful research capabilities and added Glad ForceFlex garbage bags and Glad Press 'n Seal plastic wrap to an already successful product line. P&G has a significant stake in this joint venture with Clorox, with an option to increase its stake over time.

All our high performers are, of course, paragons of **operational excellence**, since cost control and superior execution make much more predictable contributions to the bottom line than innovation. And their **talent and change management** prowess is formidable. These organizations empower their people to act like entrepreneurs and foster a culture that clearly rewards risk taking, performance and

teamwork. For example, P&G united scientists from the company's Pur water purification unit and from dishwasher detergent Cascade to help develop Mr. Clean AutoDry, a car-washing sprayer product.

These companies' leaders also set the tone by touching the products, walking the stores, and reaching out to consumers and employees, thus inspiring heightened employee engagement in the business. At Reckitt Benckiser, managers rarely wear ties, and they're known for spending time in retailers' household-cleansers aisles. Many of these leaders have helped restructure their organizations, transforming their companies into stock market stars.

To be sure, sustaining high performance in such a fast-changing industry won't be easy. Consumer demand for innovation and the pace of product innovation continue to escalate. Maturing markets and categories need continual renewal to

Procter & Gamble: Reaching out

Procter & Gamble is a US consumer products powerhouse. Its proposed \$57 billion acquisition of The Gillette Company would create a behemoth with more than \$60 billion in revenues. The corporate combination unites two innovation juggernauts. As a result, P&G would bolster its oral care portfolio and gain a stronghold in wet shaving, enabling the company to become the leader in the personal care market.

The pursuit of collaboration and partnerships is a hallmark of high performance in this sector (see story), and P&G has been a master in this area.

By linking up with Gillette, Cincinnati-based P&G would also boost its innovation capacity in a burgeoning sector of the personal care market—male grooming, a \$16 billion global market. Additionally, more men these days are shopping, and retailers want to know a lot more about them; research suggests men are much more price inelastic than women and spend up to 30 percent more on the same supermarket shop. P&G is well placed to help these men—and to benefit in the process.

The company's multifaceted Connect + Develop program is designed to enhance internal collaboration as well as to help source technology, businesses, products and talent outside of P&G. One key component of the program, InnovationNet, an intranet portal that is sometimes referred to as a "global lunchroom," helps innovators collaborate and exchange ideas across businesses, regions and functions. Innovators span the entire P&G organization, including R&D, engineering, market research, purchasing and patents.

Another interesting collaboration is YourEncore, which was created by P&G and Eli Lilly and Company (now operating independently) to leverage a network of recently retired scientists and engineers as consultants for short-term projects. Collaboration and partnerships like this are helping P&G drive down the rising cost of innovation and speed the pace of innovation.

drive growth. Partnerships are not easy to maintain. The four companies currently cleaning up will have their work cut out for them in their continuing efforts to come up with new products and features to delight their demanding consumers.

About the authors

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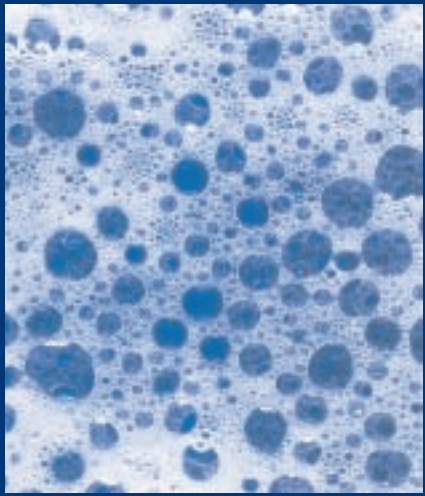
Susan S. Mann is a senior manager in the Accenture Retail and Consumer Goods & Services/Strategy groups. For

more than seven years, she has helped formulate sales and marketing, operating and M&A strategies for leading consumer products and retail clients. Ms. Mann, who is based in Wellesley, Massachusetts, has spent the past two years as Accenture's global industry program manager for retail and consumer goods; part of her responsibility in this role is to conduct high-performance business research and analysis in these industries.

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By the numbers Taking care of business

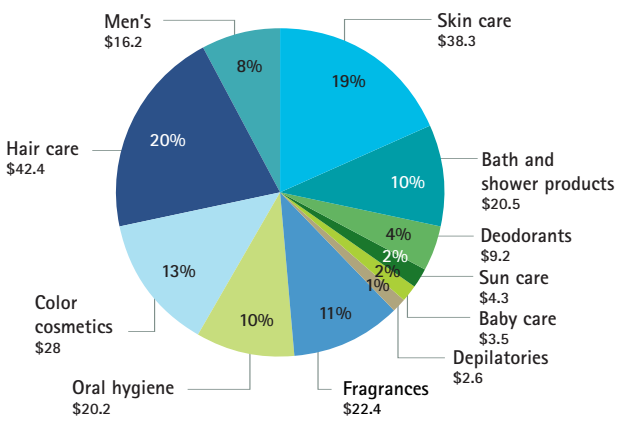
The global markets for personal and household care products are huge—and have been growing at 3.8 percent and 2.8 percent, respectively, since 1998.

The personal and household care markets are truly global and are growing.

Cosmetics and toiletries worldwide market

Global size 2003: \$200 billion*
CAGR (1998–2003): 3.8%

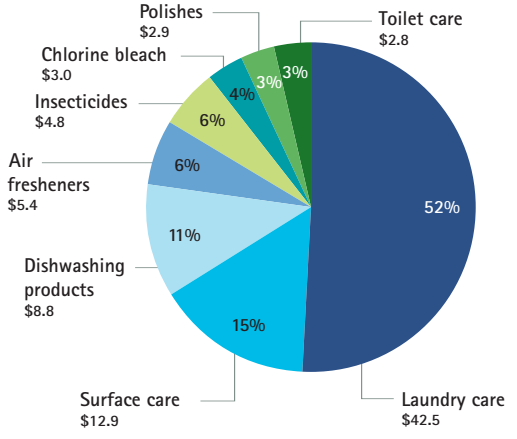
US\$ billion



Household care worldwide market

Global size 2003: \$83.2 billion*
CAGR (1998–2003): 2.8%

US\$ billion

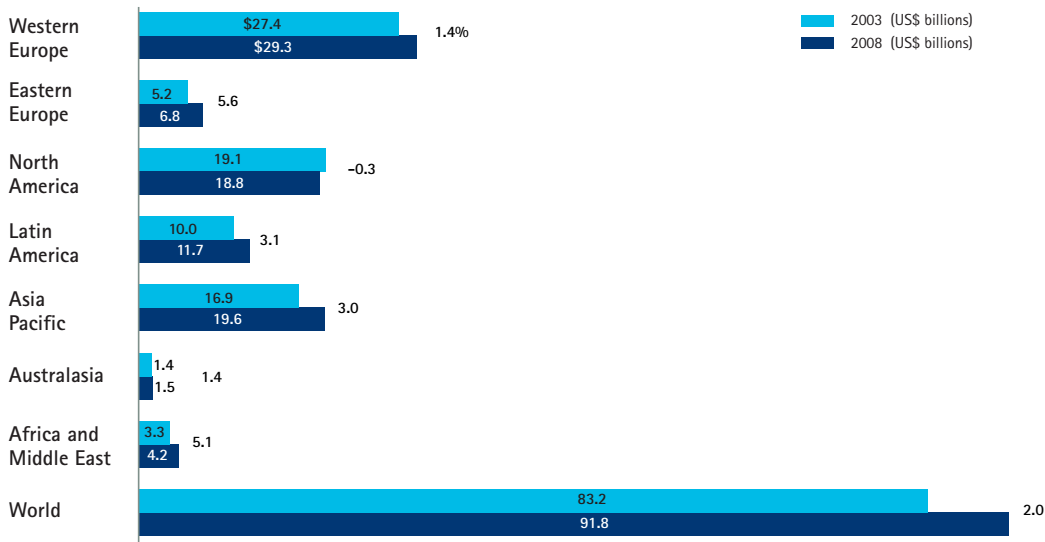


* Based on retail selling prices; the numbers in the individual segments do not add up to the global market size of \$200 billion as elements in both the men's grooming sector as well as in cosmetics are double counted.
SOURCE: EUROMONITOR

The household care market is expected to grow 2 percent from 2003 to 2008, or a total of \$8.6 billion.

Household care: Forecast sales growth CAGR (2003–2008)

US\$ billion

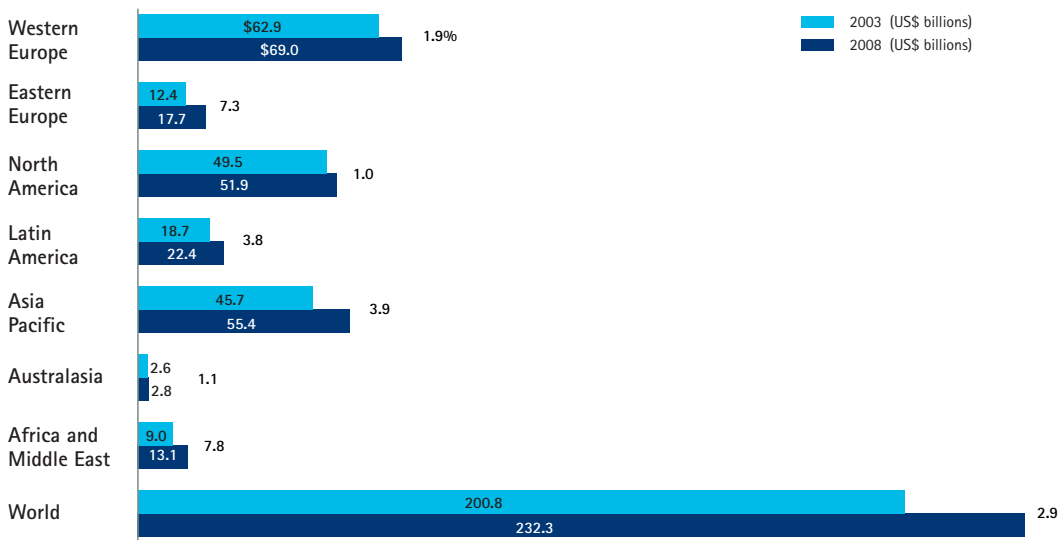


SOURCE: EUROMONITOR

The cosmetics and toiletries market is expected to grow 2.9 percent worldwide between 2003 and 2008 for a total growth of \$31 billion.

Personal care: Forecast sales growth CAGR (2003–2008)

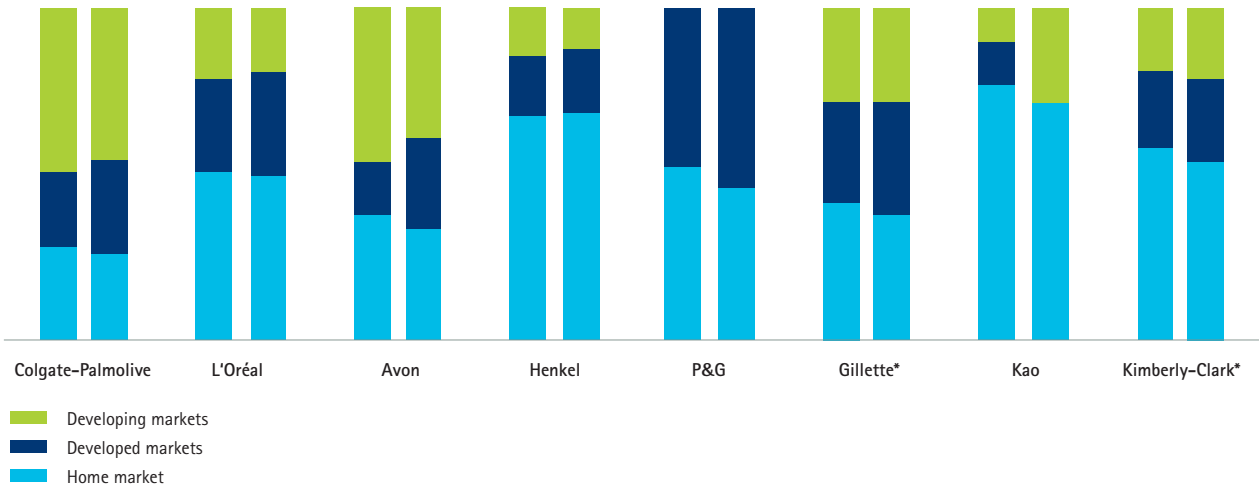
US\$ billion



SOURCE: EUROMONITOR

In response, all major players are expanding outside of their domestic markets.

