Unleashing Latin American Shopper Needs

A Study by The Coca-Cola Retailing Research Council Latin America

Conducted by McKinsey & Company

2008

Understanding Unmet Needs of Latin-American shoppers

A study by the Coca-Cola Retailing Research Council Latin America*

Introduction

In their search of sources for differentiation, modern retailers are constantly trying to anticipate the needs and desires of their current and future shoppers. Looking at their customers' in-store behavior, this is usually more of a trial-and-error process where new ideas are constantly explored than a structured research and development process.

In this search for new insights, the CCRRC LA has undertaken several projects to understand the emerging consumers, the broadest segment in Latin America. This time it commissioned McKinsey to search for those needs that are meaningful to them but aren't usually clearly expressed, staying rather in the unconscious. For this search, the CCRRC LA and McKinsey developed a specific approach for identifying needs and factoring their relevance across consumers segments in the "belly of the market". Several research techniques and methodologies were visited including the brand positioning tools and frameworks used by the Consumer Goods industry in order to put a little more science into the art of identifying shopper needs and translating them into store concepts.

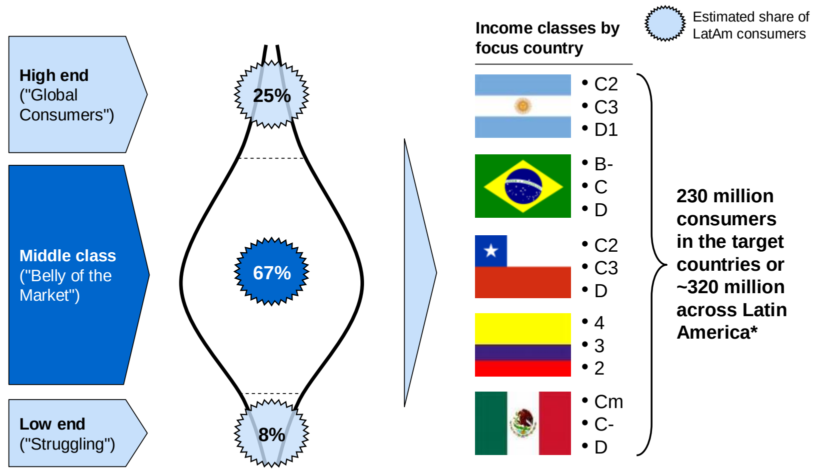
The target segment

The "belly of the market" is currently the most relevant segment of shoppers for Latin-American retailers, representing ~60% of the total population of the region or nearly 320 million consumers. The "belly of the market" refers to consumers in C- and D segments in Mexico, for example, or B-, C and D segments in Brazil, with a range of monthly household income of 500 to 2,500 US dollars on average. (*Exhibit 1*) But most importantly, they devote over ~70% of their spending to food[1]. Compared to other regions the "belly" has the same importance in Latam as it does in Russia, India or China.

* This Executive Summary was written by Jorge Lacayo, Susan Ribeiro and Nicola Cavicchio from Mc Kinsey and Dr. Guillermo D' Andrea, Res. Director of the CCRRC Latin America

[1] Consumption potential based on Brazilian data from Target Marketing; according to the source B-, C and D shoppers represent 68% of the consumption of food and beverages outside the household

THE "BELLY OF THE MARKET" REPRESENTS THE LARGEST CONSUMER GROUP IN LATIN AMERICA



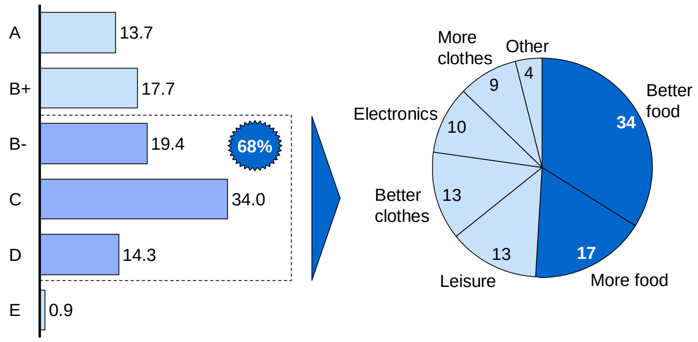
* Assuming that the same share of middle class consumers in target countries applies to the remaining Latin American countries
Source: Target Marketing, SIGMA, Iccom, Indec, Napoleon Colombia, Viewswire 1

Given the growth of the emerging middle-class, their relevance for retailers comes not only from their current demand for food and groceries but especially from their latent future potential. This potential is clearly signaled by their willingness to use any incremental income on purchasing either more or better food (*Exhibit 2*). It is estimated that this consumer segment will represent almost the entire incremental spend in food, beverage and health, beauty and personal care in Mexico over the next 5 years, representing over 18.5 billion dollars [2].

---

[2] Incremental consumption in Mexico based on INEGI's Encuesta del Ingreso y Gastos de los Hogares and excpected GDP growth for the 2008-2012 period

"BELLY OF THE MARKET" SHOPPERS REPRESENT THE LARGEST PORTION OF FOOD CONSUMPTION AND HAVE A PROMISING LATENT DEMAND



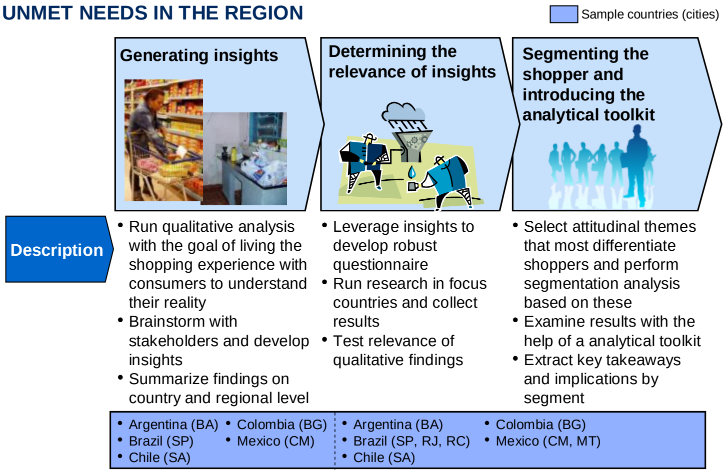
* Urban consumption of food and beverages inside the household
Source: Target Marketing; CCRRC shopper interviews (2007/08)

2

The research process

A 3 stage research & analysis process was developed to understand the characteristics of this shopper segment in Latin America, to identify their current unmet shopping needs and determine how they could influence format innovation in the near future – all of those key objectives of the study. The process was built from qualitative insights (phase 1), that drove the development of a quantitative instrument to determine the relevance of the key hypothesis for the region (phase 2) and also served as a basis to identify 5 distinct shopper segments, their commonalities, differences and significant met and unmet needs. (*Exhibit 3*) Phase 3 of the process included the segmentation as well as the development of the analytical toolkit that uses brand positioning tools to understand the key current and future needs of shoppers across retail formats.

Exhibit - 3
A 3-STEP APPROACH WAS APPLIED TO UNDERSTAND SHOPPER'S UNMET NEEDS IN THE REGION



Source: CCRRC shopper interviews (2007/08), McKinsey

3

Phase 1- Generating insights

The qualitative phased had the objective of providing an initial understanding of shopper needs and to fully grasp the role of grocery shopping within "belly of the market" consumers through several accompanied shopping trips and focus groups across the target countries[3]. After collecting the qualitative observations, insight generation workshops were held to identify 'what lies behind' shopper attitudes in terms of unmet needs

Findings were summarized and clustered on a individual country level and then compared to reach a regional perspective was composed of accompanied shopping trips and focus groups across the region and identified several key themes that are relevant to Latin-American consumers in the "belly of the market across" countries, which should drive their characterization and shopper segmentation

Phase 2 - Determining the relevance of insights

Based on the findings of the qualitative phase, a quantitative dive into these consumers was performed, looking at them in 5 key markets (Argentina, Brasil, Chile, Colombia and Mexico) in 8 cities (Buenos Aires, Mexico City, Monterrey, Santiago, Bogota, Sao Paulo, Rio de Janeiro and Recife). The understanding was reached through a set of attitudinal questions that help infer the strength of each theme across the region. The sample totaled 1,900 "belly of the market" consumers, size that assures statistical significance of the results.

Based on the factors identified, a proper evaluation of the retailing experience of these consumers in Latin-America needed to factor an additional characteristic/lever into the conventional retail pentagon.

Phase 3 -Segmenting the consumer and introducing the "innovation toolkit"

The final phase focused on identifying the differences of consumers in "*the belly"* and developing an analytic toolkit to understand their preferences and needs across shopping formats.

The innovation toolkit

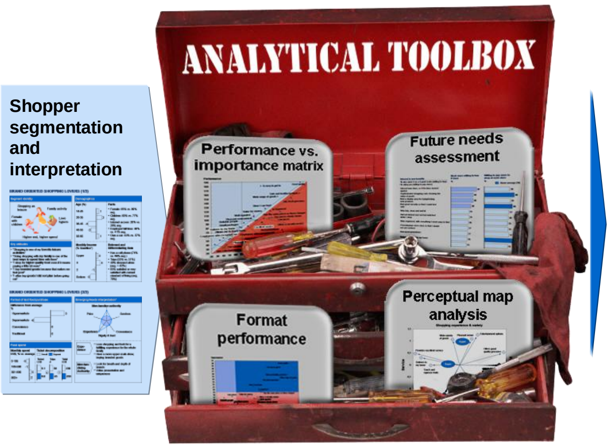
To deepen the understanding of segments and properly draw implications for retailers in terms of formats, a methodology consisting of 4 analytic tools was developed – the "innovation toolkit".

