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Partnering with China's retailers: A guide for consumer-goods companies

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Partnering with China's retailers: A guide for consumer-goods companies

Companies must tailor their key-account-management model and capabilities to the Chinese context.

The Chinese consumer sector looks vastly different today compared with just five years ago. The retail environment—both offline and online—has shifted, consumers have become savvier omnichannel shoppers, and local consumer-packaged-goods (CPG) manufacturers are giving global players a run for their money. Growth among CPG companies slowed to below five percent in 2016, down from 15 percent in 2011. It's a complex and fast-changing market that increasingly requires CPG companies to develop top-notch sales capabilities. Indeed, a recent survey indicates that CPG executives see key-account management (KAM) as the most critical capability for driving growth in China.[1]

KAM in China, however, is a relatively new concept, and many CPG companies operating in the Chinese market are currently at a low level with regard to sales skills and technologies. And in a context where the balance of power between manufacturers and retailers is just about even, KAM dynamics and considerations are very different from those in Europe or North America. What will it take for a CPG sales organization to excel in China? In this article, we examine three trends shaping China's consumer sector and their implications for key-account management.

Channel shifts, e-commerce, local competition

A confluence of trends is changing how CPG companies partner with retailers in China. These trends include channel shifts in offline retail, the continued growth of e-commerce, and the rise of local CPG manufacturers.

A changing brick-and-mortar retail landscape

After several years of double-digit growth in China, mainstream modern retailers—specifically, hypermarkets and supermarkets—are experiencing a slowdown. Their market share in grocery, for example, grew a mere 2 percentage points over the past three years (Exhibit 1). Many modern retailers have seen their overall profitability decline since 2010.

With mainstream modern retailers struggling, CPG companies have been turning their attention to higher-growth channels. Much of the growth in offline retail in China today is coming from newer modern-retail formats—in particular, convenience stores, which grew by 14 percent per year between 2013 and 2016. And the market is far from saturated: using Japan's five largest cities as a benchmark for number of stores per thousand people, the number of convenience stores in China's top ten cities could almost triple.

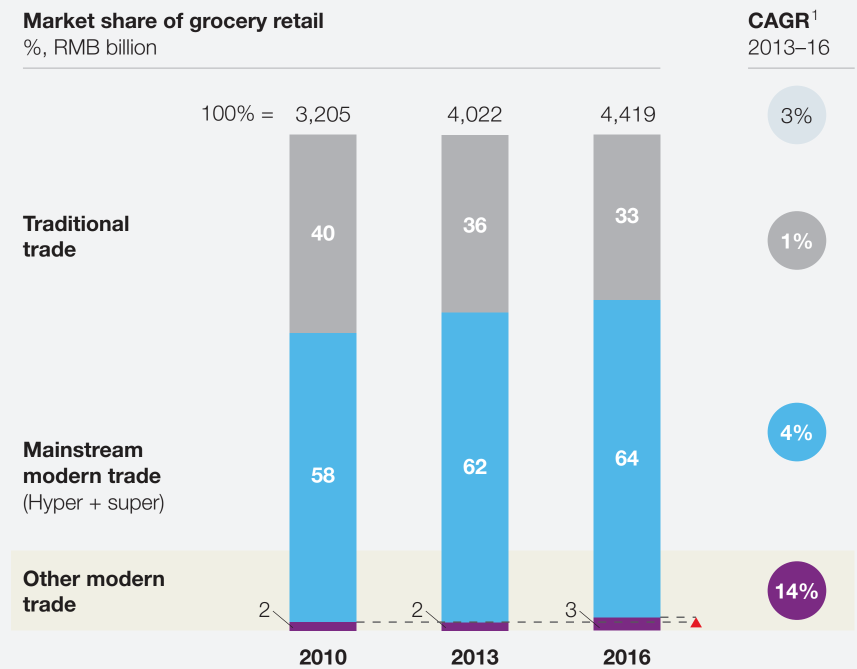
Another factor making growth more elusive for CPG companies is that consumption growth has become more geographically dispersed. Slowing demand in Tier 1 and 2 cities has forced national retailers including Carrefour and Walmart to shutter some stores in those cities and instead seek growth by opening stores in lower-tier cities, where they're increasingly finding themselves in direct competition with regional players. The regional retailers, for their part, are dominating the grocery market and expanding into neighboring provinces.

