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THE UPSIDE OF DOWNSCALE:

Marketing to low-income US food consumers in the decade ahead

Management Summary

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Who are low-income consumers?

- On aggregate low-income consumers belong to households earning less than **$35,000 per year.**
- It is at approximately this level that two significant changes in food consumption and purchase behavior occur:
  - Households are almost universally food secure
  - Expenditures on food away from home begin to increase
- Since larger families can take advantage of economies of scale, we use poverty guidelines to establish income thresholds by household size.
  - Example: 20 million people in 4-person families earning <$42,500/year would be considered "low-income" in our study because their household income is under 250% of the poverty level.

Income thresholds by household size

Number of people	Income
1	$22,499
2	$27,499
3	$34,999
4	$42,499
5	$49,999
6	$57,499
7	$64,999

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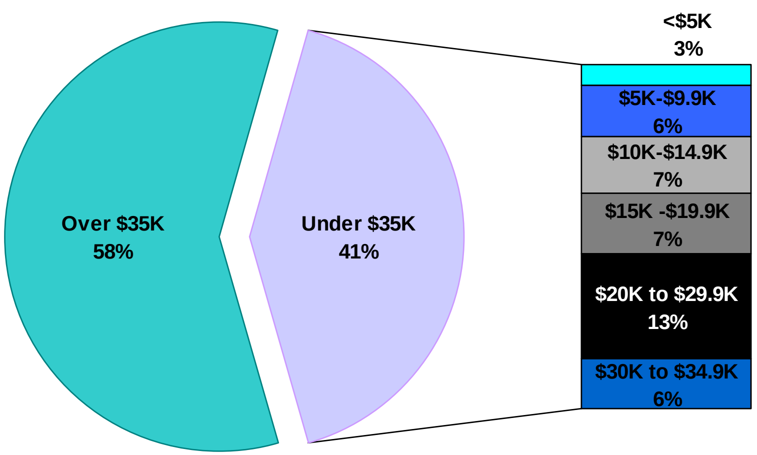
Market power of low-income consumers today

- **How big is the group?** – Low-income consumers represent approximately 45 percent of consumers. Over one-third have household incomes below $20,000 per year.
- **What do they buy?** – Purchases by low-income shoppers represent about 41 percent of retail food sales. Low-income consumers spend the most on meats, poultry, fish & eggs (26 percent) and fruits and vegetables (17 percent). Compared to consumers overall, low-income consumers spend more on fats & oils.
- **Where do they shop?** – Like most Americans, low-income consumers buy their foods primarily from supermarkets. They are, however, more likely to use alternative retailers (small grocers, convenience stores, drug store, etc.) for regular grocery shopping.

Share of Aggregate Food At Home Expenditure by Income (Before Taxes)



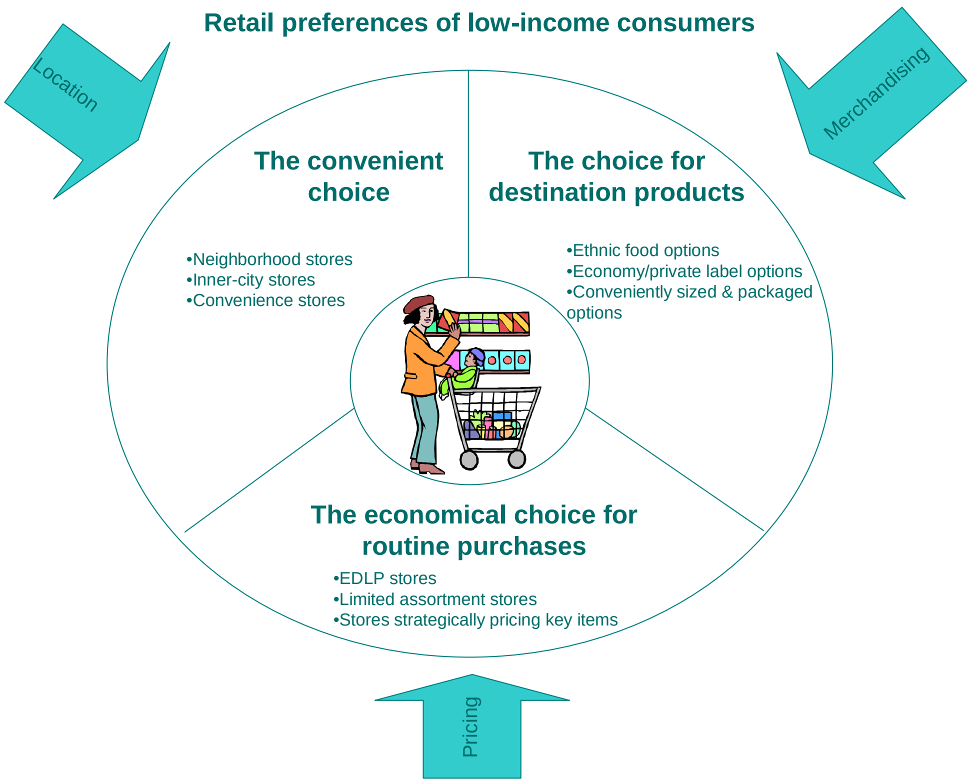
Source: PROMAR *International* estimates based data from the U.S. Bureau of Labor, 1998

Who are the low-income consumers?