The first tool consists of a comparison of the stated importance of a series of store attributes and the rating that consumers give to the same set of attributes in terms of current store performance. The objective is to determine which attributes really matter to consumers and from those the ones currently underperforming. A blend of basic attributes (e.g. has the best prices, offers the best promotions, is easy to get to) and some especially tailored the key themes of the study (e.g. has resting areas, has employees I can trust, has prices clearly shown) guarantees a holistic overview, as well as a look into some of the needs that are not currently being met by retailers. (Exhibit 5) . Exhibit 6 illustrates the analysis for the financially strapped segment, revealing how elements of trust and dignity as well as pricing seem to be lagging for these shoppers across the region.

[3] Argentina, Brazil, Chile, Mexico and Colombia

THE ANALYTICAL TOOLKIT HELPS TO IDENTIFY ACTIONABLE INSIGHTS BY SEGMENT

Shopper segmentation and interpretation



Output

- For each segment*:
  - profile and understand key needs
  - Identify most relevant store attributes valued
  - Evaluate strengths and opportunities of competing formats
  - Assess sweet spots for format development

* Reading can be done by country and by segment, depending on availability of representative sample

Source: CCRRC shopper interviews (2007/08), McKinsey

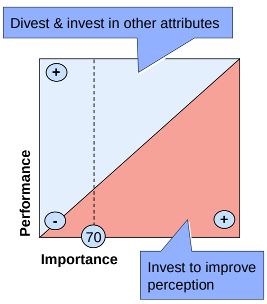
Exhibit – 5 THE IMPORTANCE PERFORMANCE MATRIX IS REACHED THROUGH THE CROSSING OF TWO QUESTIONS

BACKUP

Methodology

- Comparison of two sets of questions each with of 27 store attributes
- In the first question we asked consumers the **importance** of these attributes **when they choose the store** they shop groceries at
- In the following questions, we asked them to rate their level of **satisfaction related to their last shopping trip** for the same set attributes
- By **crossing** the top box (i.e. rated 5 on a scale of 5) **answers**, it is possible to build a **map** of relative strengths and opportunities
- A line was drawn at the **70 mark in importance**, as a way to focus actions only in **relevant attributes** (i.e. the ones to the right of the mark)

How to interpret the matrix



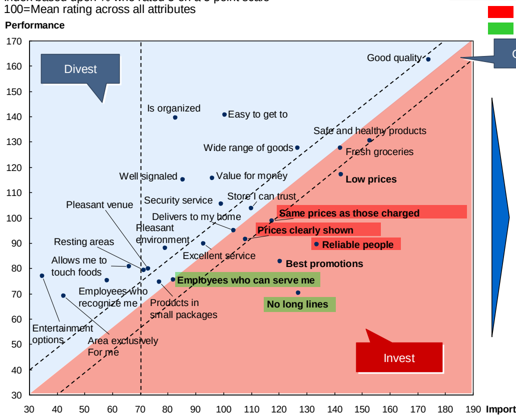
Source: CCRRC shopper interviews (2007/08), McKinsey

Exhibit – 6 EXAMPLE OF THE IMPORTANCE VS PERFORMANCE MATRIX

Comparison of Importance vs. Performance
Index based upon % who rated 5 on a 5 point scale
100=Mean rating across all attributes

Latin America

FINANCIALLY STRAPPED SKEPTICS



- **Lines and promotions are opportunities for improvement among retailers in general across all formats**
- **Offering good quality, safe, healthy and fresh products are important variables**
- **Entertainment options are not considered as important attributes**

Source: CCRRC shopper interviews (2007/08), McKinsey

The second analysis identifies future shopping behavior by asking consumers if adding certain store attributes would increase the enjoyment with their shopping trip; in addition, if consumers agree with a given statement, they are automatically asked if they would be willing to pay a little more so as to encounter that attribute in the store. This enables to rank the preferred attributes and also understand consumer's willingness to pay for them. *Exhibit 7* provides the example of the financially strapped segment. Beyond identifying the attributes that are most important for shoppers this tool can help prioritize specific actions to undertake within a format and also provide good insight into with attributes are less relevant for consumers (*Exhibit 8*)

Exhibit – 7 CUSTOMERS ARE WILLING TO SHIFT THEIR SPENDING AT STORES OFFERING CERTAIN DESIRED BENEFITS (1/2)

