POINT OF VIEW

Winning the CPG Zero-Sum Game by Uncovering Hidden Growth Pockets

FEBRUARY 2017

Growth delivered.

Executive Summary: An Active Pursuit

Shifting market dynamics are expediting the pace of change and making it more difficult to find true growth.

- New trends, emerging market entrants, and rampant merger and acquisition activity have had a profound impact on share and value creation.
- Smaller CPG companies captured 3.1 dollar share points from larger players during the past few years, with the trend continuing in 2016.
- Larger companies are rewiring their growth strategies to include mergers among like-sized firms and acquisition of smaller firms that play in high-growth market sectors.

Drive growth by finding value hidden in plain sight within key growth pockets.

- Dissecting mature categories often leads to the revelation of high-potential sub-segments.
- Adopting a top-down approach to market analysis will reduce risk and provide visibility into key growth pockets, leading to the foundation of demand portfolio strategy development.
- CPGs are capitalizing on growth opportunities by using a combination of acquisition, renovation and innovation strategies.

Reactive strategies stymie growth opportunities and breed inefficiencies.

- Acquisition strategies must be based on a common understanding of the holistic corporate strategy and available growth platforms.
- Without this understanding and senior-level buy-in, it is extremely difficult to advance against real growth opportunities.
- Reactive strategies often result in the evaluation of potential partners/acquisition candidates simply because they are "on the market" and not because they are part of a true, value-adding growth platform.

Consider a structured approach to defining a demand portfolio strategy based on identifying key growth pockets. IRI has partnered with several Fortune 100 CPG manufacturers and private equity firms to identify methods to develop playbooks for uncovering attractive target candidates to define platforms for growth.

- A top-down approach to demand portfolio strategy identifies target candidates based on their level of participation in the most attractive pockets of growth, as well as fit with the manufacturer's strategy.
- By identifying relevant opportunities that bolster corporate goals and outlining a clear path to advance against these opportunities, a top-down approach secures senior-level sponsorship.
- Even in mature sectors plagued by stagnant growth, this approach consistently yields double-digit growth pockets.

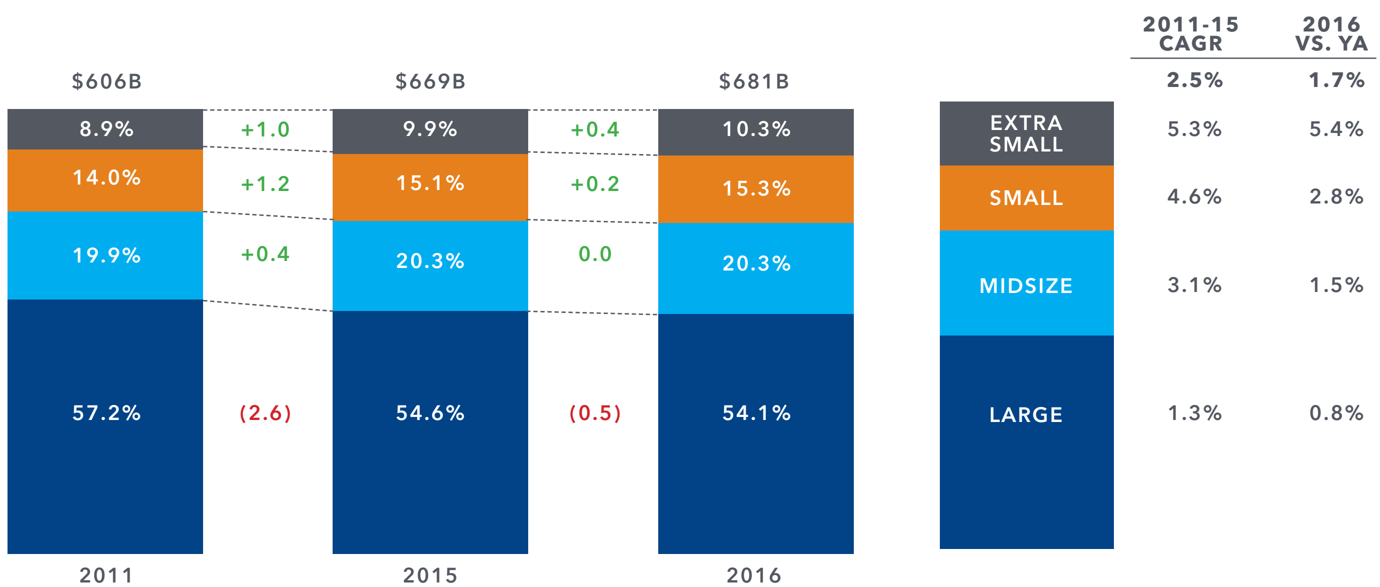
Winning the CPG Zero-Sum Game by Uncovering Hidden Growth Pockets

