Channel Migration:

The Road to Growth Has Many Lanes

September/October 2014

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Executive Summary: Dialing In on Flawless Execution

Economic conditions, demographic changes, consumer behavior and technology innovations…during the past decade, these forces converged to set off cataclysmic changes in the consumer packaged goods (CPG) industry. They spawned a consumer marketplace that demands and is adept at finding value. They have supported growth of less traditional grocery channels, such as drug, as well as emerging channels, such as value operators and the Internet. And the influence that Internet-based media, specifically, has had on consumers' path to purchase is simply profound. Ultimately, all of these forces have combined to forever change consumer engagement and the CPG shopping journey—and the evolution is far from over.

Today, the knowledge and the power lay firmly in the hands of the consumer. The good news for CPG marketers is that mobile and digital technology is exploding, generating vast volumes of data on consumer shopping preferences and behaviors. Critical to success is an adept ability to harness and transform these abundant data into insights—insights that must be the foundation for carefully targeted marketing programs that demonstrate a concrete understanding of channel usage patterns of marketers' most valuable shoppers. To provide a framework for protecting and growing share of the nearly $737 billion omni-channel CPG world, IRI conducted a granular analysis of consumers' evolving path to purchase and its impact on existing and emerging channel trends.

Sophisticated retail execution has become a critical skill among CPG manufacturers and retailers alike. To succeed, retailers and manufacturers must work as partners, embracing fast-paced joint business planning to get the right products to the right shelf at the right place and time.

Consumer engagement and the CPG shopping journey have forever changed. CPG marketers absolutely *must* adopt a strong multi-channel relevance—including a strong and seamless digital presence—or else they undoubtedly face obsolescence. **To solidify a position in the express lane along the road to growth, CPG marketers must execute well against four key strategies**:

- Protect and grow the base
- Maintain solid availability against existing and evolving channel preferences and behaviors
- Optimize marketing mix by media and retail channel
- Develop channel-specific products and packages

CPG Industry Sales Are Climbing Slowly; Change Seen with a Finer Lens

CPG industry sales reached nearly $737 billion in 2014, hampered by ongoing conservative consumer behaviors that began when the economy turned sour and became the new normal, but spurred on by technological advances and solid marketing strategies that emphasize the role CPG products play in making it easier, more enjoyable and more affordable to live well for less (SEE EXHIBIT 1).

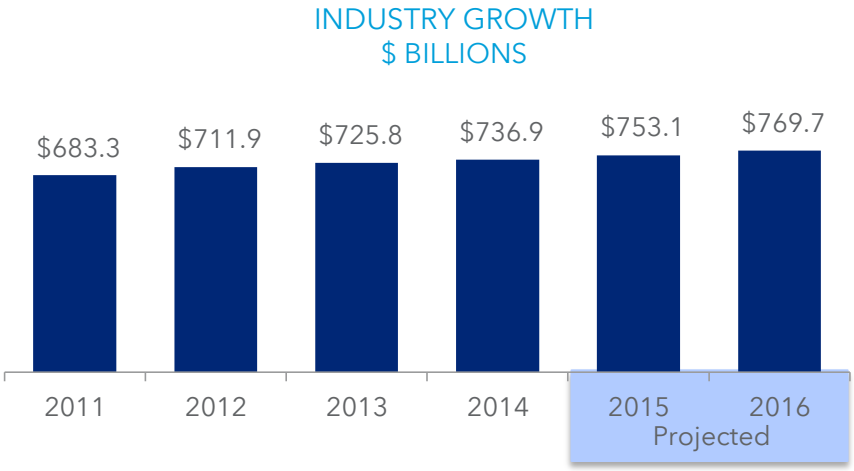
These polarized forces will continue to impact the industry for several more years, at a minimum. As a result, the period of 2011 through 2016 will be marked by fairly slow growth, averaging about 2 percent annually.

Trip mix shifts have been relatively small, too, though pantry stocking has experienced a small uptick in average basket size—today accounting for 28 percent of spending (SEE EXHIBIT 2). During the same time period, special purpose missions have subsided slightly. Today, special purpose trips account for 13 percent of trips and 18 percent of spending.

On the surface, it may seem that the industry is somewhat stagnant. A finer lens, however, reveals a starkly different picture. And, it's time to tighten those seatbelts, because change is going to accelerate in the years to come!

Exhibit 1

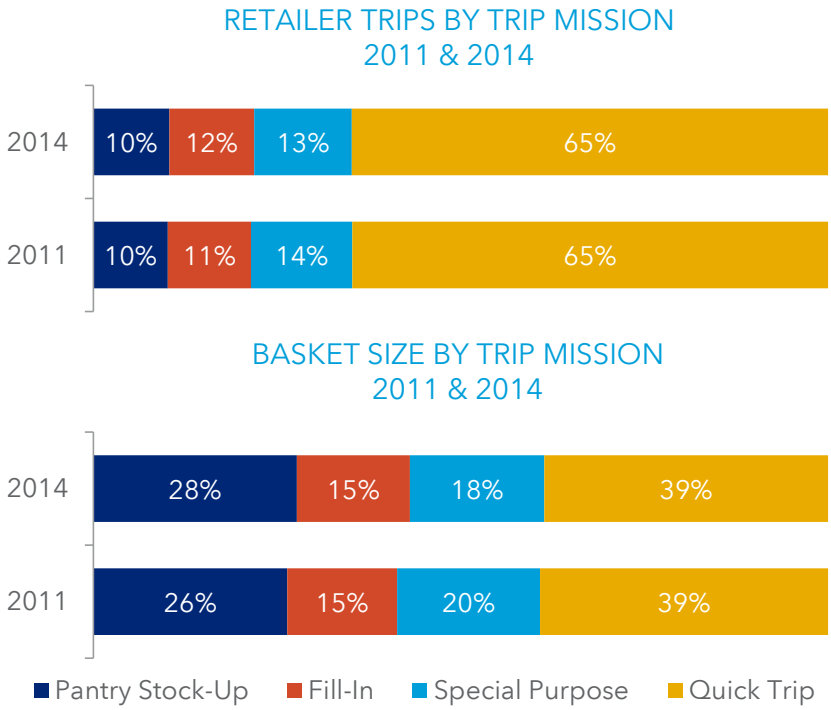
CPG industry sales are growing slowly and will reach nearly $770 billion in the next couple of years.



Source: IRI MarketAdvantage™ 52 weeks ended 5/18/2014 and same period prior years

Exhibit 2

Trip mix has remained relatively unchanged during the past few years.

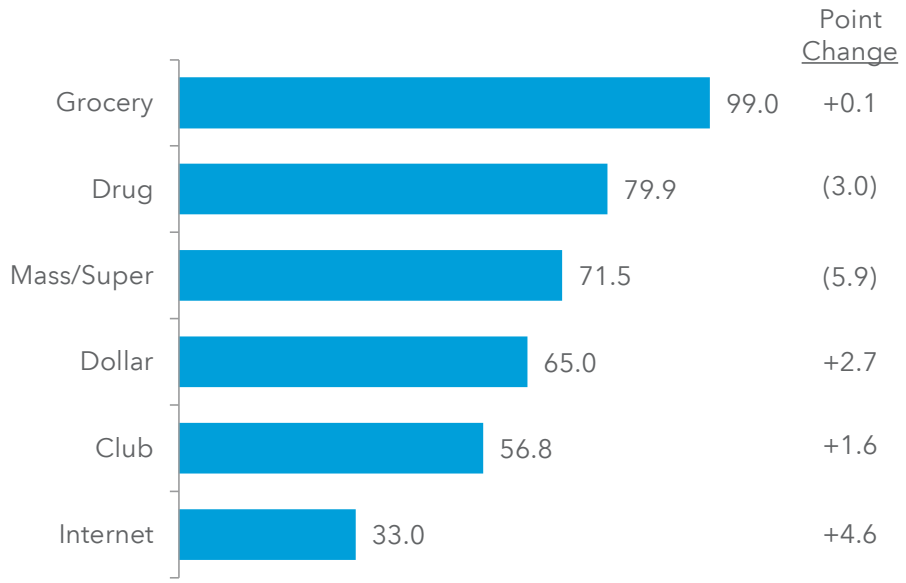


Note: Mass/Super and Grocery do not include Walmart
Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period prior year

Exhibit 3

Grocery holds nearly 100 percent penetration, but Internet and dollar retailers are making considerable inroads.

PENETRATION BY CHANNEL AND POINT CHG VS 2011



Note: Mass/Super and Grocery do not include Walmart
Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period 2011

Channel Penetration Is Shifting; Emerging Channels Are Showing Strength

For several years now, the competition within the CPG industry has been escalating.