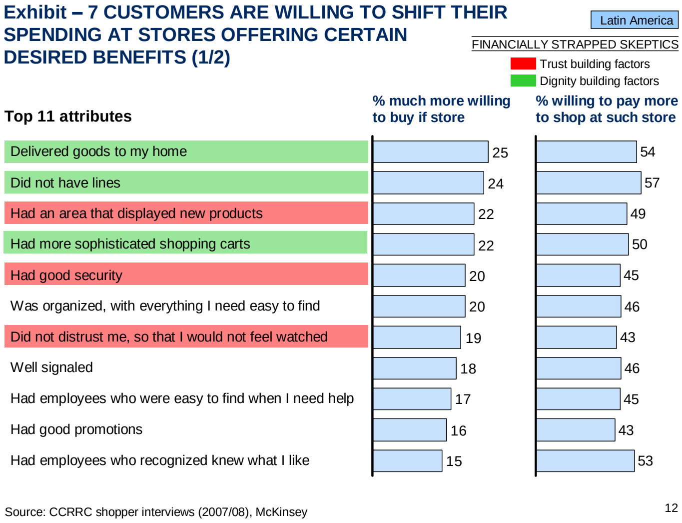
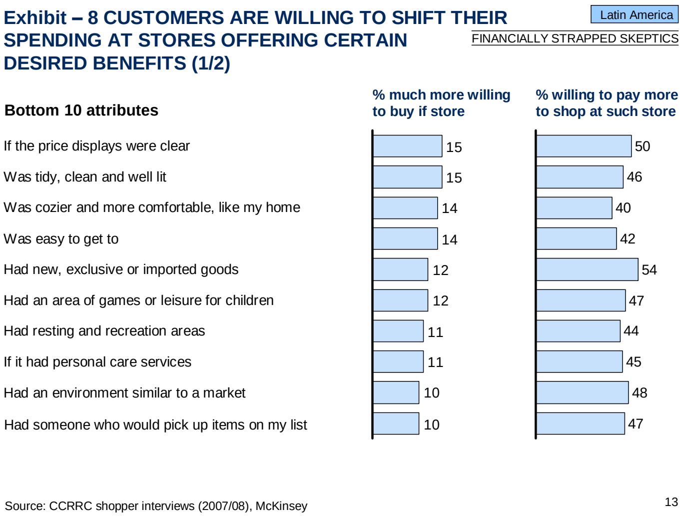


Exhibit – 8 CUSTOMERS ARE WILLING TO SHIFT THEIR SPENDING AT STORES OFFERING CERTAIN DESIRED BENEFITS (1/2)



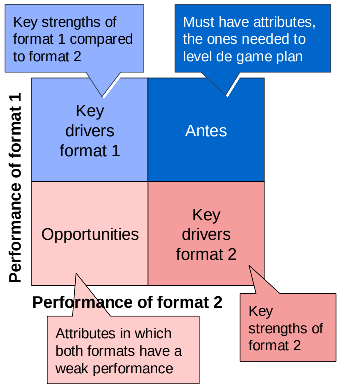
The following tool compares the performance of two distinct formats (e.g. supermarkets vs. hypermarkets, supermarkets vs. traditional stores) based on the same list of attributes used in the first analysis. It is an adaptation of the brand driver analysis applied to compare strengths and opportunities of two competing brands in a given category, commonly used by consumer goods companies as well as other marketing intensive categories (e.g. two brands of beer, luxury cars, etc.). In the context of retail, it allows to spot consumer preferences among formats and key opportunities to players focus on. (*Exhibits 9-10*) We believe that this analysis would provide extremely valuable when comparing the performance of specific retail brands that compete in the same format category.

Exhibit – 9 THE FORMAT PERFORMANCE MATRIX WAS REACHED LEVERAGING ANSWERS GIVEN FOR DIFFERENT FORMATS

Methodology

- Analysis based on **consumer evaluation** of a set of 27 **store attributes** (same ones used in the importance vs. performance matrix on page 29)
- The question **evaluated the performance** of 4 different formats (i.e. hypermarkets, supermarkets, traditional stores and convenience stores)
- The matrix is build by **crossing** the respondent's **answers** for each format (consumers have answered for one format only)
- Limits between **quadrants are determined** by the **average** for all attributes for both formats

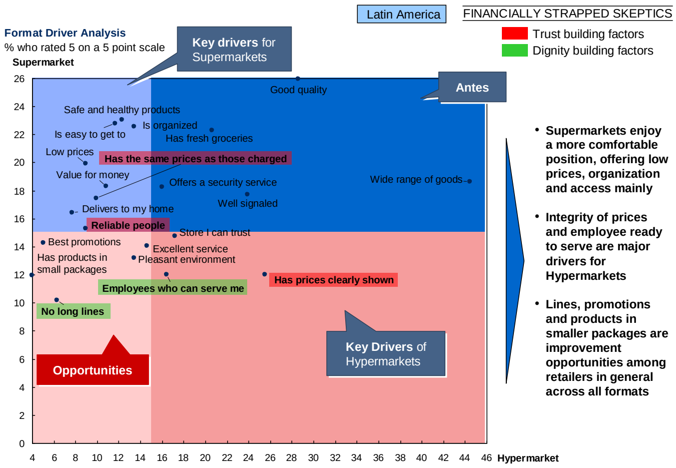
How to interpret the matrix



Source: CCRRC shopper interviews (2007/08), McKinsey

14

Exhibit – 10 SUPERMARKETS HAVE A CLEAR ADVANTAGE OF HYPERS



Source: CCRRC shopper interviews (2007/08), McKinsey

15

The fourth and final analysis is denominated perceptual map. Based on consumer response for different attributes by formats, it is possible to draw a two-dimensional map in which contrasting characteristics are opposed. Formats are then quantitatively positioned across the map – the relative location translates into its key strengths. The value of this tool is the ability to clearly recognize the current positioning of each format, as well as to identify white spaces in the retail arena. By linking the results back to the first analysis it is possible to understand which are primary drivers (i.e. the ones with a higher stated importance) and thus define the "sweet spots" for format development.

