PROCTOR AND GAMBLE: THE BEAUTY/FEMININE CARE SEGMENT OF THE CONSUMER GOODS INDUSTRY

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ABSTRACT

There were a couple of strategic business decisions that P&G could focus on: it could produce more products with natural ingredients and more men's products because these were the growing trends in the industry; or it could focus on one of its product segments such as skin products for a while and then later introduce its other products. All these were possible alternatives, but the main question to be resolved was how to differentiate P&G from its competition, and so achieve a winning edge over competitors within intensely competitive, rapidly changing immediate, intermediate, and long-term time frames.

Keywords: Strategic Management; Decision Making; Product Segmentation; Consumer Goods Industry

INDUSTRY AND COMPETITIVE MARKET: BEAUTY/FEMININE CARE GOODS

The desire to be beautiful created an industry which generates $160 billion a year. Americans spent more each year on beauty than they did on education [1]. The industry encompassed some of the following products: hair, products, skin products, feminine products, fine fragrances, cosmetics, and personal cleansing. Companies that produced beauty/feminine care products were influenced by fashion, seasons, and culture. The latest trends to affect this market were the movement by consumers towards natural products and the increased interest by men to look clean and well groomed, creating a large emerging men's market. From 2003 to 2008, as shown in Figure 1, the sale of most beauty/feminine care products, such as hair products, cosmetics, and skin products increased. Each of these beauty/feminine care products are further described in the following section.

Figure 1
PROJECTED U.S. RETAIL DOLLAR SALES OF ETHNIC SPECIFIC COSMETICS, 2003-2008
(In millions)

	Hair Care		Cosmetics		Skin Care		Total
Year	$	% Change	$	% Change	$	% Change	$
2003	$1,030	-4.0%	$367	5.6%	$118	3.3%	$1,515
2004	1,009	-2.0	387	5.5	121	2.5	1,517
2005	1,019	1.0	410	6.0	124	2.5	1,553
2006	1,035	1.5	437	6.5	129	4.0	1,601
2007	1,055	2.0	463	6.0	132	2.3	1,650
2008	1,030	2.5	493	6.5	137	3.6	1,712

This industry included companies that manufactured goods that were used to fulfill the needs of consumers. The products these companies produced included hair products, skin products, feminine products, fine fragrances, cosmetics, and personal cleansing products. Consumers used each product for their own personal reasons, but the main purposes were to make people look beautiful and feel clean.

The consumers for these products included both females and males from all age groups. Even though it was called beauty/feminine care, males were actually a large part of the consumer base because they used a lot of beauty products. Consumers also included people from different ethnic group, marital status, and also low income consumers. Consumers seemed to be more confident about what they wanted and this played a major role in determining what products were manufactured. In early 2006, a national survey of consumer goods executives showed that a majority of respondents believed that their organizations were well on the way to becoming demand-driven. Demand-driven enterprises were defined as those that not only identified real-time changes in demand, but were also organizationally prepared to profitably respond to these opportunities. The benefits of becoming more demand-driven were that the companies had 15% less inventory, a 17% better perfect-order performance, and a 35% shorter cash-to-cash cycle time [2]. So as consumers changed, the companies also changed in order to remain in the competitions with their competitors.

These products were produced in factories all over the world with raw materials ranging from materials as simple as water to chemicals such as stearic acid and sodium hydroxide. These materials were mixed in unique ways to make each product. Regardless of the raw materials or procedures used to make them, each product had to meet regulatory standards. In the United States of America, an example of such a regulatory body was the U. S. Food and Drug Administration (FDA). These standards varied by country, and they helped to ensure that these products were safe enough to be used by the consumers. After production, these products were packaged and distributed to consumers through various distribution channels such as distribution companies, individual stores, and chain store outlets. Packaging was another important factor in selling products, for example male products had to be packaged in a different way to attract them. Most times, the packets for men's products were normally dark colored to make the products look more masculine. Distribution companies were companies that bought and sold large amount of products to various retailers, who then sold to the consumers. Individual stores were stores that were owned by companies and these companies sold their products directly to the consumers from these stores. While the chain store outlets included some multinational companies such as Costco and Wal-Mart, which carried a variety of products. These stores were located in different parts of the world, such as Africa, Asia, Australia, Europe, Latin America, and North America, providing products to consumers there. Manufacturing companies had to decide if they wanted to make or buy their manufacturing materials. If they decided to buy any item they usually looked for the cheapest and most efficient source to buy from. This process was called Sourcing and it was a process that had to be continuously reviewed in order to maintain the best deals that suited the company. Advertisement was the promotion of goods, services, companies and ideas, usually by an identified sponsor. Companies used advertisement as part of an overall promotional strategy for their products. They advertised through different media such as television, Internet, print, and radio. Advertising helped to bring some awareness about the products to the consumers, so they could go out and purchase them. Due to the variety in customers and consumers, technology played a major role in this industry, making it a capital intensive industry. They required highly mechanized assembly lines which were designed for long production runs and flexibility, so that it could be easily changed to produce the same products with minor alterations. Some of the companies that produced beauty/feminine care products were Unilever, Colgate-Palmolive, Playtex products, Avon, and Estee Lauder. Since they produced products that appealed to people all over the world, they had to take into consideration various factors such as differences in skin types, body types, hair types, values and beliefs, to efficiently meet their needs. These differences were seriously considered during production in each part of the world to produce products that could be used by consumers and sold for a profit.

Competition

Competition in the beauty/feminine product was based on price, brand quality reputation, mass market presence, variety of products, brand recognition, and introduction of new products. Some of the companies in the beauty/feminine care industry were Unilever, Colgate-Palmolive, Playtex products, Avon, and Estee Lauder.

THE COMPANY

P&G was a company that manufactured, distributed and marketed consumer goods products. It was established in 1837 in the United States. It later started expanding to other countries and in early 2006 it was one of the global leaders in the consumer goods industry. It acquired its first overseas subsidiary with the purchase of Thomas Hedley & Sons Company, UK, in 1930. Also in 1915, P&G built a manufacturing facility in Canada, its first outside the US [3]. In early 2006, the company had its headquarters in Cincinnati, Ohio. In the United States, the company owned and operated 35 manufacturing facilities which were located in 21 different states. Worldwide, the company owned and operated 83 manufacturing facilities in 42 countries. P&G provided branded products and services of superior quality and value that improved the lives of consumers all over the world. And as a result, it believed that the consumers rewarded it with leadership sales, profit, and value creation. These results allowed its people, shareholders, and the communities in which they lived and worked to prosper [4]. P&G's top 10 customers were Ahold, Albertson's, Carrefours, Costco, Kmart, Kroger, Metro, Target, Tesco, and Wal-Mart The company always acquired new brands and products, either my creating them or by merging with other companies. An example of these mergers was in 1985, P&G expanded its over-the-counter and personal health care business with the acquisition of Richardson-Vicks, owners of Vicks respiratory care and Oil of Olay product lines. Also in 1988, the company announced a joint venture to manufacture products in China. This marked the company's foray into the largest consumer market in the world [5].

One of the threats that P&G faced was intense competition. It operated in an industry with rivals such as Unilever, Colgate-Palmolive, Playtex Products, Avon, and Estee Lauder. These companies operated and sold their products worldwide. Their presence in the same industry put pressure on P&G to competitively price its products and continually strive to develop innovative products. Another threat was the increase in prices of raw materials. These prices were subject to price volatility caused by weather, supply conditions, and other unpredictable factors. Lastly, the risk associated with merger integration was another threat for this company. In September 2003, P&G acquired Wella, owning 79.2 percent of the company's total shares. This acquisition contributed about $3.3 billion in sales to P&G's overall beauty business - around $1.6 billion in the professional hair care segment; $1 billion in the retail hair care segment and $800 million in fragrances. However, Wella's results (as of October 2003) were falling below P&G's stated long-term targets, giving an early indication of disruptions post its takeover [6]. Other brands acquired by P&G were Clairol from Bristol-Myers Squibb in 2001 and Gillette in 2005. In 2004, P&G did not manufacture products that were specifically for different ethnic groups, such as Hispanics and African American, and products that were made with natural ingredients. There was a high demand for these types of products because some consumers wanted to use products that were made from natural ingredients and some consumers wanted products that were made for their ethnic group.

In the United States it was virtually impossible to calculate the absolute number of companies that produced and marketed beauty/feminine care products. The field of competition was highly fragmented, for example, between those companies active in mass channels (supermarkets, chain drugstores, and mass merchandisers) and prestige channels, not to mention those active in the natural food and beauty care channel. The company size was another factor, between globally-oriented mega-corporations like

P&G and kitchen table-based entrepreneurs limited to regional or even local distribution. Although it was impossible to calculate the number of companies that produced and marketed beauty/feminine care products. It was obvious that P&G was one of the leaders in this industry because, as illustrated in Figure 2, P&G was well ahead of the industry. P&G faced various challenges in 2006, such as consumers' interest in natural products. This trend was as a result of consumers questioning the ingredients used in making products and their effects. Some activists claimed that these products contained toxic chemicals known to cause cancer, fertility problems, and birth defects. Another challenge was the stagnant sales of some products due to low product development and innovation. Duane Reade Inc.'s Divisional Merchandise Manager, Mike Cirilli, said that "The market's poor sales will only turn around with the launch of dramatically different products. We need the leaders in these categories, such as P&G and L'Oreal to come out with some revolutionary products, spend $100 million on them in advertising and get all the consumers excited again. We need excitement. Excitement and advertising spending will bring sales dollars to these categories" [7].

