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THE ASIA INNOVATION SERIES

THE CHALLENGE: What's the right entry point for emerging markets: targeting customers at the bottom or the middle of the pyramid?

Should companies target investments at the bottom of the pyramid in emerging markets, where the number of potential buyers is huge and demand is growing? Or can companies capture more value by focusing on the rapidly expanding middle market, where customers are clamoring for new options in products and pricing?



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//// **IN THE 1900s** Willie Sutton catapulted into the public's imagination when he made off with more than \$2 million in a string of daring bank robberies. Urban legend has it that when asked why he robbed banks, he responded, "That's where the money is."

Innovators who follow the Willie Sutton model aren't robbers — they simply target the largest markets. In emerging markets, that can lead in one of two directions. One approach aims for the wealthiest customers who constitute a significant portion of a company's aggregate purchasing power. Today these customers can enjoy luxury brands, world-class restaurants, and high-end automobiles. The other is to aim for the so-called bottom of the pyramid that contains the new customers who beginning to gain purchasing power products and services.

Growth-seeking companies need to be careful about defaulting to Willie Sutton approaches. The wealthiest segments in

many markets are fairly well served, and fierce competition means sustainable competitive advantage is difficult to obtain. But succeeding in the bottom of the pyramid is challenging. How many ideas can be summarized in, "If we can just figure out a way to get \$1 from each Chinese, Indian, Indonesian, Brazilian, or Nigerian consumer?" Getting that \$1 is brutally hard. Turning that dollar into sustainable profits is harder yet given the inconsistent infrastructure in many markets.

So rather than focus on where the market is today, investors should instead look to where the market is going to be. The opportunity in emerging markets seems to be clearly to the middle class.

By some measures this market will explode over the next decade. An OECD study projected that spending by Asian middle class consumers will grow from \$4.9 trillion in 2009 to more than \$30 trillion in 2020. That latter figure would consti-

tute about 60% of global middle class spending, compared to 20% in 2009. This market segment features significant pent up demand, as consumers can't yet afford the solutions available to wealthy consumers but aspire to more than the hyper-affordable options with which they grew up.

Some companies are already/have started target this segment. In 2009, Godrej & Boyce launched ChotuKool, a \$70 refrigerator targeting the 85% of Indians who found existing refrigerators too expensive and power hungry. The portable, battery-powered refrigerator is a huge hit and Godrej now plans to extend the ChotuKool brand to washing machines and other appliances.

Reaching the massive middle class is not easy. Success starts by developing deep understanding of the unique demands. For instance, the medical device giant Medtronic is focusing on increasing the company's internal capabilities in emerging markets to design, test and scale new business models such the Healthy Heart for All initiative in India. To accelerate these efforts, Medtronic recently established a dedicated business model innovation department in its Singapore office, where the company also has access to Singapore's globalized and highly skilled workforce, and sophisticated financial markets.

The next key to success is thinking holistically about innovation. Compelling products and services are great, but success in the emerging middle market can require new pricing models, production methods, and marketing techniques. For example, if you visit a Chinese department store you will see young women who act as on-the-spot promoters for their employer's products. The so-called "promoter girls" might run

counter to Western sensibilities, but they are a key marketing for many companies in China.

Ask these promoters what they use to communicate with friends, and odds are they will mention Tencent's QQ instant messenger service. Haven't heard of Tencent? Tencent is one of the world's biggest Internet companies, producing about \$1 billion in revenue per quarter. The secret to Tencent's success isn't the company's product; it is its business model. Tencent's messenger service is free, but users pay a few Renminbi to deck out their avatar with accessories. Amalgamating these micropayments turned Tencent into a multi-billion dollar powerhouse.

That is just one example of success enabled by an innovative business model — new ways to create, capture, or deliver value. The right core product or service acts as "table stakes" in emerging markets; the business model provides the sizzle and sustainable competitive advantage.

Finally, companies need to energize their local operations. Reaching the emerging middle class requires that companies ask their office in emerging markets to be innovation hot spots that generate unique insight and design and deliver market-appropriate products.