Insights into the “Belly of the Market”

Three themes appeared as being the most relevant across the region:

1) The Shopping Experience: Having a significant shopping experience is relevant to shoppers because going shopping is more to them than simply purchasing products. Given budget restrictions, food shopping is transformed into a key an entertainment option for the whole family. Consumers thus seek a more social and fulfilling experience, demand getting more services and options (e.g. food court, resting areas) when they go to a store and want a pleasant environment to enjoy what they are doing

2) Dignity: These shoppers realize the difficult position they’re in, based on their limited resources and for that reason they don’t need the stores they visit to reinforce this fact. They don’t want to be made feel as being poor, while on the other hand they want to be valued and respected as a customer and a contributor to their family, and don’t want to be left out of the experiences available to people that are better off. Another perspective points out to the fact that “belly” consumers spend most of their working time serving other people; while shopping this relationship is flipped and shoppers are empowered, having the store/product choice in their hands. So respect and service offers “dignify” consumers in that sense

3) Trust: A combination of consumer budget limitations, intense promotional levels and execution flaws has generated a strong sense of mistrust towards retailers. Shoppers don’t want to feel scammed in any way (e.g. finding different prices at the shelf and check-out, promotions of products about to expire), they want to have control over what they buy (e.g. tasting and smelling fresh products, avoidance of pre-packaged products). However, trust does not relate to a single factor or attribute, but to the whole value proposition. Establishing trust means also establishing loyalty and frequency

THE STUDY IDENTIFIED THREE COMMON UNMET NEEDS ACROSS LATIN AMERICAN COUNTRIES

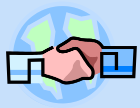
Experience

- Grocery shopping is one of the sole entertainment options for the mass market, given budget restrictions
- Shopping should be an enjoyable, fulfilling and relaxing experience for the whole family

Dignity

- Mass market lacks recognition and attention in their daily lives
- Shopping is a moment where they feel they have the right to be served
- Long lines, no in-store aid, few credit options, small spaces and paying for extra services reinforce their income constraints

Trust



- Consumers need to trust the retailers in order to be loyal
- Trust can be achieved through two main levers: products and price
- Consumers don't want to feel scammed by the stores where they shop
- Checking constantly if prices are correct and if products are fresh are main stress causes

Source: CCRRC shopper interviews (2007/08), McKinsey

4

Besides these major issues, other themes also showed to be relevant to these consumers:

- Convenience- A struggle was determined between the desire to experience the variety and organization of hypermarkets and the difficulty in accessing to them. Consumers would like to be able to solve all their problems while doing their shopping

- Search for value- Given their monetary restrictions and the importance of food in their monthly budget, value for money is always a relevant theme. Promotions are highly valued and a trigger for store selection

- The influence of others in the shopping trip- Husbands and children often present at the shopping trips tend to be a burden. Husbands question the importance of purchased products and children ask for additional items

- Relationship with technology- They have not been able so far to capitalize internet's potential, but they see their lives and shopping experience related to the internet in the future.

Relevance of the insights

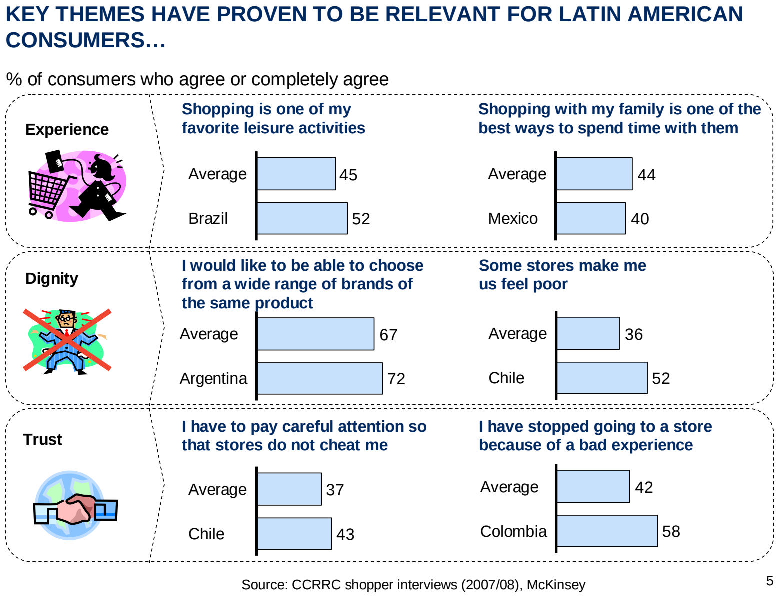
All themes proved to be relevant across the region, with some being stronger than others and a clear variation between countries that was analyzed in the second phase of the project.