Figure 2
FINANCIAL INFORMATION OF P&G AND THE INDUSTRY

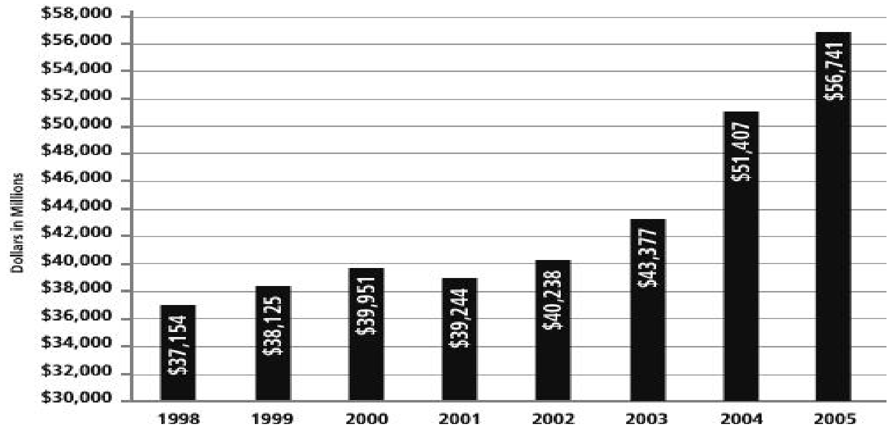
	P&G	**Industry**
Market Capital	202.67B	275.79M
Employees	110,000	2.81K
Quarterly Revenue Growth	26.90%	10.40%
Revenue	61.68B	1.74B
Gross Margin	51.05%	36.68%
EBITDA	14.42B	262.13M
Operating Margins	19.95%	7.40%
Net Income	7.77B	13.16M
EPS	2.733	1.23
P/E	22.55	22.50
PEG (5 yr expected)	2.02	2.02
P/S	3.28	2.05

The emerging men's market was another trend that was affecting the industry. The number of men spending time in front of the mirror, grooming themselves had increased. The acquisition of Gillette helped P&G to start to address this trend with products like Gillette's complete skin care for men and Gillette's Fusion. This was some of the steps that P&G decided to take to remain at the top in the beauty/feminine care segment. Following were detailed analyses of P&G's business model, as illustrated below in Figure 3 (page 6).

FINANCIAL ANALYSIS

For the past 5 years, P&G's net sales have grown, as shown in Figure 4 (next page). The company was a global leader with sales growth of more than 40%, increasing to $57 billion. P&G's profit also more than doubled in 2005 and they generated more than $30 billion in free cash flow. Shareholders received $11 billion in cash through dividends and this increased their value with another $60 billion by nearly doubling the price of P&G stock. The company has increased sales per employee nearly 40% over the past five years and even though Research and Development (R&D) investment has increased over the past years, R&D as a percentage of sales has declined from 4.8% in 2000 to 3.4% in 2005. More than 80% of initiatives succeeded in creating shareholder value, an improvement of 25% over the past three years. The productivity of P&G's product supply organization has increased at a high single-digit rate since 2000 and there had been a decrease in P&G's Global Business Services (GBS) costs by more than 15% on base business services since 2000. Companies tried to increase profit by various methods. One of these methods was to reduce cost. P&G reduced capital spending as a percentage of sales since 2000 from nearly 8% to less than 4%, without foregoing any strategic investment in growth. They also added an incremental growth point to the company's top line over the past two years with marketing Return on Investment (ROI) initiatives [8].