Early in the downturn, value channels, including dollar and mass/super, enjoyed a significant uptick in penetration, lured by *Everyday Low Price* strategies and "discount store" appeal.

Retailers in other channels fought back by employing everyday low price strategies of their own, broadening private label assortment, and more conspicuously highlighting value in their promotional efforts.

Retailers across channels have been broadening assortment of food and beverage options as a means of driving footfall and increasing basket size. Likewise, general merchandise and health and beauty assortments have also been broadened. Indeed, channels have blurred; today it is much more difficult to distinguish between retail formats based on assortment than it was just a few short years ago.

Today, six years out from the start of the Great Recession, the CPG industry looks and feels very different.

The grocery channel is shopped by nearly everyone, boasting 99 percent household penetration. But, competition is intense (SEE EXHIBIT 3).

Dollar stores have become much more numerous and a battleground in the war for share of CPG spending, capturing more than two points of penetration in just three years. On a related note, smaller format, "more urban" stores are popping up across channels—Whole Foods, Walmart, Dollar General—to name a few. It's a nod to on-the-go lifestyles and a preference for smaller, more frequent visits, and the movement is being met with success.

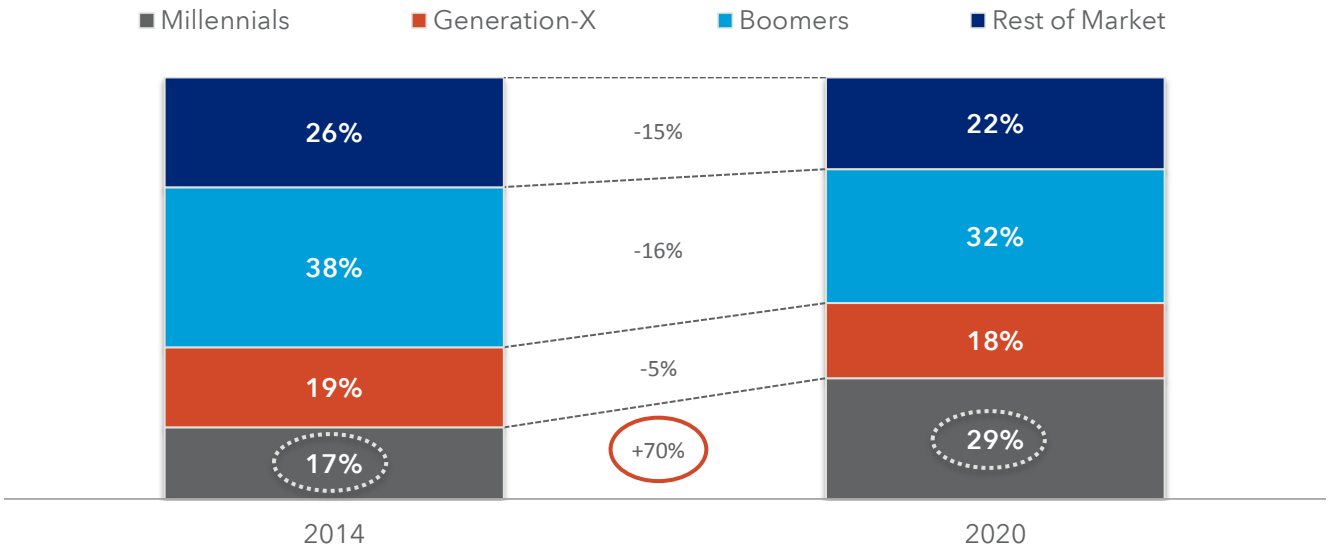
The Internet is another emerging channel. Detailed later, the channel currently accounts for about 1.5 percent of total CPG sales. But, the impact of the channel on today's path to purchase is huge and growing rapidly.

The CPG industry of tomorrow will be shaped by marketers' ongoing quest to serve cost-conscious, time-starved consumers. The battle for shelf space is escalating in intensity. The only constant is change. The pages that follow provide insights into additional forces that are molding the future of CPG.

Exhibit 4

Millennials' CPG dollar share will grow 70 percent by 2020, while boomers' share will decline during the same time period.

PERCENT OF CPG DOLLAR VOLUME
BY CONSUMER SEGMENT
2014 & 2020P



Source: IRI EconoLink™ Survey, 2013.

The Millennial Generation Will Become Increasingly Influential

Millennials currently account for just under 20 percent of the U.S. population (SEE EXHIBIT 4). Throughout the economic downturn, this group has struggled more and for longer than older cohorts.

But, detailed in IRI's recent point of view report, "*Millennial Shoppers: Positive Mindset Points to Future Growth*," the country's youngest shoppers are finally showing some level of optimism about their financial situation and beginning to open their wallets to spend.

Furthermore, as millennials grow in their purchasing power, their contribution to the CPG industry will also grow.

By 2020, IRI estimates that millennials will account for just under 30 percent of CPG dollar volume. This translates to more than $250 billion annually. Millennials are a key growth market for CPG marketers in the coming decades.

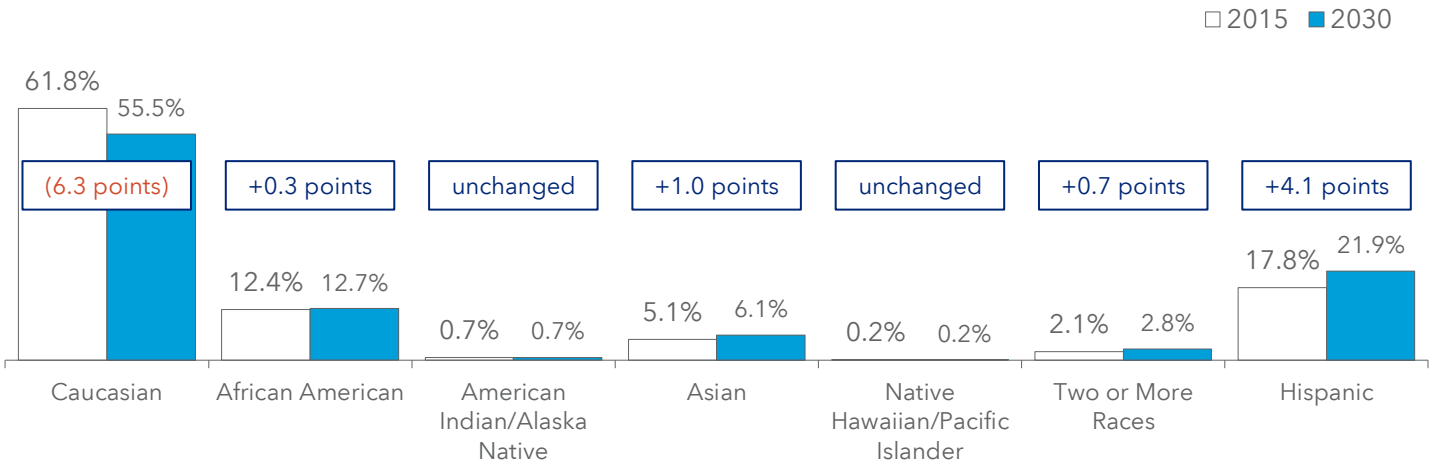
Millennials will account for nearly 30 percent of CPG spending by 2020—more than $250 billion.

Millennial shoppers consistently demonstrate unique consumption and shopping habits, which must be understood and delivered against by CPG marketers who wish to win their loyalty.

Exhibit 5

The United States is in the midst of a sweeping demographic transformation.

U.S. POPULATION PROJECTION
2015 & 2030



Source: U.S. Bureau of the Census

Increasing Demographic Diversity Will Have Profound Impacts on CPG Purchase and Consumption Behaviors

Nearly two-thirds of today's U.S. population is Caucasian (SEE EXHIBIT 5). But, the picture is becoming increasingly diverse. With diversity in culture comes exponentially diverse CPG-related shopping and consumption habits.