When looking at the desire of having a fulfilling shopping experience, results show that 45% shoppers in the region agree or completely agree[4] that shopping is one of their favorite leisure activities. Another 44% state that going shopping with their families is one of the best ways to spend time with them – in Colombia, the percentage for the same questions reaches an astonishing 72%. Finally, on average 71% prefer to shop with their children.

With the same intensity, the theme of dignity also revealed to be present among "belly" consumers in the region. 60% of shoppers agree that they would rather shop at a store that offers a wide variety of goods or different qualities and prices, even if they will never buy any of them and 67% agree that when they go shopping, they would like to choose between a wide range of brands for the same product. This indicates that a store with only low end products is not the ideal, as choice is highly valued and not having it reinforces their income disadvantage. In that sense, on average 36% agree that some stores make them feel poor – in Brazil the share is much bigger: 52%.

The importance of trust was identified among different attitudes. 37% of consumers stated that they have to pay careful attention so that stores do not cheat them (reaching 43% in Chile); 42% have stopped going to a store because of a bad experience (with 73% of consumers agreeing that rude or unhelpful staff was the key driver of dissatisfaction); and 28% stated that some of the products in retailers they shop are very unsafe (reaching 36% in Colombia).

[4] All percentages that describe consumer behavior refer to the share of respondents who agree or completely agree with the given statement in the region



Finally, the results also show the relevance of other aspects:

- Convenience: 40% believe it is worthwhile spending a little more to shop were it is closer and 35% spend as little time as possible shopping for food as they have more important things to do
- Search for value: 45% state that for most product categories getting the lowest price is very important, even if it means going out of their way
- Influence of others in the shopping trip: 50% agree that they spend more money when they take their children to shop with them
- Technology: 27% consider that they will buy over the internet in the next 5 years vs. an average of 7% that currently purchase through this channel

Dignity and Trust: the key findings

Based on the factors identified, a proper evaluation of the retailing experience of these consumers in Latin-America needed to factor an additional characteristic/lever into the conventional retail pentagon.

Traditionally, retailers look at 5 dimensions when trying to define the relationship between a specific retailing format and their target shoppers:

a. Price.- Appropriate value for product offer at every tier in range, fair prices clearly and consistently communicated

b. Merchandise authority.- Distinctive product selection that gives customer a clear "point of view" on what he/she should buy

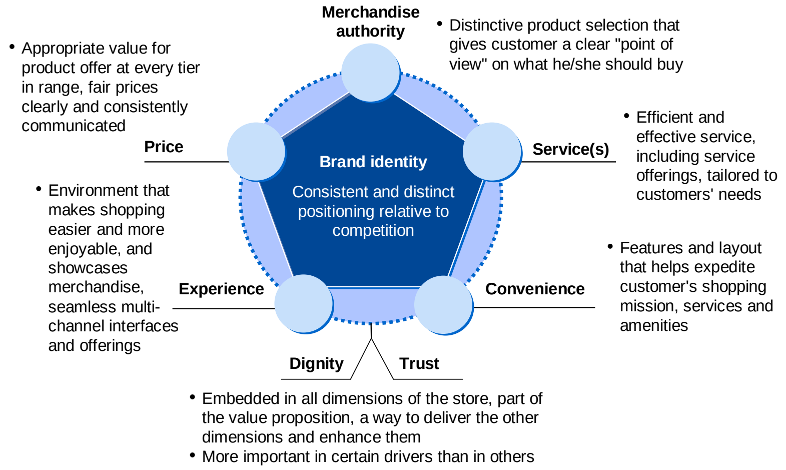
c. Service.- Efficient and effective service, including service offerings, tailored to customers' needs

d. Convenience/location.- Features and layout that helps expedite customer's shopping mission, services and amenities

e. Environment that makes shopping easier and more enjoyable, and showcases merchandise, seamless multi-channel interfaces and offerings

Our findings take us to believe that beyond price, merchandise authority, convenience/location, service and experience, retailers need to think about trust and dignity when targeting these consumers. Trust and dignity are built across the 5 elements of the retail framework and should be perceived as the result of an execution that generates both. For example, in terms of service, trust is created by having high touch and personalized service, by knowing individual consumer preferences and suggesting products, while dignity is transmitted by giving a feeling of being served, respected and valued.

