Issue 11

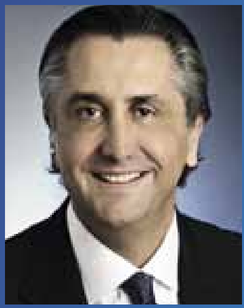
Consumer Currents

Issues driving consumer organizations

KPMG
cutting through complexity™

The trouble with food

Is price volatility undermining an entire industry?



For companies operating in consumer markets, complexity is now a fact of life. And so is dealing with change. The pace of upheaval, and the nature of the challenges being faced in the global marketplace, is evolving constantly. But the companies that will thrive in 2011 and beyond are putting processes in place, overhauling their systems and streamlining their structures to ensure they can be as responsive as the new business environment demands.

The themes forming the basis for discussion at the Global Summit of the Consumer Goods Forum in Barcelona give a strong indication of the issues clogging executives' inboxes. Operational excellence, changing consumer behavior, sustainability, the future of food and predicting the shape of tomorrow's markets are examples of the challenges that will decide which Retail, Food, Drink and Consumer Goods companies face the future with confidence. These are also topics we have tackled in this issue of *ConsumerCurrents*.

I know from discussions with companies over the past couple of years that realigning and optimizing supply chains has been a key priority. In many ways, one positive by-product of the global recession (and, to a lesser extent, the emergence of challenger brands from developing economies) was that it forced businesses to examine where their products came from, and where costs could be contained or reassigned. Sustainability and the use of technology also come into play here: as many companies with legacy systems are discovering, there is no point building a new supply chain with out-of-date reporting mechanisms while competitors react to consumer demand at lightning speed. But whether it's technology, green issues or globalization that's your key driver, it still requires courage and vision to make the investment required to overhaul your supply chain. Which is why, on page 18, we examine ways in which businesses can become more imaginative about supply chain change.

Companies with a stake in food will also be thinking about the future. Volatility of costs and worries about security of supply are making it hard to forecast accurately, and harder still to innovate in an uncertain market. On page 12, we take the temperature of the global food market and look at strategies that help mitigate seemingly constant price fluctuations, from hedging to innovative technology.

Consumer behavior drives all consumer markets companies. But at a time when consumer preferences are shifting dramatically, it takes an innovative approach to stay on top of the market. We have looked at two very different examples of forward thinking. On page 16, we visit IKEA's Chinese stores and discover how the company is forming partnerships targeting the country's growing middle class, shrugging off past disappointments in the market by investing in a strategy driven by research and best practice. On page 10, we look at the way supermarkets are diversifying beyond groceries and non-food staples, searching for growth in markets as diverse as financial services and used autos. It might sound frivolous for a retailer to hold weddings in its store (as has happened in the US), but in fact there is a sensible rationale behind diversification. As developed markets become increasingly saturated and food margins are squeezed, it makes sense to look further afield. Major retailers have brands to leverage and understand how to unlock value throughout the supply chain. But if they are to succeed in new markets, they will need to choose their partners carefully, and ensure back-end operations are correctly aligned, as we discover.

Finally, Tetra Pak CEO Dennis Jönsson gives us his take on consumer markets and innovation. You might imagine his is a company that changes very little. In fact, keeping ahead of competitors, and handling the vagaries of consumer demand, requires constant vigilance. Tetra Pak's take on the direction of consumer markets is valuable and illuminating, and chimes with my own observations. As delegates in Barcelona will no doubt discuss, we are living through one of the most volatile, but potentially rewarding, consumer environments in living memory. Capitalizing on opportunity means looking beyond business as usual.

Willy Kruh
Global Chairman, Consumer Markets
KPMG International

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Off the shelf

Will the mobile phone reinvent retail?

Forget m-commerce: geolocation uses mobile technology to drive customers in-store. But will retailers find the ROI?

Retailers are desperate to understand where their customers are. With location-based marketing, they can – to the nearest inch.

By using GPS, or 'geolocation', technology in phones and other mobile devices, consumer markets companies are targeting customers with location-based discounts and offers. The phenomenon is attracting some of the biggest names in retail, with huge consumer take-up. But ROI and privacy concerns must be overcome if it is to become a truly mainstream technology.

"Clients are telling us that location-based marketing could become the single biggest development in marketing of the last 10 years," says KPMG's **Jennie Cull**, a managing director in the US firm.

Geolocation is particularly exciting for retailers because it is used to drive footfall in bricks-and-mortar stores. Market leader Foursquare, with eight million users – largely in Japan and Europe – encourages members to 'check in' at new locations, at which point canny marketers can send them carefully selected offers. Know a Foursquare user is near your restaurant? Offer a discount if they stop by for lunch.

Early adopters include Domino's Pizza, which has encouraged customers to become 'mayor' of their local outlet by using it regularly. Starbucks identified a two-hour early afternoon period when it suffered a lull in visitors, and offered time-sensitive discounts. Start-up Placecast says its ShopAlerts – an opt-in app for shoppers – is delivering for retailers, with 79% of users more likely to visit a store as a result of a message.

Facebook Places, Facebook's location-based app, will open the technology to its 500 million users. There are still barriers to wider take-up, however. Almost two thirds of US smartphone owners do not use geolocation. And Andrew Stephen, Assistant Professor of Marketing at INSEAD Business School, says: "Privacy and intrusiveness is a big hurdle to jump before geolocation goes mainstream." It isn't hard to imagine consumers being fatigued by discount overload, or reluctant to share their movements.

ROI has also been slow to arrive, as making a direct link between notifications and purchases is tricky. Cull says: "Companies need to decide what their goal is when they start location-based marketing. Is it to get people into a store? To increase sales? To drive particular product lines?" Companies, she says, know mobile channels represent a huge opportunity. The key is unlocking it.

Nexttech

Artificial intelligence (AI)

When IBM supercomputer Watson trounced two human trivia champions on the game show *Jeopardy!* in February 2011, a new age of super-intelligent machines was foretold. Banks and armed forces would love to get their hands on an intuitive processor to make complex decisions in nanoseconds. But will AI also benefit retailers?

While Watson didn't constitute genuine AI (it recognizes natural language but is a long way from being spontaneously creative), Lluís Martínez-Ribes, Professor of Innovation in Retail at Spain's ESADE Business School, believes rapid advances in technology will allow retailers to get "much closer to the complexity of human life". That could mean analyzing and forecasting consumer behavior more accurately, anticipating economic values, brand preference and risk factors as soon as people walk into a store. Eventually, robot shop assistants could hold intelligent conversations with customers to find out what they're looking for, and offer the perfect product as they sip a complimentary coffee – taking the concept of a personal shopper to a whole new level.

China's taste for luxury

European brands dominate, but local companies have cause for hope in the world's fastest-growing luxury market

French, Italian and Hong Kong brands are finding favor with China's consumers – and the market is receptive to Chinese challenger brands, according to a KPMG survey.

The wide-ranging survey, entitled *Luxury experiences in China*, engaged more than 1,200 consumers, and found that French and Italian products grabbed the first and second positions respectively. French perfumes, fashion and bags were all leading their markets, with consumers preferring domestic alcohol brands thanks to the popularity of Chinese liquor.