Among Hispanics, for instance, large family size propels more-frequent-than-average visits to mass merchandisers and supercenters. Meanwhile, an affinity for authentic ingredients leads Hispanics to turn to ethnic markets.[1]

The Asian market segment is also experiencing exceptional growth. By 2030, more than 6 percent of the U.S. population will hail from Asian cultures, bringing with them a higher-than-average focus on health and wellness, and a relatively high disposable income.[2]

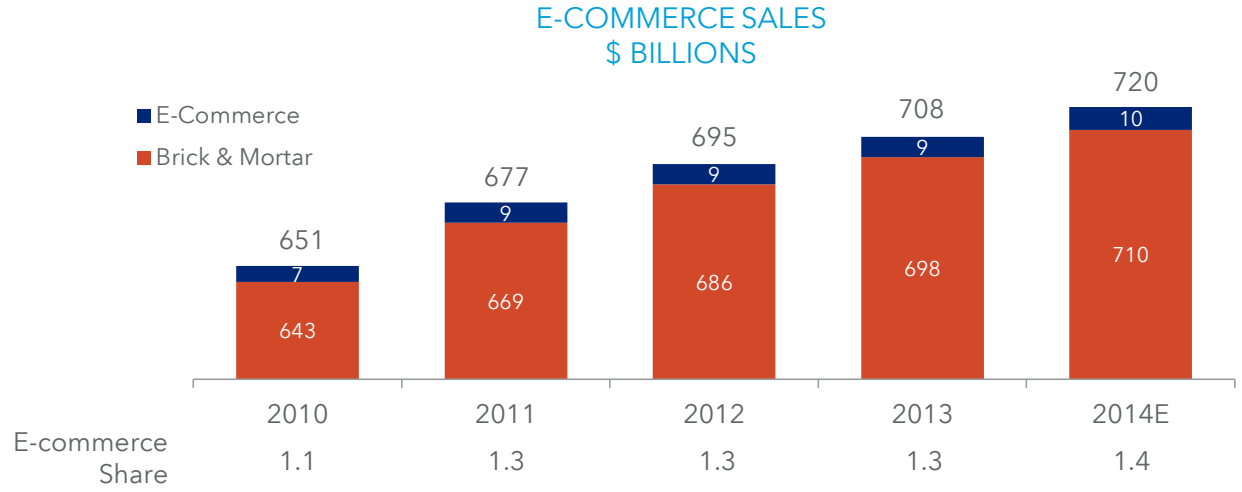
Cultural differences go beyond food and beverage-related attitudes. As detailed in IRI's *Aging America: Carving Out Growth in Mature Markets*, for instance, population shifts will have a significant impact on chronic disease profiles within the United States and consumer strategies to mitigate or live with these ailments.

CPG marketers will need to embrace diversity and serve it well. While this seems a monumental task, taking the right approach—using common cultural traits and needs that transcend country of origin and acculturation level differences—marketers *can* target effectively and impactfully.

Source: [1] IRI, Winning with the Hispanic Consumer Today; [2] Mintel, *Ethnic Foods*, January 2014

Exhibit 6

E-commerce represents a small but rapidly growing share of CPG sales.



Source: IRI, Future of E-commerce in CPG

E-commerce Will Enjoy a Rapidly Growing Slice of the CPG Spending Pie

CPG marketers must go digital or go home.

For years now, e-commerce has demonstrated exceptionally strong growth. In 2014, e-commerce sales are projected to surpass $10 billion (SEE EXHIBIT 6). Still, on the whole, e-commerce represents a mere 1 to 2 percent of total CPG sales.

This will change quickly. Several new players, including Instacart (utilizes personal shoppers to purchase items ordered at stores in select cities and deliver them to customers), Foxtrot (delivers a curated selection of beer, wine, food and everyday essentials) and Burpy (delivers anything found at Costco, H-E-B, Walmart and Whole Foods) are already making a big splash in e-commerce, and innovation in this area is rampant. Many sizable brick and mortar CPG retailers, including H-E-B, Walmart and Target, are tightening their focus on e-commerce growth, as well.

For a number of reasons, including the fact that e-commerce follows several distinct retailer fulfillment models, detailed later in this report, e-commerce share of CPG sales varies greatly at the category level.

Illustrated in IRI's *The Digital Future: A Game Plan for Consumer Packaged Goods*, prime barriers to e-commerce are price, the desire to "touch and feel" products and consumer preference for turnkey customer service (e.g. instant access to the purchased items, ease of receipt/returns). Despite these obstacles, e-commerce CPG is growing at more than ten percent annually.[1]

A number of factors support rapid e-commerce growth, including advancements in technology, increased urbanization, changing demographics and an increasing presence of the country's largest retailers on the e-commerce playing field.

And, that's just actual sales dollars. Detailed throughout this report, the Internet plays a powerful role in the sales cycle, beyond the ultimate ringing of the cash register.

Sources: [1] Silicon Hill News, 3/22/2014; [2] Tech, 8/15/2014; [3] IRI, The Digital Future: A Game Plan for Consumer Packaged Goods

The Influence of Digital Interactions Pre/During/Post Purchase Has Created an Intricate Web of Potential Pathways to Purchase

IRI recently partnered with Boston Consulting Group (BCG) and Google to deliver a project on behalf of the Grocery Manufacturer's Association (GMA). The study clearly demonstrated that digital is transforming the tried and true consumer path to purchase into a complex mesh of interactions, while having a significant influence on both online and in-store shopping transactions.

Despite growth hurdles mentioned earlier in this report, there is no doubt that digital is having a profound impact along the entire path to purchase by creating a much broader set of potential ways for shoppers to engage, particularly during the "discovery" and "search" phases of the purchase process.

Today, there are approximately 2,500 unique purchase pathways that a shopper could potentially follow.

While 22 percent of shoppers interact online in some way prior to shopping, "pre-tail" digital activity is more prevalent in some sectors, including frozen foods, personal care products and over-the-counter medications. And, across categories, pre-tail behaviors are escalating (SEE EXHIBIT 7).

And, while the use of digital during the in-store phase is currently quite low, three-quarters of shoppers indicate that they plan to rely more heavily on their smartphones and/or tablets during future shopping excursions. Retailers, in turn, are responding with tools to intercept shoppers as the moment of purchase nears.

Digital has the power to make business personal again.

~Erin Hunter; Head of Global CPG Strategy; Facebook

Exhibit 7

Though the CPG industry has been relatively untouched by digital's influence on the path to purchase up until now, the future looks quite different, with digital exerting influence up and down the purchase path.

22%

of shoppers interacted digitally in some way **prior to shopping**

4%

of shoppers used a digital device **during the shopping process**

75%

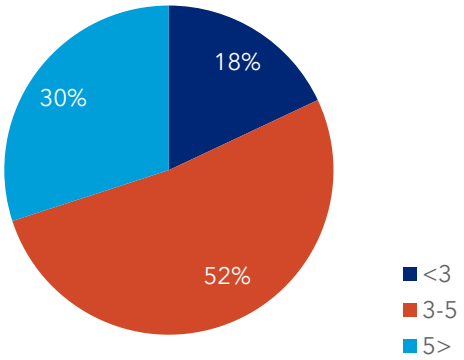
But…nearly 75% say they **plan to use their smartphone/tablet more during the shopping process in the future**

Sources: IRI Path to Purchase Study, April, 2014.

Exhibit 8

More than 80 percent of shoppers visit three or more retail channels to complete their CPG shopping ritual.

NUMBER OF CHANNELS SHOPPED

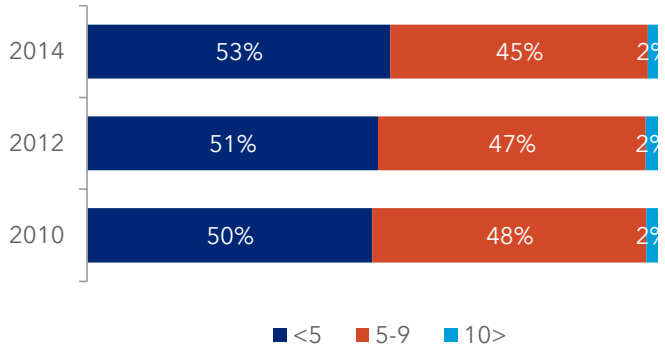


Source: IRI Consumer Network™ 52 weeks ended 5/18/2014 and same period prior years

Exhibit 9

Increasingly, consumers are confining their shopping to fewer channels—the channels they perceive to offer the best value.

CHANGE IN NUMBER OF CHANNELS SHOPPED 2014 VS. 2011



Source: IRI Consumer Network™ 52 weeks ended 5/18/2014 and same period prior years

Value Is in Consumers' Crosshairs

Following years of economic trials, the "golden ring" of CPG shopping is value. Shifting channel penetration trends go hand-in-glove with this powerful new consumer mantra. As such, managing pricing conflicts across channels—whether balancing the size/value equation or price and promotion alignment—has become critical in today's marketplace.

Today, more than 80 percent of shoppers visit three or more channels as they carry out their CPG shopping journey (SEE EXHIBIT 8).