BASED ON UNMET NEEDS OF LATIN AMERICAN "BELLY OF THE MARKET" CONSUMERS, A NEW DIMENSION WAS ADDED TO THE RETAIL PENTAGON TO UNDERSTAND THEIR RELATIONSHIP TOWARDS RETAILERS



Source: CCRRC shopper interviews (2007/08), McKinsey

6

Segmenting the consumer

In order to translate these findings into an actionable agenda for retailers, the project concentrated in how these preferences and needs may vary among the different shopping formats.

Shopping towards leisure, acceptance and preference of large formats, value of convenience, orientation towards quality and branded products, price consciousness and skepticism/mistrust are the factors that statistically most strongly differentiate consumers. The attitudinal segmentation process uncovered 5 relevant and differentiated segments within the belly of the market, each one with more emphasis towards some of the relevant attitudes identified in the region.

Based on this we defined 5 different segments to describe the different “belly of the market” shoppers:

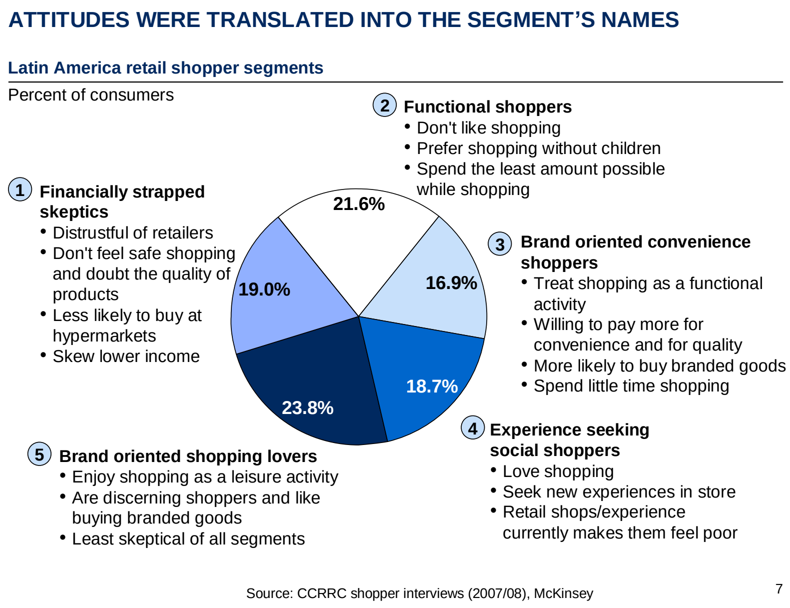
1. Financially strapped skeptics – Lower end consumers, do not trust retailers in terms of safety and services

2. Functional shoppers – Functional shoppers, want to spend as little time as possible shopping

3. Brand oriented convenience shoppers – Willing to pay more for convenience and reliable brands

4. Brand oriented shopping lovers – Love shopping; look for high quality brands

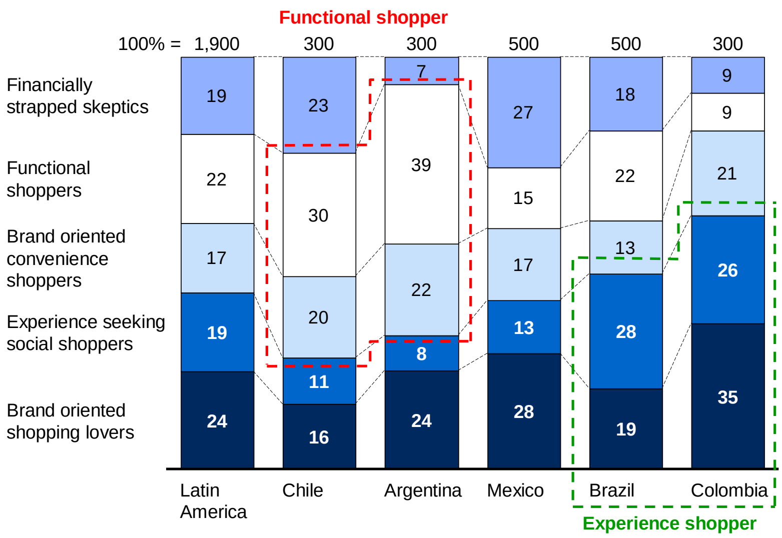
5. Experience seeking social shoppers – Look for a fulfilling shopping experience with the whole family



The presence of these groups varies across the region and within each country, reflecting to some extent the local culture, evolution of retail formats and orientation towards shopping. In that sense, Chile and Argentina have a more functional orientation towards shopping while Brazil and Colombia are more focused on experience. Mexico lies in the middle in terms of function vs, experience but is clearly more skewed towards price sensitivity and skepticism.

Each of these segments cares differently about the key factors that define them and retailers should use different levers to target them effectively. The retail pentagon is a powerful tool to help shaping specific strategies for each segment, for example: brand oriented convenience shoppers demonstrate a clear preference for two levers – merchandise authority and convenience. So retailers seeking to address this segment need to shape their formats around (i) an assortment that always carries established brands (ii) and access. If they succeed in doing so, consumers will be willing to pay more to have that trade-off.

