Winning operating models

How the best-run consumer goods companies are preparing for the future by building a bridge between strategy and organizational design

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Whether a consumer goods company is regional or global, selling toothpaste or yogurt, most executives are struggling with the same set of questions. Do our winning ideas and innovation travel fast enough across brands and geographies? Are country, category and capability structures and processes defined in a way that makes it simple to repeat winning routines? Have we taken advantage of our scale in a way that still keeps important decisions close to the consumer? Are we doubling down where we want to be best in class and cutting back where we want to be best in cost?

These are questions consumer products executives have been asking for decades, but now the need is more urgent than ever. Never before have companies faced such pressure to deliver new products to market so quickly—at a time when their organizations have never been more complicated and slower to act. New brands, new geographies, new cross-functional committees, new centers of excellence—and more—sound right as incremental improvements, but in aggregate they add the risk of expensive duplication, inconsistency, delay and complexity. And while consumer goods companies have long been lured by the prospects of growth in developing markets, they're now seeing the opportunities for real profits there—but finding they're not organized to win (see sidebar, "Is your operating model working?").

Many consumer goods companies are quickly coming face-to-face with the reality that the ways they've built their success over the last two decades won't serve them now. They're finding their investment in talent and capabilities to be in the wrong geography or focused on the wrong customers and consumer segments. They're questioning where and how the most critical work gets done and discovering that even the best strategies rarely succeed without the right operating model in place.

It's why Procter & Gamble (P&G) moved the headquarters of its skin care, cosmetics and personal care business from Cincinnati to Singapore. The consumer goods company sees the biggest opportunities for growth in these segments in Asia. It's why Goodman Fielder, a manufacturer of food ingredients and consumer-branded food and beverages, integrated its baking, dairy and home ingredients businesses in New Zealand to improve its customer relationships and capture efficiencies of scale. It's why Reckitt Benckiser reshuffled its geographic reporting lines—the company no longer is organized by contiguous geography but rather by market type: developed versus developing. And it's one of the reasons why Kraft Foods split up to help its snacks business make inroads into emerging markets. Beyond the headlines, firms are wrestling with the complicated issues of decision making, talent and structure.

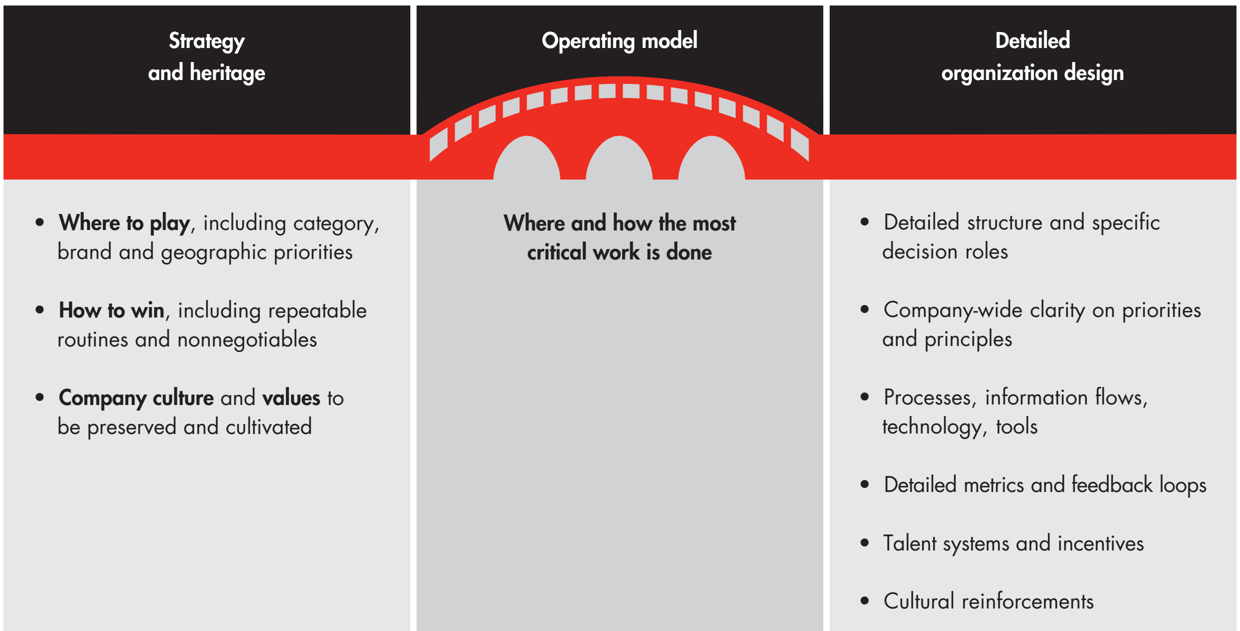
Consider the situation facing one company. It strived for nearly a decade to become truly global in scope, taking advantage of new growth opportunities in emerging markets. Yet even 10 years into that effort, it still struggled to align its resources and strategy on compelling emerging markets opportunities. It was eking out small, incremental improvements while its competitors were rapidly building out scale platforms and deriving ever greater profits from the developing markets. In fact, the company had five times as many employees in the developed world as it did in the developing. The company didn't realize that its new strategy required a more fundamental evaluation of its operating model, one that could not be accomplished through small changes, budget year after budget year.