- **Race** – Low-income consumers are disproportionately black and Hispanic.
- **Education** – While the bulk of low-income consumers are high school graduates (71 percent), they are 90 percent more likely to have less than a ninth grade education and 55 percent less likely to have earned a bachelors degree.
- **Residence** – Low-income consumers live disproportionately in the South and in metropolitan centers.
- **Household size and composition** – Low-income households are smaller than households overall. Non-traditional households – especially households headed by women– are particularly prominent.
- **Age** – Households headed by seniors and young persons are disproportionately represented in the low-income category. Low-income householders are 56 percent more likely to be headed by persons under the age of 24 and 60 percent more likely to be headed by seniors.

Food industry practices: Retailers

- To attract low-income consumers, retailers compete on the basis of convenience, value, and variety.
- Over time, pricing, merchandising, and location choices have made certain retail channels and store formats more appealing to low-income consumers.
- Supermarkets face particularly strong competition for low-income dollars from mass discounters (Wal-Mart, Costco, etc.) in suburban areas and from smaller stores (convenience, drug, and specialty stores) in urban areas.



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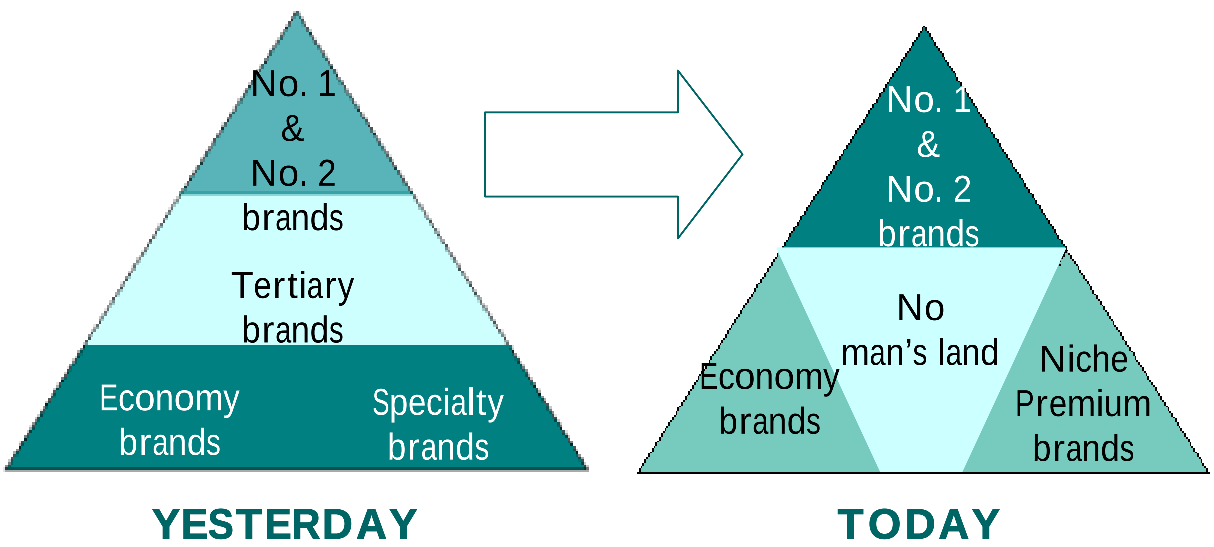
Food industry practices: Manufacturers and marketers

- **Food companies** currently operate within the context of product polarization where "middle ground" mass brands are increasingly losing share to economy and premium alternatives.

EROSION OF MASS MARKET BRANDS

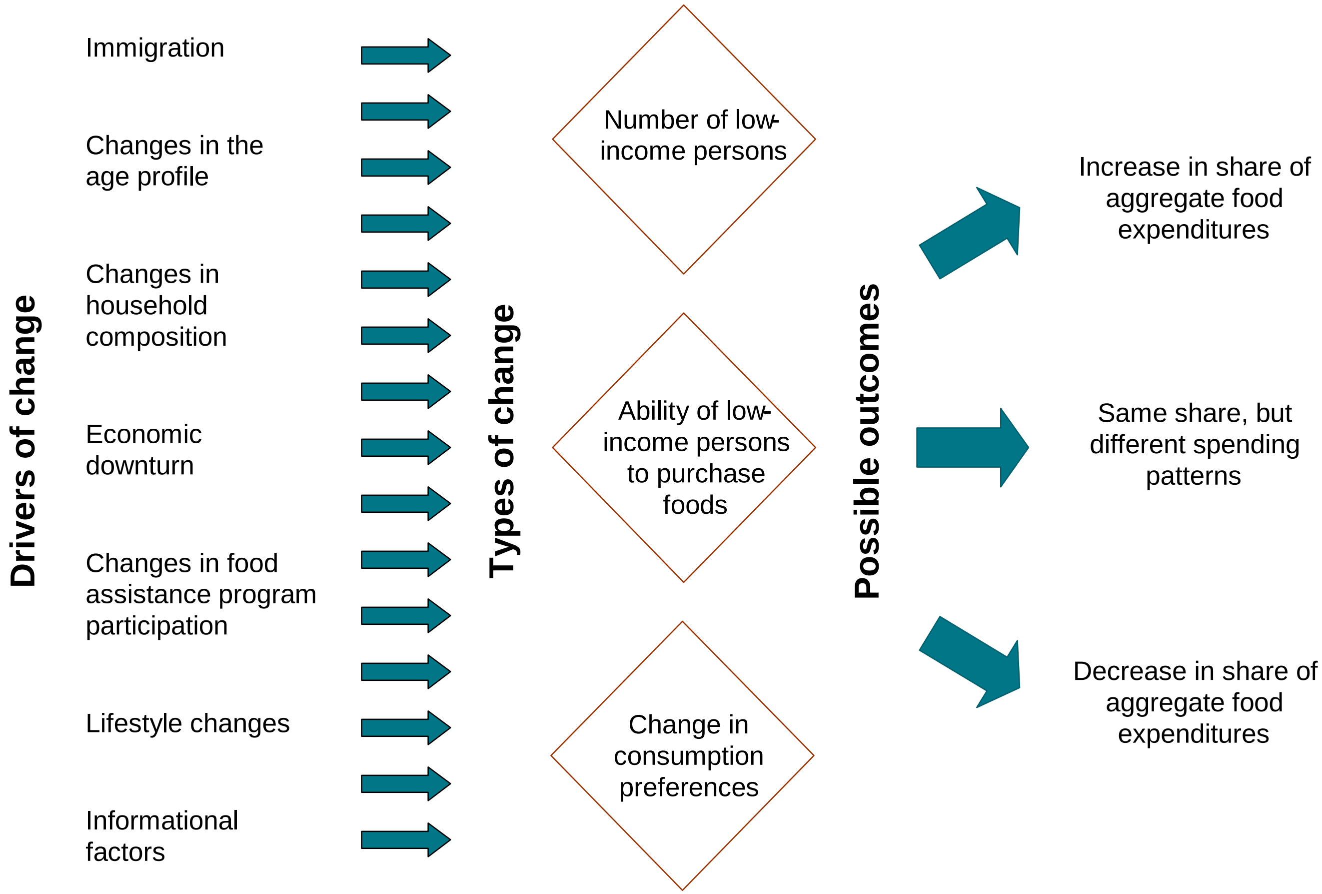


Food industry practices: Manufacturers and marketers

- **Beyond price:** Food companies have successfully appealed to low-income consumers at many different price levels. Key characteristics of these appeals include:

Positioning	Options/strategy	Dominant value points	Low-income draw
Economy	Value brands	• Value for money	Low-income consumers are more price sensitive than other consumers
Niche	Ethnic brands	• Familiarity • Authenticity • Variety	Low-income consumers are more ethnically diverse than consumers overall
Mass	Heritage brands	• Comfort • Status	Low-income consumers are more brand loyal than consumers generally

What will affect low-income demand for food over time?



How will demographic forces change how food manufacturers approach the low-income market?

- Profound demographic changes at work today will make the population older, browner, more urban, and with a more fluid family structure a decade from now.

Impact:

- Manufacturers of mainstream branded food and beverages must abandon their excessive focus on young suburban families given the growing importance of low-income consumers to their business.

- Food/beverage companies will need to understand—and address—the expectations of older and more diverse consumers and families in order to succeed in the future.

Beyond dollars and cents: How will Income inequality and anxiety affect the behavior of low-income consumers?

- **Income anxiety:**
  Income anxiety among low-income consumers is likely to increase in the future as large segments of the population face the prospect of permanently lower income in retirement and as the social safety net continues to fray.
  Impact:
  Value will continue to be important even as comfort, indulgence and health emerge as key concerns among older Americans across income levels.

- **Income inequality:**
  Growing income inequality even amid prosperity will lead to the emergence of a *struggling* class of consumers alongside the truly poor.
  Impact:
  One outcome of this will be a change in the role of status in food/beverage purchase decisions. While some low-income consumers will continue to embrace status as a way to cling to the middle class, others will consciously embrace quality and value over status and style.

How will changes at retail affect the approach of food manufacturers toward low-income consumers?

Retail consolidation:

- Retail consolidation will continue in the supermarket industry even as alternate outlets continue to claim a larger share of overall food sales.

Impact:

- Manufacturers can expect continued margin and brand squeeze from fewer, larger and more powerful players but some can find new distribution opportunities outside the traditional supermarket.

Urban store development:

- Supermarkets are becoming more serious about returning to the inner city as urban revitalization continues (and suburban competition increases). Gentrification of some urban areas may eventually displace some current low-income residents, however.

Impact:

- Food/beverage manufacturers may be able to reach low-income urban consumers more effectively than in the past and should prepare to seize these opportunities while they last.

How will food assistance policy change over time?

Two paths emerge for the direction of future food policy reform:

- **First,** in the absence of either a significant economic decline or political consensus concerning the proper direction of food policy, change is likely to be small, incremental, erratic and largely procedural.

Drivers	Pace of reform	Program application	Impact on LI demand
• Economic status quo • Political stalemate	Incremental	Procedural changes to: • Reduce costs • Alter the role of private players • Change what foods are covered	Minor changes in • Where LI consumers shop • What types of foods they buy
• Economic downturn • Political consensus	Dramatic	Increase funding, broaden participation OR Decrease funding, cut programs	Increase demand OR Decrease demand

- **A second** scenario assumes either an economic downturn or a major shift in political thought. Here we would expect to see major reforms in food assistance programs, including but not limited to the creation or dismantling of programs, changes in eligibility criteria, and changes in how the programs are funded.

How will changes in food assistance policy affect low-income consumers?

Welfare to work:

- Increased employment among the poor during the current economic boom does not necessarily mean increasing food budgets among these consumers.

- While tax breaks for the working poor have helped keep money in their pockets, changes in the Food Stamp Program to reduce or discourage participation may have more than offset these gains.

Impact:

- Dramatic declines in food stamp enrollment and benefits have led/will lead to a projected $5 to $10 billion decrease in retail food sales between 1997 and 2002.

- Food stamps extend food budgets among families at the bottom of the income scale, and reductions in food stamp outlays have meant that many low-income consumers have reduced food consumption and/or shifted to cheaper foods.

How will changes in food assistance policy affect low-income consumers?

WIC:

- The nutrition-oriented WIC program (for women, infants, and children) has resulted in better nutrition for program participants in the past. Attempts to change the nature of WIC-approved foods, however, have had mixed results.

Impact:

- Efforts to reduce the cost of infant formula succeeded in bringing costs down, but in the process transformed the sector into a low-margin business, narrowing the field of manufacturers.
- Other changes, such as including more convenient canned beans in addition to dry beans may have a more positive impact.

How will changes in food assistance policy affect low-income consumers?

School Lunch Program:

- Unlike food stamps and WIC, the National School Lunch Program has expanded significantly in recent years.
- Serving a wider population (beyond low-income consumers), the school food program may open significant opportunities for branded food and beverage companies in the future.

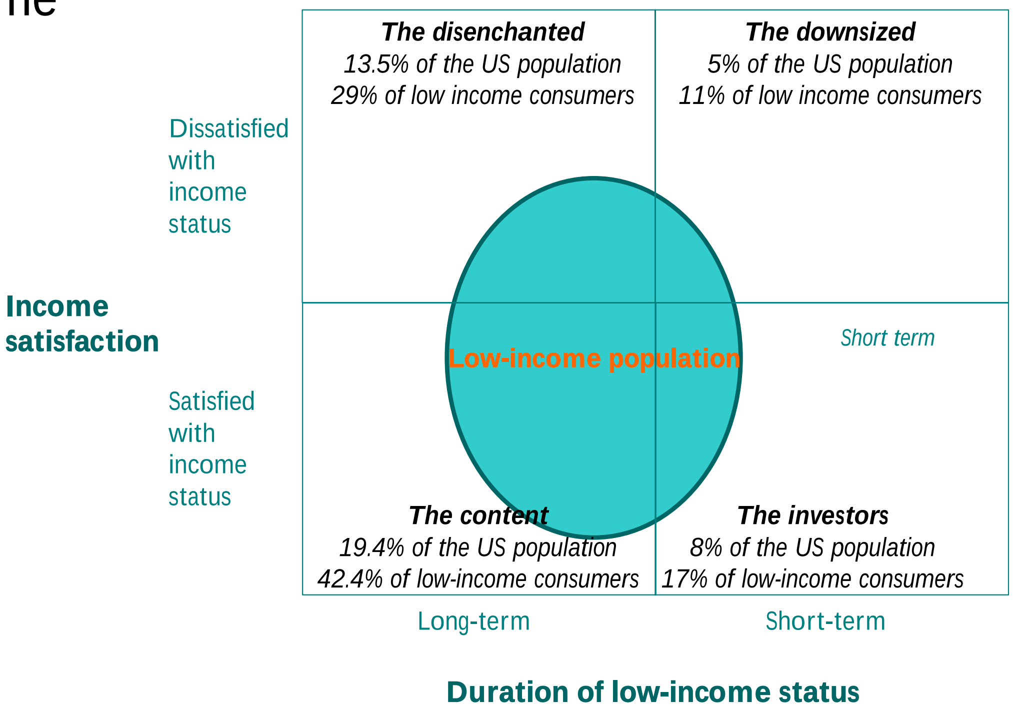
Impact:

- Key areas of opportunity include greater distribution of branded items, greater interest in highly nutritional foods, and access to other dayparts, such as breakfast and snacks.

Consumer model

- How low-income consumers view their financial future often dictates what foods they consume, where they buy their food, and how they economize on foods.

- We can group today's low-income population into four consumer types based on their financial outlook:
  - the **Content**,
  - the **Disenchanted**,
  - the **Downsized**, and
  - the **Investors**.



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Consumer types

- **The Content** accept their low-income status. The Content recognize that their incomes are unlikely to increase dramatically during their lifetimes and they are okay with it. So while they do not consider themselves wealthy and perhaps would not mind a few more luxuries, they do not see themselves as low-income or disadvantaged either. Rather, they look to a narrower reference group and find that they are doing as well as their peers and are better off than their parents.

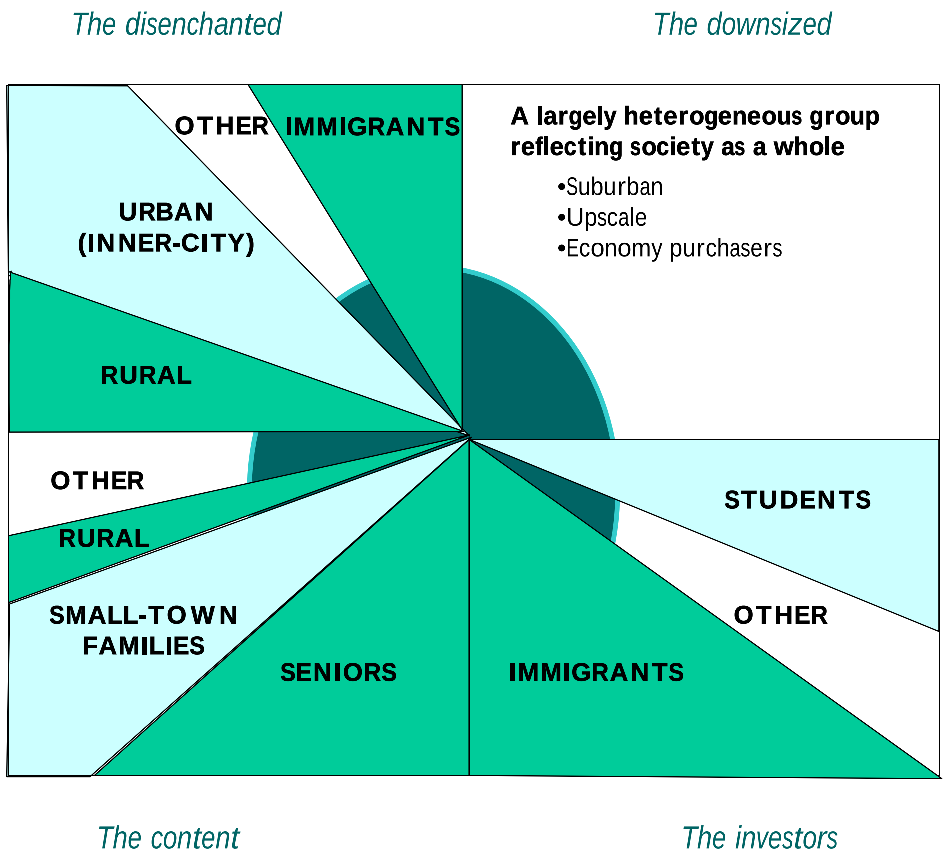
- The attitudes and perspective of **the Disenchanted** most resemble popular conceptions of what it means to be low-income. And while incomes among the Disenchanted can range considerably, it is this consumer type that has the largest share of consumers living in poverty and worried about food security.

- **The Downsized** consist of persons who are experiencing an involuntary (and presumably) temporary decline in income. Economic conditions determine the size and scope of this group.

- **The Investors** view their present low-income status as an investment in their future. Investors are reasonably satisfied with their lot in life which they believe will include better wages tomorrow. Typical Investors include new immigrant, students, and recent entrants to the workforce.

How do demographic variables relate to low-income consumer types?

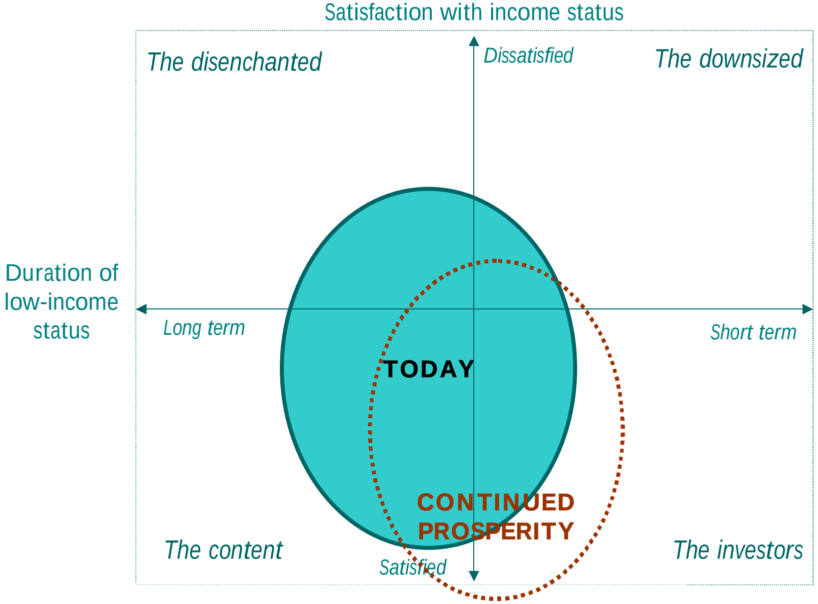
- While key demographic clusters of consumers transcend low-income consumer types, there are some associations between demographics and our consumer types.



How will low-income food expenditures change over time?

- Macroeconomic conditions will shape the financial expectations of low-income consumers, and consequently the representation of our consumer types.
- **Continued or broadened economic prosperity** will increase the financial opportunities available to all consumers and reduce the number of low-income consumers.
  - The number of Investor low-income consumers will swell as more jobs are made available to the chronically poor and underemployed.
  - The Downsized will be better able to find new jobs, and the Content are likely to raise their long-term expectations as they see new opportunities within reach for their families.

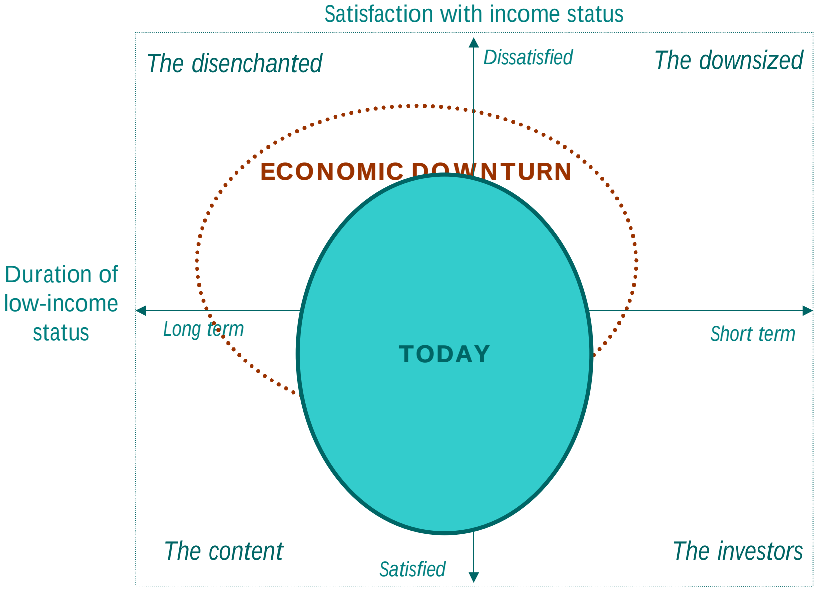
Impact on low-income consumers: Economic growth



How will low-income food expenditures change over time?

- An **economic contraction** would lead to a larger low-income population.
  - More low-income consumers will view their income status as long-term or permanent.
  - More people will become dissatisfied with their economic lot.
  - The ranks of the Disenchanted will swell as the Downsized and Investors grow more pessimistic about their long-term prospects.

Impact on low-income consumers: Economic downturn



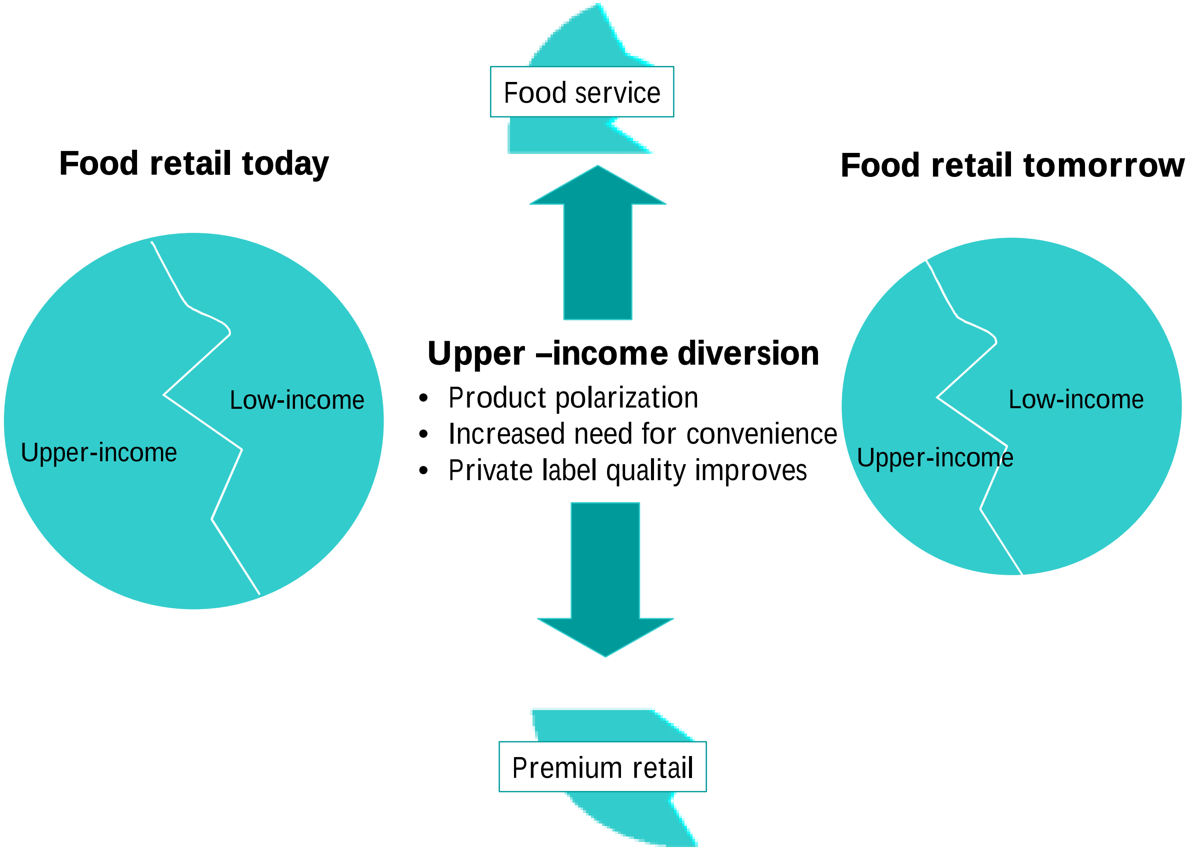
How will low-income food expenditures change over time? Demographic considerations

- Demographic changes will also influence the size and composition of tomorrow's low-income population.

Force for change	Population increased	Likely consumer type
Changing age profile	Seniors and retirees	Disenchanted
		Content
	Students and new graduates	Investors
Changing family structure	Single parents	Disenchanted
		Downsized
		Content
Government assistance reform	Low-income workers	Disenchanted
		Investors
Shifting immigration	Minority households	Disenchanted
		Investors

How important will low-income consumers be to food companies in the decade ahead?

- Over time low-income consumers will become more relevant to branded food companies. In the decade ahead, as upper-income households are increasingly drawn to foodservice and premium products, low-income consumers will become a more important portion of retail food sales.



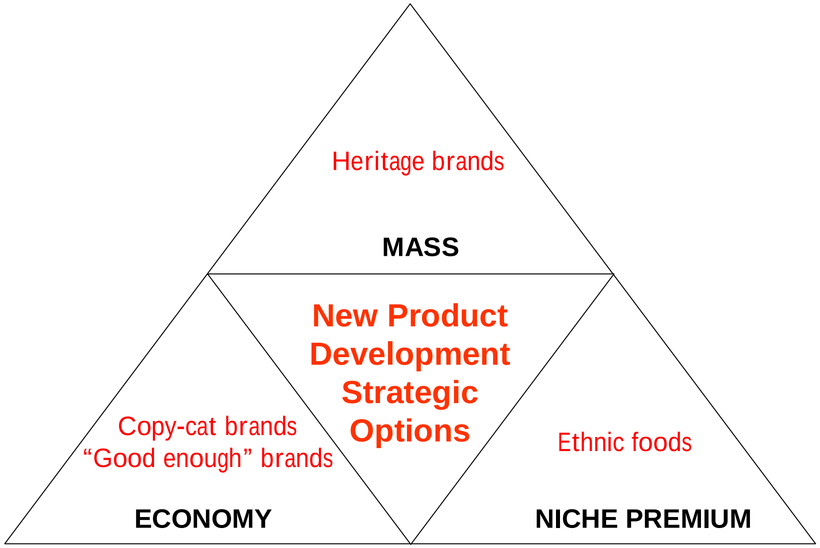
Approaches to targeting low-income consumers

- How a company chooses to approach the low-income market will depend on:
  - The price point distribution of their brand portfolio and
  - Whether their brands are growing or declining in terms of category share.

- Opportunities for reaching more low-income consumers present themselves in:
  - New product development,
  - Communication, and
  - Distribution.

Strategies: New product development

- The shopping basket of low-income consumers is diverse with products from every price bracket and every product category. However, certain classes of foods have a particular resonance with low-income consumers. Food companies that wish to develop products that target low-income consumers should look to these classes for examples of successful product innovations.
- Among economy options, food companies should concentrate on either developing less expensive alternatives to leading brands (copy-cats) or products that satisfy basic value points (good-enough brands).
- At the premium level, companies should concentrate on ethnic foods. Since authenticity is very important to immigrants among low-income consumers, mainstream companies should consider acquisition as opposed to internal development.



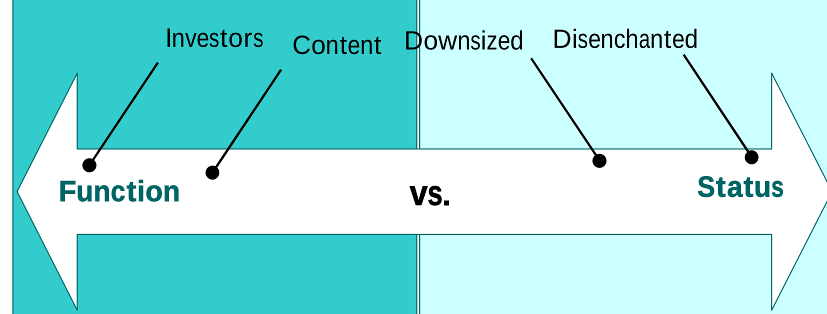
Strategies: Communication

- **Finding the right message:** No one message will resonate with all low-income consumers. In addition to looking at our low-income consumer types, food companies will have to address the underlying demographic and lifestyle factors of low-income consumers

- **Allocating resources:** Given the variety of tastes and expectations low-income consumers have, it may be best to devote communication resources to appealing to subgroups of low-income consumers rather than supporting specific products.