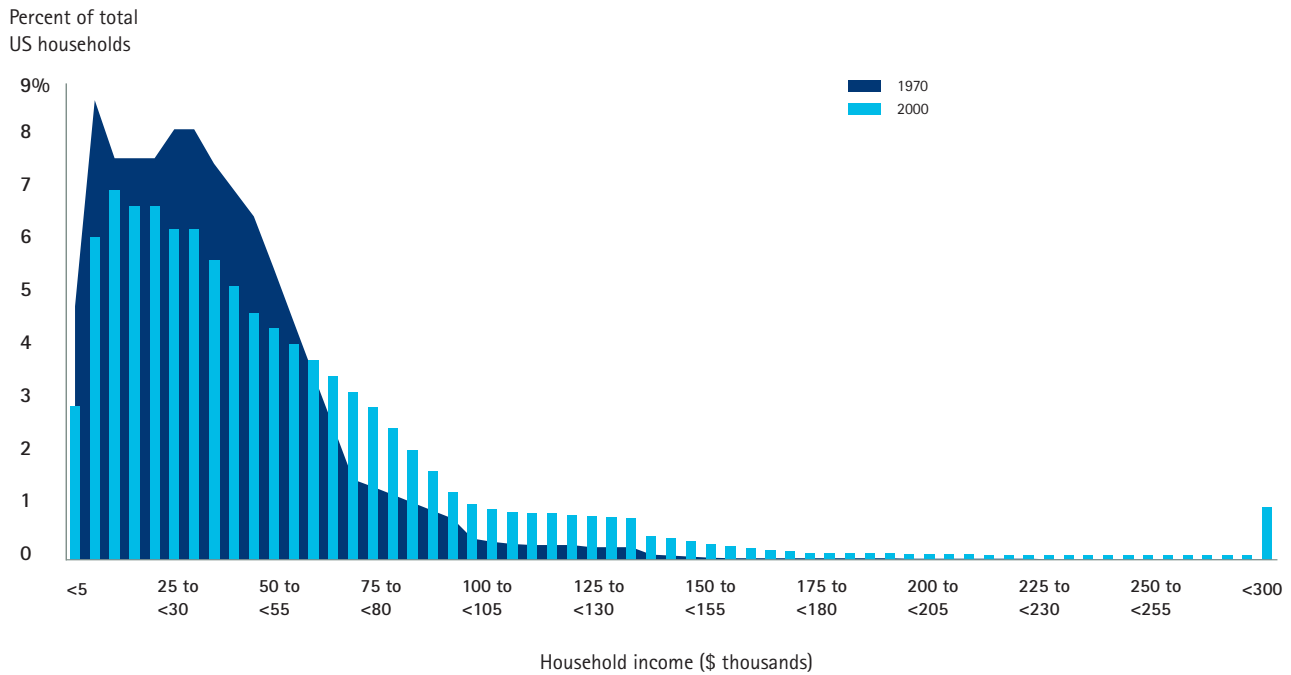
Globalization trends, 2000–2004



* 2002–2004
SOURCE: ACCENTURE ANALYSIS

Consumers are much more affluent, and are demanding value-added products.