As consumer goods companies set new strategies to win, they often tinker by changing or adding roles and responsibilities. But they often do so without considering the broader operating model. They "fall off the bridge" that links strategy to detailed organization design. That's what happened to a consumer goods company that launched a global snack brand. The company had a solid strategy of local marketing supported by global capabilities. The trouble was that it failed to spell out decision accountabilities. Countries positioned the brand differently, line extensions went in a range of directions and the company was faced with unintended complexity. Eventually, the company took another look at its operating model. It laid out new principles for revised decision accountabilities: who set brand direction, when it could be tweaked, what the process was. Only then did its snack food brand begin its path to success.

Operating models, defined

In its simplest form, an operating model dictates where and how the critical work gets done across a company *(see Figure 1)*. It serves as the vital link between a company's strategy and the detailed organization design that it puts in place to deliver on the strategy. But what the snack food producer and so

Figure 1: Operating models are a critical link between strategy and detailed organizational design



Source: Bain & Company

many other consumer goods companies have learned is that it's necessary to define a consistent and appropriate operating model *before* making detailed changes to an organization's design.

Imagine that you want to build a house. You would likely start with a vision for the lifestyle you want to live and the activities that matter most to you. You would think about how much space you need and what you can afford. If you have a large family and enjoy cooking, you would likely dedicate space differently than if you had a passion for film or cars. Think of this as your house strategy. If you started purchasing countertop materials or sofas based on that strategy alone, you would almost certainly make costly errors. You need to figure out a floor plan, the flow of the house and how different rooms would be used. Think of an operating model as that floor plan and flow. It needs to be in place before you make detailed design decisions.

Operating models have six elements

Many executives think of an operating model as just boxes and lines—that is a mistake. In our experience, winning operating models have six elements that work together.

- **Superstructure** that encompasses a company's primary business units and how the profit and loss statement (P&L) maps to them. It also includes any shared entities reflecting the appropriate role of the center and its operational footprint.

  Typical questions: Do categories or countries own the P&L, and what shared services are appropriate? Should they be provided by the center or region?

- **Accountability** principles for where and how decisions are made and executed.

  Typical questions: Where in the organization are brand positioning or innovation decisions made? How should we balance the benefits of consistency with local consumer preferences?

- **Governance forums and management cadence** that enable priority cross-group processes and interfaces to support strategic and operational decisions.

Typical questions: Do we have the right forums and debates so that the big ideas get the resources they need and the right investment trade-offs are made?

- **Talent requirements** to make the operating model work.

  Typical questions: Where do we need general management talent versus functional talent? Will we need different types of talent and skills going forward to achieve our brand goals?

- **Key strategic metrics** that align the top team and the broader organization around clear strategic objectives and priorities.

  Typical questions: What are the three most important metrics for measuring our success? Is it winning share with a key market segment? Boosting innovation and renewal rates?

- **Behavioral expectations** that establish how to work together, acknowledging a company's unique cultural heritage but also what needs to change to make the team work more effectively in the future.