The shift is easier said than done. It requires rethinking reporting relationships, talent management, rotational assignments, compensation, and more. Insights can only come from spending significant time in the marketplace. Executives must go beyond parachuting into a market and staying in five star hotels. They need to get out and experience life the way the customer experiences.

BRUCE BROWN

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Bruce Brown oversees the company's innovation program, its 8,700-person global R&D organization, and P&G's Corporate Innovation Fund and FutureWorks organization for creation of new business opportunities.



//// **AT PROCTER & GAMBLE**, we often find ourselves asking: How does a company know what is the right entry point for emerging markets? It's an interesting question, because there is no simple answer.

At Procter & Gamble, our growth strategy is to "touch and improve more consumers' lives, in more parts of the world... more completely."

Our growth strategy centers on three opportunities. We improve lives in more parts of the world by innovating and expanding geographically into new white spaces where we

have not been competing. We improve lives more completely by innovating to improve existing products, creating or entering adjacent categories, and driving regimen use that broadens our product portfolios. We can improve more consumers' lives by innovating and expanding vertically, up and down value tiers.

We currently serve 4.2 billion consumers with a goal to reach 5 billion by 2015. Limiting ourselves to only serving consumers in the "bottom" and even the "middle" tiers will keep us from achieving this goal. While these two groups remain a

critical part of our long-term growth strategy, we must also serve high-end consumers who are willing to purchase premium priced brands.

We determine our point of entry by first understanding where we have the “right to win.” This not only includes categories, but pricing and consumer tiers as well. Importantly, for us to enter a tier we have to be able to provide our consumers a winning value proposition versus all relevant competition. We achieve superiority and delight our consumers by following three key principles:

1. Defining the target consumer: We build relationships with our consumers to understand their needs, wants, current living environment and threshold for value.

2. Designing for the consumer: We design a product with the intention of delighting our consumer. This may result in expanding our portfolio into whitespaces where a product is not currently offered or creating a new-to-the-world innovation. This does not mean taking a high-end product and diluting it down to fill gaps for various regions or consumer tiers.

3. Executing for the consumer: After we design a product we must be able to effectively deliver it to them. This includes creating a manufacturing system to make the product, and developing a launch and marketing plan to sell it to the intended consumer.

These principles are easier to execute for the “middle” and “high” end consumer tiers, as well as the “bottom” tier if we have a relevant product offering. The consumers who have not yet been served are more challenging, as they require innovative thinking and unique product solutions.

For our biggest global categories we want to offer a portfolio of products that serves all consumer tiers by providing unmatched innovations at various price points. We see this approach come to life in our male grooming category in India with Gillette Guard, Mach 3, and Gillette Fusion.

Gillette Guard was developed as a “bottom” tier solution for men shaving in India. According to our research, nearly one billion men are shaving with double-edge razors because there was no better affordable alternative. So we took a fresh approach to every element of our innovation process, from consumer understanding to design to manufacturing. We cre-

ated a razor uniquely designed for these men while carefully managing cost.

Mach 3 is a “middle” tier line of razors that we expanded into the Indian market. This system offers price conscious consumers a comfortable shave at an affordable cost. It works off a three-blade shaving technology with anti-friction blades that gently glide over the face.

Gillette Fusion is a “high” tier brand created to help men reduce the discomfort they experienced during shaving. We designed a razor using advanced shaving technology that consisted of a 5-blade shaving surface. The blades were placed significantly closer together to help reduce pressure and we designed an enhanced precision trimmer to get help with additional spots like side burns.

In the U.S., we take a similar approach to reach all consumer tiers within our laundry category.

Ultra Era powder detergent was developed as a “bottom” tier detergent or for the value-conscious consumer, that provides powerful ingredients that help break down stains without all the extras. Our research shows that this consumer wants to provide her family with strong performance in the laundry category while living within a budget.

Gain detergent is a “middle” tier brand that targets consumers who desire good performing detergent, but most importantly, a unique scent experience. Our teams invested in research and development to expand the brand’s scent portfolio, so customers can enjoy fragrances such as Lavender, Island Fresh, Floral Fusion and Apple Mango Tango.