Still, shopper behavior is changing, and these changes are reframing the CPG industry. Increasingly, shoppers are confining their journey to fewer CPG channels—those channels they perceive as offering the best value (SEE EXHIBIT 9).

Creating demand across multiple interconnected and complex channels is challenging and will become even more so as more nodes crop up along the path to purchase. Increasing shopper complexity makes this already-challenging job even more difficult—yet simultaneously critical.

Demonstrating an ongoing ability to provide value to *each and every* shopper is essential to ongoing success.

Granular—*individualized*—targeting and execution is the only way to elicit consistent shopper response.

Increasingly, shoppers are confining their shopping to fewer CPG channels—the channels they perceive as offering the best value.

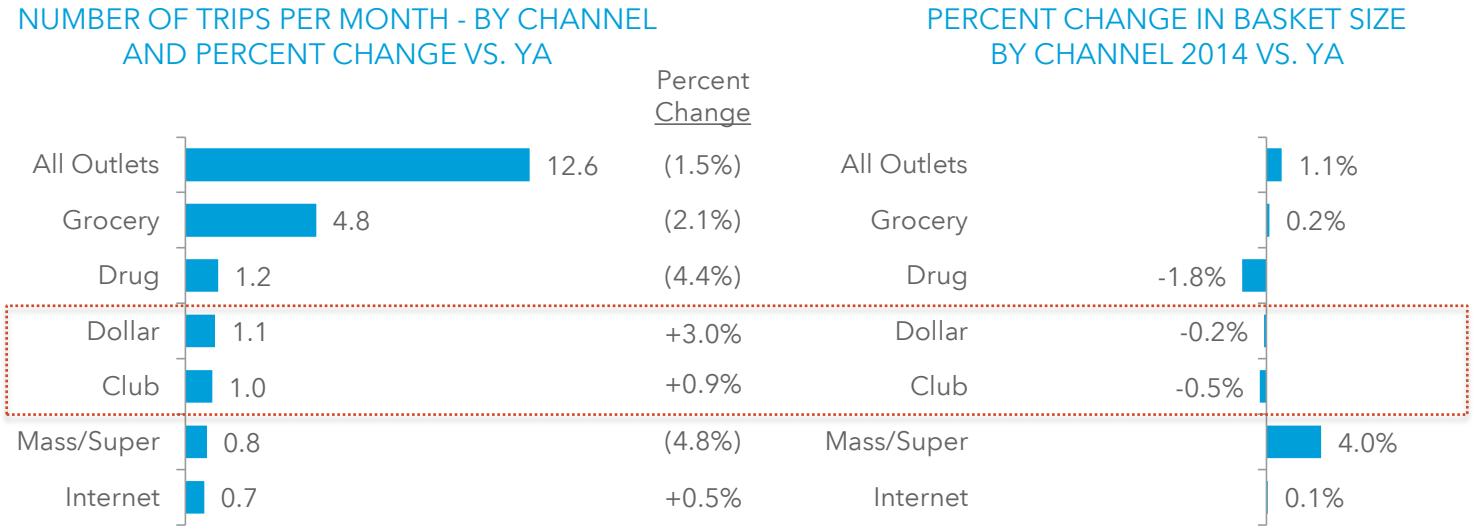
43%
2012

I have a few stores I regularly shop for groceries

49%
2014

Exhibit 10

Overall trip frequency slipped during the past year, but per trip spending crept up; dollar and club saw noteworthy trip gains.



Note: Mass/Super and Grocery do not include Walmart; Not all channels represented.
Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period prior year

Trip and Spending Changes Underscore the Ferocity of Consumers' Acceptance of Emerging CPG Channels

During the past year, grocery and drug channels experienced negative trip frequency and flat to declining basket size (SEE EXHIBIT 10). The Internet saw a modest uptick in both frequency and per trip spending.

Meanwhile, emerging value-oriented channels showed resilience. Dollar channel trips were largely flat and average basket ring rose. Club baskets slipped slightly, but trip trends outpaced industry average and more established grocery, drug and mass/super channels by a wide margin.

These shifts underscore the depths of consumers' willingness to try new channels and banners along their pursuit of value. With many of consumers' recession-driven cut-backs still widely pervasive, there is no sign that the pursuit of value will diminish.

In fact, evolving consumer trends, including the building momentum of millennial shoppers, suggest that this quest will continue for years—perhaps decades—to come.

Illustrated in IRI's recent POV, "Millennial Shoppers: Positive Mindset Points to Future Growth," millennial shoppers—and this group comprises nearly one-quarter of the U.S. population—exhibit unique price comparison strategies and shop multiple stores to seek out the best deals.

These shoppers are new to CPG. They have not established habits and they are not likely to shop a certain channel/banner simply because their parents shopped there. Millennials are talking to their friends, associates and anyone on social media about where to find the best deals.

CPG marketers must adjust their strategies to align with behaviors of up-and-coming shoppers, including millennials, while not taking their "eyes" off their base.

Exhibit 11

The grocery channel is struggling to maintain share amidst intense competition and powerful wave of economic, demographic and technological influences.

INDEX OF CHANNEL SHARE AND POINT CHANGE VERSUS YEAR AGO
(INDEX AVERAGE = 100)
BY CONSUMER SEGMENT

	Grocery		Drug		Mass/Super		Dollar		Club		Internet	
	Index	Share Pt. Chg.	Index	Share Pt. Chg.	Index	Share Pt. Chg.	Index	Share Pt. Chg.	Index	Share Pt. Chg.	Index	Share Pt. Chg.
$35K OR LESS	98	-0.7	105	-0.5	112	0.9	**193**	**0.2**	56	0.2	106	0.0
$35K TO $69K	99	-0.5	99	-0.5	108	0.8	91	**0.1**	90	0.1	98	0.1
$70K TO $99K	102	-0.3	95	-0.3	94	0.3	55	**0.0**	124	0.5	89	0.1
$100K OR MORE	103	-0.5	100	-0.2	77	0.6	33	**0.0**	152	0.2	106	0.1
HISPANICS	95	0.1	**117**	-1.0	100	**0.4**	91	0.2	122	**0.8**	104	0.1
HH W/KIDS	102	-0.6	82	-0.8	110	1.0	83	0.2	107	0.3	77	0.0
MILLENNIALS	102	-0.8	91	-1.7	115	1.8	99	0.5	80	0.3	101	-0.1
GEN X	101	-0.3	92	-0.6	105	0.5	90	0.1	104	0.3	89	0.0
BOOMERS	98	-0.6	100	0.0	95	0.6	106	0.0	106	0.1	103	0.1

Note: Mass/Super and Grocery do not include Walmart
Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period prior year

Grocery and Drug Are Losing Share to Competing Channels

Grocery share of spending is quite similar across key consumer segments. In the face of prolonged intense competitive pressure, the channel is seeing share slip across many key segments as well (SEE EXHIBIT 11).

Across other CPG channels, share trends sometimes vary rather drastically across consumer segments.

The drug channel, for instance, wins disproportionate share of spending from Hispanic shoppers—a segment that spends heavily on beauty and personal care products. But, this segment also tends to have larger household size, which, coupled with prolonged economic pressures and strong propensity to spend at Walmart, is hastening shifts in spending to mass/super and club channels.

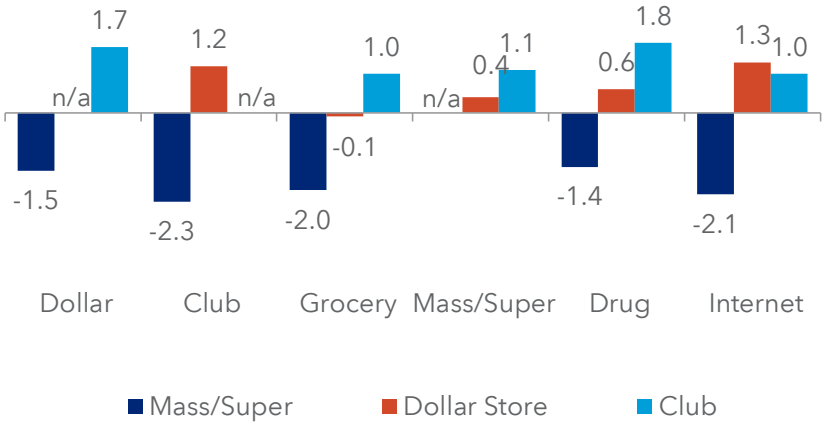
Lower earning households spend disproportionately in the dollar channel—nearly double the average rate. While higher-earning households still index on the low side, the channel is effectively defending the base across all consumer segments, thanks to ongoing efforts to hone assortments, spruce stores and diversify formats.

