Marketing & Sales Practice

Strike Up the Brands

Top-Performing Portfolios Require a Well-Orchestrated Management Approach

McKinsey&Company

Overview

Brand portfolios are growing at a breakneck pace, creating challenges across the value chain. Consumers are overwhelmed by the abundance of branded offerings. Retailers are pushing back to maintain room for their own private-label offerings. Manufacturers are frustrated by disappointing returns on their portfolio investments.

What's the answer? There is no single remedy, but we believe manufacturers can improve performance by taking a more proactive approach to managing their brand portfolios. A winning formula requires attention to three improvement levers:

- Restructuring the portfolio, not for the success of individual brands but for the portfolio as a whole
- Developing a stronger customer-versus-category perspective for the portfolio to align brands with consumer needs and to identify new growth opportunities
- Adopting a capital-allocation mind-set to highlight investment trade-offs among brands to optimize spending across the portfolio

These levers must be underpinned by an organizational structure that views portfolio management as a top priority. Such a commitment is critical because a successful portfolio transformation will be a long journey - spanning several years - that requires ongoing assessments of potential value creation versus risks across the portfolio. The impact of this approach, however, may be worth the wait: Experience suggests that an effective portfolio strategy can generate 5 to 10 percent increases in top-line growth and up to 15 percent profitability improvements.

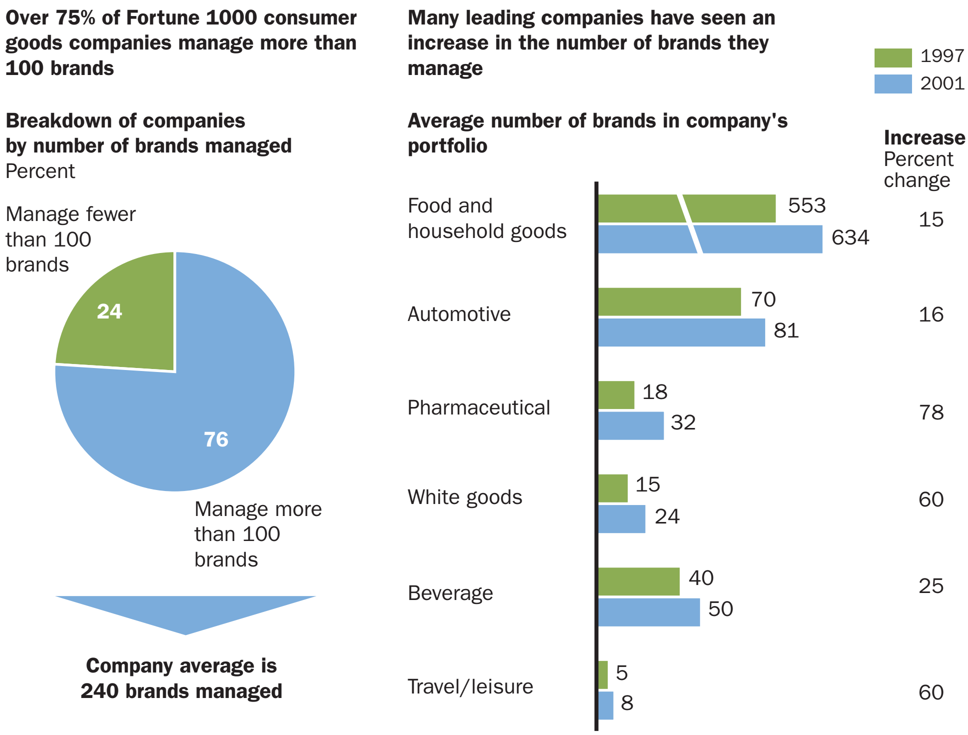
Brand portfolios are expanding at a staggering rate in many industries: pharmaceutical companies upped their average number of brands by 78 percent from 1997 to 2001; beverage manufacturers increased the size of their portfolios by 25 percent over the same period; companies in the food/household goods industry added 81 new labels to their portfolios, pushing the average number of brands beyond 630.

Indeed, more than three-quarters of the 25 consumer goods companies in the Fortune 1000 manage more than 100 brands, including sub-brands and line extensions *(see Exhibit 1)*.

We see four main drivers behind this surge. The first is the steady stream of M&A activity over the past decade. Mergers announced worldwide experienced an 11 percent compound annual growth rate (CAGR) from 1992 to 2000. Often in these deals, a targeted brand acquisition – Pepsi purchasing Gatorade, for instance – brings with it a legacy of additional brands – Rice-A-Roni, Cap'n Crunch, etc. While the performance of mergers is not wholly dependent on how well the brand portfolio is managed, research shows that historically 70 percent of mergers fail to create value.

