



Price Pack Architecture: A Proven Strategy for Sustainable and Profitable Innovation

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Executive Summary

Keep Growth in the Crosshairs

Driving growth in today's low-growth marketplace is challenging, and beefing up the bottom line has become a critical growth strategy.

- The stability of the consumer packaged goods (CPG) market provides some protection against steep declines during times of market duress, but it also makes finding sizable and sustainable growth more challenging
- Innovation helps drive growth, but it is not reasonable to rely solely on new products for growth
- Cost-cutting can only go so far

Giving "Outside-the-Box" Innovation New Meaning Will Drive 2 to 5 Percent Jump in Profit and Increasing Revenues

Margins are under pressure in the face of climbing commodity prices and conservative purchase patterns. Innovation, particularly premium-tier innovation, has been well received, but it is not enough by itself.

- CPGs must provide consumers what they want, when and where they want it, at a price point that enhances, rather than detracts from, their overall perception of value
- Price pack innovation, such as bundling or alternative pack sizes, can legitimately drive shopper willingness to pay a higher price point
- Recent price pack innovations have yielded premiums ranging from 84 percent to more than 200 percent

Disconnects Between Price and Innovation Disciplines Are Threatening Growth Opportunities

Done right, price pack architecture ensures consumers can find a viable selection of products that meet their needs at the price points they are willing to pay, driving portfolio growth and enhancing a brand's overall value proposition.

- Consumers' desires and price sensitivity vary based on many complex factors
- In today's world, pricing and innovation are often viewed as completely separate issues and addressed by very different resources
- To get it right, price and innovation teams must synch up

Framework to Win: Ensuring Price Pack Architecture Success

Maximizing price realization in a way that builds true and sustainable bottom-line growth will require price and innovation disciplines to align against three key principles:

- Knowing the consumer at a granular level
- Understanding the full value case
- Mapping out the path to commercialization

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Keep Growth in the Crosshairs

Scanning recent headlines can make one believe that the current CPG environment looks quite bleak.

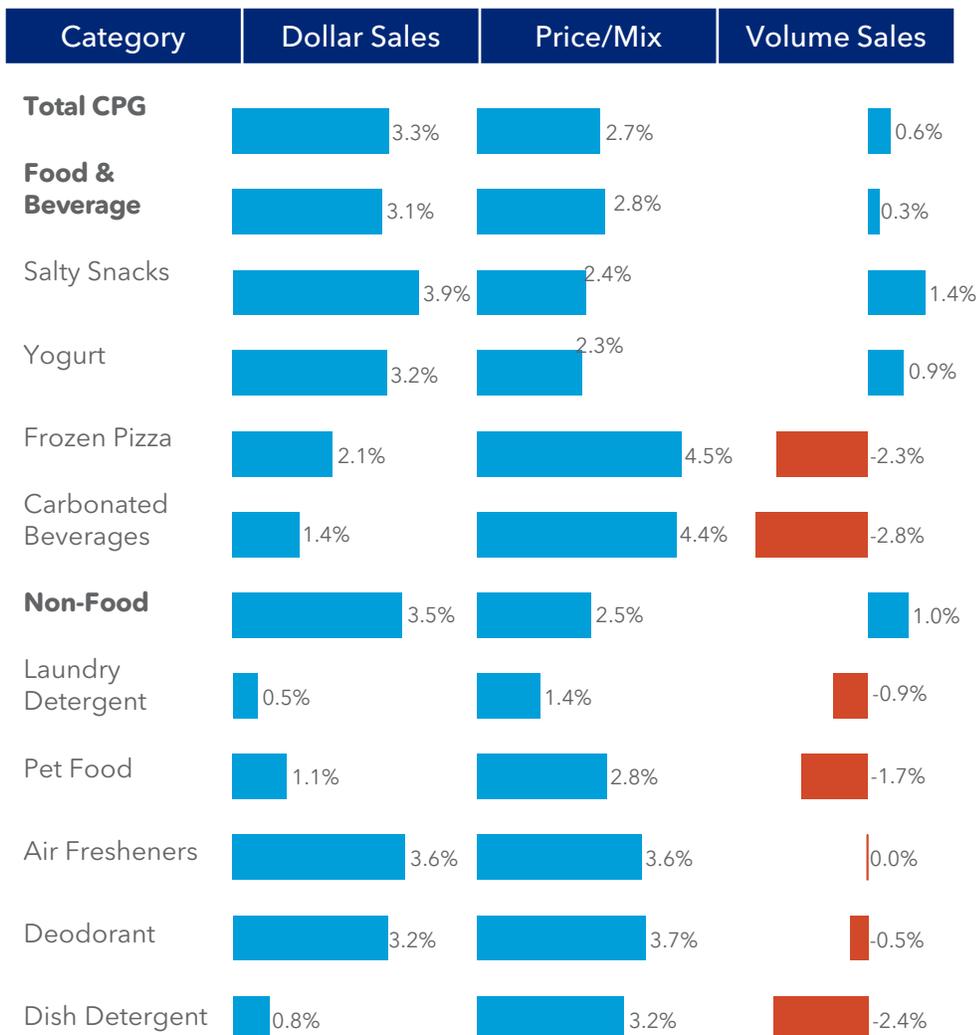
Driving growth in today's low-growth marketplace is challenging, to say the least. Activist investors continue to pressure big food companies, such as Mondelez, to cut costs aggressively in pursuit of driving bottom-line momentum.