The survey found that digital media was an important method of brand engagement, and that 57 luxury brands were now recognized as the marketplace grows more crowded. Consumers are now buying luxury goods to treat themselves, not simply as status symbols: more than half gave "to reward myself" as a reason for buying luxury items.

Nick Debnam, Partner and Asia Pacific Chairman, Consumer Markets, KPMG China, says: "China continues its march towards becoming the largest luxury market in the world. Year-on-year, as this market becomes more crowded, it is harder for luxury brands to enter this space. We also see rising brand recognition. Brands need to be innovative and explore new marketing avenues."

For more information, visit **kpmg.com/retail**

M&A starts motoring

Dealmakers are anticipating increased confidence in mergers and acquisitions in the months ahead – and prospects for consumer markets companies look particularly positive.

The annual Knowledge@Wharton/KPMG LLP survey of executives at US public companies and financial institutions found that 65% were more optimistic about the deal environment today than they were a year ago. The more stable economic environment, support from debt and equity markets and improved buyer confidence were cited as the three biggest factors.

Rob Coble, a partner with KPMG in the US's Transaction Services practice, says: "Multinationals have a record amount of cash on hand. Having done whatever they could to conserve cash in 2007-8, interest rates are now relatively low, capital is relatively available and they are more likely to spend."

Coble says the basic consumer goods sector is particularly likely to see M&A activity during the coming year, though luxury goods will remain behind the curve. Private equity, he adds, is also likely to return to prominence: "Distressed assets are generally out of the cycle, so there will be plenty of good opportunities for private equity firms."

Visit **kpmg.com** for further in-depth analysis, as well as other surveys and publications.

Trend **Spotting**

Growth isn't India's only story

Behind the headlines, fraud and mismanagement in Indian supply chains eats away at margins. **Deepankar Sanwalka**, Head of the Risk and Compliance Group, KPMG in India, explains how companies can fight back

A visit to any Indian retailer confirms the importance of the country to multinationals. India is undeniably a key growth market to numerous FMCG companies. Famous brands now jostle for shelf space with local favorites, a dramatic shift from just a decade ago. But those same shelves often tell a different story. We have worked with companies that have seen their products counterfeited to an astonishing level of detail, including packaging replicated from the original. Local soap has been represented as coming from a major Western brand. Food past its expiry date finds its way to local market stalls.

Fraud and mismanagement in the supply chain hurts every company operating or selling in India, even if its own products aren't involved. Owing to the nature of their business and subsequent rapid growth, consumer market companies focus on creating markets rather than creating controls. The fallout affects every part of business: from advertising agencies who fail to pass on rebates, to procurement processes where 7% of revenues are lost in kickbacks. Sustainability and third-party manufacturing risks like child labor, environment and health and safety issues lead to regulatory and reputation risks. It is a glaring fact that the grey market has roots deeply entrenched – counterfeiters have built their own supply chains to import goods from China, a sector now attracting interest from organized crime gangs.

"India has reached a tipping point with fraud and corruption"

India is well-versed in these matters, thanks to politically related graft scandals that have dominated the media. KPMG in India's 2011 *Survey on Bribery and Corruption* found 68% of the country's executives believe corruption is inhibiting GDP growth. More than half say India will attract less foreign investment than its peers if it does not reform, and almost all think corruption skews the corporate playing field and inhibits capital markets.

While to some this suggests business is powerless to fight a culture of corruption, I believe it shows India has reached a tipping point. We are unafraid to wash our dirty linen in public. Democratic processes and a free press are increasing scrutiny of power, and recent regional elections have rewarded strong governance. Now it is the turn of business to get its house in order.

Leaders could begin by leveraging business intelligence to analyze trends and transactions in detail. They should examine the culture of ethics: more businesses are introducing compliance offices and, in many cases, Chief Risk Officers. For those entering into joint ventures and other transactions, including outsourcing, robust due diligence and third party audits help understand who you are doing business with.

Liberalization of rules surrounding foreign direct investment in retail would clearly bring more professional processes and infrastructure to the sector, and remove many of the middlemen muddying the journey from manufacturer to consumer, each link adding to supply chain risk. But businesses need not, and should not, wait to act.

First person

"Consumers have adapted to a new way of living. They're not about to just go back"

Tetra Pak CEO **Dennis Jönsson** on China, India – and why consumer behavior has changed for good

Recession has changed the landscape for consumer markets companies, says Dennis Jönsson

Some companies are spun off from successful parents. Some ride the coat-tails of a growing market. But few are as closely associated with disruptive innovation as Tetra Pak. Since it first revolutionized the food industry 60 years ago with the invention of carton packaging, it has risen from homegrown Swedish company to multinational market leader with operations in more than 170 countries.

Today, the company founded by Ruben Rausing and still privately owned by his descendants is the market leader in aseptic packaging, a technology commonly associated with milk. Its products are used for everything from juices and still drinks to soup and wine, and it has diversified into providing processes and service solutions for manufacturers and retailers.

As a key supplier for almost every consumer markets multinational, Tetra Pak is uniquely placed to assess industry trends. And it must be feeling buoyant, having introduced a new bottle-shaped aseptic milk carton in May 2011 that could rival plastic packaging. At the company's global headquarters, a stone's throw from the shores of Lake Geneva in Pully, Switzerland, CEO Dennis Jönsson – a Swedish-born Tetra Pak veteran of 28 years who has held the top job since 2006 – told *ConsumerCurrents* why he won't rest in his pursuit of growth in even the most stubborn of markets.

How would you characterize consumer market confidence at the moment?

Looking back to 2008-9, we had a financial crisis, coupled with the melamine crisis in China. Through that period we weren't sure what we were seeing, and to some extent the results coming back from the market reflected that. China is our biggest market, and a hiccup there is felt across the company.

So, for us, 2010 was surprising. Most of our markets had a very positive and strong recovery, beyond what we had expected. The outlook today is much better. Like any company, we get a lot of feedback and we can see that consumer confidence is up in most places, more so in developing than developed markets.

Do you believe recession has changed consumer behavior for good?

During tough times, consumers adapted to a new way of living. Once you realize certain things are not as bad as you feared, you don't just go back to the way things were. A lot of consumers chose retail brands they might not otherwise have considered. Those trends are here to stay: we will see some correction, ▸

but consumers are finding some of those brands offer more than they expected. Today's retail brands are here to stay. And they are trying to position themselves in a completely different way to 20 years ago, catering to consumer need not just through value but by leading in many areas. We have to adjust and adapt. In the past, retailers were the customers of our customers. Today, in many cases, they are our direct customers.

Would it be fair to say you have had increased conversations about cost over the past couple of years?
It's nothing new for us. Over the past 15 years, we've seen a tremendous shift in the value chain that has put more and more power in the hands of retailers. That has translated into price pressure for us. We have been working with our own suppliers, collaborating and creating agreements with them, because the key to meeting the demands our customers put on us is price stability.

When financial crises happen, we are impacted less in the short term than other companies. We don't need to over-react to short-term problems. At the same time, our customers have been hit and because of that cost is a natural conversation. You adapt, you focus on productivity, your own supply chain and continuous improvement, as ways of meeting those demands.