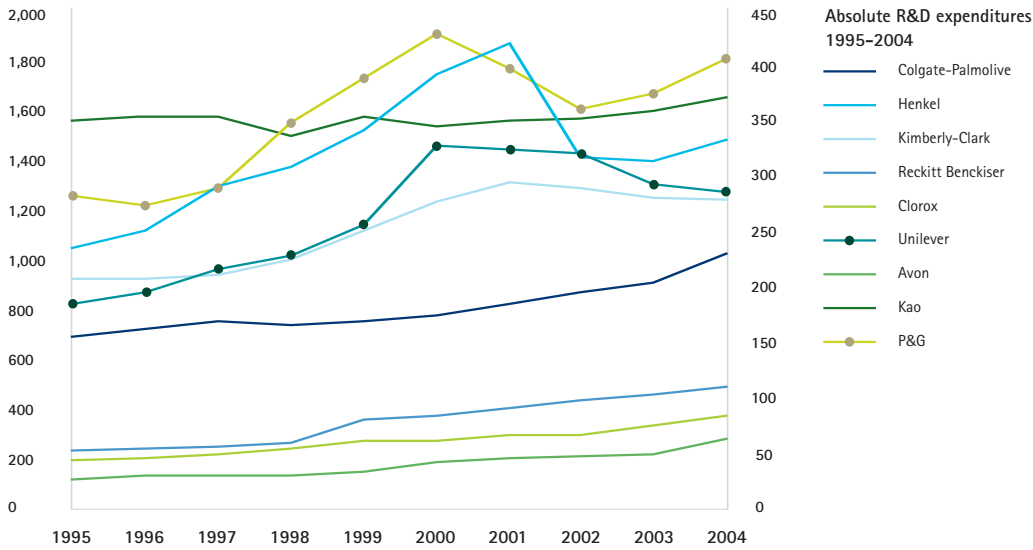
US household income distribution
1970 and 2000



SOURCE: US CENSUS BUREAU PUBLICATION: "MONEY INCOME IN UNITED STATES: 2000"
ALL VALUES IN 2000 CPI-U-RS DOLLARS [REAL DOLLARS]. INCREMENTAL VALUES INTERPOLATED FROM LARGER INCREMENTS WHEN NOT AVAILABLE.

Success in innovation is becoming less about research and more about development.
 Although high-performance companies have spent more in absolute terms on R&D . . .

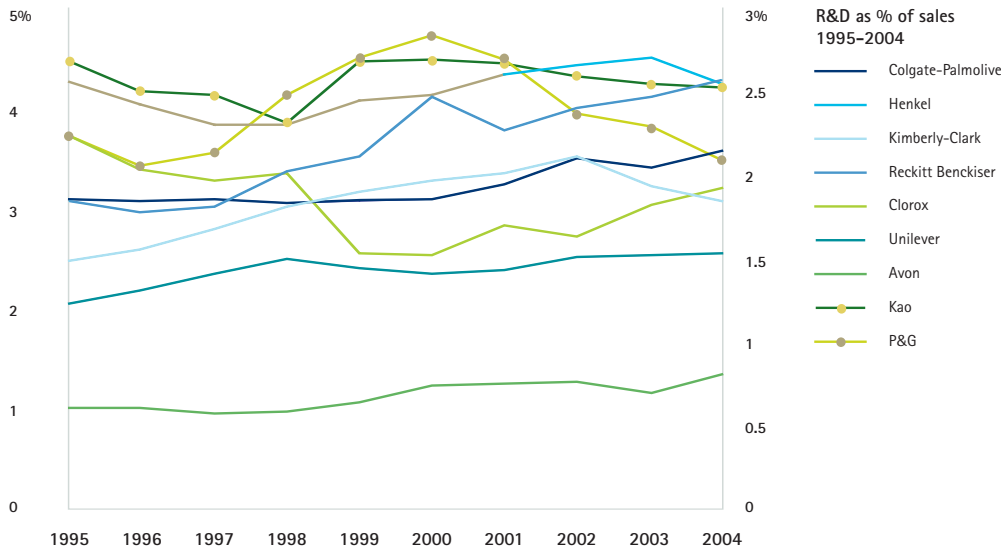
Absolute R&D expenditures: 10-year trend
 (P&G and Unilever left axis, all others right axis)



SOURCE: ACCENTURE ANALYSIS

. . . they have offset this against higher sales from better commercialization
 of innovation.