Second, companies are using new brands and new products to drive growth across a range of increasingly mature sectors. The rush to capture the latest trend often leads to an abundance of brands, witness GM's 15 entries in the SUV category.

Exhibit 1 **A Proliferation of Brands**



Source: IRI InfoScan Reviews data; J.D. Power and Associates; Evaluate; McKinsey analysis

A third major force behind surging brand portfolios is the rapid increase of controlled or private-label brands across a range of categories. Most major apparel retailers have introduced private-label lines, and new store labels have become prominent in a range of other consumer categories such as hardware and tools.

The final driver is manufacturers' own hesitancy in pruning current brands to make way for new ones. Companies challenged to deliver both top-line and bottom-line growth view the consolidation or elimination of brands as too great an uncertainty. For these companies, the perceived risks of brand housekeeping outweigh the benefits of an easier-to-manage portfolio.

Complexity Along the Value Chain

The trend toward brand proliferation has made life increasingly complex for consumers, retailers, and manufacturers alike.

Consumers face a relentless barrage of products (the number of brands on grocery store shelves, for example, tripled in the 1990s from 15,000 to 45,000) along with the requisite pitches for them: the average American is exposed to 5,000 daily advertising messages, compared with 1,500 for the average citizen 40 years ago.

Many *retailers* have become increasingly discerning about the brands that fill their space for two primary reasons: they are seeking to keep their own cost structures in check (sourcing from fewer manufacturers, for instance, will increase their purchasing power and simplify their ability to manage categories), and they also want to carve out space for their own newly minted brands.

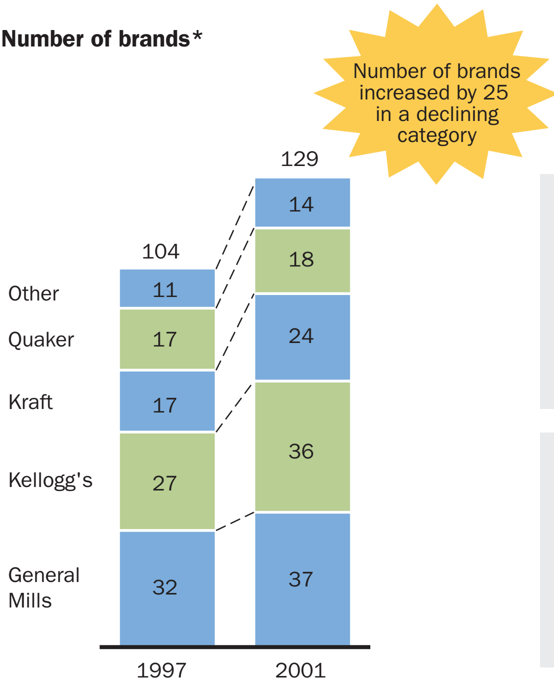
Manufacturers, forced to provide a more compelling value proposition to retailers, have responded not by pulling back, but by introducing a steady stream of new brands in an effort to spark growth. These companies are discovering, however, that new products do not necessarily translate into market share growth *(see Exhibit 2)*. In a crowded category, only the top performers tend to grow, while weaker performers lose ground as the landscape becomes littered with more and more offerings that are not meaningfully differentiated from one another.

Not only does a larger portfolio often fail to deliver expected returns but also the complexity of managing multiple brands imposes additional hidden costs across an organization. A growing portfolio affects the entire brand life cycle: from product development and sourcing (more R&D resources, increased raw material stocks) to manufacturing and distribution (more labor schedules to coordinate, higher shipping costs) to sales and channel management (increased training needs, a decrease in per-brand focus by the sales force) to marketing and promotions (more documentation, a need for greater coordination of marketing

Exhibit 2 **Fragmentation in Mature Categories Makes It Difficult for Expanding Portfolios to Perform**

Number of brands*

READY-TO-EAT CEREAL CATEGORY



Top 25% of volume

Number of brands 1997	Number of brands 2001	Per-brand market share, Percent 1997	Per-brand market share, Percent 2001
9	8	2.8	3.1

Bottom 75% of volume

Number of brands 1997	Number of brands 2001	Per-brand market share, Percent 1997	Per-brand market share, Percent 2001
95	121	0.8	0.6

* Brands with less than 0.5% national market share are not included
Source: IRI InfoScan Reviews data; company Web sites; McKinsey analysis

vendors and agencies). In addition, as new brands are added, marketing resources are often stretched, rendering some under-resourced brands vulnerable to competitors.

With these factors in play, why are manufacturers so hesitant to trim back their portfolios? Once they invest in a new brand or a line extension, companies have a legitimate concern that if they pull the brand, they won't get the shelf space – or the revenues – back. In practice, the economics of eliminating a brand often appear unattractive. Our experience indicates that the remaining brands in a portfolio may need to capture as much as 45 percent of the volume of a discontinued brand in order to break even. This is more than what most companies would consider "fair share" – the amount of volume they expect to recapture from the lost brand.

A Portfolio Prescription

With a more crowded playing field and less efficient underlying economics, manufacturers may find themselves hard-pressed to resolve these brand-related issues. Companies cannot stop launching or acquiring new brands, nor should they casually lop off a significant portion of their portfolio. But they can become smarter about managing their portfolios – as opposed to individual brands – in a way that can affect top- and bottom-line growth.

Tapping into these sources of value requires a more structured approach to portfolio management that comprises three main elements:

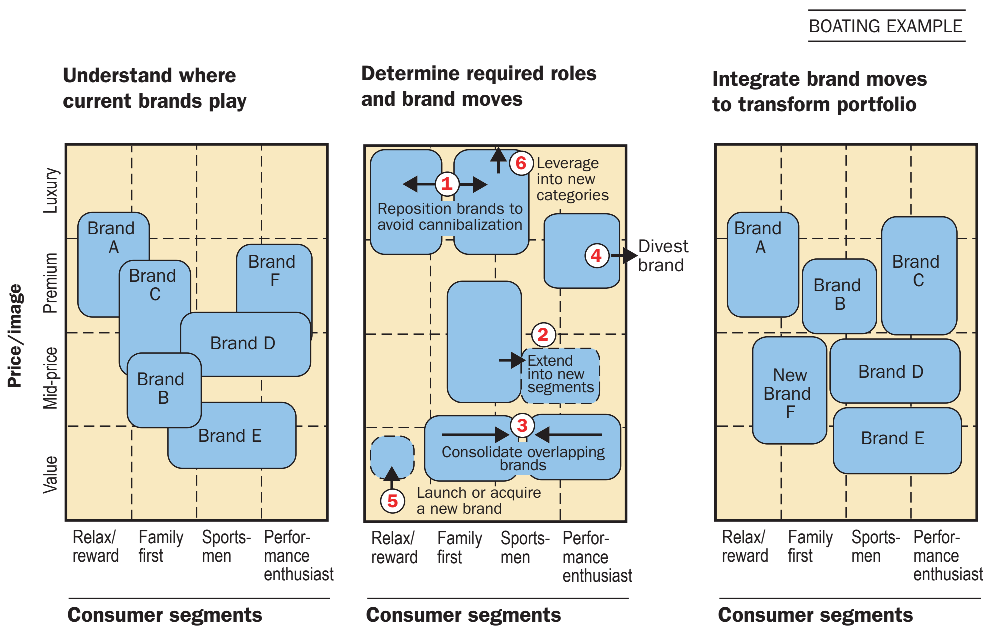
- Positioning your brands to deliver success for the overall portfolio;
- Developing a stronger customer-versus-category perspective across all the brands in the portfolio;
- Adopting a capital-allocation mind-set for brand investment.

Position brands to deliver portfolio success over individual brand success

A winning brand strategy does not necessarily beget a winning portfolio strategy. Brand teams are adept at optimizing performance of their individual brands – and often are supported by organizational structures and incentives that historically reward successful brands, even to the detriment of other brands in the portfolio. A more effective approach requires aligning the portfolio so that all brands, not just the flagship or core brands, can prosper in their designated roles. This focus on the greater good involves three activities *(see Exhibit 3)*:

1. Understand where current brands play. The key to understanding the current brand positioning lies in mapping how your brands – and those of your competitors – align with consumer needs (as opposed to customer demographics, which typically drive brand-alignment efforts).

Exhibit 3 **Three-Phase Approach to Aligning the Brand Portfolio**



2. Determine required roles and brand moves. Where do individual brands have the greatest opportunity to play in the future, and what will it take to evolve them into this space? Brand roles must be established based on consumer and strategic opportunities: Is Brand A better suited to be a prestige/luxury leader to address Segment 1, or a technology/design innovator to address Segment 2? Is Brand B fulfilling an important price-positioning role for the channel? In many situations, there are alternate paths forward for a brand, as historical positioning lacks the clarity necessary to deliver successfully against any specific consumer segment. In the absence of clear positioning, consumers often position the brand for themselves, resulting in a murky and diluted equity.