Figure 4
P&G'S FINANCIAL DATA – NET SALES

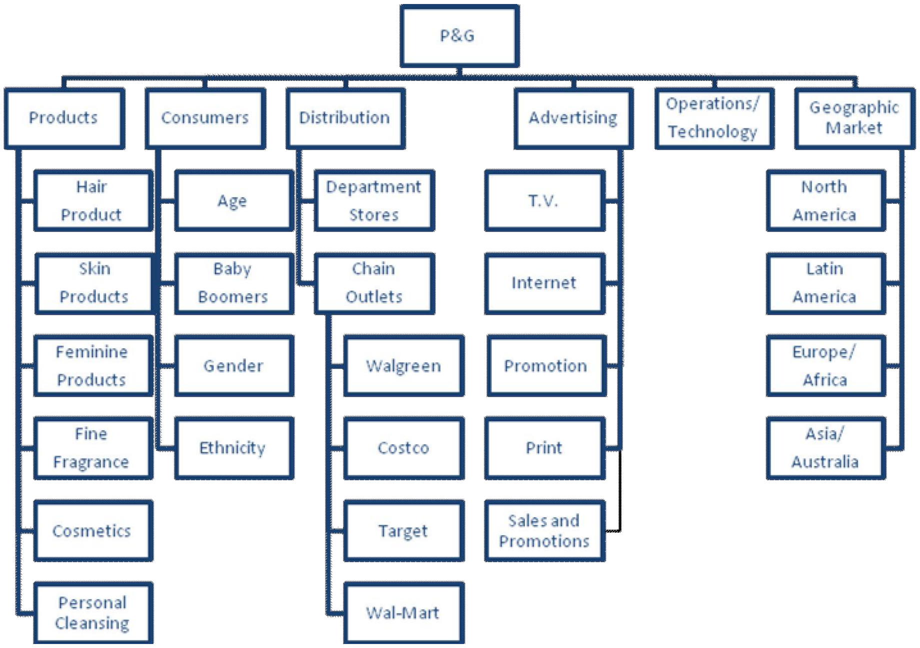


Amounts in millions except per share amounts	Years Ended June 30 2005	2004	2003	2002	2001	2000
Net Sales	$56,741	$51,407	$43,377	$40,238	$39,244	$39,951
Operating Income	10,927	9,827	7,853	6,678	4,736	5,954
Net Earnings	7,257	6,481	5,186	4,352	2,922	3,542
Net Earnings Margin	12.8%	12.6%	12.0%	10.8%	7.4%	8.9%
Basic Net Earnings per Common Share	$2.83	$2.46	$1.95	$1.63	$1.08	$1.30
Diluted Net Earnings per Common Share	2.66	2.32	1.85	1.54	1.03	1.23
Dividends per Common Share	1.03	0.93	0.82	0.76	0.70	0.64

MANAGEMENT STRATEGY

One of P&G's strategies was to build existing core businesses into stronger global leaders. In 2005, the company grew market share, profit, and sales in all its core categories, such as its beauty and health segments. These increases were achieved by the decision to reach more consumers, especially low income consumers and the acquisition of Gillette. This acquisition increased the brands, products, and consumers of the company. Another strategy was to develop faster-growing, higher-margin, more asset efficient businesses with global leadership potential. In 2005, this was evident in the beauty segment, where sales nearly doubled to $19.5 billion and profit more than doubled to $2.9 billion. This growth was also noticed in the Health Care segment, where sales doubled to $7.8 billion and profit more than tripled to $1 billion. These two segments made up 47% of P&G's sales and 50% of the company's profit [9]. Internationally, P&G tried to regain growth momentum and leadership in Western Europe, by introducing new products and increasing advertisements. In 2005, the Western Europe volume went up mid-single digit and on average it went up twice the rate of Western Europe Gross Domestic Profit (GDP) growth. At the end of the year, the company's brands growing share in categories accounted for more than half of Western Europe sales. Another major strategy for P&G was to increase growth among lower-income consumers in developing markets, such as Nigeria and Ghana. To attract these consumers, P&G changed the package, making them small and reducing the quality of the packaging, so it was more affordable for these consumers. This strategy has delivered mid-teens volume growth, on average, in these countries.

Figure 3
P&G



LOOKING TOWARDS THE FUTURE

Since 2000, A.G. Lafley and his colleagues have been successful in trying to maximize the strengths of the company, while also reducing its weaknesses. They have worked to increase P&G's brands, net sales, and profit. In 2005, male consumers became more interested in beauty products, and to satisfy this need and other issues the company were facing, P&G acquired Gillette. It also entered a major multimedia marketing partnership with Viacom Plus in 2001, to create more ways to reach its consumers. The first alternative was for P&G to expand and build existing core businesses, such as the health and beauty segments. It decided to do this by reaching more consumers, especially the low income consumers. These segments would be expanded to include new brands and products which would attract such consumers. The already existing products would be altered by reducing their sizes and changing their packages to reduce their prices. Doing this would make it easier for consumers to buy them. The second alternative was for P&G to focus and expand just on its skin care segment of the beauty/feminine care segment. The company would focus and specialize just on these products. It would produce different types of products for each ethnic group, products that had natural ingredients (such as herbs), and more skin products for men. It would have to sell all its other products, such as its hair products, cosmetics, feminine products and fine fragrances. The money from the sale of these products would be used to acquire more brands and products in the skin care segment. Lafley and his colleagues had a tough choice to make. These and other alternatives needed to be considered very carefully before reaching a decision which will impact the Company's future substantially.

A set of references available upon request from Marc Gartenfeld, mdj13j@aol.com.