Acquisitions, such as this year's Heinz-Kraft deal, that have focused on cost-cutting and zero-based budgeting have taken deep root in the manufacturing psyche. Indeed, the bottom line has become ever more critical, even beyond topline growth, for several players.

It is a simple fact that, unlike high tech or real estate, consumer packaged goods companies experience significantly less volatility as a whole. This stability is good, in that manufacturers face fewer sharp declines across the industry.

However, it also means that growth curves are less sudden and steep. After all, CPG demand faces far more limitations, in that consumers are unlikely to eat significantly more calories or greatly expand personal and home care routines just because their finances are better or an advertisement wins their favor.

Figure 1



Source: IRI POS database, MULO + C, 52 weeks ending 10/04/15.

Ongoing sustained growth is more likely to occur from achieving a higher price/mix per volume than by selling more product.

Indeed, the nature of the CPG market, particularly in today's slow-growth environment, explains why we often see, across numerous large

categories, that growth comes more from achieving a higher price/mix per volume than from selling more product (see Figure 1).

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Giving “Outside-the-Box” Innovation New Meaning Will Drive A 2 to 5 Percent Jump in Profit While Increasing Revenues

As explained in IRI’s recent point of view, *Effective Premiumization Strategies in CPG Can Achieve 10-15 Percent Topline Growth*, shoppers have proven willing to pay more for products that allow them to meet specific needs and wants. As a result, premium-tier products have gained share in all of the 10 fastest-growing CPG categories during the past five years.

But not everyone is winning in the race to drive premiums. This is especially true since the start of the Great Recession, when consumers made significant sacrifices in all areas of daily living to rein in spending and ride out the storm. The economic recovery has not brought back the previously well-established annual cycle of largely inflation-driven price increases. To the contrary, existing products are seeing largely stagnant or even decreasing price points despite underlying commodity cost increases, further pressuring margins for retailers and manufacturers alike.

While new product launches, such as the sidebar example here, can sometimes drive consumers to pay a significant premium over mid- and

lower-tier solutions, innovation does not always have to be a significant, disruptive change in the underlying product and its benefits. Simpler, more consistently achievable alterations to price pack architecture—such as changes in pack size, packaging or bundling—can be just as impactful, provided they align well with overarching market and consumer trends (see Figure 2). Combining the current focus on executional excellence with an eye on ever more profitable growth through better price realization can be truly powerful, increasing bottom-line profits by 2-5 percent on a strengthening revenue stream.