Do you expect further volatility in food prices?
When you have the sort of surges of demand we have in countries like China, coupled with the events we have seen in North Africa, it only enhances the volatility we are already seeing across all commodities. We are trying to secure enough supply to meet surging demand.

How have recent events in Japan and the Middle East affected your supply chain?
We're lucky because we have such a strong supply chain, it hasn't affected us. We're not dependent in any major way on one particular site or country. We have focused on supply chains in our major growth markets. It proves that what we've been doing for many years is right.

Supply chains are part of the risk management analysis we do on a regular basis. We try to establish a supply chain footprint that enables us to shift supply whenever we need to. If you go back 20 years, we were largely dependent on Scandinavia because that was where the company had its origins. But as we saw more growth outside Europe, we have accelerated supply chain development.

The Indian market remains undeveloped, with only 20% of milk sold in packaging

"China changes all the time, and if you're not up to speed you risk being overrun by local competitors"

A lot of companies are questioning the globalization of supply chains. Do you believe it will continue to work for you?
I don't believe it would have been healthy in terms of risk or logistics to have continued to rely on any single geography. It also provides us with a natural hedging: costs and revenues are based as much as possible on local currencies.

Tell us about the aseptic bottle-shaped carton and the innovation process behind it
It's a completely new system and so far the feedback from customers, initially in Europe, is extremely positive. We believe it has the potential to make a big impact on the industry.

Around 10 years ago, we decided we had to structure our innovation processes, methodologies and tools much better. It's important to have a mix between internal and external inputs, including local markets and customers. We strongly believe in open innovation. No company can be good at everything, and that forced us to embrace partnerships with suppliers offering new technologies and competencies. Involving our customers at the start has been the biggest change.

What further innovations can there really be in the packaging market?
Packaging might all look the same to a consumer, but it can involve a lot of innovation. Our new packaging, aside from being innovative in terms of shape,

is so easy to open and pour from. Innovations like the Tetra Classic [Tetra Pak's original packaging system] don't come along every year. But we look at every type of innovation. Otherwise, you might focus too much energy on the 'big bang' rather than a process of continuous innovation.

How will you innovate in the US, a notoriously difficult market for you?
The US is different. We look at it in terms of other products as well as milk. When you have such a highly developed system of chiller cabinets, the impact of ambient milk products is lessened. In the US, 85-90% of milk is sold in gallons, so coming in with a liter product means looking at the market and its opportunities through a different lens. Our new packaging is a new way of gaining consumers, although it will remain a niche market. Milk has been a commodity in the US for a long time, so we are looking for companies to come in with new types of products, and we are having a lot of constructive discussions around that.

How do you view the Chinese market at the moment?
We started in China in the late 1970s, but didn't see dairy picking up until the turn of the century. Today, it is our biggest market so we have seen the benefit of hanging in there and not giving up because it doesn't work out immediately. We still see a lot to be done. Consumption of white milk is still only six liters per person per year, compared to 57 liters in Europe. That shows you the potential.

Milk is mainly consumed in larger cities. In third-tier cities, consumption is insignificant. Multinationals see China accelerating: we have seen a lot of new companies entering the market. The key is having a local base, understanding local consumers and adapting quickly. Things are changing all the time, and if you're not up to speed you risk being overrun by local competitors.

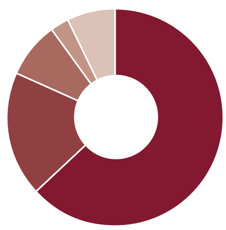
We are already working on local assembly, sourcing and R&D. But we are accelerating all these activities. The underlying problem is the demand for milk in China and the short supply.

Many economists believe consumer demand in China is slowing, and growth may have been overstated. Do you see any signs of that?
I don't think that applies to milk. We saw a little tiny bit of slowdown but that was due to the melamine crisis and it has picked up again. I believe consumers trust milk again. We have seen actions by the government to establish and enforce processes and rules. Some smaller companies have closed because they could not fulfil the requirements.

Do you worry about Chinese competitors?
We worry about any competitor. But our fiercest competitor is the plastics industry, and in some ways that is worse than a single company. If you look at China, the last time we counted there were 16 companies, all of whom want to play a global role as soon as they can. That is a huge number. We are on our toes, focused on continuing to provide our customers with standards of product and levels of service that are better than those offered by our competitors, be they in China or elsewhere.

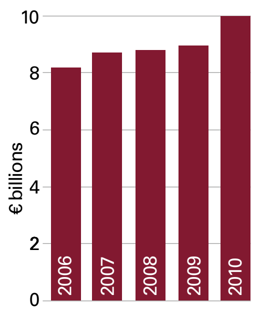
Do you think liberalization of retail in India is back on the cards?
Five years ago, we really thought it was happening. There's still a lot of willingness to see a more liberal retail environment, but it will happen very slowly. Despite being the biggest market for dairy products in the world, only about 20% of milk is packaged. Whether retail is opened up isn't the issue: it's about seeing a more developed retail environment, whether with local or international players. If you open things up, that will happen at a considerably faster pace.

More than milk
Products sold in Tetra Pak packaging, 2010
Source: Tetra Pak



- Liquid dairy 63.2%
- Juice & nectars 18.5%
- Still drinks 8.3%
- Wine & spirits 2.8%
- Other 7.2%

Packing them in
Tetra Pak net sales by year
Source: Tetra Pak



What can you do to stimulate growth in developed markets?
We've started looking at different areas of growth beyond our core business. We've identified processing and services and are ensuring we have the right resources in place. We've also identified new types of product such as Tetra Recart, a carton alternative to canned and glass food packaging. We are seeing a tremendous interest that is now being translated into strong demand, and retailers are really supporting it.

Do you foresee acquisitions being part of your future growth?
Being the size we are, I don't think you'll see major acquisitions but we continually look at companies that complement our business in core areas, have interesting technologies or specific competencies.

How has being a private company helped you during market upheaval?
The benefit of being private is that you can take a long-term approach without being overly concerned about short-term results. Our owners' support allows us to take risks, to make investments that might take time to deliver, such as the ones we made in China or Russia.

What has working at so many different levels of the company taught you?
To ask the right questions. I might not have all the answers, but being able to ask forces people to think twice about things. Having been involved in so many areas gives you a natural curiosity, and enough understanding about how things work to have a meaningful discussion.

I'm very intense, but informal. I believe in people and teams, having a good understanding of who you work with. No one person, no matter how great, can make a real difference without a strong team around them.

What's been your biggest mistake in business?
Underestimating others, be it individuals or competitors.

What's the best piece of advice you've been given?
"Never take work home" is one that comes to mind. It's something I've tried to live up to.

Diversification

Is there anything supermarkets can't sell?

From low-budget movies to mortgages, the biggest retailers have made diversity their watchword. But can they remain profitable and mitigate risk as they move away from their core competency?

When a young model is found murdered during Paris Fashion Week, a defiant investigative journalist travels the world to find the truth behind her death. Her mission brings her up against brutally ambitious designers and shadowy oligarchs. But will she become the next victim?

It sounds like the staple of a satellite channel's afternoon schedule. But *Paris Connections*, adapted from a Jackie Collins novel, is more than a straight-to-DVD movie. It is a recent brand extension from Tesco, which entered a joint venture with Amber Entertainment to create movies for sale in its British stores and online.

