Can retailers and manufacturers ever cooperate in more than operational ways - in ways which actually help the consumer goods industry overcome its most fundamental challenges? Ten years after the founding of the ECR movement, it is becoming evident that while the core theory of ECR was spot on, there is still an awful lot more that could be done.

The original argument for ECR was that increased cooperation between manufacturers and retailers in areas such as supply chain management and category management would unleash a double string of benefits. Lower costs would protect margins, and the sharing of insights and the sharper of focus of category management would trigger increased demand. Together, such initiatives would lead to faster growth, at less cost.

As it turns out, many gains have been made - especially on the cost savings front. But growth has proved more elusive. Counter-trends such as the accelerated rise of discounters and the overcapacity that still plagues many categories mean that competition has intensified, leading to price deflation in many European markets and a declining overall 'share of purse'. In several large European countries there' s been serious deflation in grocery prices over the last ten years.

Overall a lack of differentiation and innovation by both retailers and manufacturers is encouraging consumers to become more promiscuous and eroding brand loyalty. And price competition between manufacturer and manufacturer, and between retailer and retailer, is intensifying - encouraging and educating consumers to look for even more discounts and promotions. The net result is that efficiency gains made via ECR initiatives

Raising the game to a new level

MILAN REPORT

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ECR benefits are often competed away at the retail level. How can manufacturers and retailers realise the benefits? Collaborative differentiation may be answer

are being competed out and passed on to the consumer (Exhibit 1).

So, as well as reducing costs, we need to find ways to stimulate growth: to generate genuine consumer enthusiasm.

Yet, traditional - even 'traditional ECR' - strategies are of little help to improve this situation. We need some fresh thinking.

Currently it's difficult for retailers to differentiate themselves using manufacturers' 'A' brands (except on price) and private label is the only way for them to differentiate in the product arena. If we continue to do business in this way, the results will be ever more retail focus on price and own label, increasing commoditisation of categories, declining R&D leading to less real innovation and therefore reduced consumer value. This, in turn, will encourage consumers to shop even more on the basis of price, thereby increasing the doom loop's momentum.

So what is the answer? One way forward is via *Collaborative Differentiation.*

Collaborative Differentiation is based on both consumer and shopper segmentation: it happens when a retailer and manufacturer work together to deliver a unique value proposition to critical shopper segments, on specific purchasing occasions (such as bulk, top up and indulgence) leading to profitable growth for both parties (see Exhibit 2).

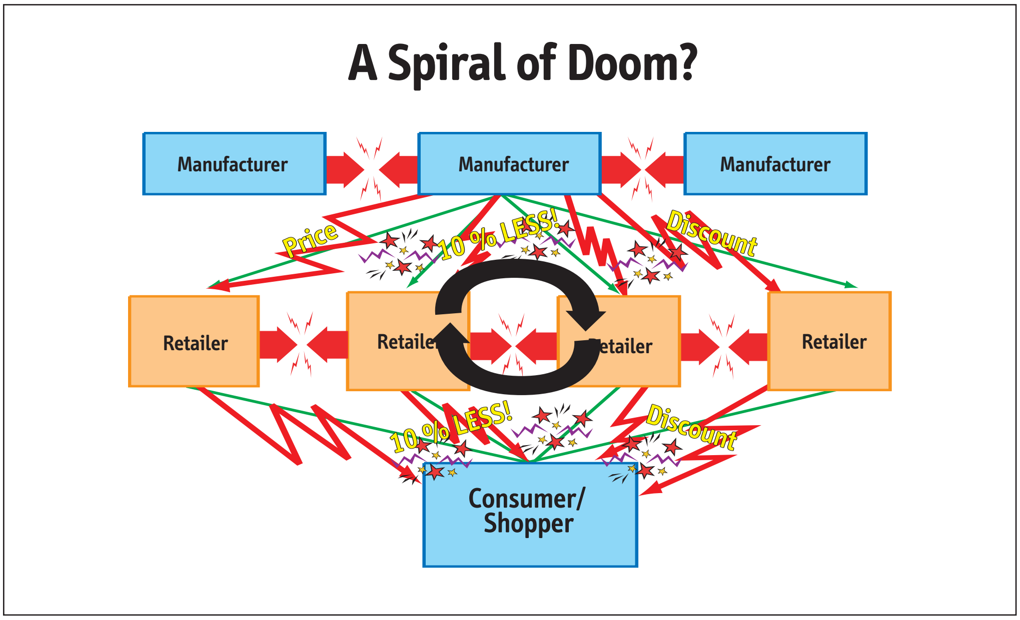
With the added input of customer relationship management tools and techniques, it offers an alternative to traditional business strategies that revolve around economies of scale and price competition.

Collaborative differentiation could flourish in four main areas, depending on individual manufacturers' and retailers' own marketing strategies. They can work together on jointly identified shopper/consumer segments, and one or both sides can go one step further to include one-to-one/CRM initiatives as well (see Exhibit 3).

Here are some examples of these four broad approaches to Collaborative Differentation.