  Typical questions: Should we shift away from a consensus decision style to speed up decisions and encourage greater accountability? What aspect of our current culture or DNA is key to our success, and how do we enhance it even further?

The universal truths

For consumer goods companies, the trick is finding the model that makes it simple to execute winning routines over and over again in a cost-effective manner. For example, if the key to a company's strategy is deep consumer insights that accelerate brand growth or perfect execution at the point of sale, the model to support that capability would be different than if the strategy was focused on category creation in emerging markets. While Bain research suggests that there is no single best-practice operating model, companies that build the most effective operating models follow four universal truths.

Get fit for purpose. Pick any two consumer goods companies, and it's likely that about 70% of their respective operating models look remarkably similar. For example, many consumer goods companies have centralized their supply chain and IT functions and have moved manufacturing to the most cost-effective locales. And for most consumer goods companies, the top talent is handled by global HR. But the 30% of the operating model that is different—and reflects the company's particular strategy, portfolio and culture—can make or break the company. The best operating models suit a company's unique profile: its categories and brands, strategy to win, culture and heritage (see Figure 2). Most important, winning companies adapt their operating model to their repeatable routines for success—how they apply their core assets, greatest strengths and processes in new contexts—thereby generating further growth and profits.

Few companies match the experience of brewer AB InBev when it comes to repeatable routines as the foundation for continuing and successful growth. The company built its scale through a succession of acquisitions, joint ventures and partnerships, creating synergies that continuously improve margins. It maintains those margins through low-cost production and operations. AB InBev's operating model links to its repeatable formula for success in a host of important ways. For example, the company maintains a distinctly strong M&A integration capability, and its performance management systems focus on EBITDA, or earnings before interest, taxes, depreciation and amortization, rather than any other key metric.

Even within the same category, there can be widely different operating models. Pernod Ricard and Diageo both compete in alcohol-based spirits, but each has a different brand and selling approach. Diageo developed a few big global brands. Pernod has a relatively larger collection of smaller local brands, and even for its global brands, the company permits more local customization. As a result, the two companies developed different operating models. A far more centralist model at Diageo helps the company make the most of its scale. A far more decentralized model at Pernod provides the flexibility to meet local needs. Each model is appropriate not only for each company's unique strategy, but also for their brand development, differentiated capabilities and culture.

Furthermore, the right operating model carefully considers a company's DNA, culture, values and management philosophy; it looks at what is working well

Figure 2: The right model will vary based on the nature of the company's categories, brands and culture

Potential for greater localization		Potential for greater globalization
Fragmented brand portfolio	Portfolio/product complexity	Consolidated brand portfolio
Innovation driven by emotional responses to products		Innovation driven by technical improvements
Local brands	Category attributes	Global brands
Mix of repertoire and regime behaviors		Consistent repertoire or regime behaviors
Different local consumer preferences		Similar global consumer preferences
High level of regulation across markets		Limited regulation across markets
Low capital intensiveness needed		High capital intensiveness needed
Local and distinct ways of working and autonomy	Company DNA, culture and values	Globally consistent ways of working
Historically empowered local business units		Historically strong central command

Source: Bain & Company

and what needs to change. For example, Unilever has historically empowered its local business units, whereas P&G's heritage is one of central command. These cultural differences lead to different operating models. At P&G, global categories traditionally owned P&Ls, but at Unilever, it's the regions that owned P&Ls. And while operating models are tailored to a company's culture, they also need to be flexible to meet changing requirements. In fact, both Unilever and P&G are adjusting their operating models as their marketplaces change—both companies are shifting more toward the center of the global versus local operating-model spectrum in a way that works for them. Unilever is becoming more category driven to help make resource allocations and objectives more straightforward and transparent. At the same time, P&G is creating multiple-category plans for top-priority developing markets, integrating multiple categories and multifunctional capabilities to reduce costs, speed products to market and boost the odds of success.

External factors, too, play a major role in how an operating model reflects a company's unique position. For example, companies selling in heavily regulated markets emphasize localization more than their counterparts in relatively unregulated markets.