Supermarkets have always sold more than just groceries. Thirty years ago Japanese retailers tapped into the country's "economic miracle" by offering financial services. Today, their global successors are selling everything from real estate to pets – and the appetite for diversification is growing.

The UK and its largest retailer, Tesco, is especially innovative – fierce competition and a maturing market has meant innovation is a way of life. Supermarkets account for three-quarters of food sales by revenue. In 2010, NEMS Market Research found that only 5.9% of consumers had not bought non-food products from a supermarket in the previous six months. Faced with such saturation, they must try new formats, look abroad or move beyond core sectors.

Tesco's list of diversifications is dizzying. The company has a catalog sales business, owns a record company, and sells fuel, financial services and pharmacy goods. It plans to build homes, and has dabbled in used autos. Verdict Research says supermarkets own 42% of the homeware market, and are growing in music (41%), clothing (28%) and white goods (25%).

Tim Clifford, a KPMG retail partner in the UK firm, says three factors are driving diversification worldwide. First, bigger stores have meant more efficient supply chains. Secondly, CRM and customer data have exploded – Tesco has insights into the habits of 16 million loyalty card holders – with opportunities to monetize relationships. Finally, e-commerce and new business models mean serving customers beyond the store network.

Professor Josh Bamfield, Director of the Centre for Retail Research, says: "Because people use supermarkets routinely, there are fewer barriers to brand stretch [than other retailers]. The question is whether they have the expertise."

Clifford adds: "If you own a relationship with a customer and sell them things that are appropriate and relevant, there's no limit. But appropriate and relevant are the key words."

To date, financial services have been especially appropriate. Tesco Bank's 2010 profit of US$433m was up 5.6%, although UK supermarkets' financial services account for less than 5% of the loan market. The aim is not just profitability: keeping credit card transactions in-house cuts out interchange rates, and Tesco has spoken about the risk analysis benefits of understanding customers. The retailer has shown that customers who use its credit card spend 30% more in store, and bank customers are 25% less likely to visit a rival grocer. Walmart has taken the trend further, opening "money centers."

Nine happy couples take advantage of a supermarket chain's "recession-busting" 99-cent wedding offer in Los Angeles

Diversification involves risk. Challenges include managing supply chains very different from the traditional grocery chain, and recruiting and retaining talent in non-traditional areas such as telecoms and financial services. And, says Clifford, not all extensions are transferable: "Just because something works in the UK doesn't mean it will work in Japan. Outside the core grocery business, the differences can be huge."

"Some major retailers are perpetual innovation engines – it's hard for others to catch up"

You can also become too diversified. Investing in spin-off subsidiaries was a major factor in the undoing of Daiei, once Japan's largest supermarket, which required government intervention when its debt-to-equity ratio hit 9:1.

Clifford believes CEOs must think about the business model for new ventures, including the impact on the organization, and what kind of financial return would be attractive. They might also have to adjust management information and reporting, especially in a multi-channel environment. "Diversification has put the spotlight on joint ventures and alliances," he says. "Companies have to select the right partner and manage that relationship." Some retailers, he adds, enter joint ventures expecting to later buy out their partner or re-enter the market on their own if successful.

The trend is being repeated worldwide. Carrefour's new hypermarket format is based around a substantial non-food offering; Brazilian giant CBD has acquired a majority stake in electronics retailer Globex Utilidades; Walmart has entered the movie download market, and Poland's Biedronka is selling airline tickets.

Rivals will need new strategies – and a focus on cost – to keep pace. As former Tesco CEO Terry Leahy saw it, the retailer is a shark that must "keep moving – or it will sink." Clifford concludes: "Some major retailers have built their operations up over years and it's hard for others to catch up. Certain companies are perpetual innovation engines."

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Tim Clifford is a strategy partner in KPMG in the UK. Based in London, he is part of KPMG's retail sector team.

Hungry

Chinese workers harvest rice: emerging economies are driving demand

for certainty

Volatile food commodities are making long-term forecasting a guessing game. How will multinationals rethink their strategy?

Being CFO of a food multinational in 2011 is a complicated business. When input prices were in a downward spiral and global inflation was relatively stable, food companies could sit back and watch while many of their peers battled a permanently depressed market. Not any more.

A once-dormant market is suddenly highly volatile. The UN's Food and Agriculture Organization says its index of 55 common food commodities surged 25% in the year to January 2011. At the start of 2011 sugar and meat were at all-time highs. The record levels set in 2008 have been surpassed and overall prices – in real and nominal terms – now sit at, or close to, their highest in two decades.

The political upheaval of the Arab Spring, and instability in southern Africa, can be traced to the high cost of food. More trivially, but no less markedly, multinational food companies are trying to manage price pressures that were unimaginable years ago.

The International Monetary Fund calculates that between 1974 and 2005 real food prices, adjusted for inflation, fell by nearly 75% as improved technologies dampened costs. Compare this with 2007, when the UN food prices index rose by 40% in a year. Or with a wheat price which now can routinely rise or fall by 15% in two days. Over the 12 months to May 2011, corn prices rose 80% in the futures market; oats were up 70%, wheat 54% and soybeans 37%.

The problem is not necessarily price itself. Rising input costs are universal and will broadly be absorbed by consumers. And after a 30-year lull, only a reckless optimist would not have expected food commodities to rise at some point. The real quandary is increased volatility and the difficulties it causes for forecasting. How can you decide whether an acquisition or investment will deliver when the price of raw materials seems so intangible? How can consumer demand be accurately gauged when pricing levels in a decade's time could fall within a huge range of variables?

Unsurprisingly, tried and trusted strategies are increasingly unfit for purpose. And that means multinationals are thinking again about food.

Unstoppable rises

Commodity pricing is particularly troubling for multinationals because it leaves them relatively powerless, at the mercy of markets they cannot control and may not fully understand. "There are two things companies can do about food prices," says **Brian O'Neal**, Senior Risk Manager for KPMG in the US. "They can get better at supply management or they can take volatility out of the question by hedging. They can't influence the price themselves – no company is big enough to move the market for extended periods of time."

Hedging, once exotic, is becoming the *de facto* method for dealing with volatility (see page 15). But O'Neal says executives should examine why they are undertaking it: "Hedging by itself does not necessarily reduce costs. It isn't a price-saving technique. If you hedge all the time, you're still subject to the commodity cycle." It also won't turn a poorly performing company into a good one, he cautions: "If your job is converting maize to cereal, your profitability is tied to how well you perform that task. And hedging can't exist without reference to capital costs. If it costs more in charges and overheads to hedge than you think you can gain, you shouldn't do it." Hedging is an imperfect strategy, but it is becoming ubiquitous by default – if your rivals are insulated to ▸

some extent against price rises, your business ends up doubly exposed.