This fragmentation within modern trade—large national accounts competing with many important regional accounts—makes KAM in China much more complex and resource-intensive than in developed markets. Whereas CPG companies in the United States might devote disproportionate resources and attention to about 25 key accounts, in China that number can be closer to 50.

Big gains in e-commerce

Some of these key accounts will be online retailers. China's online retail market, already the world's

Exhibit 1 **The growth of mainstream modern grocery formats in China has slowed in recent years.**



[1] Compound annual growth rate.
Source: Bloomberg; Euromonitor

largest at approximately $830 billion, is also the fastest growing. For the past three years, its compound annual growth rate has been 38.1 percent, almost thrice the US rate of 13.6 percent. In 2017, China's e-commerce market is expected to surpass those of Europe and the United States.[2] Online and multichannel retailers are therefore crucial players in China's consumer-goods ecosystem, to a greater extent than in developed markets.

And Chinese consumers aren't just buying Chinese products from Chinese websites. Cross-border e-commerce is experiencing explosive growth, powered by Chinese consumers' desire for lower prices and higher-quality products. Cross-border e-commerce is projected to account for 9.2 percent of the country's total online retail market by 2018.[3]

Not surprisingly, more than two-thirds of Chinese consumers are omnichannel shoppers. Online-to-offline commerce is pervasive: according to McKinsey's 2015 iConsumer survey, half of Chinese consumers switch between online and offline three to four times before making a purchase. About 67 percent shop on mobile devices.

Competition from Chinese manufacturers

Global CPG brands still dominate traditionally Western product categories such as chocolate and cheese, but in many CPG subcategories—including subcategories of packaged food, soft drinks, beauty products, and home-care products—Chinese brands are steadily winning share. Retailers are looking beyond big brands in their efforts to meet growth expectations and are happy to give (physical and virtual) shelf space to local brands. This makes it essential for big CPG companies to nurture strong relationships with key retailers; otherwise they risk continuing to lose share to local manufacturers. Many local companies are relatively unsophisticated with regard to KAM capabilities and IT systems, but the most ambitious are slowly catching up to their Western competitors.

A focused framework for key-account management

In light of these trends, CPG companies must sharpen their focus on their KAM model and capabilities (Exhibit 2) while bearing in mind China-specific nuances.[4]

Based on our work with leading CPG companies in China and around the world, we estimate that overhauling an average company's KAM model and capabilities can yield growth rates that are 5 to 10 percentage points higher than for the category as a whole and can reduce sales expenses by 0.3 to 0.5 percentage points.

Fine-tune the model

CPG companies in China typically divide their retail customers into three broad segments based on geographic reach: national companies (with a presence in at least ten provinces and revenues exceeding $1 billion), regional giants (operating in at least two regions and looking to expand nationally), and smaller regional players. This basic segmentation determines account-team structure and resource allocation, but, in our view, it fails to tap into the full potential of key-

Exhibit 2

Companies must sharpen their focus on their key-account-management model and capabilities.

Model	Capabilities			
Fine-tune the model	**O**verhaul capabilities	**C**ommit to collaborate	**U**pgrade negotiations	**S**upercharge insights
• Customer-portfolio management • Tailored account-team structure • Omnichannel governance	• Tailored training sessions • Learning-and-development organization • Performance-management metrics	• Full-value-chain power partnerships • Cross-functional collaboration • Structured process for joint business planning	• Cross-functional negotiations preparation • “Retailer-back” negotiation strategy	• Granular and prescriptive insights • Advanced, real-time analytics • Insight translation and communication

Source: McKinsey analysis

account relationships. We recommend the following three fundamental changes to the KAM model.