The Winners in Premiumization are Providing Consumers Exactly What They Want, When and Where They Want It, at a Price Point That Enhances, Rather Than Detracts From, Their Overall Perception of Value

Most shoppers realize that they can save 40 percent or more on the same number of washes if they opt for Tide liquid detergent over Tide Pods. However, the convenience provided by a premeasured, no-mess, no-spill packet of detergent that can be simply tossed into the machine with the laundry has proven a worthwhile trade-off. Despite the higher price point, since their introduction in 2012, Tide Pods have grown to nearly \$500 million in our annual tracked sales, and have outpaced the growth of the laundry detergent category by more than 10 times.¹

¹ IRI POS database, MULO + C, 52 Weeks Ending 10/04/15

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Figure 2

Recently Successful Price Pack Innovations ²		
Innovation	Details	Reasons for Success
 <p>Pepsi Mini Cans</p>	<ul style="list-style-type: none"> Re-introduced in 2013 by PepsiCo Smaller cans allow consumers to indulge in carbonated beverages with reduced calories and sugar intake 100% premium in price per ounce vs. standard Pepsi cans L52 Dollar Sales: \$40.5 MM 	<ul style="list-style-type: none"> Carbonated soft drink consumption per capita has steadily decreased during the past several years, to its lowest rate since 1986³ Across a wide swath of categories, nearly half of customers claim selecting smaller portion sizes as a key health strategy⁴
 <p>Perdue Perfect Portions</p>	<ul style="list-style-type: none"> Introduced in 2014 by Perdue Individually wrapped boneless, skinless chicken breasts facilitating efforts for consumers to control portions 84% average premium over other Perdue packaged chicken L52 Dollars Sales: \$90.6MM 	<ul style="list-style-type: none"> In 2015, 38% of consumers claim to put more effort into making nutritious and healthful meat and poultry choices, and 42% claim selecting smaller portion sizes as a key health strategy⁵ Health conscious shoppers have demonstrated up to 25% more willingness to pay a premium than other segments⁶
 <p>McCormick Recipe Inspirations</p>	<ul style="list-style-type: none"> Introduced in 2011 by McCormick A recipe card including a combination of pre-measured herbs and spices to speed novice cooks in preparing healthy meals that avoid routine flavors 203% average premium per volume vs. spices and seasonings as a whole L52 Dollar Sales: \$1.1MM 	<ul style="list-style-type: none"> Smaller households are increasing as millennials delay marriage, seniors maintain independence longer, and the birth rate declines⁷ Meal solutions skew towards these households, due to their preference for convenient, easy-prep meals Similar easy-prep solutions, like value-added meat, have also outpaced the growth of all other meat in recent years⁸
 <p>Chobani Flip</p>	<ul style="list-style-type: none"> Introduced in 2012 by Chobani, around the time that Müller Corner made its way to the U.S. market Single serve, highly portable packs with natural snacking ingredients in compartment to be “flipped” into yogurt 10%+ premium in price per ounce vs. traditional Chobani Greek yogurt L52 Dollar Sales: \$164.2 MM 	<ul style="list-style-type: none"> Snacking frequency has increased across all day parts, especially in the afternoon, up to 69% in 2015, from 51% in 2010⁵ Consumers claim that convenient sources of protein throughout the day have helped with maintaining tighter control over portions Portable snack offerings from Nutella (+96%) and Sabra hummus (+48%) outpaced multi-serve packs in dollar sales CAGR, 2011-2014
 <p>Cascade Platinum Action Pacs</p>	<ul style="list-style-type: none"> Introduced in 2013 by Procter & Gamble Powerful formula reduces time spent cleaning dishes by eliminating need for pre-wash with a pre-measured, single-use pack 200%+ premium in price per ounce vs. traditional Cascade Dishwasher Detergent L52 Dollar Sales: \$16.1 MM 	<ul style="list-style-type: none"> Home care manufacturers developed single-dose packs following successful model of K-cups single serve coffee The primary driver of purchasing a new product is to “get housework done in less time,” reported by 71% of triers⁹ Growth in laundry detergent pods (+74%) outpacing total laundry detergent category (-2%) in dollar sales CAGR, 2010-2014 Time-saving cleaning products like all purpose cleaning wipes (+6%) significantly outpacing the challenged household cleaning aisle (+1%) in dollar sales CAGR, 2010-2014

Recent innovations have leveraged innovative packaging and pricing strategies to yield premiums ranging from 84 percent to more than 200 percent.