The mature consumer packaged goods industry is in a constant state of dynamic evolution, as new trends, emerging new entrants, and rampant merger and acquisition activity shift share and value creation among market participants. Company size and dominance are not equivalent to sustainable growth. Rather, large companies today are being inspired by smaller ones and adding them to their portfolios. Examples abound. In 2016 alone, Hormel Foods acquired Justin's; Dr. Pepper Snapple Group acquired Bai Brands; and Conagra Brands acquired Frontera Foods. The case for change is clear: Large companies are constantly pressured to grow, but growth has been more consistently achieved by their unencumbered, smaller competitors. During the past several years, large consumer packaged goods (CPG) companies lost 3.1 dollar share points, valued at more than $20 billion, to smaller, more nimble, more flexible competitors. These smaller companies are winning because they have the ability to spot dynamic consumer trends and the flexibility to quickly act on them, particularly those that can command a premium in a particular niche.

EXHIBIT 1

Smaller players have traditionally grown faster, capturing share from larger companies.

$ Sales % of Total Store



~$20B in Industry Sales Have Shifted Away from Large Companies to Smaller Players Since 2011

Note: M&As accounted for in company size categorization. Small: <$1B, midsize: $1B-$5.5B, large: >$5.5B sales in 2016; excludes PL sales.
Source: IRI ILD POS database, 2011-2016, MULO+C; IRI Consulting analysis.

Changing market dynamics are shrinking time and expediting the pace of change, leading to several large companies' search to evolve and revitalize their path to growth. Large companies have achieved momentum through mergers among like-sized firms and participation in high-growth categories through the acquisition of smaller firms.

Identifying strategic platforms for growth and determining the most relevant strategies to participate in them is key to prospering in today's stagnant and mature CPG marketplace, where most gains come from taking share away from competition. Clearly and accurately defining the universe from which pockets of growth will be derived is critical. If the scope is too narrow, it renders the effort myopic. If the scope is too broad, it becomes difficult to implement and access due to organizational dynamics and the buy-in necessary to creatively pursue adjacencies.

CPG Marketers Must Invest to Obtain a Granular Understanding of Growth Pockets That Are Significantly Outperforming Other Segments.

Granularity is required when identifying "growth pockets," as often large, mature categories need to be dissected and analyzed in detail to uncover sub-segments that can spark innovation and drive growth. As top growth pockets are identified, a company can participate in them through:

Acquisition—**Buy** into them

Renovation—**Borrow** ideas and inspiration

Innovation—**Build** them

How a company decides to participate in selected growth pockets is highly dependent on overall strategy, existing core competencies, risk appetite, and merger and acquisition budget. Ultimately, the level of attractiveness of a growth pocket will depend on an assessment of external variables, as well as target candidate internal assessment variables.

Drive Growth by Finding Value Hidden in Plain Sight within Key Growth Pockets

Focused identification of growth pockets can help reinvigorate the way CPG manufacturers approach a commoditized and mature category. Undertaking a holistic top-down approach can yield a set of double-digit growth pockets that provide an entirely new lens through which to view a mature market. Having a clear lens into growth potential greatly reduces risks and provides visibility to outsized gains. For instance, growth in a large category like commercial bread may be stagnant, but growth in a sub-segment, like better-for-you (BFY) organic sliced bread or dinner rolls, may be beyond double-digit rates.

An accurate perspective into how a company wants to participate in specific growth pockets helps provide direction to the company's overall strategy, both at the corporate and business unit levels. Opportunities may exist to renovate a very large business unit (borrow), execute a game-changing acquisition (buy) or find inspiration that drives an organization to the next level of competitiveness (build).

Reactive Strategies Stymie Growth Opportunities and Breed Inefficiencies

Many times, when a proactive approach to growth development is not being followed, a company's corporate development division may be fraught by paralysis, caught in an endless cycle of evaluating companies that become available for sale, but not having a common growth-platform understanding that allows acquisition strategy to be aligned with corporate strategy. These CPG manufacturers are caught in reactive mode. They are not sure how to strategically identify, approach and advance real opportunities. In these instances, companies often end up acquiring brands simply because they come up for sale.