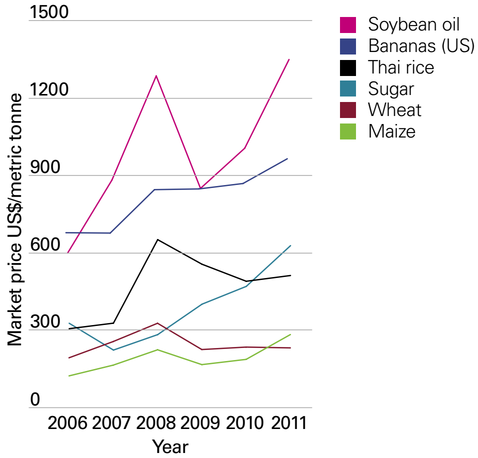
Almost every company is examining its supply chain, looking to optimize, broaden its supplier base where appropriate and ensure security of supply. Many are also radically rethinking pricing. Christopher Fraleigh, CEO of North American Retail and Foodservice at Sara Lee, told a forum in March: "What we've developed over the last five or six years is a much more sophisticated, value-based pricing approach. When commodities increase, we have a pretty good feel, based on where we are, where our competitors are, how much price we can take. We've been raising prices pretty steadily."

Fraleigh explained that Sara Lee's price rises encompass 20-50% of its portfolio at any one time: "When we talk about adjusting pricing, this past year it has largely been either an absolute increase in our list price, or a lot of times we will adjust our trade spending, When hot dogs or breakfast sandwiches go on sale, they may go on sale three times in a year instead of four times; or the depth of the discount may be a little bit less in price. That tends to have a little bit less 'sticker shock' from a consumer standpoint."

Food giant Kellogg's announced a change of tack in 2011, adopting a strategy of raising prices sharply after a year of heavy discounts and deep promotions that meant it was swallowing a rise in grain prices. "We lost some of our momentum in 2010," the company's CEO John Bryant told analysts. "We're trying to get that back."

Kraft says its 3.7% global price rise was enough to cover a 7% rise in input

The price isn't right
Volatility of common food commodities, 2007-11
Source: World Bank



costs in Q1 2011. But commodities create more losers than winners. Meat processors, reliant on corn and soybeans to fatten animals, are facing huge spikes. Luxury chocolate makers are seeing cocoa prices soar. Unlike Kellogg's, whose products are mostly staples, such discretionary purchases are on the chopping block in a weak consumer marketplace. As Bryant puts it: "There's not a lot of places for consumers to go for a cheaper food than, say, a bowl of cereal with milk at 50 cents a serving."

"Established food brands can benefit from the fact that, while their own food input prices are rising, so too are those of their competitors," says **Ian Starkey**, a Consumer Goods and Retail partner in KPMG's UK practice. "If the price differential between an own-label product and an upmarket alternative is reduced, consumers may be more likely to make the jump to the premium product. There is certainly a competitive upside of price inflation for such companies."

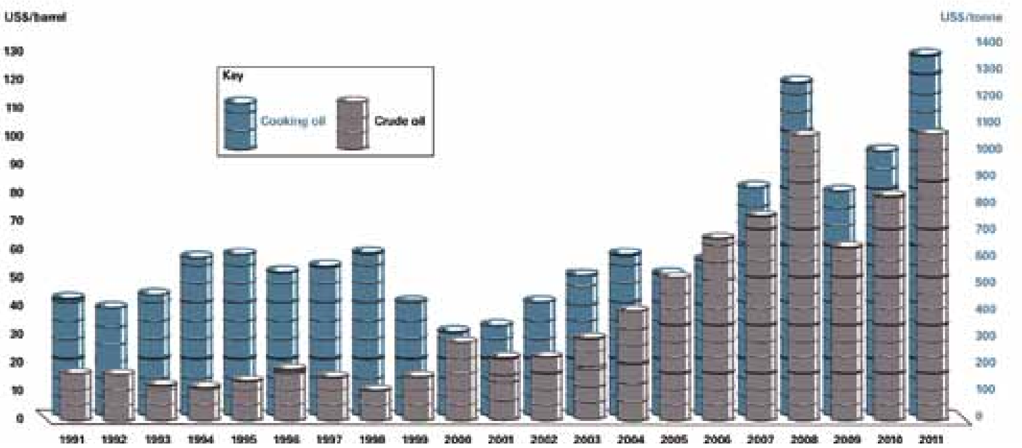
New rules

Clearly, the consumer landscape is changed radically by high cost pressures. And, while developed economies may be protected by regulation, there are dangers of a dark side. "The turbulence in the economy and pressures on corporations may mean a squeeze on the supply chain. It is conceivable that as suppliers try to retain business in a highly competitive market they start doing the wrong thing," says **Hitesh Patel**, a partner at KPMG's UK Forensic practice. "As the cost of food products goes up, unethical business practices such as price fixing cartels, bribery and corruption to secure lucrative contracts, substandard or counterfeit products being passed off as premium quality, or shortchanging in volume on delivery, to name a few, will become more likely. We are more likely to see problems like suppliers cheating on deliveries or even tampering with food. Bribery and corruption are also liable to rear their heads, although this is more likely in emerging markets than in developed economies."

Countries with well-developed supply chains cannot insulate themselves against volatility. Pricing strategy and hedging can help, but many multinationals now see geopolitical solutions as the long-term key to cooling markets.

Speculators are one target. Starbucks President Howard Schultz believes coffee

Liquid gold: why crude isn't the only fluctuating commodity
Crude oil price vs cooking oil price, 1991-2011
Source: World Bank



Crude oil is traditionally viewed as the nexus of commodity volatility. And yet when it comes to fluctuation, many food staples are every bit as unpredictable.

The price of cooking oil has changed radically in recent years. And applying a simplified measure of standard deviation (which looks at percentage price changes in markets from year to year) to measure volatility of crude oil and cooking oil over the past two decades yields some interesting results.

While crude oil has a standard deviation of 24.5, cooking oil is not far behind on 22.6. Little wonder commodities traders across the world are increasingly looking beyond more traditional markets in their quest for profits.

price hikes – costs have risen from 45 cents per pound a decade ago to around US$2.30 today – cannot be blamed on supply or demand issues. "Through financial speculation – hedge funds, index funds and other ways to manipulate the market – the commodities market is in a very unfortunate position. This has resulted in every coffee company having to pay extraordinarily high prices for coffee," he says.

Schultz calls for greater transparency in the commodities market and says that, at the very least, buyers should be identifiable. Anti-poverty campaigners have likened the commodities market to pre-crash sub-prime in regulatory terms.

But hedge funds cannot be responsible for every market dynamic, and the rational economics view states that aberrations will be corrected in the long term. The key questions are how and when. Rice offers one intriguing example. It fell 10% in the first two months of 2011 and is currently trading at around half its 2008 price, on the back of bumper crops among major growers such as Thailand, Vietnam and India. The UN claims that without falling rice prices, food riots in early 2011 would have been more widespread.

Rice production has been boosted by improved farming technology and the introduction of new hybrid seeds that can increase yields by as much as 20%. Genetically modified (GM) crops such as these, though politically explosive and far from universally proven, are one lifeline for food groups. More widespread acceptance of GM technology would offer more certain yields and predictable forward volumes across many different commodities.

"Although the debate on GM crops is often an emotive one, it is clearly one that needs to be had," says Starkey. "Increasing pressure on crop prices – in particular as resources are diverted by the growing demand for biofuels, such as the demand for corn to be used for ethanol production – is going to make that discussion more vital."