² IRI POS database, MULO + C, CY 2010-2014 and 52 weeks ending 10/04/15

³ Beverage Digest, “Special Issue: US Beverage Business Results for 2014,” March 26, 2015

⁴ The Power of Meat 2015 201 Analytics Presentation

⁵ Ibid

⁶ IRI Analysis

⁷ U.S. Census, “Current Population Survey, 2013 Annual Social and Economic Supplement”

⁸ IRI “Maximizing Growth for Value-Added Meat, 2/24/2015

⁹ IRI “New Product Pacesetters,” April 2015

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Disconnects Between Price and Innovation Disciplines are Threatening Growth Opportunities

The essence of price pack architecture is to provide consumers a viable selection of products that meet their needs at the price points they are willing to pay, driving portfolio growth and enhancing a brand's overall value proposition in the outlets where they shop for any given purchase occasion. This is no simple task. After all, there are more than 318 million households in this country. Each of these households will undertake countless different shopping trip missions during a lifetime, and even for a single

shopper, the mindset within each mission will impact everything from product need and pack size selection to channel preference and price sensitivity. For this reason, new product innovation and pricing are inextricably intertwined.

Unfortunately, for many in today's CPG landscape, pricing and innovation are viewed as completely separate issues. As such, these issues are addressed by different resources with polarized skill sets and disparate approaches.

Framework to Win: Ensuring Price Pack Architecture Success

To maximize price realization in a way that builds true and sustainable bottom-line growth while supporting shopper loyalty and category share, CPG marketers should consider taking a step back and focus on creating a powerful price pack architecture. Doing so will require price and innovation disciplines to align against three key principles.

Know the Customer at a Granular Level

CPG marketers must understand how their key and target consumers shop for specific needs and how those needs play out across different trip missions. For instance, a monthly stock-up trip at a warehouse store will look very different from an immediate consumption purchase

Excessive Reliance on Breakthrough Innovation as a Growth Driver is Perilous

While successful new product launches contribute significantly to growth, relying excessively on breakthrough innovation as a growth driver is not recommended. Followers of IRI's annual [New Product Pacesetters™](#) will note that the ranks of manufacturers bringing to market disruptive innovation vary greatly from year to year. For example, four of the top 10 2013 New Product Pacesetter manufacturers were not among the ranks of 2014's biggest winners. And outside of General Mills and Kellogg's, those that did make the grade both years saw a significant decline in the number of Pacesetter products they produced between 2013 and 2014.¹⁰

¹⁰ IRI New Product Pacesetters 2013 and 2014

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at a convenience store, even though the same product is being purchased in each situation.

For products that are already in the market, it is possible to rely on a host of historical data that reflects actual, in-market performance when making projections around future behaviors. However, when searching for new white-space innovation opportunities, the picture is different. The way a shopper interacts with the existing portfolio will provide some input into what the shopper values and how much he or she will be willing to pay to meet those needs. In this situation, however, additional market and consumer research, along with advanced analytics and vast industry expertise, will also be critical in identifying unmet needs.

Understand the Full Value Case

It is critical to understand that unmet needs may lead to disruptive new product opportunities, but they may also point to opportunities for price pack innovations. Understand that the right innovation may be as simple as bundling or alternative pack sizes and these tweaks can legitimately drive shopper willingness to pay a higher price point. Determining specific needs will require a collaborative effort to study pricing sensitivity metrics and simulate a full financial and volume impact across retailers, product lines and customer types.

Map Out the Path to Commercialization

Commercializing price pack architecture innovation must also be

a collaborative effort. Competition for shelf space is fierce. To win space and increase compliance, manufacturers must invest to understand the goals of each particular retailer partner—the goals for the store and for the aisle(s) in question—and demonstrate a compelling financial and strategic sell-in story.

To ensure a unified lens, IRI recommends price and innovation disciplines work together through a comprehensive three-phased approach to price pack architecture opportunities—Ideation, Validation, and Commercialization—to ensure that existing and new products fully capitalize on opportunities across the price/value spectrum (see Figure 3).