Two Roads, One Goal

IRI has worked with several Fortune 100 CPG manufacturers and private equity firms to identify two key methods to develop value-adding, effective playbooks that help companies uncover attractive target candidates and develop a robust demand portfolio strategy that is intrinsically connected to consumer demand and the company's value proposition:

- Top-Down Approach is favored by manufacturers and selects potential target candidates based on their level of participation in the most attractive pockets of growth, as well as fit with the manufacturer's strategy.
- Bottom-Up Approach focuses on identifying fast-growing companies and their capabilities first, and then filters them based on strategic priorities.

Both approaches are relevant and not mutually exclusive. The rest of this article will focus on the top-down approach. The bottom-up approach and an integrated way to leverage both of these strategies will be addressed in an ongoing series of articles.

EXHIBIT 2

Two Methods for Developing a Playbook

	Key Findings	Implications
Top-Down Approach	• Identifies **growth pockets** among food and beverage categories • Within these growth pockets, **best companies** are identified and **vetted based on criteria developed in collaboration with clients. Potential criteria may include premium and health and wellness positioning, accessibility and extendibility**	• Focus on growth pockets and category attractiveness yields: » **Growth sustainability** (Category + Company) » **Long-term investment horizon** • This type of approach **resonates with manufacturers** because it supports long-term growth strategy
Bottom-Up Approach	• Reveals the **fastest-growing companies across F&B regardless of the category performance** • By definition, companies derived from this approach will: » Tend to be **smaller** (highest growth rates) and » May be **King of the Island** (single player conquering less attractive categories)	• Focus on company growth regardless of category attractiveness yields: » Focused view on **company growth** » **Short-term investment horizon**

A consolidated top-down and bottom-up approach provides benefits from both methods and helps manufacturers identify a holistic list of potential acquisition candidates.

Identifying and Capitalizing on Pockets of Growth– The Art and Science of the Top-Down Approach

The top-down approach provides a well-structured path for identifying strategic growth platforms and determining the most relevant opportunities and how to act on them. As these initiatives often set broader corporate goals and direction, they require sponsorship from top executives, ensuring the appropriate flexibility to explore all pockets of growth. These are not only available within new, adjacent areas, but also may be hidden within existing business lines, requiring the appropriate level of seniority to challenge current approaches and philosophies.

For example, a food and beverage company with some participation in the frozen meals category approached IRI looking to grow its business inorganically and develop a demand portfolio strategy in frozen and refrigerated meals. Identifying growth in a category that is almost stagnant (0.2 percent annual decline versus 1.4 percent growth in food and beverage as a whole) was not an easy task. Yet undertaking a holistic top-down approach yielded a set of growth pockets, each with $100MM+ in size, yielding double digit growth. These growth pockets provided an entirely new lens through which to view a mature market. This outcome would not have been possible without the support of top executives willing to challenge the status quo.

EXHIBIT 3

Top Growth Pockets in Meals Category

Top-Performing Meals Category

Dollar Sales and Volume Sales, CY 2011-2014 and 52 weeks ending 4/17/2016, MULO+C

