

# Maintaining Profitable Growth in Volatile Times

In an atmosphere charged with consumption and cost volatility, companies must give up overarching strategies and adopt granular, innovative and focused approach



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**V**olatility is the new normal in India. On the demand side, consumers, the life blood of growth, are increasingly unpredictable. With high food inflation, 150 million households are cutting back on several discretionary categories. Equally, with higher EMI payouts, many of the top 50 million households are postponing purchase or construction of a new home, upgradation of a car or a new kitchen durable.

On the supply side, commodity costs and interest rates are increasingly unpredictable. This volatility in both consumption and cost has led to unpredictability in business growth and margin. To respond to these changes, companies must shift from a 'growth forgives many things' approach (predicated on speed) to a 'targeted, margin-accretive' approach (predicated on flexibility). This approach must focus on three areas: shaping a resilient growth portfolio, crafting a margin-enabling pricing approach and strategically managing costs.

## **A RESILIENT GROWTH PORTFOLIO**

From a portfolio approach that is based on rapid expansion across (all) segments and geographies, companies must get granular, bet on growth that is resilient. There are three ways of looking at this growth.

► **Pockets of category resilience:** With volatility, behaviour changes in ways internally consistent to consumers — as they manage their lives and wallets — but often surprising to players — who have a siloed category view of consumption. For example, three behaviours are increasingly visible.

First, substitution. As consumers postpone the purchase of a big category — e.g., new flat or a bigger car — they 'indulge' themselves through higher spends on categories such as a holiday expensive fragrances or apparel. Second, cocooning. As consumers move to 'budget-based' discretionary spending, the battlefield moves into the home! Popcorn and home-delivery spends increase as a movie in the theatre is replaced by a film on DTH. Third, slower penetration growth as new consumers sampling categories slows down given high inflation. Companies must, therefore, understand how the role of their category is evolving.

► **Pockets of geographic resilience:** Different markets (cities and states) respond differently in tough times. This is a function of underlying growth drivers of the local economy. (Refer my last ET column, *Don't Bet Your Money on India, Bet on its States*, August 15, 2011, where we discussed four factors that are drivers of economic growth: female literacy, private capital, infrastructure and size of government). In a market that is volatile overall,



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and medium enterprises are likely to remain vibrant. A cement player, for example, may, therefore, need to focus on winning in this channel. And a food player might need to highlight the out-of-home channel for certain categories.

## **A MARGIN-ENABLING APPROACH**

From a mechanical cost-plus margin pricing approach, volatility requires a dynamic pricing approach that explicitly trades off margin and growth. Clearly, this is no longer a call taken by marketers or finance people but becomes a top table decision. Pricing, therefore, requires two critical trade offs, in addition to smart communication.

► **The tradeoff between volume and margin:** In volatile times, companies need to have a new discussion based on category behaviour and competitive intensity. The real question is whether it is worth trading off long-term volume for short-term profit. In certain categories, it may be easier to make the trade-off towards margin since consumers will come back once the dust settles. On the other hand, where there is fierce competition, it may be important to go for volume or risk losing the lifetime value of consumers. The longer-term cost

cannot apply the same one-size-fits-all pricing approach to all customers but tailor pricing to role and behaviour of each segment. Where category penetration is growing rapidly, for example, holding on to opening price points or currency price points for small packs is important even at the cost of margin. On the other hand, where core customers are critical to profitability, pricing for them must deliver disproportionate value keeping lifetime value as the metric. So, companies must make tradeoffs, changing the margin expectations from different slivers of the customer portfolio.

► **The need for smart pricing communication:** Finally, in a volatile market, price communication matters. For example, the rate of adoption of the same tariff offer for a telecom company, communicated in two different ways by SMS, varied by, up to 100%. Equally, how price changes are affected is critical. In certain categories, empirical evidence suggests that taking

these skills are no longer enough. Cost must be now assessed with an additional lens of risk. This increasingly demands three new skills. First, ensuring supply security by revisiting the business model to examine a further case for integration (both backward and forward). Second, smart substitution for the critical raw material, through a deep understanding of customer switch points and innovative design-to-cost. Third, a more dynamic and strategic approach to buying commodities. Again, like in pricing, procurement strategy is a top table agenda.

Managing volatility in India calls for a learning organisation. From a premium on speed, and the mindset of a land grab, businesses must become increasingly granular and innovative. This calls for flexibility, rigour and being extremely targeted in execution.

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