Figure 3

IRI Approach to Price Pack Architecture

<p>1</p> <p>Ideation: <i>What are the opportunities?</i></p>	<ul style="list-style-type: none"> • Current price pack architecture vs. competitors • Drivers of success for competitors in entering the market • Historical evidence of premiums customers have been willing to pay • Learnings from other, similar categories
<p>2</p> <p>Validation: <i>How big are they and which should we pursue?</i></p>	<ul style="list-style-type: none"> • Potential market size for target customers and channels • Requirements for financial and commercial success • Estimates of consumer demand through behavior-based tests and models • Likelihood of cannibalization for existing products we and competitors offer • Feasibility of meeting minimum success criteria and contingency plans
<p>3</p> <p>Commercialization: <i>How do we convince retailers?</i></p>	<ul style="list-style-type: none"> • Objectives and performance concerns for specific retailers • Alignment between our category vision and opportunities vs. retailers • Support mechanisms retailers will expect

Identifying opportunities, determining their potential, and convincing retailers that the products will attract shoppers at the recommended price points are critical to achieving a successful price pack architecture strategy.

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Case Study: Spreads Manufacturer Turns to Price Pack Strategy to Beat Back Private Label Threat

Bridging the gap between price and innovation can reap significant rewards in this situation by encouraging trial.

After playing a pivotal role in growing the broader spreads category for some time, this flagship brand found itself under assault from a number of lower-priced, private label alternatives. These lower-priced options capitalized on the fact that price proved to be the key barrier to trial among shoppers who had not yet made a purchase from this new, growing category, while also providing a cheaper product for more price-sensitive current shoppers.

IRI conducted an extensive analysis of current and potential consumers to determine what product attributes were desired and the price these shoppers would pay to get these attributes. Using these learnings, IRI guided the manufacturer to combine the adoption of better-aligned price positioning on existing products with the introduction of new, smaller pack sizes that, while more expensive on a per-volume basis, carried a lower absolute price that allowed an easier path to trial.

In partnership with IRI, the manufacturer built a compelling case for adoption of the new pricing guidelines and smaller pack sizes. The brand went beyond securing its existing market share to increasing penetration by over 3 percent and dollar sales by 17 percent, all while growing margins a staggering 10 percent.

Conclusion

The CPG industry is embracing a variety of strategies to carve out growth in the face of challenging industry dynamics and a slow-growth marketplace. Belt-tightening and new product innovation are contributing to growth, but costs can only be reduced so much and consistently and repeatedly providing the new, market-defining item is not feasible.

Price pack innovations are far more sustainable, and despite their simpler nature, can carry significant premiums when they are executed with the surgical precision that comes only from a forensic understanding of the needs and wants of core and target consumers, combined with the correct overarching strategy, advanced

analytics and deep industry know-how. Manufacturers that successfully undertake price pack innovations will be rewarded with more profitable growth through price realization and find true and sustainable growth that offers a distinct competitive advantage.

Price Pack Architecture: POINT OF VIEW

A Proven Strategy for Sustainable and Profitable Innovation

Resources

IRI can help you accelerate growth by making the most of your price pack architecture strategies. Our approach and capabilities will generate significant revenue increases, drive market share growth and foster increased shopper loyalty. These include:

Business Growth Strategy

IRI Growth Consulting can help define growth realization initiatives based on pockets of growth and white spaces in CPG manufacturers' current categories and help align portfolios and drive sophisticated growth strategies to capitalize on growing segments. Past engagements have helped uncover pack sizes, price points, and other easily achievable innovations that shoppers are willing to pay for.

Pricing Analytics

IRI's Price and Trade Advantage™ provides detailed simulations of price shifts across each retailer's full category, capturing not only the impact on the items receiving a price change, but across all related products. Additionally, IRI's host of primary research methods, including discrete choice, virtual shelf testing and other leading approaches, leverages actual customer behavior to assess the role of price, quantify price trade-offs, and fine-tune pricing for new products before they even reach store shelves.

Retailer Selling Stories

IRI can also help develop a strategic storyline for retailers to convey the total financial benefit of price pack opportunities and the value proposition for new pack offerings. This can create a call to action for the retailers to partner with the manufacturers to drive growth and maintain stronger compliance following the initial agreement.

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