Manage the paradox of scale. An operating model that centralizes activities to take advantage of scale makes sense when it can reduce costs, help develop expertise and ensure consistency where needed. But it isn't always the right answer. It can distance decision makers from frontline insights or add process complexity. Consider the experience of a packaged food company that wanted to reduce costs by moving most marketing decisions from local countries to the regional level. Regional decision makers failed to invest in a particular country-specific product. But one local marketing team knew the brand had a powerful, loyal following in its country and that sales could mushroom with a carefully crafted local campaign. Following much debate, some marketing decisions ultimately were pushed to the local level—and the local team was proven right. A single, innovative campaign turbocharged sales.

Winning companies set a high bar for any activity performed by the center. Just as they invest only where it matters most and cut back on everything else, they also centralize only where it makes the most sense. They ask a fundamental question: Can it be performed better or cheaper or less distractingly by the center?

Centralizing may be the right move for an activity like commodity hedging. It may be the correct approach for global vendor management, training best practices or to manage a sales excellence program. But based on our experience, many activities are better *not* done by the center, things like sales execution and local competitive research to traditional trade partnerships and local hiring.

Companies with winning operating models carefully strike a balance. Consider the situation at a multinational brewer, which implemented a highly effective way to manage sales, balancing global capabilities and local needs. As is often the case, the local countries managed sales—selecting the actual sales execution metrics, setting up the local organization responsible for measurement and linking salesforce compensation with key performance indicators (KPIs). But in this case, the center holds a critical piece of the sales function, providing the overall architecture, process and measurement system for KPIs. This simplifies the process dramatically and helps the front line focus on perfect sales execution.

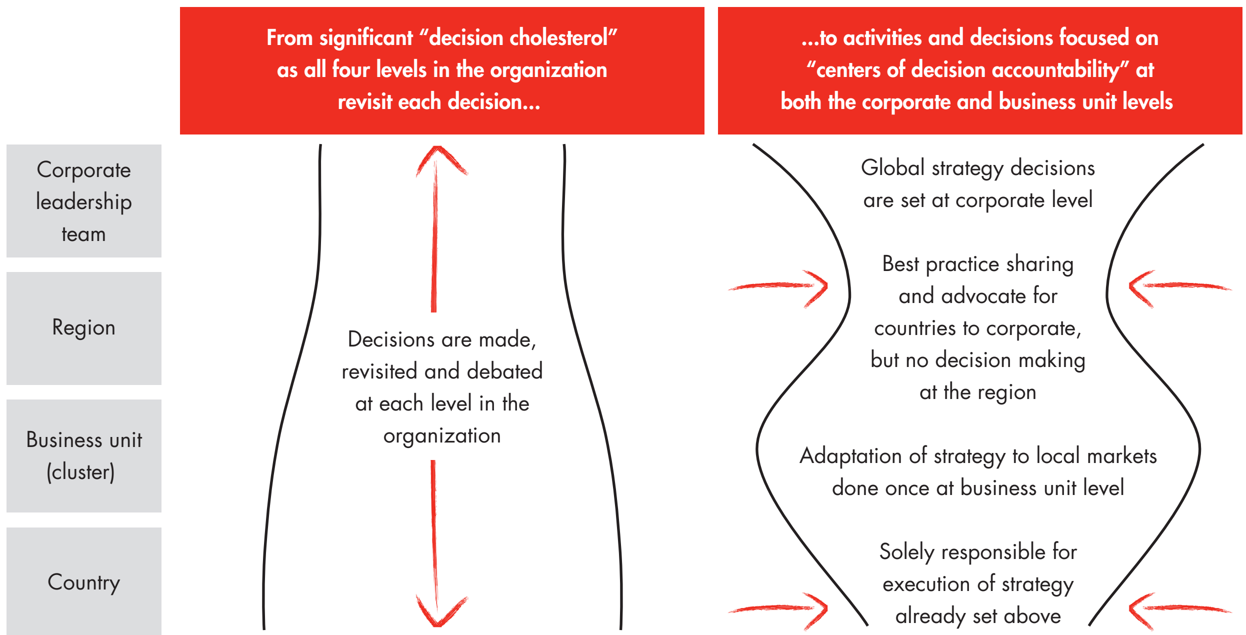
Prevent decision congestion. Bain's global study of 760 companies has demonstrated that a company's financial performance is highly correlated to its decision effectiveness. The research showed that top-quintile decision-effectiveness companies earned their shareholders on average, almost 6 percentage points more per year than other companies. Top-quintile decision-effectiveness companies also delivered similar improved performance on return on invested capital (ROIC) and revenue growth. That makes intuitive sense as well: Companies that make high-quality decisions, make them quickly and implement them effectively are able to win more contracts, get to market faster and otherwise beat out rivals. So it's no coincidence that the best operating models are built to make critical decisions quickly, and with the right amount of effort.