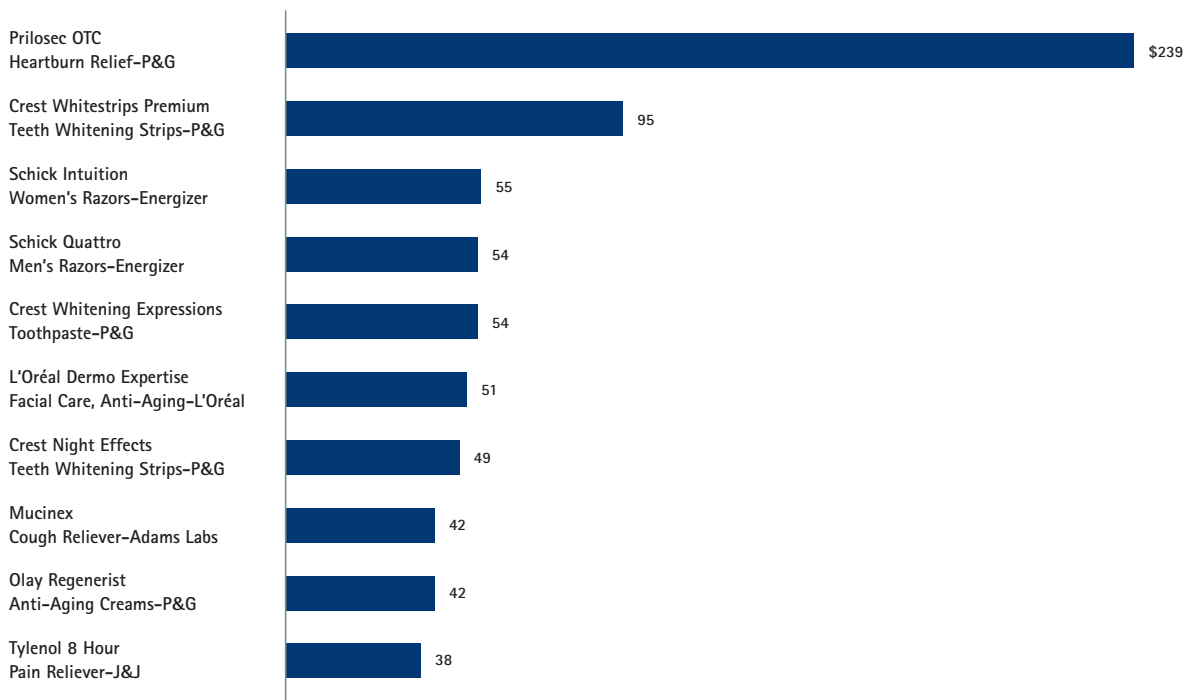
R&D expenditures as % of sales, 10-year trend
 (P&G and Kao left axis, all others right axis)



SOURCE: ACCENTURE ANALYSIS

The majority of innovation comes from extending product lines, although the benefits of blockbuster products are great.

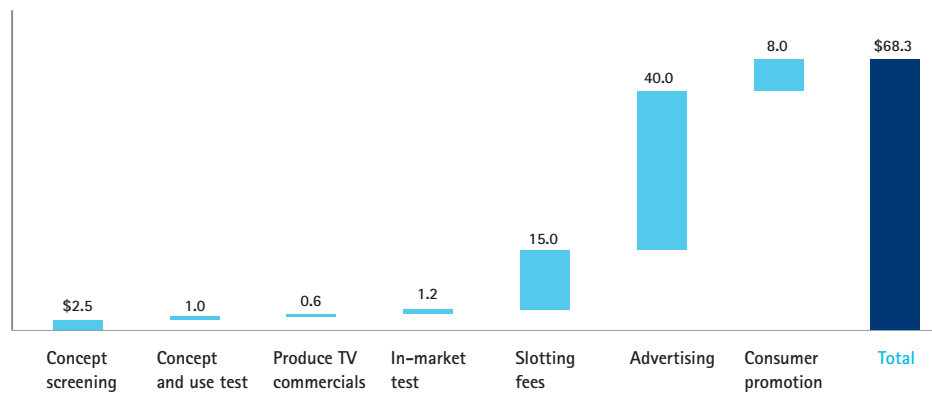
Best-selling new products, 2003–2004 (\$ millions)



SOURCE: IRI, TIMES & TRENDS, MARCH 2005

But the costs and risks of launching truly innovative products are high.