GM could also dampen some of the social concerns surrounding food security. Jeffrey Sachs, an economist at Columbia University and special adviser to UN Secretary General Ban Ki-Moon, has said: "We've entered a new global scenario with respect to food, hunger and conflict … an era where things are likely to get tougher, not easier, in terms of production. We're hitting boundaries that are very important to understand and very important to counteract."

Referring to the ideas of the 18th-century economist Thomas Malthus, who grimly predicted that one day the human population would grow to the point it could no longer feed itself, Sachs added: "We think we've beaten the Malthusian challenge for the last two centuries, but Malthus still has a spectre hanging over us. What we've not proved is that we can feed the entire planet on a sustainable basis for the long term."

For CFOs, feeding the planet is only one part of profitability. But it is increasingly difficult to separate food security, increasing demand from emerging economies and the power of market speculation, all of which contribute to volatility. To many analysts, the timing of agribusiness Glencore's record IPO is a sign that markets may have peaked. Shrewd commentators will take any glimpse of certainty they can get their hands on.

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To hedge or not to hedge?

How trading is helping multinationals get a handle on commodity costs

When Anheuser-Busch InBev, the world's largest brewer, announced its Q1 2011 results, most analysts focused on how US unemployment and monsoon conditions in Latin America had kept drinkers from reaching for their favorite tipple. For CFO Felipe Dutra, however, the results represented a small triumph for forward planning: by hedging its barley position throughout 2011, AB InBev had been insulated against hikes which saw prices double during one tumultuous six-week period in late 2010.

Hedging – effectively, betting on future prices by buying at a set position – is the mainstay of most commodities traders' working day. But now it is spreading from the trading floor to boardrooms such as Dutra's, as food and drink manufacturers decide the volatility of raw material prices has simply become too hot to handle.

The very largest multinationals have always included a hedging function in their finance department, often to buy oil for their transport fleets. Now, many more mid-tier businesses are considering it, including food service companies with wafer-thin margins and 'just-in-time' supply chains. Corn, soy beans and dairy products have joined coffee and sugar on the list of commodities being bought, generally on 18-month or two-year contracts to mitigate agricultural cycles.

Generally, consumer markets companies which hedge buy a commodity at an index price using a linear instrument. More complex derivatives instruments are off the menu for now. Even so, says KPMG's Brian O'Neal, it is advisable to bring in staff with trading experience to supplement the finance department: "Although it is a tool for management, hedging is very complex and requires a significant infrastructure, including controls, an IT capability to track forward positions and a derivative accounting function.

"Hedging is a strategic commitment which needs to be embraced by every level of the organization and the investor base. Failing to communicate that it is a tool, not a way of predicting the price, can be disastrous." It can be difficult to explain making a wrong call if shareholders don't understand the aim of hedging in the first place. It can be even harder to explain accidentally taking control of a futures contract, which O'Neal says has happened to at least one food company.

Back to the drawing board

IKEA is rethinking its China strategy with plans for ambitious partnerships. Will it succeed where other Western homeware retailers have failed?

At the two-storey IKEA in the prosperous Chaoyang area of Beijing, everything is super-sized. The Swedish furniture-maker's flagship Chinese store is its second largest in the world. Families, migrant workers and students flock to take advantage of hot dogs priced at a bargain 3RMB, 1RMB ice creams and refillable soft drinks in the spacious cafeteria.

In the display area, couples queue to pose for snapshots among the furniture and picnic on the showroom sofas. Others doze on the famously comfy beds.

The only part of the store where there's room to maneuver is the checkouts. Although IKEA attracts 23 million visitors to its eight Chinese stores each year (it first opened in Shanghai in 1998), it admits sales had until recently been disappointing. But unlike some Western competitors – which are largely pulling out of the country – IKEA (known in China as 'Yi Jia') seems determined to find new ways to tap into Chinese spending power.

In March 2011, newly formed Inter IKEA Centre Group (IICG) announced plans to partner with French supermarket chain Auchan, Chinese electronic chain Suning Appliance and cinema operator Jin Yi Film to develop three super-malls in first- and second-tier cities, thanks to a US$1.2bn investment over five years.

It is an ambitious move, and marks a totemic shift into the property market. IKEA will act as both landlord and anchor tenant for the malls, renting space to other brands targeting the Chinese middle class. IKEA's phenomenal ability to draw footfall will virtually guarantee a crowd, and the chain plans to double the number of stores it has in China by 2015.

The market, however, remains puzzling. China has experienced a huge home ownership boom over the past two decades, hitting 80% in urban areas from a standing start. Foreign home furnishing brands have piled into the country, but many failed to foresee problems ranging from pricing and government bureaucracy to rampant counterfeiting and high duty rates.

China's consumer mentality has also proved challenging. With cheap labor readily available, home-buyers are not attracted to 'do-it-yourself' decorating, while chains face stiff competition from local stalls and independent warehouses that sell a wide range of furnishings. Kingfisher, the British owner of the B&Q chain, closed stores in the country after two consecutive years of losses.

IKEA – the world's largest furniture retailer by sales – has fared better,

IKEA's stores attract interest from the aspiring middle class – but are they buying?

becoming a desirable brand for China's aspiring white-collar classes. Crucially, it has adapted its strategy to suit the market. One example is the company's self-assembly products, which have little resonance in China. IKEA now offers delivery and assembly services – attracting customers who might be put off by instruction manuals.

Another issue is pricing. Many shoppers come armed with cameras, measuring tapes and catalogs. Eager to own functional IKEA designs, but unable to afford them, they customize cheaper versions from local shops. IKEA has slashed its prices dramatically in response, with an almost two-digit annual percentage drop.

That has increased sales but led to brand issues, says Ben Cavender, Associate Principal for China Market Research Group. "IKEA came into the market fairly early, before any other brands, and it positioned its products relatively high," he says. "But the market has grown in terms of quality and

FACT FILE
Name IKEA Group
Founded 1943
Headquarters Helsingborg, Sweden
CEO Mikael Ohlsson
Employees 127, 000
Key markets Germany, US, France, UK, Italy

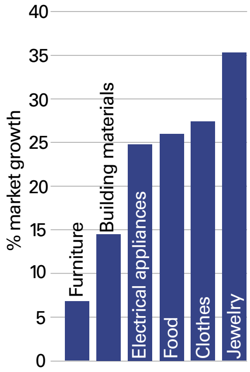
design expectations, so it has run into a real brand identity problem. Either it is going to have to go mass-market and compete better on cost or it's going to have to find a way to move upmarket."

Despite this, IKEA has the distinct advantage of being a private company, giving it the space for a 'wait and see' approach to a difficult market and allowing a more phased expansion than its competitors.

"It takes a long time to build relations in China, but once you do you can capitalize a lot on them,' says **Per Gustafsson**, a KPMG retail partner in the Swedish firm. 'IKEA does not have to consider shareholder value in the short run. It can build the business in the long term, rather than satisfy the stock market every month."

At a time when the Chinese government is encouraging an economy driven by domestic consumption, rather than exports, "the timing of its expansion might be excellent," he adds, although many fear inflation could dampen growth.

LAGGING BEHIND?
Growth rates of key consumer-facing markets in China, 2010
Source: National Development and Reform Commission



China has a haphazard approach to mall development, with frequent poor management and little attention to planning or tenant-matching. At the extreme end of the market, some malls offer pirated items on one floor and upmarket brands on another, while layouts can be chaotic and unappealing. IKEA can now control the way its brand is presented and managed.