Unfortunately, it's not uncommon to find important decisions delayed as they work their way through multiple layers within an organization. For example, a global consumer goods company observed that it was allowing each of four layers in the organization to debate every major aspect of brand marketing *(see Figure 3)*. Even though the corporate level, led by the chief marketing officer (CMO), believed it was setting the overall brand strategy, every decision associated with that was debated at the regional marketing level and, to an extent, at the strategic business unit and country levels. The company realized it couldn't let each decision be reviewed and questioned at four levels. It clarified accountability principles for each of the four levels so there was clear ownership for different types of decisions. No longer is each level reopening debate and rehashing choices.

Now, the CMO determines brand strategy. Regional marketing is responsible for best practice identification and sharing—but not decision making on these topics. The strategic business unit level (a cluster of countries) adapts brand strategy to local market environments. The country level is solely responsible for executing the brand strategy developed at the corporate level. The company found it far more efficient and effective to streamline the number of levels involved in decision-making accountability—in this case, limiting much of the accountability to the corporate and strategic business unit levels. It is no surprise that the company increased speed to market and got better results with this simpler approach. The company recently achieved its first global launch of a new brand, something that had been previously beyond its reach.

Remember: "Soft" factors matter. In our experience, operating models fail when a company diligently creates a superstructure and accountabilities but doesn't adequately consider the soft issues of the organizational model, such as the interfaces that enable people to work together. It's a lesson one company learned the hard way. The multinational recognized it was falling behind in innovation, so it hired a team of innovation experts to boost that capability. But it never determined how the group would interface with the rest of the company. The team was great at the innovation process, at devising different ways to look at consumer needs, for example, and at determining what new solutions consumers want. But it had no clear procedure in place for sharing those ideas with the rest of the company. As a result, few of its ideas got transferred outside of the group. The company didn't become any more innovative. Those with the best operating models have learned that if a team sits separately from the rest of the organization, forums and interfaces are necessary to allow for sharing

Figure 3: Global CPGs may have multiple layers in the organization, but they should limit decision accountabilities to two



Source: Bain & Company

throughout the organization. Otherwise, even a carefully crafted superstructure or well-defined system for accountabilities won't deliver improvements.

How to get there

Rethinking how and where critical work gets done may sound daunting, but consumer goods companies that apply these universal truths often are able to make the most important changes—addressing the biggest pain points—within months. They just as speedily begin to reap the rewards. Decisions are made more quickly. Talent and assets are deployed in the right places. Performance is improved, and the company is on a path to successfully pursue its strategic choices for the years ahead. For example, one large consumer goods company created regional hubs for its Caribbean operations, where most of the work is now done. The move, combined with new joint venture partnerships and selective divestitures, helped the company prevent an expected 15% shortfall in profits.

Unfortunately, beyond the quick wins, too many companies falter in their efforts to redefine their operating models. Some face financial pressure and can't invest in new capabilities. Some lose stamina for changes after an initial wave of implementation. Others redeploy talent, as other priorities emerge. It is easy to get off track.

In our experience, companies that get this right take a holistic approach. They view their organizations as more than a collection of lines and boxes. In addition to structure, they place equal importance on the interfaces and behavioral expectations. They thoughtfully develop design criteria to help them choose among operating model options (see sidebar "The importance of design criteria"). They focus on decision accountabilities. They work collaboratively to redefine their operating model, relying on workshops that involve all key stakeholders. And they think about change management from the outset through implementation.