- **Tracking change:** Depending on the consumer type in question, companies will need to monitor economic trends, food policy reform, mobility and immigration patterns in order to anticipate shifts in the outlook and expectations of low-income consumers.

Communication strategies and consumer types

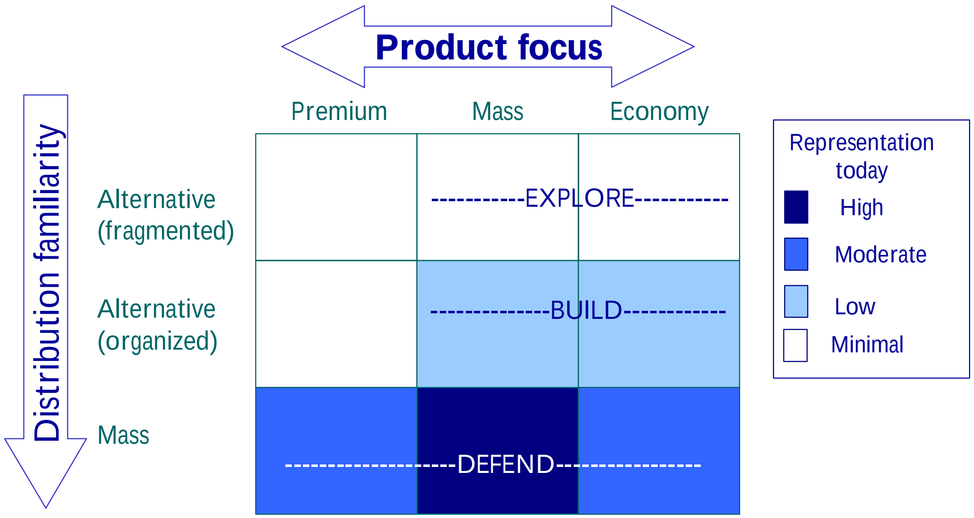


Advertising emphasis:	Usage advertising	Image advertising
Key message:	Nutritious & convenient mea	Reward, treat, “little indulgence”
Imagery/theme:	“Smart Shopper”	Relevant aspirational imagery

Strategies: Distribution

- To better analyze where food companies are currently selling and how this will change in the decade ahead we have grouped the various store formats that sell groceries as follows.
  - **Mainstream** Primarily chain supermarkets and some larger independent and affiliated grocers
  - **Alternative organized** Chain drug stores, convenience stores, dollar stores and mass discounter
  - **Alternative fragmented** Small independent grocers and specialty stores.

PRESENCE OF THE LEADING BRANDED FOOD COMPANIES



Strategies: Distribution

- Overcoming format constraints: For companies hoping to increase their outreach to low-income consumer through distributors, finding retailers that successfully serve low-income consumers will be key. Companies can look to the following approaches:

Leveraging company resources	Many food companies can look to their experience in distributing their non-food products through alternative retailers such as drug stores and convenience stores.
Marketer to marketer cooperation	Companies with limited access to alternative retailers may wish to form strategic alliances with more experienced food companies.
Partnering	Food companies can work with traditional retailers to support/develop programs targeting low-income consumers and expand activities in inner-city stores.
Packaging and other accommodations	Many retailers who do not normally sell many food products face considerable space and logistical constraints. Food companies can build relationships with these retailers by working with them to overcome or accommodate these constraints.
Work with wholesalers	As more wholesalers recognize the importance of distributing to low-income areas, food companies would do well to build on these relationships.

Prospects by product category

- Snacks and frozen foods are poised to grow most among low-income consumers, while dairy and bakery products will likely only experience marginal gains at most.
- Using a five star scale (1=low, 5 = high) we have denoted the relevance for the following basis of competition for each product category.

		All food and beverages	Bakery	RTE Cereal	Non-alcoholic beverages	Frozen foods	Dairy	Snacks
Overall		☆☆☆	☆☆	☆☆☆	☆☆☆	☆☆☆☆	☆☆	☆☆☆☆1/2
Consumer points of value	Price	☆☆☆	☆	☆☆☆	☆☆☆☆	☆☆	☆☆☆☆	
	Convenience	☆	☆☆☆☆	☆☆☆☆☆	☆☆☆☆☆	☆☆	☆☆☆☆☆	
	Indulgence	☆☆☆☆	☆☆	☆☆	☆☆☆	☆☆☆	☆☆☆☆	
Sector readiness to meet low-income needs	Willingness to innovate	☆	☆☆	☆☆	☆☆	☆	☆☆☆☆☆	
	Strength v.s non-branded competition	☆	☆	☆☆	☆☆☆	☆	☆☆	
	Distribution	☆☆☆	☆☆☆☆	☆☆☆☆☆	☆☆	☆☆☆	☆☆☆☆☆	