Paul French, Director of Shanghai-based retail consultancy Access Asia, believes IKEA is "creating the retail park concept which hasn't developed in China as it has in Europe," following the lead of Tesco's Lifespace shopping centre, which opened in early 2010 in Qingdao. Tesco is the anchor tenant and developer, renting retail space to specialty retailers, restaurants and entertainment concepts.

Fifty thousand people alone visited on the opening weekend, and there are plans for 23 similar developments. But Tesco, like IKEA, is still chasing the holy grail of Chinese retail – turning browsers into buyers.

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Supply chains used to be simple – but globalization has changed the rules for good

The four daunting challenges facing your supply chain...

...and how to overcome them

How harnessing technology, predicting consumer demand, embracing sustainability and understanding risk can help your business face an uncertain future with renewed confidence

When Gavin Chappell, Supply Chain Director of Walmart-owned UK supermarket Asda, tried to explain the pressures he faces in his job, he cited former US Defense Secretary Donald Rumsfeld's famous remark about known knowns, known unknowns and unknown unknowns.

The known unknowns, Chappell suggested, included the retail climate and the performance of individual promotions. The unknown unknowns in retail supply chains were troubling: true vendor production capacities and overall stability. The other unknown unknown he could have identified was the likelihood of a natural disaster like the Japanese tsunami. Chappell also said forecasting, traditionally a known known, was in danger of becoming a known unknown: "Forecasts are getting worse, not better. And they will continue to get worse."

To illustrate how unpredictable consumer demand had become, Chappell revealed that in April 2011, soft drink sales at one Asda store had been twice as high as a store only 10 miles away.

As the abundance of knowns and unknowns suggests, these are troubled times for supply chains. The uncertainty is compounded by intense change and a growing sense that existing models aren't up to the job, particularly in retail. A 2011 report by KPMG, *Supply Chain Complexity: Managing Constant Change*, interviewed leading supply chain directors. It concluded that many supply chains were incapable of keeping pace with change.

> **"You have to accept that risk avoidance is a cost – whose cost is an emotive debate"**

Andrew Underwood, KPMG's Head of the UK Supply Chain practice and a partner in the UK firm, says: "The developments in the global economy, the need to become aware of risk, the drive for sustainability and the requirement to deliver what the customer wants on the shelf all mean retailers need to look further down their supply chain and make sure they understand it all properly."

Underwood says basic priorities have changed. "Many directors of retail supply chains have been focused only on cost and getting the chain as lean as possible, but it can't be so lean you don't have flexibility when something goes wrong."

Sahir Anand, who analyzes technology and process management in retail for Aberdeen Group, says: "The traditional supply chain needs internal and external transformation and overhaul."

The best-performing retailers are already finalizing plans to transform their supply chains over the next five years so they are aligned to economic reality, can manage escalating cost pressures and are flexible enough to meet increasingly unpredictable consumer demand. But whether your company has begun the transformation process or not, there are four key considerations you should factor into your thinking. ▸

1 Risk is almost certainly more complex than you think

"You have to accept that risk avoidance is a cost – whose cost across the partners within the supply chain is an emotive debate," says Underwood. Spreading your demand may mean you don't enjoy all the benefits of volume purchasing. The good news is that boardroom appetite for risk is changing: leaders are coming to accept they need a risk response program."

Anand says retailers must gauge risk more effectively: "An ever-expanding network of suppliers, inflationary pressures and low-cost global sourcing requirements have all led to increased supply chain risk. Retailers and suppliers find it difficult to predict risks, but they need to model them."

By modeling risk, retailers can clarify some of the unknown unknowns. The tsunamis of 2004 and 2011 showed how global and elaborate retail supply chains had become. In some cases, companies believed their suppliers wouldn't be disrupted, only to discover the real origin of their products lay somewhere else: the company they had been dealing with was just a link in a chain.

Cost management is also a key part of risk. Aberdeen Group research suggests that one in three retailers is afflicted by increasing supply chain volatility. And this is driving up costs. "Supply chain volatility is due to several factors, such as increasing lead times, too much (or too little) pipeline inventory, cross-channel demand growth, manufacturing delays, quality non-compliance and other sourcing inconsistencies such as sourcing shifts," says Anand.

2 Sustainability will only become more important

The retail supply chain's carbon footprint is constantly being scrutinized. The issues are not always as simple as the headlines suggest. It might sound environmentally absurd to fly roses to the UK from Kenya when so many are grown in the Netherlands. Yet retailer J Sainsbury's eco-audit found that the carbon footprint for Kenyan roses was 4.5 times lower than for Dutch roses. The yield of roses in Kenya was twice as high, and the packaging they were transported in was more robust, reducing waste.

Many retailers have acted decisively, prompted by the realization that there is a win-win here: they can improve their image and reduce costs.

By introducing a responsible sourcing and procurement plan which includes every stage of the retail supply chain – from sourcing to waste management and end-of-life recycling programs – retailers can justifiably position themselves as green and provide detailed consumer information to back up their claims.

Technology can help here. There is an array of enabling technologies which can automate business processes, integrate cross-functional process components and effectively identify, quantify, track and report key sustainability drivers, actions and outcomes. This effectively retrofits efficiency into retailers' assets, optimizing the performance of products.

But sometimes the best ideas are the simplest, and come with a bolted-on business case: Best Buy has been building the ability to handle end-of-life white goods in its US stores for several years. It has constructed an efficient, well-optimized system that can make the low-margin business of reusing, refurbishing or recycling electronic items pay off. In 2011, it unveiled a Buy Back program that pays consumers for obsolete products, and doesn't send them to landfill. The result: enhanced green credentials and the chance to resell items to cash-strapped consumers (opening a whole new segment). And, of course, customers visiting Best Buy to dump old products are far more likely to look for a replacement in store…

3 Cutting costs may mean investing

In their continual quest to slash costs, retailers have turned to two predictable solutions: outsourcing and technology. Outsourcing – either to 3PL companies who manage everything beyond transport or lead logistics providers

"Many people have focused only on cost and getting the chain as lean as possible. But it can't be so lean you don't have flexibility"

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Companies are considering new, more responsive relationships with suppliers

(4PLs) who integrate every company in the supply chain – has tempted many. Underwood says: "There's always a risk if you outsource, but there is a cost/benefit rationale and there are good 3/4PLs out there whose data can be checked."

Sometimes, technology can make a basic difference. Underwood says: "There are opportunities for retailers to leverage technology to a greater degree. They know the technology is there, but until recently it's just not been affordable enough to put in place." The food industry has world-class expertise in tracing and tracking produce. Yet Aberdeen's research suggests that one in four of the best-performing retailers cannot easily see, across the enterprise, how much stock they are holding and where that stock is.

Too many retailers were content to update their technology piecemeal. Not any more. Many are consolidating legacy supply chain technology across geographies, removing the ongoing cost of ownership and the difficulty of integrating with more up-to-date software, which handles e-procurement and visibility management, for example. Of course, this comes at a cost, with investment increasing in business intelligence technology for supply chain reporting and performance management, collaborative forecasting, planning replenishment and supplier scorecards.