Internet share of spending is fairly consistent across most consumer segments. Gen X, households earning $70,000-$99,999 annually, and those with children are notable exceptions. Here again, though, retailers are effectively defending the base.

Exhibit 12

Protecting and cultivating core shoppers is critical to growth.

MASS/SUPER, DOLLAR AND CLUB CHANNEL PENETRATION POINT CHANGE 2014 VS. YA AMONG HEAVY SHOPPERS ACROSS CPG CHANNELS



HEAVY SHOPPER CHANNEL SPEND AND INDEX VERSUS HEAVY ALL OUTLET SHOPPERS (INDEX AVERAGE = 100)

	Channel Spend; $ Billions	Index vs. All Outlet Heavy Buyers
Grocery	$208.5	119
Mass/Super	$30.4	126
Drug	$40.8	144
Dollar	$13.4	165
Club	$59.2	116
Internet	$8.3	132

Note: Mass/Super and Grocery do not include Walmart; Not all channels represented
Source: IRI Consumer Network™ 52 weeks ended 8/10/2014 and same period prior year

First, Defend and Grow the Base

It's simple: The best source of growth is existing customers—keep them; grow them.

But, in the CPG world, channel shifting has become quite commonplace. Dollar retailers, for instance, are winning heavy shoppers from across competing retail channels (SEE EXHIBIT 12). Mass/super, on the other hand, is losing heavy shoppers to most competing channels.

The pursuit of value will not subside in the next couple of years. Consumers are becoming increasingly adept at finding the best deals, which points to a likely escalation in channel surfing behavior.

Losing shoppers is quite costly to CPG retailers, particularly when heavy shoppers—the top one-third of spenders in a channel—make a change. Illustrated in the chart at the top of this page, heavy channel shoppers outspend other shoppers by a wide margin. So, if even a small share of heavy shoppers leave, the revenue hit is substantial.

It's cheaper, easier and more effective to retain current shoppers than it is to acquire new ones.

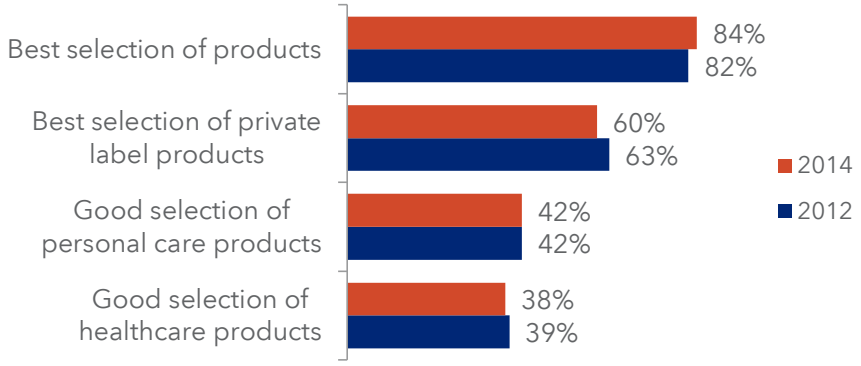
And, of course, a key marketing premise: It's cheaper, easier and more effective to retain current shoppers than it is to acquire new ones. Every core shopper retained translates to significantly less in new shopper conversion spending.

The pages that follow provide detailed insight into how marketers must go about defending their base.

Exhibit 13

Ensure consumers can find what they want, where they want it…every time.

KEY ASSORTMENT ATTRIBUTES FOR A SATISFYING SHOPPING EXPERIENCE – PERCENT OF CONSUMERS



Source: IRI 2014 Brand & Retailer Loyalty Survey

Get the Right Products to the Right Place at the Right Time

Consumers are changing how they shop, where they shop and when they shop. In this rapidly changing environment, keeping up with evolving trends is not an option. This is Darwinism of the retail variety… survival of the fittest.

Technology is playing a massive role in the CPG transformation. Changes on the consumer behavior end have been discussed throughout this report. But, technology is impacting CPG marketers, too.

There is no longer "an average shopper." Consumers are individuals and they want to be treated as individuals.

Through the use of advanced analytics, CPG marketers can and must provide that individualized level of service. This means going beyond tailoring assortment to different stores, banners, regions and demographics. Tailor assortment to different channels, including brick-and-mortar and online, as well.

First and foremost is getting the right products to the right place at the right time. More than 80 percent of shoppers note that having a good product selection is key to an enjoyable shopping experience (SEE EXHIBIT 13). To be a good selection of products, assortment must meet the needs of the shopper.

Six in 10 shoppers look for a good selection of private label products. But, in some channels/banners/ categories, this number is much higher. Marketers must invest to understand when and where this is the case and adjust assortment accordingly. The same goes for healthcare selection, personal care selection and so on throughout the store.

With this done, promotional programs come into play. Here again, individualized development and execution will elicit the most powerful shopper response.

This is a herculean task. With hundreds (even thousands) of stores, tens of thousands of SKUs to manage, and numerous hand-offs and points of contact, mistakes are going to happen. Realistically, the greater the granularity of the process, the more opportunity for mistakes. It's a challenge for all retailers—big and small, sophisticated or not. But, odds of avoiding these mistakes certainly improve when retailers and manufacturers work as a team.

Exhibit 14

Trip missions play a major role in determining CPG channel selection.

TRIP MISSION AS PERCENT CHANNEL DOLLAR SALES

	Grocery		Drug		Mass/ Supercenter		Dollar		Club		Internet	
	Mission Share of Sales	Pt. Chg. vs. 2010	Mission Share of Sales	Pt. Chg. vs. 2010	Mission Share of Sales	Pt. Chg. vs. 2010	Mission Share of Sales	Pt. Chg. vs. 2010	Mission Share of Sales	Pt. Chg. vs. 2010	Mission Share of Sales	Pt. Chg. vs. 2010
Pantry Stock-Up	45%	(0.4)	1%	+0.1	31%	+2.3	7%	+0.4	33%	**+1.4**	6%	(2.4)
Fill-In	20%	(0.2)	17%	**+2.1**	21%	+0.8	18%	+0.7	21%	(0.7)	6%	(0.8)
Special Purpose	11%	+0.2	28%	(0.4)	27%	(2.1)	30%	+0.0	23%	(1.3)	22%	(0.7)
Quick Trip	25%	+0.4	54%	(1.8)	22%	(1.1)	46%	(1.1)	24%	+0.5	66%	+3.9

Note: Mass/Super and Grocery do not include Walmart; Not all channels represented
Source: IRI CSIA™ 52 weeks ended 8/10/14 and same period year ago

Keep Product, Price and Promotional Strategies in Lock Step with Evolving Trip Mission Patterns

A consumer becomes a shopper when a need arises that necessitates a shopping trip and the planning process begins. A variety of factors, including specific purchase needs, time constraints and budgetary considerations, are all part of this process. These factors, and more, will impact the shopper mindset—his or her trip mission. Trip mission, in turn, will inform a variety of shopping behaviors, including channel and store selection, product bundles and basket size.

Grocery, mass merchandise/ supercenters and club stores, for instance, are primarily pantry stock-up channels (SEE EXHIBIT 14). Drug, dollar and the Internet, meanwhile, capture most of their sales during quick trip missions.

During the last several years, though, trip mission patterns have changed considerably. Club channels are getting more of their dollars from pantry stock-up missions. Drug is playing more of a fill-in role. These shifts underscore the channel blurring phenomenon that is taking place, and they will continue in the coming months and years.

Keeping in lock step with evolving trip mission patterns is tricky. Manufacturers must keep pace with consumers—their needs, wants and mindsets during any given trip mission.

Simultaneously, manufacturers must be working to protect valuable shelf space. To do so, manufacturers must ensure that their brands—including product, packaging and pricing—are meeting the goals of their retailer partners, both in terms of volume growth and margin goals and, of course, delivering consumer value.

Exhibit 15

Grocery and mass/supercenter channels are losing share across several CPG departments, to the benefit of value and emerging channels.