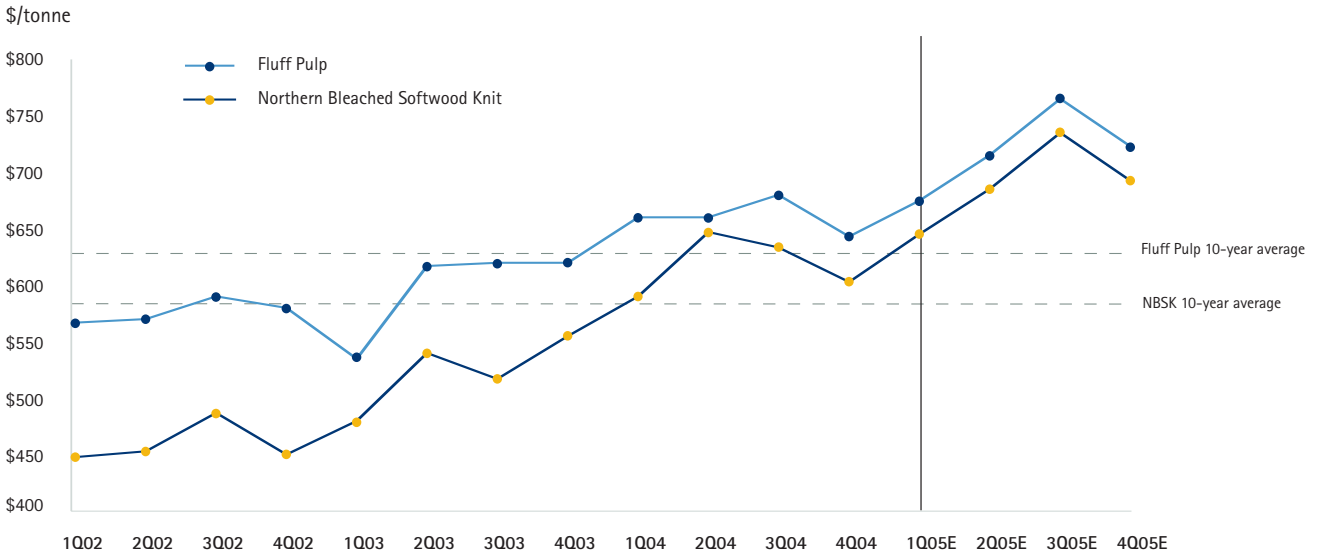
Average new product launch costs



SOURCE: IRI

Commodity costs are rising, putting pressure on margins. Prices in pulp—as well as resin, energy and other imports—are higher.

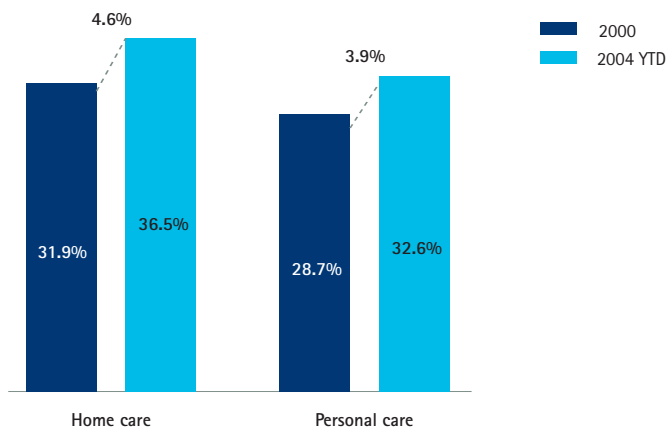
Pulp pricing, 2002-2005E



Northern Bleached Softwood Knit is used in cardboard packaging.
 Fluff Pulp is used in paper products such as disposable diapers and feminine hygiene products for absorbency.
 SOURCE: AMERICAN FOREST & PAPER ASSOCIATION AND SMITH BARNEY

And there is an increasing use of promotions to drive sales in the household and personal care categories, which again increases the cost of doing business.

% of units sold on promotion in the United States



SOURCE: JP MORGAN ANALYST REPORT, "FIRST SIGN OF AGING" A PERSPECTIVE ON GLOBAL HPC, OCTOBER 6, 2004

Companies are jockeying for market position and focusing on core brands.