Three of the world's biggest FMCG companies – Kraft, Procter & Gamble and Unilever – have turned to demand sensing products which use pattern recognition to analyze data and help them get a better steer on forecasting. Unilever expects to reduce forecast error by 25%: the type of result that suggests major software investments could pay off.

4 There is no short cut to gauging consumer demand

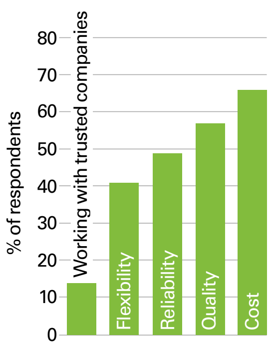
Deciding what consumers will want, when and why has never been more difficult. Underwood says: "Since the turn of the century, consumer demand has been increasingly volatile. The globalized marketplace and the rapid adoption of the internet has created new demands on companies and their supply chains. New distribution models and increased competition from online rivals have forced retailers to become more responsive to the needs of their customers and seek new levels of flexibility in supply chains."

There is no easy fix here, despite the advances technology like demand sensing offers. Anand says retailers must "intensively map" how they plan to meet demand and take an integrated view of data from right across the supply chain.

Retailers are looking to increase flexibility by running distribution centers seven days a week, exploring new transport options, requiring an order placed one day to be fulfilled the next, and asking suppliers to manufacture for agility, placing less emphasis on capacity utilization and more on lean, short runs.

Compared to other industries in the KPMG survey, retail performed relatively weakly when it came to managing inventory and working capital in its supply chain. Some retailers hope to make dramatic cost gains by having suppliers hold stocks further down the supply chain or implementing vendor-managed inventory, where a supplier guarantees to hold a certain level of stock.

Links in the chain
The most important attributes of a supply chain, according to global manufacturers
Source: KPMG International



The only way to build supply chains that can withstand volatility is, Underwood suggests, to develop collaborative processes and networks with other companies in the supply chain, or turn to logistics providers who can supplement your network. The KPMG survey suggested retailers have some catching up to do – the industry is poor at information-sharing and collaboration.

The scale and volume of challenges facing the retail supply chain director seems head-spinning. But Underwood believes they should find boards receptive to their problems: "There is now an appetite for their plans. If there isn't, they need to make sure their case is heard." Only then will unknown unknowns be matters for the military, not retailers.

The virtual route to happy customers

Airlines are an easy target for complaints – but the internet gives them a cost-effective way to change perceptions

Even in an industry where expecting the worst is a pre-requisite for operational efficiency, February 14, 2007 was awkward for JetBlue Airways. In what became known as the Valentine's Day Massacre, an ice storm in the eastern US grounded almost 1,200 flights and stranded tens of thousands of the low-cost carrier's passengers.

The three-day snafu could have been disastrous for JetBlue's bottom line. Yet by the third quarter of 2007, JetBlue's revenues were up 22%, defying analyst expectations. In Q1 2011, with much of the industry in the doldrums, the company remained profitable.

While operational adjustments and executive reshuffles have been credited with avoiding a repeat of 2007, JetBlue's untarnished reputation is also down to the way it has used the internet, and social media in particular. Founder and then CEO David Neeleman took to YouTube within hours of the ice storm to issue a straight-to-camera apology. An email to ticketholders has become a case study in corporate apologies. The result was no significant downturn in bookings.

JetBlue doesn't just use social media for damage limitation. It was one of the first major brands to join Twitter, and now has more than 1.6 million followers. It uses the service to directly interact with customers. Morgan Johnson, JetBlue's Manager of Corporate Communications, says: "When travellers have more knowledge, it helps them keep calm. It can change the dynamics in the airport, and that makes all our lives a lot easier." On a separate Twitter feed, it offers last-minute deals to fill empty seats: a form of Web 2.0 inventory management.

Airlines' customer service is helping them reduce attrition and cut costs, and others could learn from their experiences. A study by Genesys concluded that airlines lose around US$650m annually in avoidable churn through poor customer service. Consumer markets companies lose almost twice as much.

Airlines have learned that customers are happy to blog or share positive experiences – and they're taking the fight to them via social media. Delta Airlines monitors Twitter and often steps in when passengers tweet their dissatisfaction. Malaysia Airlines lets passengers book through Facebook and move seats to be near their friends. KLM's 'Surprise' campaign saw the airline present travellers waiting to board their flights with the perfect small gift, having researched their interests using social media. The result of these 'random acts of kindness': one million views of KLM's official Twitter feed in a month.

"If it's made easy for customers to have issues resolved online, they'd rather do that than spend 10 minutes on an automated phone service," says **Tom Skoog**, a KPMG retail services partner in the US firm. "It also enables companies to serve customers more holistically – anybody from the CEO down can answer." But he cautions that clear ownership is vital: the web is often seen as a marketing concern, but customer service is an operational issue.

Web-based initiatives needn't be expensive: at the same time as being lauded online, JetBlue was quietly shedding customer service costs. It now allows reservation agents to work from home, eliminating call centers. Neeleman, who is now CEO of Azul Brazilian Airlines, even served as a flight attendant – though, like social media engagement, that had more to do with being seen to care than scrimping on cabin crew.

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Insights

KPMG member firms provide a wide range of studies, analyses and insights for the Retail and Food, Drink and Consumer Goods (FDCG) industries. For more information, please visit **www.kpmg.com/retail** or **www.kpmg.com/FDCG.**

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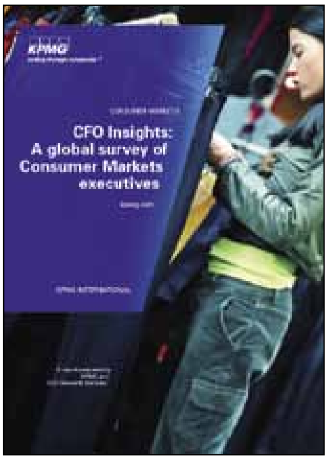

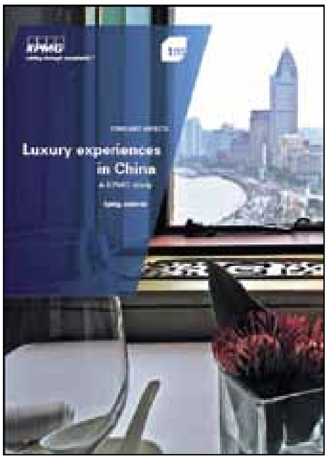

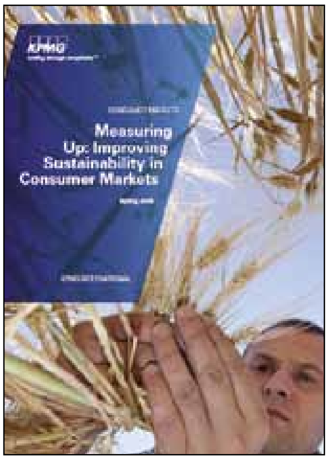

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Luxury experiences in China
This survey of Chinese consumers highlights the consumption trends and key drivers for luxury goods in China. The report includes 10 case studies of well-known luxury brands in China.

Measuring Up: Improving Sustainability in Consumer Markets
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