CHANGE IN CHANNEL SHARE OF DEPARTMENT SPENDING

	Grocery	Drug	Mass/ Supercenter	Dollar	Club	Internet
BEVERAGES	**(0.3)**	+0.1	0.0	0.0	+0.2	+0.1
FROZEN	(0.1)	0.0	(0.2)	+0.1	+0.1	0.0
GENERAL FOOD	**(0.3)**	+0.1	(0.1)	+0.1	+0.2	+0.1
LIQUOR	(0.1)	+0.1	(0.1)	0.0	**+0.5**	0.0
REFRIGERATED	**(0.3)**	0.0	+0.1	0.0	0.0	0.0
BEAUTY	+0.1	0.0	0.0	+0.3	+0.3	+0.2
GENERAL MERCHANDISE	+0.2	0.0	(0.3)	0.0	+0.2	+0.1
HEALTHCARE	0.0	+0.1	(0.2)	+0.1	+0.4	+0.1
HOME	(0.1)	+0.2	(0.5)	+0.1	+0.3	+0.1

Note: Mass/Super and Grocery do not include Walmart; Not all channels represented
Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period prior year

The Distinction Between CPG Channels Is Becoming Increasingly Blurred

The lines of demarcation between CPG channels has blurred, and the distinction between channels is becoming increasingly convoluted. During the past year, for instance, the grocery channel has lost share in core food and beverage departments—refrigerated, general foods and beverages (SEE EXHIBIT 15). Club is a notable winner in beverages and general food, while also gaining about one-half share point in liquor.

Mass/super also lost ground in a number of departments, including home care and general merchandise, once again to the benefit of club.

Dollar channel share is holding steady across major departments, with slight up-ticks here and there, including more noteworthy gains in beauty.

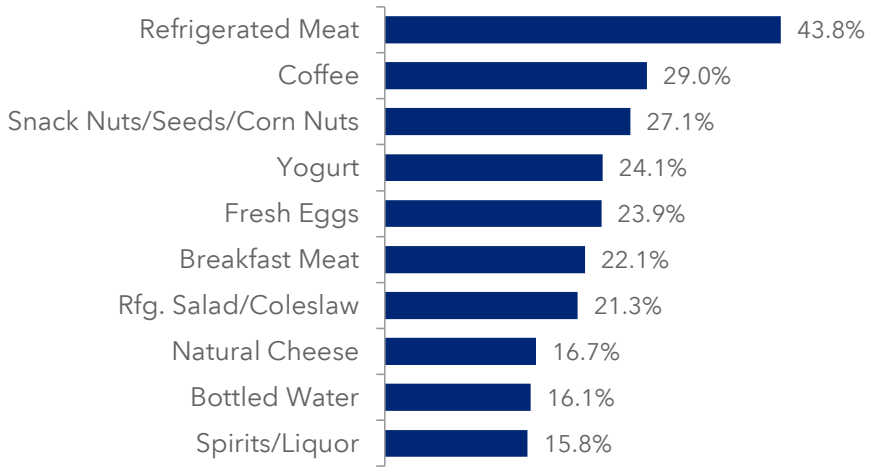
Consumers are key beneficiaries in the battle for share of spending. But manufacturers also stand to win—in the form of simplified logistics due to demand smoothing and inbound efficiencies.

The key to capturing these benefits is understanding the channel preferences and behaviors of key and target consumers and delivering against those wants and needs.

Exhibit 16

The ranks of the fastest-growing CPG categories illustrate the powerful influence of home-based eating trends on the industry.

TOP GROWTH CATEGORIES
PERCENT CHANGE IN DOLLAR SALES ALL OUTLETS
2014 VS. 2011



Note: Based on dollar sales growth 2014 v 2011; among top 50 CPG categories

Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period 2011

Align Assortment with Unique Shopper Needs

Retailers, too, must invest to understand the many and varied needs of those who shop their stores.

The ranks of the fastest-growing CPG categories illustrate the powerful influence that home-based eating trends are having on the industry (SEE EXHIBIT 16). But, a look at top-growth categories across channels demonstrates that consumers are turning to varied and sometimes even unexpected channels to fulfill their CPG needs.

To compete in an environment where shoppers are more selective than ever of where they shop and choosing stores that suit their individual budgets and lifestyles, retailers must work closely with manufacturers to allocate precious shelf space.

Through comprehensive joint business planning, retailer and manufacturers must establish an optimal mix of categories, brands, pack sizes and price points. Given the pace of change today, these efforts must be ongoing, involving consistent measurement and on-the-fly adjustments to stay on plan.

TOP GROWTH CATEGORIES
BY CHANNEL - TOTAL U.S.
LISTED IN ALPHABETICAL ORDER

GROCERY
Coffee
Refrigerated Meat
Spirits/Liquor

DRUG
Cold/Allergy/Sinus Liquids
Lip Treatment
Wine

MASS/SUPER
Coffee
Refrigerated Meat
Yogurt

DOLLAR
Cigarettes
Fz. Dinner/Entrees
Milk

CLUB
Rfg. Salad/Coleslaw
Snack Nuts/Seeds/Corn Nuts
Yogurt

INTERNET (MAIL ORDER)
Coffee
Dog Food
Weight Control

INTERNET (DELIVERY/PICK UP)
Canned Fruit
Deli Meat
Canned Beans

Source: IRI CSIA™ 52 weeks ended 8/10/2014 and same period 2011; IRI MarketAdvantage™

**Notes: Mass/Super and Grocery do not include Walmart; Top growing categories among 50 largest categories in the channel; For Internet, top growing among 25 largest categories.*

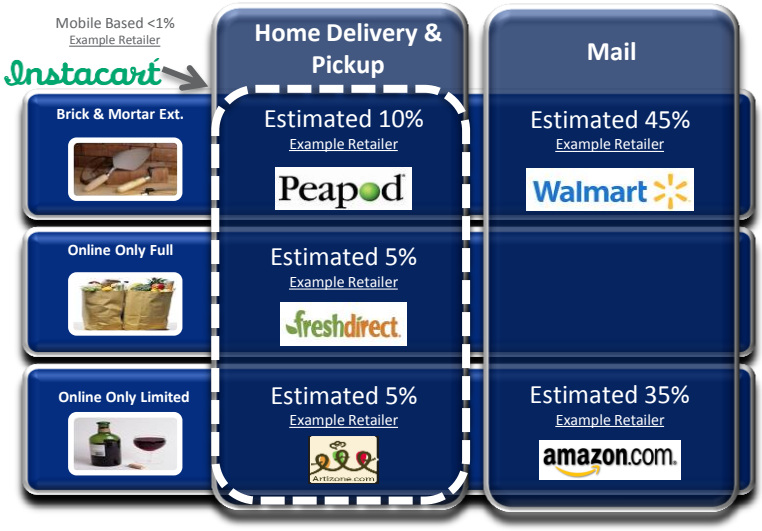
Exhibit 17

E-commerce is marked by several distinct retail models; understanding these models is critical to ensuring alignment against consumers' needs and wants.

E-COMMERCE SALES
$ BILLIONS

	$ Billions
Mail Delivery	$8.0
Store Pick-Up/Home Delivery	$2.0

E-COMMERCE CPG RETAIL MODELS
WITH ESTIMATED SHARE OF TOTAL



Source: IRI Consumer Network™; IRI Analysis

Invest to Understand Existing and Evolving E-commerce CPG Retail Models

Digital is here to stay. Noted earlier, an increasing number of influential brick and mortar retailers are establishing and/or enhancing their online retail presence.

All CPG marketers looking to survive and thrive in the new digitally-enabled world invest to understand existing and evolving e-commerce models.

Online CPG is not a single cohesive channel. It operates under several different models, each of which sells products very differently (SEE EXHIBIT 17).

About 20 percent of online CPG sales are made through retailers that offer in-store pick-up (order online; pick up at the store or other designated retailer location) and/or home delivery (order online; product delivered to the home delivery via store-owned delivery fleet). Generally, these orders look very similar to the regular weekly shopping basket.

Peapod is currently leveraging both of these models. Peapod started as a delivery service but more recently began building out a store pick-up service. Pick-up is viewed as a way to give consumers a taste of the Peapod home delivery service, with the hope they might start using it eventually. It is also an option for people who might meet the minimum purchase ($60) required for delivery and/or to avoid paying a delivery fee and tip.[1]

The remaining 80 percent of sales are ordered online and shipped to the consumers' home via the U.S. Postal Service, FedEx, or UPS. Amazon and Walmart both play in this world.[2]

Store pick-up is generally a free service; mail and home delivery requires a surcharge. In some instances, delivery charge is waived over a certain order threshold.

Sources: [1] Boston Business Journal 9/16/2013; [2] Reuters 6/4/2013

Exhibit 18

The tradeoff between convenience and price is a critical factor in determining whether to purchase online or in the store.

COMMON PRODUCT CHARACTERISTICS BY E-COMMERCE RETAILER FULLFILLMENT MODEL

HOME DELIVERY & PICK UP

Perishables

Heavy

MAIL

HBC

Bulky

Source: IRI Consumer Network™; IRI Analysis

Align e-Distribution Strategies Against Consumers' Most Pressing Considerations: Time, Money and Convenience

Due to logistical and regulatory considerations, product offerings across these three models differ rather significantly.