3. Integrate brand moves to transform the portfolio. With the proper targeting and roles defined for each brand, the portfolio can be transformed. This is a complex process, as there are any number of brand "moves" available to the portfolio manager: competing brands must be separated; redundant or ineffective brands must be eliminated or consolidated; and/or gaps must be filled by leveraging existing brands into a new category, launching new brands, or acquiring a brand from a third party. A critical issue to manage throughout this process is the domino effect – repositioning one brand often requires realignment across multiple brands in the portfolio. To account for this dynamic, alternate brand moves should be evaluated based on holistic portfolio scenarios, versus discrete brand events.

The resulting portfolio may look quite a bit different, depending on consumer dynamics and strength of brand assets. For example, the "one brand per segment" rule of thumb is not always the optimal portfolio strategy. Consumers may require multiple brands to meet their needs for variety or novelty. Additionally, it may be appropriate to eliminate well-positioned, sub-scale brands over time in favor of extending a powerful equity across categories. The objective is to minimize cannibalization, capture value more efficiently, and accelerate growth for the entire portfolio.

Develop a stronger customer perspective

In our experience, a company's view of a category in which it competes often is static and incompletely informed by the consumer's perspective. It's important to understand the broader context in which consumers make their choices – including the range of possible alternatives they consider. This means defining portfolios and brands not by category, but from the perspective of the benefits – both functional and emotional – that consumers derive from them (and those of competitors).

Does a consumer say, "I want to chew gum?" or does she say, "I want to freshen my breath?" The former is a narrow view of the category; the latter recognizes the consumer's real need, which provides a clearer view into the interactions of various brands (e.g., chewing gum versus mints versus breath strips). The categories in which you compete should include product "substitutes" that offer the same relative benefits to the consumer.

This broader view of the portfolio has the added benefit of helping you identify new opportunities as well as potential competitive threats. By looking beyond the "usual suspects," you can identify – and attack – opportunities by leveraging existing brands in new categories or by developing new brands to capture unmet customer needs.

While adopting a consumer view of the competitive space will enable the portfolio to tap into additional sources of margin, this stance must be balanced against your company's capabilities. Some portfolio opportunities may appear attractive through the consumer lens, but they may be economically unattractive based on their fit with existing manufacturing or distribution capabilities.

Adopt a capital-allocation mind-set

Too often, portfolio investment priorities stem from historical or institutional biases toward the best current brand or other near-term benefits. When managers face trade-offs among brands, funding usually goes to the plans that offer the most tangible near-term returns. Although this strategy may seem appropriate, it can destroy value over time (e.g., building plans based on coupons or other discount activity at the expense of longer-term equity building). A successful portfolio design must be supported by forward-looking investment decisions; therefore, a winning approach involves translating the mind-set of capital budgeting into one of budgeting brand investments across the portfolio.

This effort requires the same consistent consumer context in which all of the brands can be discussed – thus providing a common approach to evaluating investment across the entire portfolio.

Many companies have adopted ROI-related criteria instead of brand-specific measures such as share of voice or share of market. Resource allocation then can be based on a brand's ability to achieve the objectives of the portfolio based on common metrics. This, in turn, makes investments across the portfolio more transparent to all brand managers.

The most successful investment approaches, however, go beyond ROI metrics, which often simply reward the big, the tangible, and the immediate. Investments should be based on the strategic role of a brand and an assessment of its long-term potential. Many investments in branding pay back over different time horizons, based on where the brand is in its life cycle or what the investment is designed to achieve. The goal is to develop a consistent set of metrics for a particular type of goal (e.g., maintenance versus growth versus investment) and to measure all brands accordingly.

Making the Commitment

Defining effective portfolio management would be incomplete without a discussion of how companies should organize to succeed at it – and how long the transformation will take.

Employing a systematic approach across the company, with senior-level accountability, is the key to developing consistent and clearly defined objectives and criteria for all brands. Although there is no single organizational model to follow, we believe successful companies will build three key elements into their portfolio management structures.

1. The most important organizational requirement is a portfolio manager. A surprisingly large number of companies have no single individual who actively manages the brand portfolio for anything other than budget allocation decisions. The portfolio manager must have line responsibility and must be explicitly tasked with articulating a portfolio strategy. Depending on how dynamic the portfolio is, the CMO or VP of marketing often can take on the role of portfolio manager; a full-time position usually is not required. However, in our experience, this often requires a more proactive, top-down approach to brand planning than typically exists.