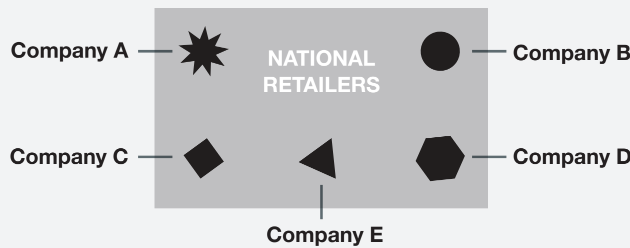
Shift from customer segmentation to 'customer-portfolio management'

CPG companies should view their customer base as a portfolio and determine the distinct business role that each retailer plays in that portfolio. Examples of roles might be growth driver, profit driver, scale builder, future prospect, or margin extractor (Exhibit 3). A retailer's assigned role should then inform the manufacturer's profit-and-loss expectations, investment level, collaboration style, negotiation posture, and account-team capabilities as it seeks to serve that particular retailer.

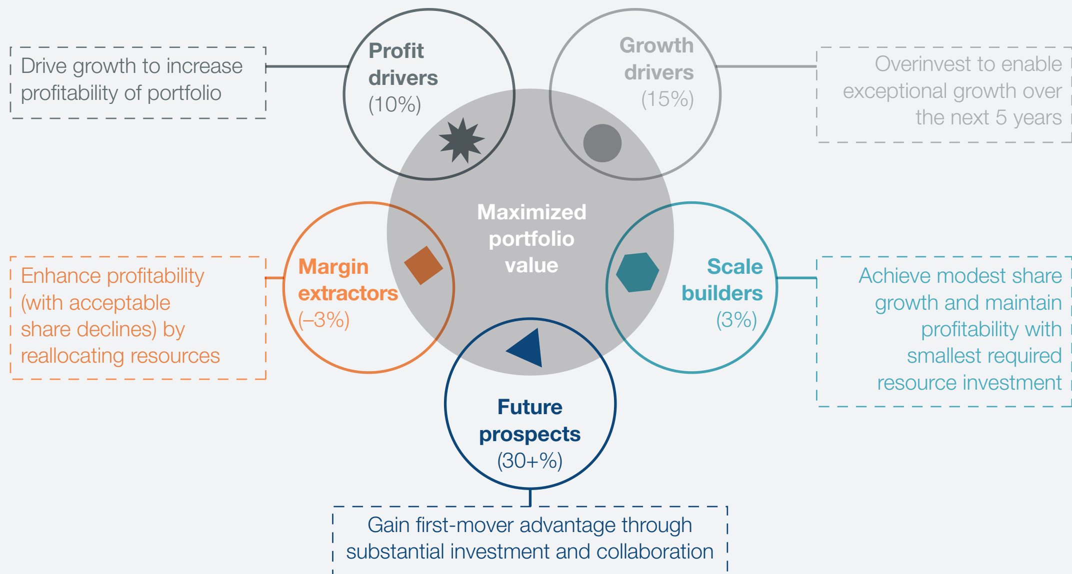
Exhibit 3

Portfolio roles inform the business objectives and expectations for each customer.

In traditional customer segmentation, all national retailers are treated the same ...



... but in customer-portfolio management, companies are treated differently based on their role.



Source: McKinsey analysis

A portfolio approach is particularly effective when dealing with a large number of diverse retailers. Using this approach, instead of investing aggressively in every national retailer, a CPG company might actually reduce its investments in one or two national retailers.

Tailor your KAM structure to your customer base

Once a CPG company has determined portfolio roles, how should it structure its KAM organization to best serve its most important customers? In our experience, successful companies follow one of three organizational models, depending on their customer base (Exhibit 4).

A CPG company that places equal emphasis on traditional and modern accounts is likely to have a KAM organization separate from—and just as empowered as—its sales organization. At companies that serve mostly small regional retailers, the KAM organization tends to be a subset of the sales organization. And companies that focus on large modern retailers typically divide their sales staff into key-account teams, some serving one retailer exclusively and others serving multiple retailers.

In all of these models, a dedicated team serves each of the most important accounts. But even key-account teams that serve several smaller retailers should strive to make themselves available and accessible to every one of their accounts.

Set up omnichannel governance

With the proliferation of offline and online channels, managing channel conflict becomes more of a concern. Within the online channel alone, for instance, CPG companies must manage relationships with online marketplaces or dealer stores such as Tmall, general e-tailers such as JD.com, flash-sale players such as VIP.com, and cross-border platforms.

