BRINGING FMCG BACK TO GROWTH

was the subject of the speech,
delivered by Mr. M.S. Banga,
Chairman, Hindustan Lever Limited,
at the Annual General Meeting,
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Bringing FMCG back to Growth

An organisation which successfully stands the test of time is one that transforms itself in line with changes in the environment. Hindustan Lever's continued success in India over the past 75 years is marked by conscious transformations, building on the past and reshaping for the future.

During the sixties we altered the holding structure to reflect the aspirations of Indian shareholders. In the seventies we diversified into non-FMCG businesses in line with government policy. In the eighties we developed a new business system to compete in the low price segment of laundry. The nineties saw the consolidation of Unilever group companies with HLL, as well as acquisitions.

As this millennium dawned, it was apparent that a new India was emerging very fast. We needed to revamp our portfolio and business enablers to remain competitive. In short, we needed yet another transformation. We have engaged in this exercise for the last few years and a new Hindustan Lever has indeed emerged. The benefits of this are already visible in growth. Indeed we are confident that we will deliver sustainable growth for the company in the coming months and years. Before I dwell upon the transformation, I will briefly touch upon the crisis of growth faced in recent years by the FMCG industry.

The Crisis of Declining Markets

Through the nineties, the FMCG markets grew at almost 15% per annum in value. Suddenly, in 2000, FMCG market growth stalled and then declined for the next four years. It is important to understand why this happened.

The rapid opening up of the economy resulted in many new avenues of expenditure for the consumer’s growing income. A sharp drop in interest rates from 18% to 8% led to explosive demand for consumer durables like white goods, two-wheelers and automobiles. After all, one could drive out of a car showroom in a Maruti 800 with a down payment of only Rs. 2000! The home ownership market grew exponentially as the average age of a home loan borrower dropped from 50 in 1999 to 30 in 2004. Mobile phone ownership and usage exploded due to its amazing lifestyle and convenience benefits as well as lower prices. Entertainment, Leisure and Travel sectors also boomed.

The lure of new avenues of expenditure in products and services led to consumers restricting their spends on FMCG. It is not that they bathed less often or brushed their teeth less often or indeed washed their clothes less often. But they did downtrade to lower priced substitutes from higher quality brands. For example, a consumer buying six tablets of Lux in a month went to buying three of Lux and three cheaper brands.

Or a consumer buying Surf Excel for her clothes mixed it with a cheaper powder. As a result of this shift in spending patterns, the FMCG market declined in value in the last four years creating a major challenge for growth.

The new Hindustan Lever: Focussed on FMCG

In 2000, 75% of our sales came from FMCG businesses. The rest came from several non-FMCG businesses which were not profitable, and did not offer prospects for long-term leadership. Besides, they were a drain on the core FMCG business, both in terms of resource and focus.

We decided to disengage from all non-FMCG or commodity businesses. In all, we have divested and discontinued 15 businesses including Animal Feeds, Speciality Chemicals, Nickel Catalyst, Adhesives, Thermometers, Seeds, Mushrooms etc. with sales of Rs.1,750 crores as in 1999. I would like to assure the shareholders that the company derived excellent value from these divestments.

Today we are a focussed FMCG company with our branded business accounting for over 90% of sales, consisting of 35 brands across 20 categories. These will be our main engines of growth, with higher levels of resource concentration, be it technology, people talent or media spend.

Building blocks of a strong Foods business

In Foods, we see enormous growth potential in leading the evolution of consumers to branded and processed foods. Over the last few years we have focussed on putting in place the building blocks of a strong Foods business. Historically our Foods business was fragmented and lacked scale. It was often commoditised with low margins. We recognised that changing food habits would require considerable investment, which the current business simply could not afford. Therefore we divested the non-value added parts like Vanaspati. We have consolidated our portfolio and improved the gross margins by over 13% through product mix and cost reduction. We have also cleared the supply chain of all old stock and geared up for fresh availability on shelf. Today, our Foods business has a healthy gross margin and a supply chain driven by freshness. The Foods business will now invest for growth through relevant innovation.

FMCG still offers enormous potential

As the largest FMCG player it was up to us to reverse the downtrading to realise its true growth potential. We could achieve this by raising the bar and becoming world class in what our brands offered and how we worked. Nothing less would do.

Penetration levels in several of our categories and consumption levels in all of our categories is low by any comparison. Across the world, we have seen a strong correlation between income levels and the size of FMCG markets. Over the next 10 years, per capita income in India is likely to touch China's current levels. At those levels, the FMCG market will be over Rs.100,000 crores from a current value of Rs.40,000 crores. This is an opportunity that we are well poised to seize.

Why we will win

Portfolio of Strong Brands

Our main challenge was to reverse the downtrading in our categories and re-establish the relevance of our brands in the mind of the consumer. In 2000, we had 110 brands, many undifferentiated and lacking scale. We chose to focus on 35 power brands covering all consumer appeal and price segments. We are already seeing the benefits. Six brands – Brooke Bond, Lifebuoy, Lux, Fair & Lovely, Rin and Wheel – have emerged as mega brands in the last five years, each with sales of more than Rs.500 crores.

Better Value

The first step was to ensure that we offered world class quality and real differentiation backed by technology to give us the advantage over low priced competition. We have invested over Rs.400 crores, or 5% of sales, in the last three years to upgrade our brands.

In several cases we reduced prices to make our brands more affordable. Better quality and more affordable prices have increased the value to the consumer.

We have also launched several low unit size and price packs for single use to make our brands more accessible to all income groups. For example, we were the first to introduce a branded toothpaste in a tube at Rs.5 and a branded quality shampoo in a bottle at Rs.5.

Bigger Role in Consumers' Lives

Perhaps the most significant change has been to move our brands beyond merely making functional claims to playing a bigger and deeper role in the lives of consumers. We had to move from selling a soap or a detergent to something far more important and central to the consumer's life. How often have we heard someone say, "A soap is a soap is a soap!" Or indeed, "All detergents clean clothes as well".

In the case of Lifebuoy, it was only when we associated it with the promise of health and protection against disease that it claimed a larger space in the consumer's mind. It moved from being a mere soap to a health essential. Today Lifebuoy, our oldest brand, has grown at over 15% for the last three years.

Similarly, in the laundry market, Surf Excel went well beyond the benefit of 'great clean' by saving two buckets of water with every wash. Imagine the importance of that benefit to consumers in cities, who often get running water for only a couple of hours a day. Surf Excel is one of our fastest growing brands today.

Both Lifebuoy and Surf Excel have succeeded because they are relevant to two key concerns of the Indian housewife: family health and the scarcity of water.

In addition to the growing consciousness of health, consumers today are looking for ways to look good and feel good so that they can get much more out of life. In short, consumers are seeking Vitality in their lives. Our portfolio of 35 power brands is uniquely positioned to offer nutrition, hygiene and personal care benefits and thereby deliver Vitality.

Technology, the Key Differentiator

Our brands and sound understanding of the local consumer are supported by a world class Research and Development capability. We have over 200 of the brightest scientists and technologists based in India.

Our recent reorganisation leverages the talent pool from across 16 global technology centres, of which four are in India. In all, we have over

4,000 high quality minds across Unilever working relentlessly to provide new benefits that make a real difference to our consumers.

Winning with Customers

Hindustan Lever has historically had a strong bond with its customers. We have strengthened this and reinvented the way we manage our distribution channels and our customers. The sales structure has been transformed to leverage scale and build expertise in servicing Modern Trade and Rural Markets. We have also delayered our sales force to improve our response times and service levels.

Our customers are serviced on continuous replenishment. This is possible because of IT connectivity across our extended supply chain of about 2,000 suppliers, 80 factories and 7,000 stockists. We have also combined backend processes into a common Shared Service infrastructure, which supports our units across the country. All these initiatives together have enhanced operational efficiencies, improved our service to our customers and have brought us closer to the marketplace.