Tide Pods is a “premium” brand that will reach U.S. store shelves in 2012. This unique product offers consumers a three-chamber unit dose that provides the benefits of cleaning, stain fighting and brightening. But most importantly, convenience. Our research shows that only 68% of consumers are satisfied with the amount of time and effort the laundry process takes to get excellent results. Tide Pods provide a chemistry matrix for excellent results, while making laundry simpler and less time-consuming.

For us, innovation is a primary driver of long-term growth. It is essential that we continue to invest in innovation and develop products that will reach across categories and all consumer tiers.

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“MUCH HAS BEEN” said about the historic shift from the developed West toward the fast-growing middle class of the emerging markets, particularly China and India. Numerous companies turned their attention to Asia in the belief that the vast numbers of consumers and their rising spending power would translate into enormous market opportunities.

There are significant differences however, between the West and the East when it comes to realizing the potential opportunities afforded by the rising emerging markets middle class. Traditional Western market strategies — such as establishing a position and securing one’s place in the market — do not necessarily work where tens of millions of new customers enter every year, exhibiting little brand loyalty. Competition is ruthless. Exacerbated by the ready flow of funds from the West, competition exists even in markets that would be largely uncompetitive. In the Indian mobile market for example, there can be more than ten operators in a local market, all selling the same services at rock-bottom prices.

Anyone chasing the middle of the market is chasing fool’s gold. When it comes to middle class customers in Asia, there is no middle. There is no average preference, and there is no average brand that consumers either need or want.

Any company entering the middle of the market with an average offering will soon face competition from the top, or rapidly emerging competition from below, from good-enough products that leverage enormous scale advantages gained through catering to the lower economic classes.

The emerging markets middle class consumers often have two reference points. Their first reference group is the lower-income tier they or their generation may have emerged from very recently. But their aspirational reference group is the highly visible, wealthier upper class consumer who can afford to buy products and brands not merely to meet everyday basic needs, but to fulfill emotional motivations.

The result is an eclectic demand pattern in these emerging middle class markets. Consumers are savvy and discerning, empowered by the widespread availability of information. For some product categories, these consumers may welcome “good enough products” that serve their needs at low price points. These consumers expect increasingly higher standards, whether from local high quality manufacturers or Western brands at affordable prices. It is entirely likely that these

consumers will not trade up to middle of the road products, and instead will trade-off and make purchases in other categories that fulfill the wants, aspirations and desires that only strong brands or higher order value propositions can meet.

The company that enters the middle of the market with an average offering will find it extremely difficult to compete profitably over time. As consumer markets evolve rapidly in Asia, an organization that has been built for operational efficiencies and scale advantages in the middle of the market must morph into an organization that is able to successfully design, manufacture and market higher-end, more premium products. This is difficult for any firm. It is also extremely difficult to change brand perceptions built in the middle of the market, especially in the highly fragmented Asian markets. It would require huge investment, effort, and time to reposition an “average” or “good enough” brand. So companies have two choices. They can enter at the bottom of the market and compete for consumers based on a lower price value proposition. This will require realizing enormous operations efficiencies to be able to match relentless local competitors who are willing to accept razor thin margins in exchange for large volumes. Companies who choose this route need to innovate along an ever improving feature set and hope that consumers are willing to pay for improved functionalities.

The second strategy is to target the middle by positioning themselves at the higher end of the market and appealing to wants, aspirations and desires that only strong brands can provide. At this end of the market, companies must invest in innovation, marketing, branding and customer service. We believe this is the only viable position for most Western companies to capture a profitable share of the emerging middle class market in Asia.

This requires companies to understand the ecosystem that drives demand in the local context. It is vital to delve deep into the local and cultural context of purchase and consumption — consumers’ local realities and the complexities of their daily lives. We call this process the mapping of the ecosystem of demand. More than focusing on consumers’ needs or unmet needs, this includes gaining a holistic perspective of consumers’ wishes, desires, fantasies, goals and frustrations — uncovering the entire spectrum of potential demand opportunities and developing opportunistic strategies to tap into these.