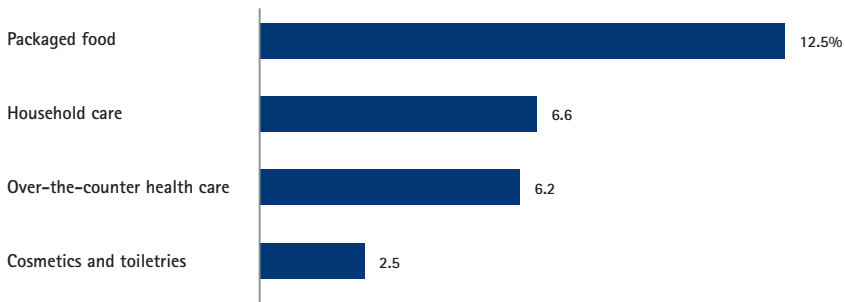
Household and personal care M&A and divestiture activity

Year	Acquirer	Company acquired	Strategic benefit
2005	P&G	Gillette	Market share leadership in personal care
2005	Alberto Culver	CosmoProf	Expands distribution of professional beauty products
2004	Lehman Brothers	Unilever home care brands	Unilever divests low-growth noncore brands
2004	Gillette	Rembrandt brands (Den-mat)	Enters fast-growing teeth whitening category
2004	JW Childs	P&G's juice business	P&G divests lower-priority juice business
2004	Clorox	Henkel's 29% stake in Clorox	Henkel sells stake to fund Dial acquisition
2004	Colgate-Palmolive	GABA Holding	Enhances European oral care offerings
2004	Henkel	MAS detergents in Mexico	Strengthens Mexican detergent business
2004	Henkel	Dial	Access to North American market and strong value-priced detergent brands
2003	P&G	Colgate's European detergents	Builds detergent presence in Western Europe
2003	P&G	Wella	Increases presence in professional hair care and expands geographic coverage
2003	Reckitt Benckiser	Clorox SPB & X-14 brands in Brazil	Boosts insecticides and surface care shares in LA
2003	P&G	Glide brand (Gore & Associates)	Increases presence in oral hygiene
2003	Estée Lauder	Darphin	Expands presence in premium skin care

SOURCE: EUROMONITOR; S&P INDUSTRY SURVEY OF HOUSEHOLD NON-DURABLES

High-performance businesses focus on meaningful innovation and fewer power brands, which helps them stave off private labels more effectively than packaged food companies.

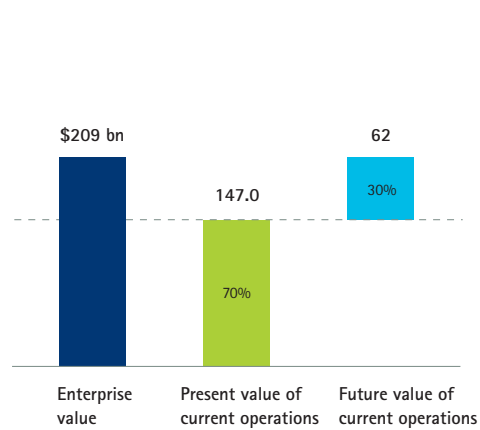
Private-label penetration (2004, % value)



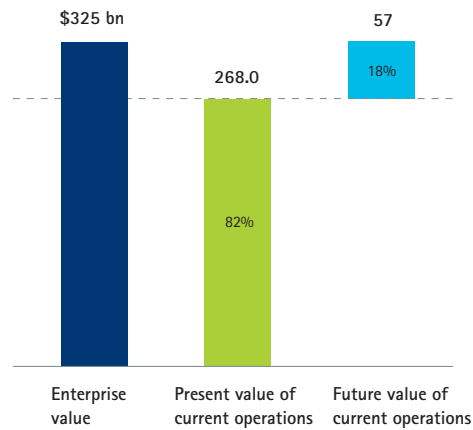
SOURCE: EUROMONITOR

The market has significantly higher expectations for growth for high performers versus their peers, which is ultimately reflected in their enterprise value.

Corporate value of operations, high-performance business



Corporate value of operations, rest of peer group



■ Value driven by current assets performing as they do today
■ Value the market expects from future investment plans

SOURCE: S&P, ONESOURCE, YAHOO FINANCE, ACCENTURE ANALYSIS