Our Acorns: Investing in our Future

In our pursuit of growth, we have also begun to nurture some acorns for the future. These are both new businesses and new ways of engaging with consumers.

Our entry into Water Purifiers, through Pureit, shows great promise. Pureit delivers 100% protection against all water-borne diseases. It provides water which is as safe as boiled water, without needing electricity or continuous tap water supply. At 17 paise per litre, it is extremely affordable for the common man. We have launched it in Tamil Nadu and are fine-tuning all aspects of the business system before a phased national launch.

In urban India, Hindustan Lever Network (HLN) is our direct selling initiative selling a special range of products. It already reaches 1,400 towns with over 3 lakh consultants. Besides reach, HLN enables direct interaction with consumers and customises solutions for them to give them a complete brand experience.

Project Shakti, launched in 2001, complements our rural reach in small villages in partnership with underprivileged rural women from Self-Help Groups. It has been extended to 60,000 villages in 12 states, already touching 75 million people. By the end of the year, Shakti will cover 100 million people.

Underprivileged rural women need a sustainable source of income. Shakti is meeting this critical need, in most cases doubling the household incomes of the Shakti entrepreneurs' families. In addition, it is spreading health and hygiene awareness through the Shakti Vani programme, and providing access to livelihood-related information through the iShakti community portal. This path-breaking initiative combines the company's business interest with our ongoing commitment to the development of rural India.

Our People & Organisation

We have restructured the company, integrating eight Profit Centres into two Divisions – Home and Personal Care (HPC) and Foods. The result is a simpler and leaner organisation, less hierarchical with fewer levels and greater empowerment. This has eliminated complexity and speeded up decision making. Today the company is far more youthful in attitude and spirit. There is greater openness and transparency.

Our people have led this transformation. This has not been easy at times. In fact, it has involved a lot of pain. Not everything that was done worked first time. But we kept moving forward, learning from experience, determined to drive change and make it stick. We are all totally committed to our goals and will accept nothing less. There is a sense of confidence as the labour bears fruit, and a conviction that we will win.

The Transformation: Investment in the Future

To ensure that Hindustan Lever remains competitive in the long-term, we have made significant investments in product quality, pricing and marketing. As I mentioned earlier, the investment in product quality alone has been in excess of Rs. 400 crores, or 5% of our sales.

In addition there has been the cost of defending our market position. Recently an international competitor attacked our laundry business led by a price reduction of as much as 50%. We acted with speed and determination leveraging all our past experience in India and internationally. We have been able to fully protect our market leadership and share, albeit sacrificing short-term profit. We made this necessary trade-off as market share is the best means of sustaining future profit. Over time, our stronger market positions will surely lead to greater long-term profit.

Despite these significant investments to strengthen the long-term competitiveness and the costs of defending our strong market position, we still remain one of the most profitable companies in the country.

Conclusion

In recent years, the FMCG sector declined due to downtrading. Our transformation has resulted in a new HLL, which has successfully faced this challenge and reversed this trend. It has done so by substantially strengthening our brands and building capabilities. This has already begun to yield benefits and we are returning to growth. Volume growth is being followed by value growth, which in turn will bring profit growth.

India is one of the most exciting markets offering great potential. Over the next 10 years, the per capita income in India is likely to double. In FMCG, there is an opportunity to catalyse penetration, increase usage, and upgrade consumers. As a result, the FMCG market is expected to grow to over Rs.100,000 crores from its current base of Rs.40,000 crores.

We in the new Hindustan Lever see an exciting opportunity for growth. We have 35 powerful brands covering all segments, with leading market positions in most. Today, these are stronger and more relevant to the consumer than ever. Our people are energised by the scale of the opportunity and determined to seize it. The scale of our business and operations gives us the resources we need. We are very confident of delivering sustainable profitable growth.
