

Managing in a downturn

Marketing strategies for fast-moving consumer goods

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The current recession is the most brutal economic downturn in a lifetime. One industry where the consequences of the recession are felt particularly hard is the fast-moving consumer goods (FMCG) industry. In the past, this industry was dominated by such well-known manufacturer brands as Ariel detergent, Nescafé coffee, Philadelphia cream cheese, Flora margarine, and Pampers nappies. However, in recent decades, so-called private labels or store brands – brands owned by retail giants such as Wal-Mart, Tesco, Carrefour and Aldi – have made huge inroads, especially in western Europe and the US. Today they control 20 per cent of the US FMCG market, 35 per cent in Germany, and more than 40 per cent in the UK. Much of the loss of market share of manufacturer brands is initiated in economic downturns. Faced with a pressing need to save money, shoppers turn to (cheaper) store brands. They discover that the quality is good and, consequently, many stick with the brand when the economy improves again.

Our research, spanning several decades of purchasing behaviour and multiple recessions in countries across the globe, shows that the growth of private labels in recessions leaves permanent scars on manufacturer brands. Will it be any different this time? It is possible, but this will depend on how brand managers respond to the current downturn. Brands that take a proactive stance and treat the recession as an opportunity are likely to come out of the recession stronger than before. In this article, we describe what they should do. Two issues drive the outcome of how brands make it through the recession: their equity at the onset of the recession; and investments in the brand during the recession.

Brand equity

How strong is your brand? Is it a brand with many loyal buyers that people know and trust and are willing to pay a price premium for? Or is it a weak brand, commanding little loyalty and esteem? In sum, is your brand equity high or low? Strong brands enter the recession in a much more favourable position than weak brands. They are on the shelves of more retailers, have more shelf space and have a larger and more committed customer base. Marketing budgets for stronger brands also tend to be higher.

In recessions, retailers across the world devote more shelf space to their own brands (especially since they also command a higher margin). For example, to cater to the increased price sensitivity of UK consumers in the wake of the economic downturn, Tesco launched on September 17 2008, its fourth line of private labels, called “Discount Brands at Tesco.” Sales of Tesco’s discount and value ranges are up 65 per cent on last year, and one in four shoppers now purchases these ranges. This puts a pressure on the number of national brands the retailer still carries. Retailers are less likely to kill brands with a strong and loyal customer base.

High-equity brands are also better insulated against the switching to private labels behaviour that is ubiquitous in recessions, if only because loyal customers incur higher switching costs when buying non-preferred items. High-equity brands are known to suffer less, and to recover faster, following a product-harm crisis. The same holds true when faced with an economic crisis.

Brand investments in recessions

In recessions, shoppers have a natural tendency to switch to private labels in order to save money. The logical thing for brands to do is to counter this tendency by either lowering their own price, or by offering sufficient non-price reasons to consumers to buy their brand. Our research, spanning more than two decades of actual marketing behaviour, reveals that most brands do exactly the opposite. First, brands can counter the price advantage of private labels by ramping up their own price promotions (temporary price reductions). Consumers are more price-sensitive in recessions, so offering more price promotions makes a lot of sense. Surprisingly, price promotion activity for most brands actually decreases in recessionary times.

Second, the brand can counter the price advantage of private labels by increasing its investments in advertising or new product activity. Both provide non-price reasons to purchase the manufacturer brand – image and improved functional performance, respectively. However, our research shows that advertising and innovation activity decreases in recessions.

Marketing research is also one of the first victims in a recession. These outlays are discretionary, and offer an easy way to reduce costs. Unfortunately, in bad economic times, it is more difficult to convince consumers to buy your higher-priced brand. Optimal matching of your brand with consumer needs is even more necessary in difficult times, but evidence shows that brand manufacturers prefer to operate without this crucial guidance during recessions.

Why do companies manage brands in such a counterproductive way? After all, their brands are their most valuable assets. Cutting back in recessions on price promotions, innovation activity and advertising saves money in the short term, but undermines the long-term equity of brands. We believe that it is due to a toxic combination of short-term perspective that characterises the decision-making of many managers and the tremendous pressure on the bottom line in recessionary times. The easiest way out is to cut costs, and since price promotions, advertising, new product introductions and marketing research are largely discretionary costs, they can easily be cut in the short term.

However, this behaviour weakens the equity of brands and negatively impacts on shareholder value. We studied the stock price performance of 26 global companies over a 25-year period and found that annual growth in shareholder value for companies that do not tie their advertising investments to the business cycle is 1.3 per cent higher compared with companies that do let their advertising investments depend on the business cycle. This translates into billions of dollars of shareholder value that are destroyed annually by adopting this erroneous practice.

In sum, companies often do the wrong thing by reducing marketing expenditure despite compelling evidence that it pays to not follow the general trend of cutting back during a recession. Put differently, one should start to treat those marketing expenses as strategic investments, rather than as short-run costs that can easily be cut when the going gets tough. Note that “going against the trend” can be in absolute terms (strong form) or in relative terms (weak form). Indeed, by holding brand expenditures at pre-recessionary levels, while other brands spend less, one may still increase one’s share of total market communications.

Four scenarios

By combining two dimensions of brand equity at the onset of the recession and brand investments in the recession, we get four scenarios.

	Brand investments
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		Reduction in brand investments	No reduction/increase in brand investments
Brand equity	High	(1) High loss potential	(2) Recession is opportunity
	Low	(3) Survival game	(4) Double or nothing

Brands in cell (1) run the distinct danger that their equity will be significantly eroded in the current recession. They start from a favourable position, but their behaviour will lead to a significant weakening of their position vis-à-vis private labels and the brands in cell (2). Managerial decision-making for these brands is overly cautious and focused on the short-term. These brands should emphasise activities that keep their customers satisfied (and, hence, retain them), rather than focus on cost-saving activities. Indeed, customers lost during the recession may never come back, even when the economy's outlook improves again.

For brands in cell (2), the recession is an opportunity to pull ahead of their short-sighted competitors in cell (1). Their proactive behaviour will strengthen their (relative) position, not only in the recession period, but also in subsequent years. Brands in cell (3) are in the worst possible situation: they start weak, and their management makes the wrong decisions. They are prime candidates to be de-listed by retailers who are pushing their private labels in recessions – and many of them will. Their brand equity will decline, and many will not even survive the recession.

The brands in cell (4) have the opportunity of a lifetime to fight back. They start in an unfavourable position – their equity is low and, in normal times, it would take tremendous marketing investments to break through the competitive clutter. However, given that most brands cut back in recessions (and, hence, belong to cells (1) and (3), brands in cell (4) are able to increase their share of total market communication in the category dramatically by maintaining or – even better – increasing their marketing investments. But it is a risky strategy – if it is poorly executed, the anticipated increase in sales and profits will not materialise and the brand may be discontinued.

Conclusion

Just as slumps in the stock market offer great opportunities for courageous investors, slumps in the real economy offer great opportunities to courageous managers. All evidence indicates that a proactive strategy is associated with increased brand success and shareholder value. If you wait till the good times come back, you ignore the advice given by the legendary ice hockey player Wayne Gretzky: "I skate to where the puck is going to be, not to where it has been." Recessions are not for the faint-hearted but who said that fair weather makes great managers?

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