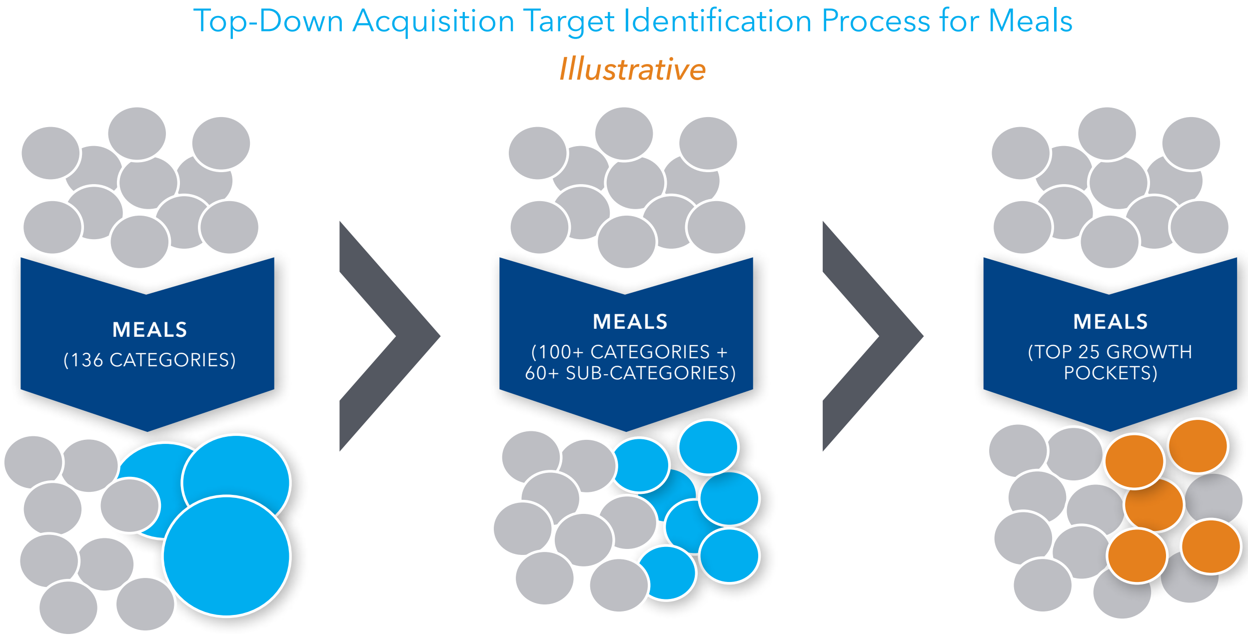
Category	L52 $ Sales ($MM)	2011-14 CAGR	L52 vs. YA	L52 Vol. Sales vs. YA	PL Contrib. to Growth
BFY Ethnic-Focused Entrees	$280	6.7%	12.2%	8.0%	11.0%
Growth Pocket 2	$275	8.0%	11.9%	11.5%	2.1%
Growth Pocket 3	$260	31.2%	23.2%	32.5%	60.0%
Growth Pocket 4	$450	18.2%	10.5%	7.2%	55.0%
Growth Pocket 5	$2,100	7.5%	11.0%	5.1%	34.7%

Source: IRI ILD POS databases; IRI Freshlook database; MULO+C; IRI Consulting analysis.

To identify key opportunities, traditional meal categories were dissected across myriad UPC-level attributes and variables, including type of meal, packaging, better-for-you meals versus more indulgent meals, flavor, Hispanic versus non-Hispanic themed meals, and others. Part of this includes defining BFY in terms of ingredient claims, packaging innovation and consumer benefits.

EXHIBIT 4

Top-Down Approach



Success in identifying growth pockets springs from finding sizable sub-categories that are driving growth in the short and medium term. For example, frozen meals have declined in sales during the past year, yet within frozen meals, better-for-you single-serve entrees and better-for-you multi-serve entrees have been growing steadily, in sync with health-and-wellness and convenience macro trends.

If the better-for-you single-serve frozen meals growth pocket has a handful of key players that vary in size, it is likely that a company interested in participating in this growth pocket could do so through:

- **Acquisition (Buy):** How the company decides to absorb its acquisition can vary from "full integration" of the target's capabilities into the organization (changing the target's brand to that of the company's) to "full independence" of the target's operations (letting it continue to grow organically but under new ownership).
- **Renovation (Borrow):** A company may seek to learn from a target candidate to renovate its existing business. Continuing the example of the company that was interested in better-for-you meals growth pockets, it may decide to change part of its current frozen meals business to produce an offering similar to that of the target.
- **Innovation (Build):** A company can choose to build the capabilities directly and thus gain participation into the growth pocket. In our previous example, even though the company has a presence in frozen meals, penetrating the better-for-you single-serve frozen meals growth pocket may not be entirely feasible through renovation. The company's capabilities, for example, may be vertically integrated into traditional, artificial ingredients. To gain access into the organic or non-GMO sector of the BFY space, for instance, the company would need to change the source of its ingredients, including significant costs added to its value chain. In this scenario, gaining entry through acquisition would likely be faster and more efficient.

