How consumer-facing companies can speed up, as economies slow down (PART 3)

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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)

Retailers: efficiency, balanced pricing approach and private label emphasis

Retailers can adopt similar pricing approaches that are likely to work for CP manufacturers, such as discounting lower-demand products and reinvesting in high demand products.

In an example of the approach some companies are already taking in the fluid environment, many retailers have reacted to abating energy and shipping costs in the third quarter of 2022 by maintaining high product prices to conserve margins.

With consumers buying less or seeking lower price alternatives, retailers can also benefit from consumers' broader acceptance of private labels and value brands by introducing these in more discretionary product categories as shoppers show a willingness to switch. We are seeing many grocers introducing new budget price ranges and being rewarded with high demand from shoppers.

The EY Future Consumer Index found that 28% of consumers are planning to buy more store-branded products in the future. This rises to 61% of consumers who are willing to try store-branded fresh food and 53% who are willing to try store-branded packaged foods.

Another strategy for retailers to consider is rationalizing stock-keeping units (SKUs) to increase focus on high-margin products. Additionally, streamlining the inventory procurement process allows retailers to:

- Minimize purchasing lead times
- Enhance inventory visibility
- Enable the cash conversion cycle
- Ensure greater flexibility to adapt to changes in consumer behaviors and economic conditions

An example of a company that benefitted from SKU streamlining is an American food and tea company that reorganized the products in its personal care segment in 2008 to focus on high margin items only. Between 30 and 40% of SKUs were discontinued, which helped increase SKU velocity, reduced working capital and business complexity and improved operating efficiencies.

Retailers have opportunities to deepen the connection with shoppers by educating them on how to get the most for their money and from the products they buy. They can promote recipe ideas that make food go further; and are driving sustainability by wasting less – retailers in some countries have acted to remove unhelpful "best before date" stickers from some products and are once again promoting ugly fruit (a must, given the heatwave-stricken harvests across Europe).

Organizations can consider the efficiency of their store footprint to reduce store-related expenses while reallocating capital to online channel innovation. Successful companies are using technology, such as data analysis and automation to contribute to unconventional retail staffing approaches. For example, companies EY has worked with are using retail "rescue squads" to support teams at understaffed stores, category-level analysis to improve staffing allocations (via ey.com US) and special programs with schools to hire work-eligible students for simple tasks.

ACTIONS TAKEN THEN AND NOW

- ▷ In 2008–2012, a US retailer adopted a strategy that combined defensive financial streamlining with a revised marketing strategy to increase three-year total shareholder return by 103%. It reduced its debt-equity ratio, streamlined stores and SKUs, and increased supply chain efficiency through improved packaging, use of cross-docking centers and truck-weight optimization and efficiency. It changed its marketing strategy, shifting away from big ticket and discretionary items toward consumer staples and an increased focus on its private-label brand.
- ▷ The 2008 recession saw the rapid rise of discount retailers, whose value proposition of low prices on a limited range of private label products became the industry standard and pushed them into the mainstream, driving a growth trajectory that has persisted to this day.
- ▷ A British DIY retailer opened 38 new "compact stores" (less than 2,000 square meters) in 2021 to increase penetration in urban areas, while also rolling out new brands in kitchen and lighting areas. It has also invested in technology upgrades to improve its e-commerce capabilities.

Weathering the storm

CP companies and retailers may also find it useful to combine strategies for growth in some areas with financial belt-tightening or efficiency moves in others.

- Reduce leverage now as much as possible to conserve cash, improve access to capital and prepare for the rising cost of servicing debt
- Reduce back office and cost-of-goods-sold overheads to optimize prices while maintaining enough cash and margin buffer to weather a more sustained recessionary period
- Pursue asset-light opportunities to curtail overhead costs and focus only on core operations. For example, companies can rationalize product portfolios and consider the impact of private label and how to counter it (for CP) or exploit it (for retail)
- Consider various steps to reduce costs and increase resiliency in their global supply chains.
- Increase communications and commitment to key vendors to have the right goods in the right place at the right time to limit supply chain disruption.
- Invest in technology integration across the value chain, including automated vendor management, artificial intelligence and machine learning in demand planning, augmented or virtual reality in selling and autonomous delivery.

ACTIONS TAKEN THEN AND NOW

- ▷ A major home improvement retailer generated US$5.1 billion of cash flow from operations in 2009 and was able to reduce its long-term, debt-to-equity ratio to 44.7% compared with 54.4% at the end of fiscal 2008.
- ▷ A US-based home products chain combined cost-cutting steps with strategic growth moves. It reduced planned capital expenditure by 37% in 2022 and closed 150 underperforming stores in addition to other cost-cutting measures. The company divested a retail business to streamline its portfolio and product line and invested in new distribution centers and IT systems to strengthened supply chain infrastructure. The company has made strategic, market-facing investments, as well as, expanding its store network through a new partnership and augmenting its customer loyalty points program across its different retail brands.

Summary

It may seem counterintuitive to view recession as a time to focus on innovation and growth levers, but experience shows that retailers and consumer products companies that can prepare for the coming downturn with an emphasis on a value, growth and a consumer-centric marketing approach are likely to outperform their competition in the long run. While executives should be aware of the current downturn and how it is different from past recessions, valuable lessons can be learned from companies that succeeded through tough times in the past by investing in innovation to grow while also improving operational efficiency and reducing costs in non-strategic areas.■