Exhibit 4

Leading consumer-packaged goods companies in China tailor their KAM[1] organizational models to their customer base.

Customer base	Equal emphasis on modern and traditional trade	Mostly smaller regional retailers	A few large modern accounts
Organizational model	Dual emphasis	Regionally focused	Account-driven matrix
Differentiating features	• National sales director at same level as national key-account director • Regional sales managers at same level as regional key-account managers	• Large, stand-alone sales organization • Key-account organization as subset of sales organization	• Sales teams organized by account • Functions (eg, finance, logistics, IT) also organized by account
Elements common to all models	• **Dedicated account teams for the most important accounts** • **Regionally managed field teams** • **Dedicated functional support for top accounts**		

[1]Key-account management.

Source: McKinsey analysis

Should a single account team handle both offline and online channels? Or should CPG manufacturers establish a separate KAM team for online retailers?

One way to decide is by mirroring the retailer's structure. If, for example, a retailer's offline and online businesses are closely integrated, then one account team might handle both. If, however, the online business operates autonomously from the stores, then the CPG company might opt for two distinct account teams.

The biggest CPG manufacturers, when seeking a special relationship with a major multichannel retailer, have in certain cases appointed a group manager who oversees all matters relating to that account. Such a structure enables greater client coverage and facilitates information sharing, often leading to better and faster decision making—but, of course, it's costly to hire a large team of people to serve a single retailer.

Regardless of the specific account-team structure, omnichannel governance is critical for coordinating assortments, pricing, and promotions to avoid channel conflict. A company might decide to sell different pack sizes or different SKUs in each channel, or recommend slightly different retail prices across channels. Recommended prices shouldn't vary too widely, however, lest they confuse and alienate cross-channel shoppers. Price differences also give distributors in China an incentive to engage in arbitrage—for example, buying the lower-priced products in one region and selling them at a larger markup in another—which is often at odds with the manufacturer's purposes.

Overhaul capabilities

Changing the KAM model is an essential step, but a new model won't achieve its purposes if a company neglects to bolster sales capabilities. CPG companies should train KAM staff on a range of skills such as understanding a retailer's business style and decision-making processes, developing account tactics and strategies, and setting agendas for client meetings.

These training sessions shouldn't be ad hoc events. Rather, companies should formalize a capability-building infrastructure—ideally, a dedicated learning-and-development (L&D) organization that resides within the human-resources department but is supported by the sales team. Some local CPG companies have hired talent from global companies like P&G or Unilever and tasked these new hires with setting up L&D organizations modeled after those at their previous employers. An L&D organization can be a powerful retention tool—which is especially important in China, where employees tend to job-hop frequently.

For companies that don't have the scale to build an L&D organization, one option is to work with third parties such as universities, reputable sales-training companies, and individual trainers who specialize in KAM. On the other end of the spectrum, large multinational companies might consider establishing a "sales university," the most comprehensive (and resource-intensive) option for a capability-building infrastructure. A sales university designs tailored learning programs for all high-priority sales roles.

Regardless of which type of infrastructure a company chooses, a robust performance-management system, with clear metrics linked to strategic goals, is crucial to success. The most effective systems measure results instead of activities and offer a balance of financial and nonfinancial incentives.

Commit to collaboration

Amid slowing growth, retailers have become more open to collaboration beyond typical contract terms. CPG manufacturers can take advantage of that openness. In particular, key-account teams must be trained to do the following:

- *Collaborate in every part of the value chain.* The best key-account managers work with retailers on both demand generation (such as

joint innovation and product development) and cost reduction (such as collaborative inventory management). An infant-formula company, for instance, worked with a retailer to determine optimal staffing for the baby-products department across its stores in China.

- *Facilitate cross-functional collaboration, both internally and externally.* Sales organizations won't work effectively with a retailer if they're not good at collaborating with their own colleagues. The most successful account teams regularly tap functional experts within their company to counsel retailers on a range of topics. One CPG company formed an advisory team to provide expert support to its key accounts in China—for instance, bringing an innovation executive to a meeting with a retailer to give updates on the innovation pipeline and to help develop ideas for exclusive products.