Mail services are less likely to offer perishables and liquids, including alcoholic beverages, due to ease of spoilage, weight and legal obstacles. As a result of these limitations, orders delivered via mail services tend to be more limited, only including fill-in items and/or bulk products that shoppers prefer not to lug home during their weekly grocery shopping trip. Hard-to-find items, such as health and beauty care products that are less available in the physical grocery store environment, are also more prevalent in this model (SEE EXHIBIT 18).

To maximize efficiency and return on e-commerce investment, CPG marketers must invest to understand existing and evolving e-commerce CPG models and how those models fit with the needs, wants and behaviors of key and target consumer groups.

The tradeoff between "touch and feel" and convenience versus price is a critical factor in determining whether to purchase online or in-store.

Online CPG shopping saves the time of traveling to the store, but this savings has a cost in delivery fees, which can be one of the largest barriers to e-commerce CPG shopping trials. Due to these expenses, home delivery is more palatable in more urban areas with higher population densities offering a more-affluent-than-average shopper base.

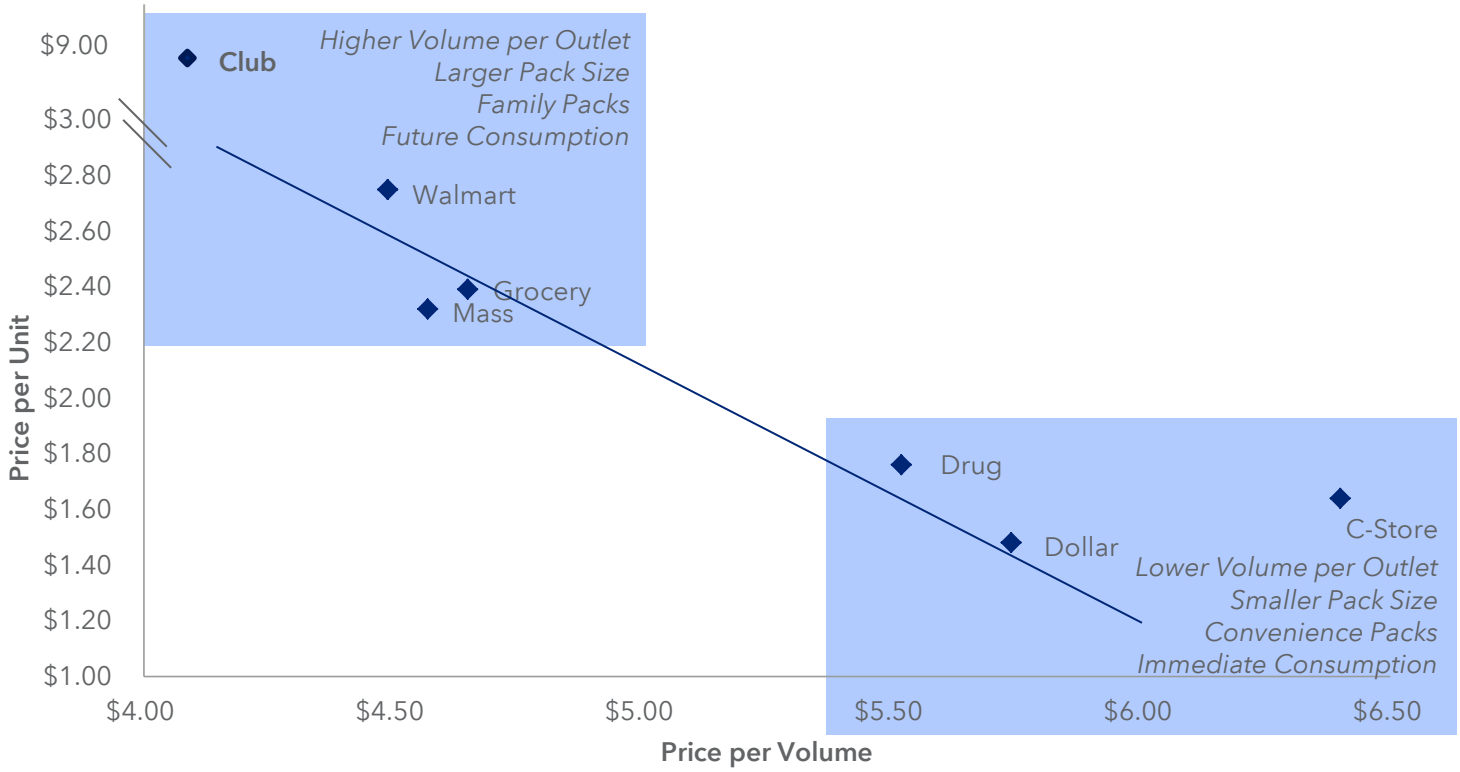
Successful e-commerce CPG strategies will align precisely with the needs, wants and behaviors of key and target consumer segments.

CPG marketers looking to play in the e-commerce space must strike a delicate balance—a balance that will change on a market-by-market basis. Playing the game well will certainly pay off, for it will unlock your company's share of the more than $1 billion in annual growth generated by e-commerce CPG.

Exhibit 19

***ILLUSTRATION**: Price must reflect pack strategy and value requirements for each individual CPG channel.*

A SNACK BRAND'S PRICE POINTS VERSUS VALUE AND PACK STRATEGY



Source: IRI ILD POS database; L52 WE 06/16/13, MULO+C

Create Demand-Based Pack and Price Solutions That Are Customized at the Channel Level

Best-practice price-and-pack strategies will balance consumer needs against retailer partner needs. As such, manufacturers must understand unmet shopper needs and usage occasions, as well as how demand is expressed within each CPG channel.

For instance, a major snack brand developed smaller packs at a higher price per volume for distribution to lower volume, more immediate-consumption channels, such as convenience, dollar and drug stores (SEE EXHIBIT 19).

Meanwhile, for club, mass/supercenter and grocery stores, where volume is higher and consumption is more "down the road," larger packs, suited for family consumption, and at a higher price per unit but lower price per volume, were distributed.

By offering price points and associated pack formats that appeal to different consumers for different need states, the snack brand manufacturer not only drove year-on-year growth, but also gains in both penetration and frequency.

Customer Success Story

More Detail Enables Better In-Store Performance

Granular Understanding of Each Store Leads to 1 to 2 Percent Sales Boost

Challenge

Management of a leading U.S. brewer faced a challenge: how to achieve growth in a mature and stable market where it already enjoyed impressive market share. Through the brewer's store delivery system, the trade marketing group could adjust product assortment in each of the 200,000-plus stores through which they sold product. The core of the challenge: The brewer distributed more than 600 SKUs, but the typical store had shelf space for about 60: What are the right items to stock in each store? The trade marketing group knew that stocking the right items in each store would grow sales 2 percent, an extra $74 per store per week, or a potential $770 million in incremental sales annually.

Approach

The manufacturer contacted a number of expert sources to help address this challenge. No one would touch it, except IRI. IRI realized the most significant obstacle to developing store-by-store assortment strategies was lack of competitive information on a week-by-week and item-by-item basis.

While the brewer could get its hands on more than 75 gigabytes of data, that was just half of what was needed to provide accurate store-level planning.

Clearly, a new solution was in order. By integrating multiple brewer and IRI data sources, the team was able to impute a complete data set for all stores.

IRI developed a unique analytic approach and utilized it to create an assortment optimization strategy for each store based on shopper loyalties to approximately 25 key beer attributes, such as package and quantity, flavor, style and brand.

Each store's assortment recommendation reflected the specific attributes preferred by that store's shoppers, but also reflected store constraints, such as shelf and refrigerated space.

The trade marketing group then delivered these recommendations to each route driver through the brewer's mobile devices and internal network.

Results

A third-party expert evaluated performance of the initial pilot and reported it had, in fact, achieved the desired 2 percent portfolio growth in stores that implemented the recommendations versus a control group.

The initial pilot achieved the desired 2 percent portfolio growth in the test stores vs. the control stores.

The new process also dramatically improved new product forecasts by enabling creation of more realistic sales targets.

Impact

Managers are now closely linking sales planning and innovation functions to create more realistic sales volume, distribution and shelf space allocation that reflect the entire portfolio. Production planning, operations, logistics and category management teams are also adopting this improved planning capability.

The brewer is also tapping the planning capability to optimize its portfolio across more than 250,000 bars, restaurants, lodges and similar venues.