The consumer products industry's vast transformation is bringing tremendous opportunities for both growth and profits. But as they pursue those opportunities, too many companies are encountering a troubling fact of life: Old operating models simply aren't serving them anymore. As times change, operating models need to keep up.

The importance of design criteria

The process of revising an operating model is made easier—and the odds of success improve—by first laying out design criteria to help make discerning choices and investment trade-offs. Design criteria can help you break deadlocks or avoid the political or emotional decision. A design criterion could be "We will aggressively replicate our winning brand strategy approach across markets" or "We will design to encourage world-class teaming between the marketing and sales functions." Design criteria also serve as an acid test for companies to see if they stayed true to the problem they were trying to solve.

A company's design criteria are dictated by its strategy for where it wants to compete—its category, brand and geographic priorities—and how it hopes to win, including its repeatable routines for success. We've often found in our work with clients that a company may have a strategy but will need to make it more granular for setting design criteria. It does this by considering critical sources of value, such as its differentiated capabilities and "nonnegotiables." Lacking those inputs, a company can't know specifically how to design the operating model for what it needs to deliver.

For example, in a workshop setting, one beverage company identified its distinct sources of value. Among them: It wanted to win with a particular target customer, 25-year-old males. Identifying this source of value enabled the company to understand the importance of dramatically improving marketing assets to reach this customer segment. As a result, cost reduction targets for marketing were set lower than for other functions. The company identified other sources of value, too, which ultimately were reflected in its design criteria. It wanted to be best at point-of-sale execution, and it wanted to be able to act with agility. These were the capabilities where it invested to be best in class. The others—everything from supply chain to elements of consumer marketing to back-office functions like finance—received less investment.

In choosing design criteria, companies must also look at the decisions that matter most, typically in areas such as brand positioning and pricing. For example, a company whose most important set of decisions revolves around consumer pricing and promotions will want to emphasize related capabilities as part of its design criteria.

In addition, winning companies use their unique DNA as an input to design criteria. They decide how to build on the best elements of their culture, value and heritage. One consumer goods company, for instance, is a relationship-focused company. The culture places importance on actually knowing colleagues personally and being able to pick up the phone and work with them. Informed by these two factors, it chose design criteria around "we take it personally," which conveys a desire to win, but also that success at the company was going to be built through people helping other people. Another consumer goods company prides itself on its world-class, relentlessly repeatable local execution. So one of the company's design criteria centered on furthering the advantage of local execution. Therefore, country managers were freed up from responsibilities that diverted them from focusing on local marketing execution, local field sales and channel marketing. As these two companies illustrate, design criteria are highly personal but also highly important for helping a company craft the right organization to carry out its strategy.

Is your operating model working?

Every company has an operating model. But not all are simple, effective and supportive of the company's goals. How to know if you have a problem? In our experience, if you can say "yes" to 10 or more of the questions below, you are in good shape. If you score 7, 8 or 9, you may need to refresh elements of your operating model. If you have 6 or fewer points, your entire operating model is likely more complicated and costly than it needs to be.

1. Can 100% of your extended leadership team name the same top three sources of value and how your company measures success?
2. Is your top-quartile talent focused on your company's most important priorities?
3. Are country, category and capability structures defined in a way that enables your company to achieve its strategy?
4. Do ways of working across brands and geographies allow winning ideas and innovation to travel across organizational boundaries and be adopted more effectively at a faster rate than they were three years ago?
5. Do you perform your centralized activities better and cheaper—and less distractingly—than they could be performed elsewhere in your organization?
6. Do you have two or fewer true centers of gravity throughout the organization (i.e., layers of organization with substantial decision-making authority or substantial resources)?
7. Do your management forums bring the right people together at the right time to address the most challenging, interdependent opportunities or problems, with minimal bureaucracy?
8. Have your strategy, budgeting and planning processes dynamically aligned talent and financial resources with priority opportunities?
9. Does your company make and execute high-quality critical decisions faster than the competition?
10. Is it clear how the top 20 critical strategic and operational decisions are made in the organization (for example, who makes the decision, and with what input)?
11. Have your company's general and administrative costs as a percentage of revenue decreased in the last three years?
12. Does your company have consistent and effective ways of working together that reflect its culture and produce positive outcomes?

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