EXHIBIT 6

IRI's Internal and External Growth Pocket Attractiveness Levers

Category Attractiveness	
Accessibility	*Can the target provide accessibility to other channels or new types of packaging?*
Category Extendibility	*Is the category broad enough?*
Brand Extendibility	*Is the target brand limited to one category and can it be leveraged as a platform?*
Availability	*Is the candidate available for acquisition?*
Aligned to Positioning	*How are the target's brands positioned?*
Other	*Other?*

Internal Target Acquisition Candidate Attractiveness	
Category Performance	*What are the category tailwinds and how is growth being driven?*
Consumer Demand	*Who is driving demand?*
Channel Dynamics	*What is the opportunity to drive growth through distribution?*
Competitive Intensity	*How competitive is the market?*
Role of Brand	*Are brands playing a big role?*
Price Tier Opportunity	*Are there opportunities to differentiate within specific price tiers?*

By addressing the right strategic questions and gaining a perspective that leveraged IRI's proprietary data and strategic analytic tools, the CPG manufacturer was able to uncover growth platforms that would help it achieve meaningful differentiation and create value for its shareholders. Growth pocket insights were then prioritized based on recommended variables driving sustainable growth and low contribution of private label to growth. Top categories were identified to begin mapping recommendations addressing where the company should play within the meals landscape.

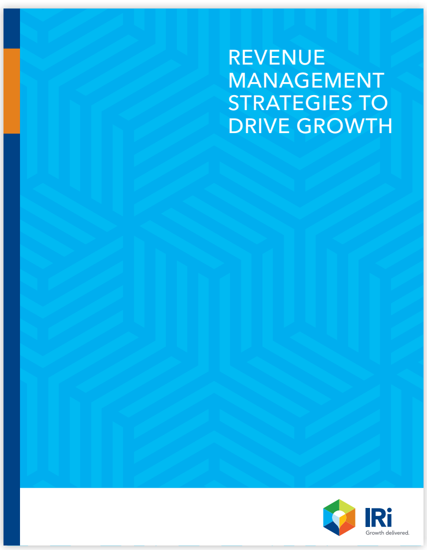
The combination of different growth pockets helped provide the foundations for defining strategic pillars for growth. Results yielded the better-for-you frozen meals single-serve growth pocket. Grouping this growth pocket with other better-for-you meals growth pockets led to the development of an overarching better-for-you food growth platform. This growth platform was an alternative to growth that placed bets on the company's existing frozen meals business, tapping into the broader BFY foods space, which is ripe with opportunities for diversification, leading to rapid growth.

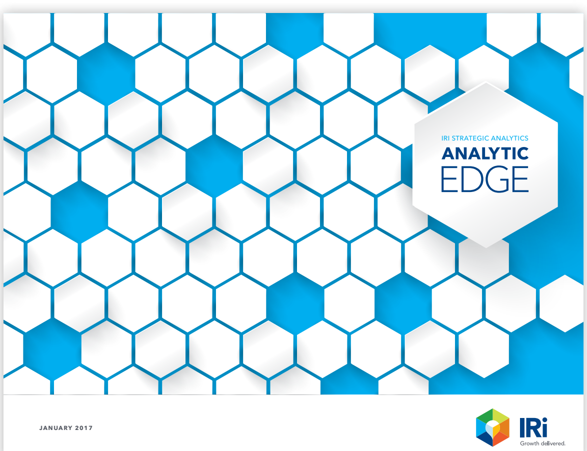
Winning Big by Identifying Growth Pockets

IRI's experience clearly shows that a proactive approach to growth is a winning approach. The top-down approach to winning with growth pockets provides a proactive, fact-based method to view tired, commoditized categories in a new light by giving actionable insight into what drives growth.

IRI Growth Consulting has successfully partnered with leading CPG manufacturers leveraging this proactive path to growth. Through this partnership, companies have been able to follow a distinct demand portfolio strategy that will help identify acquisition and inspiration targets through growth platforms. Winning with growth pockets matters, as an accurate understanding of actionable growth opportunities may lead to outsized gains of potentially hundreds of millions of dollars in additional growth.

Other Recent Publications





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ABOUT THE PRACTICE

IRI Strategic Analytics helps CPG and retail clients grow by enabling competitively advantaged, shopper-centric business decisions, and leveraging predictive analytics and prescriptive solutions in combination with deep strategy, analytic and activation expertise. In 2016, IRI Strategic Analytics had 200+ clients, 300+ client engagements across 400+ categories and 45 percent growth in its solutions installation. Most importantly, IRI Strategic Analytics identified over $500 million in growth impact for clients.

ABOUT IRI GROWTH CONSULTING

IRI's Growth Consulting is one of the four capabilities within IRI Strategic Analytics, in addition to Revenue Growth Management, Marketing Productivity and Retail Productivity.