Framework to Win

Consumer engagement and the CPG shopping journey have forever changed and the evolution is far from over. CPG marketers absolutely must adopt a strong multi-channel relevance—including a strong and seamless digital presence—or they will undoubtedly face obsolescence. To solidify a position in the express lane along the path to growth, flawless execution is essential.

Retain current shoppers and consumers by delivering against each shoppers'/consumers' most pressing needs and wants.

- Drive purchase frequency and share with a value-oriented and narrow assortment of high-demand categories.
- Retailers and manufacturers: Collaborate to ensure effective in-store inventory management across key categories and brands.
- Stay connected with existing shoppers by providing easy access to relevant information at various points throughout the shopper journey.

Align assortment and distribution strategies against consumers' preference and channel behaviors to get the right product to the right place at the right time.

- Align distribution strategies against preferred trip types, channel preferences and store locations of key consumers.
- Invest to ascertain a 360-degree perspective on key shoppers/consumers, including online and offline sales, including behavior around similar or substitute categories and brands.
- Tailor assortment to account for the growing presence of e-commerce, identifying where categories that are well suited to online shopping may be able to cede in-store shelf space.

Optimize marketing mix against unique characteristics and considerations at the channel level.

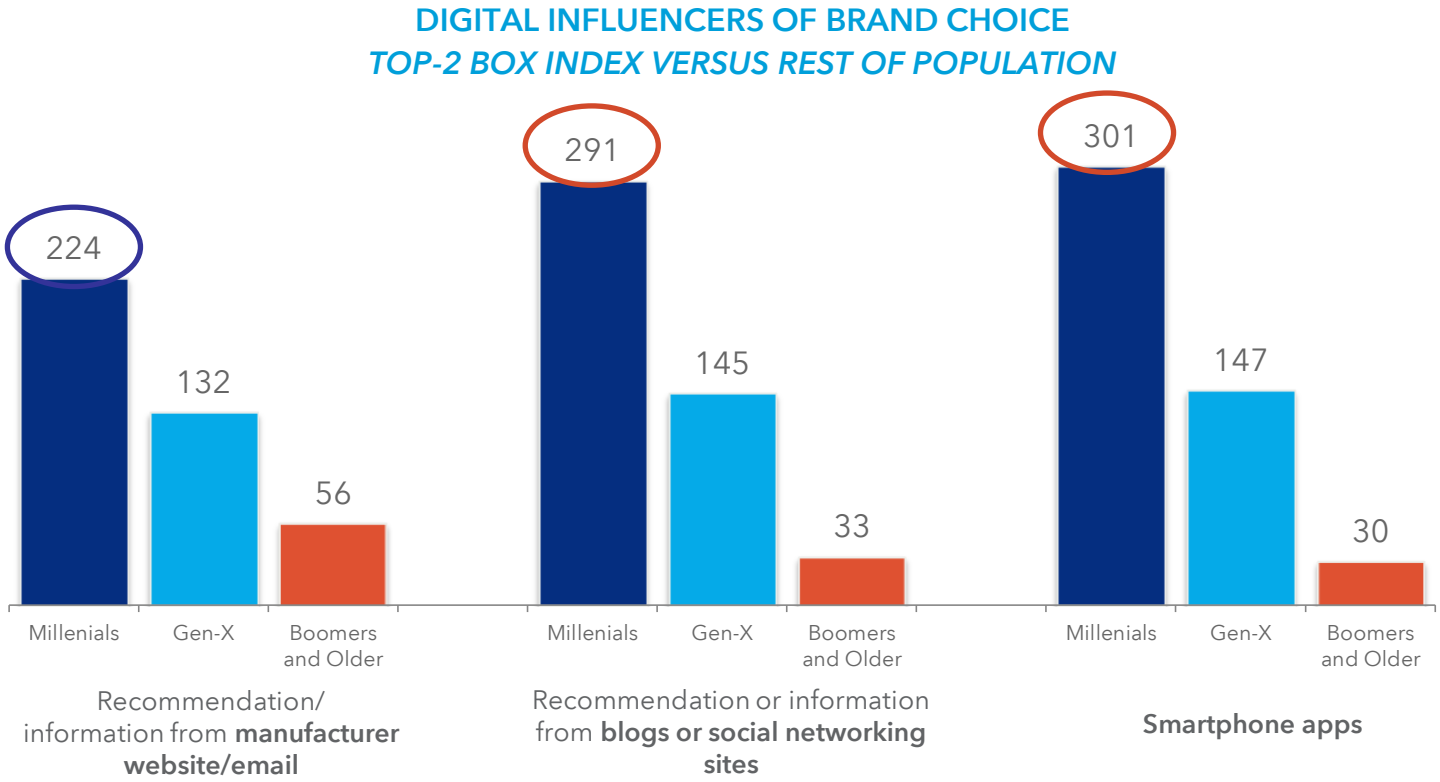
- Develop pricing strategies that focus on driving volume growth, and avoid programs that bring dollar value growth at the expense of volume.
- Tailor product packaging, pricing and promotional programs at a granular level to account for shopper mix down to the store level.

Create demand-based products and packages.

- Invest to understand where and how to strengthen collaboration between retailers and manufacturers to minimize and/or overcome stumbling blocks in execution.
- Manufacturers: Invest to understand where your categories/brands sell most and where growth is happening and align distribution strategies accordingly.

The New Shopper Journey: Creating a New Shopper-Centric Roadmap for Growth in a Changing World

Millennials are most open to digital influencers.



The New Shopper Journey is IRI's latest research into the dynamics that are changing the U.S. CPG landscape for manufacturers and retailers. This study focuses on four areas. **Millennial purchasing power** will overtake that of boomers between now and 2020. As a percentage of CPG dollar volume, millennials' share will grow 70 percent, while that of boomers will decline 16 percent. **Uncertainty about the U.S. economy** continues to be a cloud lingering on the horizon for many shoppers. Nearly 40 percent of U.S. households consider themselves "challenged" in today's economy. **The impact of digital and social media, combined with the ubiquity of mobile devices**, is accelerating the transformation of how Americans shop. Eighty-two percent of shoppers turn to their smartphone to help with shopping, and literally 75 percent of those aged 25-29 sleep with their phone. The **ethnic composition** of the U.S. shopper continues to change dramatically. Hispanics will account for 53 percent of U.S. population growth between 2010 and 2020, more than three times faster than the next fastest-growing group.

This new research serves as an information cornerstone for companies as they update their core strategies, including: product, pricing, packaging, promotion, assortments and store layouts.

For more information, contact Donna Wydra at donna.wydra@iriworldwide.com

Resources

FOR MORE INFORMATION

Please contact Susan Viamari at **Susan.Viamari@IRIworldwide.com** with questions or comments about this report.

If you enjoyed this report, you may be interested in the following IRI products and services, which provide customizable insights into the evolving path to purchase:

To fuel iterative consumer and shopper analyses on the fly, turn to ***IRI Consumer and Shopper Insights Advantage™***

Leveraging IRI's revolutionary Liquid Data Platform, CSIA serves up Trial & Repeat, Product Switching, Basket-Level Co-Purchase, Category Leakage, and other key consumer analyses to better inform brand marketing decisions and protect and grow business at retail.

For insights generated by longitudinal consumer purchasing, shopping, attitudinal, demographic and geographic information, turn to **IRI Consumer Network™**

This nationally representative panel of households tracking purchases with hand-held barcode scanners delivers extensive demographic profiles to enable in-depth analysis of purchase behavior across standard or custom-defined consumer segments across channels.

To segment efficiently and target powerfully by identifying, quantifying and tracking distinct consumer/shopper groups who share economy-related attitudes and behaviors, rely on **IRI EconoLink™**

IRI's EconoLink is a latent class segmentation based on actual shopping behavior and consumer attitudes—especially about the impact of economic conditions – that helps manufacturers and retailers understand and respond to the new demands of shoppers across the economic continuum.

To clearly and accurately define categories and boundaries, drive understanding of competitive sets, uncover areas of white space and possible exploration, identify competitive relative areas of strength and weakness, and guide 4-P recommendations at retail, turn to **IRI's Hendry Market Structure™**

IRI's Hendry Market Structure is a product segmentation model that uses in-depth analysis of transaction-level data to reveal the true competitive structure of a category and the consumer purchase decision process.

About IRI. IRI is a leader in delivering powerful market and shopper information, predictive analysis and the foresight that leads to action. We go beyond the data to ignite extraordinary growth for our clients in the CPG, retail and over-the-counter healthcare industries by pinpointing what matters and illuminating how it can impact their businesses across sales and marketing. Move your business forward at **IRIworldwide.com**

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