2. The portfolio manager must be given a mandate to identify the role of each brand within the portfolio and the implications for brand

performance and investment. Many times, the portfolio manager either is not sufficiently discriminating among brands in the portfolio ("All our brands are growth brands") or does not actually allow the brand role to play out in the P&L. This can result in the goals of brand managers becoming misaligned with the broader portfolio, leading to poor portfolio performance.

3. Management must clearly define the roles of both the portfolio manager and the individual brand managers. Both sides must be explicitly engaged in order for the process to be successful. Without brand involvement, the portfolio solution will not take hold within the organization. On the other hand, without adequate support and attention from the portfolio manager, the process will likely bog down in disputes among various brand managers.

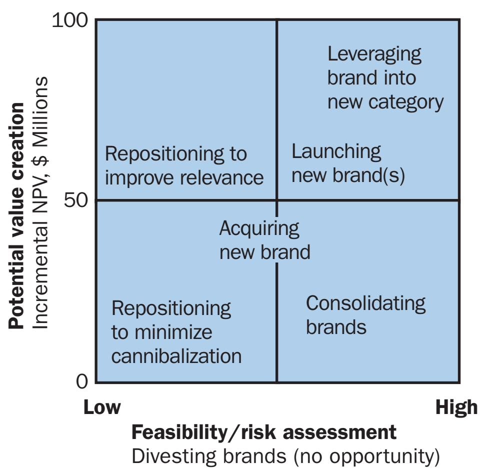
Strong commitment from top management also will ensure a smooth rollout of the portfolio transformation plan. A successful rollout requires prioritizing the right combination of brand moves, based on potential value creation and a feasibility/risk assessment *(see Exhibit 4)*. Some moves can be made more quickly than others, and each may have a different set of investment requirements. The plan must balance the need to transform the portfolio with constraints on investment, organizational capacity, and a consumer understanding of what you are doing.

When committing to a portfolio transformation, management needs to understand that the transition won't happen overnight. A full portfolio transformation is, at minimum, a 3-year journey. It also is not a one-time event. Brand portfolios are dynamic, thanks to customer trends, competitive activity, and brand life cycles, and as such require periodic monitoring and adjustments. A one-time realignment will result in an underperforming portfolio. Reexamining the portfolio too often, however, is an unnecessary outlay of time and money. Examination should take place periodically or when triggered by a major event, such as the launch of a major new product or an acquisition in which a significant number of new brands or potential new brands are added to a current category.

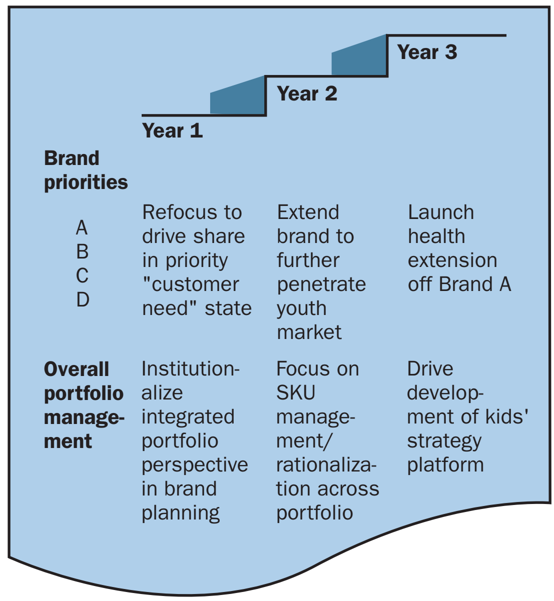
Exhibit 4 **Prioritizing the Transformation Plan**

FOOD EXAMPLE

Prioritizing portfolio moves
3-year plan



Portfolio transformation plan



A healthy and carefully integrated brand portfolio can be one of a company's strongest strategic advantages. In a time when the forces at work in many industries are leading to increasingly complex portfolios, companies need to focus on superior portfolio management in order to increase the returns they receive from the brand assets they have – and those they plan to develop.

– *Steve Carlotti is a Principal and Mary Ellen Coe is an Associate Principal in McKinsey's Marketing & Sales Practice.* *The authors wish to acknowledge Christopher Halsall, Katy Kendall Furton and Tamara Jurgenson for their contributions to this article.*

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