How consumer-facing companies can speed up, as economies slow down (PART 2)

ISAAC SARPONG: Isaac is the Partner in charge of Tax Services. He has over 26 years' experience in the provision of multi-faceted advice to both local and international clients in taxation, accountancy, audit & assurance, and corporate law, among others. Isaac is a Chartered Accountant, a Chartered Tax Practitioner and a Lawyer.

Building a better working world

A recession is coming — consumer products and retail companies that can take it as an opportunity to innovate are likely to emerge stronger.

(CONTINUED FROM PREVIOUS EDITION)

In Asia, real GDP growth has slowed sharply in mainland China with household spending, housing activity and manufacturing output restrained by the zero-COVID-19 policy and a worsening property sector downturn that has led some people to boycott mortgage payments. The slowdown in economic activity in China is weighing on growth across its major Asian trading partners. Meanwhile, in Japan, the post-COVID-19 pandemic consumer spending recovery is still not complete, and momentum is slowing as higher inflation is squeezing household incomes.

In In the US, the high inflation environment is weighing on consumer morale and purchasing power, and it is forcing many households to dip into savings and borrow to finance outlays.

While consumers remain willing to spend, many families, especially those at the lower-to-median end of the income spectrum, are feeling increasingly constrained by elevated prices and rising interest rates.

Consumers have evolved

More than ever, brands are investing in ways to develop stronger consumer relationships, and companies that can continue to find ways to anticipate consumers' needs and improve the buying experience are likely to fare better in downturns.

The COVID-19 pandemic significantly affected consumers around the world, hastening the adoption of new values and behaviors. Greater access to information and choices in the products they buy have driven down loyalty, enabling them to switch brands easily. Consumers' expectations of the companies they buy from are higher and they continue to be more concerned with sustainability, wellness and social issues.

Under the strains of the pandemic, consumers forged new buying habits driven by the desire to work and shop from home, and many switched to private label products to economize. As we move into an uncertain landscape, many of the habits solidified during the pandemic are proving helpful now.

There are signs people may already be reining in spending in anticipation of difficult times. The November 2022 edition of the EY Future Consumer Index shows that people are worried about the future, with 62% not expecting the economy to recover within the next 12 months and 58% expecting their living costs to increase over the next six months. Their fears are being reflected in a change of behavior:

- 34% of consumers are substituting their normal purchases with new brands, and 28% are switching to private label
- 52% would consider buying private label home and household care products
- 50% are purchasing less expensive alternatives

EY Future Consumer Index

62%

of global consumers do not expect their country's economy will recover within the next 12 months.

CHAPTER 2

Challenges bring opportunities

The recession presents challenges but also opportunities to gain a competitive edge.

The trends present challenges and opportunities, for both CP companies and retailers. Companies in both sectors will be squeezed between inflationary costs — from transportation to labor — and weakening demand as consumers become more sensitive to rising prices and interest rates.

To compete effectively, brands need to reinvent their relationship with consumers, who are seeking meaningful differentiation from the companies they buy from, not just brand promises. Their products need to tell a story that shows how they can have an impact in areas that matter to consumers, such as health and wellness, higher-quality ingredients or sustainable environmental impact.

With the access today's consumers have to multiple shopping channels and vast information sources, it's important for companies to be visible. Retailers have physical stores, but digital channels are available to all, and CP companies can benefit from developing independent channels such as direct-to-consumer.

Companies that combine these efforts with changes to improve efficiency, such as creative uses of technology, can gain a competitive edge. Digital solutions are especially important because they can be the basis for significantly improving consumer relationships.

Consumer products: Connect with consumers with value adding strategies

In past recessions, many CP companies pulled back on marketing and advertising spending to cut costs. Those that did this, however, found that their smaller "share of voice" hurt brand awareness and market share once the economy picked up again.

Savvy competitors maintained their marketing spend and were able to gain market share in many cases. For many companies, the lesson is to resist the temptation to cut marketing expenditures, and, where possible, hold marketing and advertising budgets steady or even increase them to grow share of voice.

As companies invest in their brand, they will need to think carefully about their message to get the most from their advertising budget. Organizations need to align their approach with consumer values such as the demand for greater authenticity and transparency, personalization, emphasis on health and the environment, convenience and value. Instead of cutting prices, companies can add value to product portfolios through a combination of product innovation and premiumization with strategies that create opportunities to connect with consumers and their evolving expectations.

Pricing considerations will be of paramount concern, and, in an inflationary environment companies will need to maintain profitability by managing the squeeze between elevated input costs and weaker demand as price-sensitive consumers pull back on outlays and shop for less expensive alternatives. To do this, many companies will need to offset rising input costs by increasing the value of their products and increasing productivity. Price-sensitive consumers will shop for lower cost alternatives, but value-driven consumers will remain loyal. Low-demand products, on the other hand, will face substitution or delisting from major retailers.

As retailers emphasize own-label products and reduce shelf space for brands, CP companies must re-evaluate channels to consumers. CP giant Unilever is an example of a company that has invested in its direct-to-consumer capabilities while expanding its global reach. It partnered with the Chinese e-commerce company Alibaba to launch a new digital incubator to create new beauty and personal care brands for an online flagship store to reach more customers in China.

Companies can also explore opportunities to expand footprints in high growth markets and can consider reshaping the core business through M&A, such as considering value-led, sustainability-related growth opportunities, or through divestitures or spin-offs, to generate new value.

Japanese beer maker Kirin is going through such a transition, diversifying its traditional beverage line to reposition itself as a health beverage company. New products include probiotic drinks, teas and alcohol-free beer. It is also spending to improve its environmental image with new programs for sustainable packaging, supply chain operations and plastic bottle recycling.

ACTIONS TAKEN THEN AND NOW

- In 2008 and 2009, a US-based food products company acquired premium alcohol brands and revaluated its product mix across its core markets, and increased focus on premium and high margin brands. The premiumization strategy helped improve gross margin by 3.7% in the third quarter of 2009.
- A German beauty and home goods company is preparing for a likely recession by launching multiple products in new categories, such as beauty care, laundry and home care. It invested in a new innovation center in 2022, expanded production capacity and has acquired a company to increase its direct-to-consumer and digital capabilities. It has also made cost optimization moves and invested in sustainable product packaging.■

(CONTINUED IN NEXT EDITION)

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Find out more:

Address: 60 Rangoon Lane, Cantonments City, Accra. P. O. Box KA16009, Airport, Accra, Ghana.
Telephone: +233 302 772001/772091
Email: info@gh.ey.com,
Website: ey.com