DISTRIBUTION OF SEGMENTS ACROSS COUNTRIES



Source: CCRRC shopper interviews (2007/08), McKinsey

8

The same rationale can be applied to each of the 5 segments, depending on the current format portfolio and the corporate medium term strategy. Nevertheless, some key beliefs of the retail pentagon cannot be ignored when going through this process:

1. Differentiation: To be successful a retailer needs to be famous for something
2. The value proposition can be truly distinctive on only one or two dimensions
3. Whatever the proposition, the role of price must be clear
4. Industry baseline standard must be achieved on all dimensions

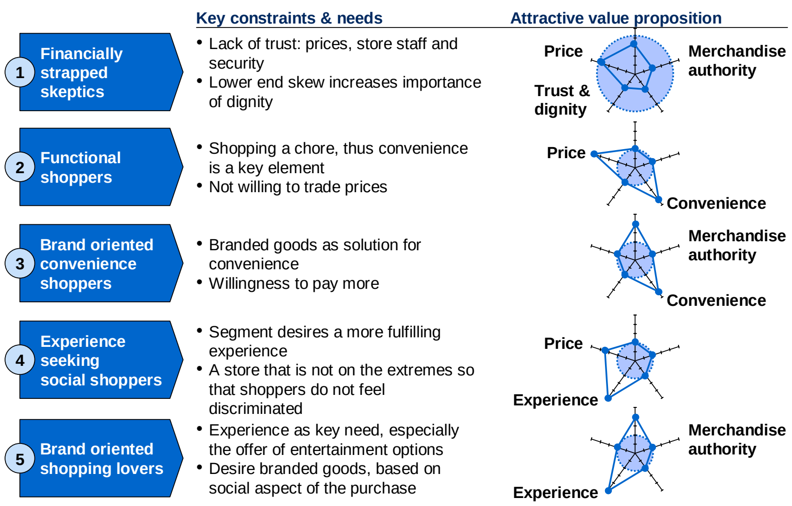
Using the described toolkit and applying the perceptual map, we intend to recognize the current positioning of each format, as well as identify white spaces in the retail arena. By linking the results back to the first analysis it is possible to understand which are primary drivers (i.e. the ones with a higher stated importance) and thus define the "sweet spots" for format development.

For example,

Financially strapped skeptics are lower end consumers, which spend on average less on food, have a lower car ownership and who show a strong skew towards being less loyal and distrusting retailers. From their perspective the analysis shows that retailers are missing the mark on having shorter lines and reliable staff, offering both low and consistent prices and good promotions. When looking beyond the simple meaning of the attributes, it is possible to spot a correlation between the characteristics of the segment: shorter lines is related to dignity; low prices and good promotions to their lower end skew; and reliable staff and prices can be translated into the lack of trust. These people also believe that home delivery, short lines and availability of a display area to try and test new products are relevant elements of innovation to have. Again, when looking on what lies behind these attributes, the themes of access problems, dignity and trust can be respectively spotted.

Brand oriented shopping lowers on the other hand see the world differently and value a distinct set of attributes, looking more for experience than trust building factors. Having excellent service is an example of a relevant attribute that stores currently underperform and consumers look for new elements such as security service, leisure areas for their children and new/imported products and brands.

KEY INSIGHTS BY SEGMENT



Source: CCRRC shopper interviews (2007/08), McKinsey 16

We believe that the insights derived from this study through the analytic toolkit provide a different lens to look at shoppers and define formats that address their needs. The Exhibit above summarizes the most relevant insights for each segment across Latin America based on the entire methodology.

ALTHOUGH LOOKING AT AVERAGE NUMBERS IS MISLEADING, COUNTRIES SHOW COMMON TRAITS IN TERMS OF CONSUMER NEEDS

	Key drivers	Current needs	Future needs
Overall LatAm	• Good and fresh products	• Shorter lines / waiting time	• Area to test new products • Security service
	• Easy to get to	• Reliable staff • Store I can trust	• Clean and tidy stores • Air conditioning
	• Safe/trustworthy products	• Prices clearly shown • Security service	• Sophisticated shopping carts • Don't feel watched while shop
	• Wide range of goods	• Prices clearly shown • Organized	• Clean and tidy stores • Sophisticated shopping carts
	• Wide range of goods	• Prices clearly shown • Excellent service	• Home delivery • Sophisticated shopping carts
	• Safe/trustworthy products	• Prices clearly shown • Store I can trust	• Organized • Sophisticated shopping carts

Source: CCRRC shopper interviews (2007/08), McKinsey

17

Finally, we can offer a perspective at a country specific level highlighting the most relevant drivers, current needs and future needs that retailers may explore further in order to develop appealing formats, tuned to the specific segment needs.