- *Establish a structured process for joint business planning.* Frequent dialogues with the retailer help an account team gain a deep understanding of the retailer's biggest concerns and priorities. They also provide ample opportunity to discuss a variety of joint initiatives. When an oral-care company collaborated with a retailer on shopper research, it learned that shoppers cared more about brand origin than brand name when buying oral-care products. The manufacturer and the retailer jointly launched and promoted a line of imported toothpaste, which appealed to Chinese consumers looking for trade-up options. The new line drove significant sales and margin.

Upgrade negotiation skills

Even as they become better collaborators, key-account teams must also become savvier negotiators. Although negotiations in China tend to be less adversarial than in Europe or the United States (mainly because even the biggest retailers don't wield as much power in China as they do in developed markets), negotiating skills are nevertheless valuable. One reason is that global retailers operating in China often expect CPG manufacturers to agree to trade terms set in developed markets—which heavily favor the retailer—rather than developing terms specific to the Chinese market. Historically, CPG companies have simply accepted the developed-market terms. But in an environment of slowing sales growth and increased competition from assertive local manufacturers, it becomes imperative for CPG companies to seek more favorable trade terms.

To secure its desired outcomes, each key-account team should tailor its negotiation postures and tactics to each retailer. This requires first developing a detailed understanding of each retailer's strategy and needs, and then deciding on negotiation posture and tactics, prioritizing topics for discussion, and agreeing on entry and walk-away points. Some CPG companies in China have appointed a negotiations coordinator responsible for leading negotiations preparation, integrating cross-functional perspectives, collecting and disseminating cross-customer insights and best practices, and tracking negotiation outcomes.

Supercharge insights

Finally, the most successful CPG sales organizations in China will be those that can best harness the power of data and analytics to generate distinctive insights. On this front, the online channel is a logical place to start, since e-commerce and social networks offer a wealth of data. CPG companies can take full advantage of those data by finding the right partners. Leading companies in China have already begun working with digital partners to improve marketing effectiveness, for example. By examining aggregated mobile-phone data as well as consumers' browsing history and transactions on popular platforms (such as Qzone and WeChat), then comparing these data with phone numbers from its own customer database, a CPG company can identify "statistical twins." For instance, it can figure out which customers are likely to be young

adults living in Tier 3 cities.[5] The company can then create customized promotions aimed at current and potential customers with similar profiles.

That said, companies shouldn't just rely on online data; they should fully commit to generating offline insights as well. The days of the Chinese retail market being data-starved are long gone. Point-of-sale data and loyalty-card data are available from retailers, third-party firms have household-panel data and consumer research, and demographic data can be obtained from mobile-service providers—giving CPG companies no excuse for lagging behind on insight generation. Companies can build up their insights capabilities in-house, through outsourcing, or both. Many large companies keep certain core capabilities in-house but outsource operational tasks such as consumer-data management or in-store execution.

All signs point to further disruption—and, of course, opportunities—in the Chinese retail market, particularly in light of the seemingly unstoppable growth of e-commerce. Today, it remains to be seen which way the balance of power will tilt, but inevitably some players will win while others will struggle to survive. By sharpening their focus on their KAM model and capabilities, CPG companies will be investing slightly ahead of the curve—positioning themselves for future success and ensuring that they remain relevant, regardless of what channel disruptions may lie ahead. ■

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[1] For highlights from the 2015 McKinsey Asia Customer and Channel Management Survey, see Cristina Del Molino, Pavlos Exarchos, and Felipe Ize, "Achieving customer-management excellence in emerging markets," September 2015, McKinsey.com.

[2] See Fang Gong, Alan Lau, and Kevin Wei Wang, "How savvy, social shoppers are transforming Chinese e-commerce," April 2016, McKinsey.com.

[3] See Chenan Xia, "Cross-border e-commerce is luring Chinese shoppers," *McKinsey Quarterly,* February 2016, McKinsey.com.

[4] See Kari Alldredge, Brandon Brown, and Max Magni, "Playing catch-up: How to partner with the retailer of the future," June 2016, McKinsey.com.

[5] Companies must not share consumers' names or other personal information. In all data-mining and data-sharing activities, companies must be sure to abide by local privacy laws and regulations.

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