Relevant segments. A perennial dilemma for mums is that kids prefer to eat white bread, but their mums consider brown bread to be healthier. The development and introduction of Blue Band Bread between Unilever and Albert Heijn in the Netherlands tackles this dilemma. The consumer proposition is a white bread that contains all the nutrition and fibres of brown bread. Branded with one of the

Exhibit 1:



most trusted family brands in the Netherlands, Blue Band (a margarine brand), it solves a targeting issue for Unilever and a shopper issue for Albert Heijn.

In a pilot between Champion supermarkets and Lever Fabergé in France both the manufacturer and the retailer ran analyses of their respective consumer databases to identify customers who were particularly valuable to both the store and to the brand(s). These customers were mailed with an offer to create better category sales and store traffic.

Manufacturer-driven insights into core consumer needs. Some manufacturers possess extensive consumer databases, strong consumer propositions, and even own communication channels such as TV programs. In this situation manufacturers can use all these instruments to drive a specific shopper segment towards a specific retailer by personal mails and in-store offers.

Retailer driven: Tesco's Clubcard database is used to target certain shopper segments with manufacturer promotions.

Integrated strategy: No cases known as yet.

Summary

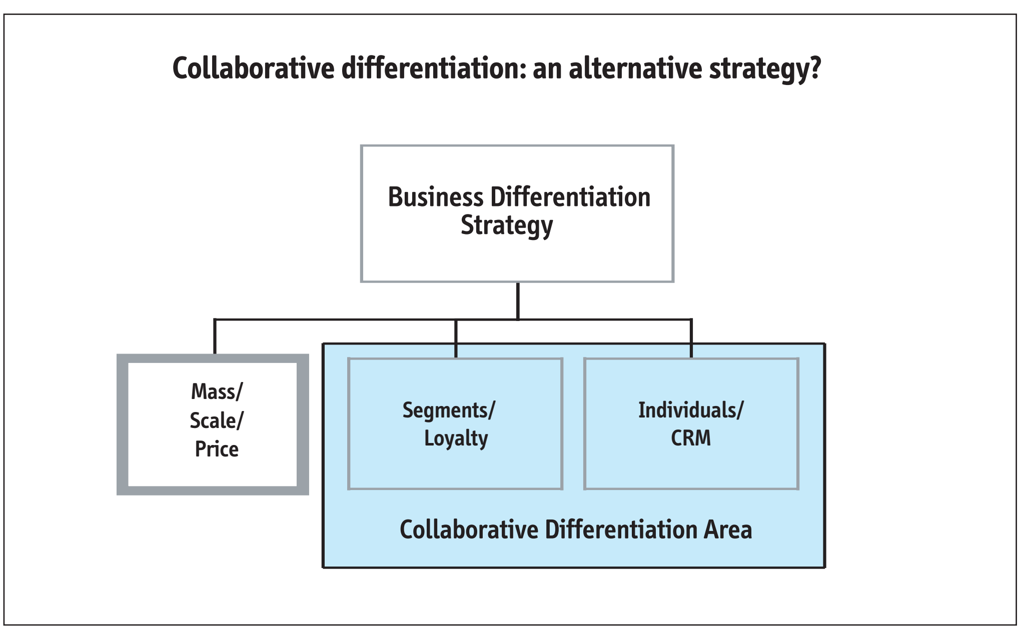
The implications of Collaborative Differentiation are significant for both manufacturers and retailers. Manufacturers will need to revisit their product design (modules, variants), production processes (to allow for low scale volumes), planning paradigms, communication channels, and brand positioning.

Retailers will need to develop skills in consumer targeting (marketing focus), selective pricing (consumer value planning), assortment planning and service development. Both sides will also need to develop their collaboration skills in areas such as collaborative consumer relationship management, collaborative new product development, co-branding and collaborative communication.

Collaborative Differentiation also raises many thorny questions. These include:

- Do the business models of retailers and manufacturers conflict? (price/cost focus vs differentiation/added value focus)?
- Can a retailer's and a manufacturer's objectives be aligned?
- Is selective distribution of A-brands possible (penetration)?
- Can retailer-specific A-brand variants exist sustainably?

Exhibit 2:



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- Are these marketable under the umbrella of A-brands?
- Does the premium realised from differentiation outstrip current scale-focused approaches?
- Can retailers position themselves as sharply as A-brand products?

The answers are not clear. But what is clear is that the doom loop must be reversed. At the moment, many ECR benefits are being competed away, passed through the hands of retailers and manufacturers to consumers, who are spending the money they save on increasing health insurance, pension provision, taxes and energy consumption. Even holidays can be considered to be a competitor of our FMCG sector. Of course, investing in price might be the best thing a retailer can do. But there are other options, such as investing in new in-store experience, and in new products to re-engender consumer excitement. So the message from manufacturers to retailers needs to be: 'How can we help you invest the money in the best possible way - one which benefits consumers, retailers and manufacturers?' Collaborative Differentiation may be one way of doing this.

Exhibit 3: