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EMERGING AMBITIONS

P&G's Global Target: Shelves of Tiny Stores

It Woos Poor Women Buying Single Portions; Mexico's 'Hot Zones'

By ELLEN BYRON July 16, 2007; Page A1

LEÓN, Mexico -- Every day, Martina Pérez Díaz spends about five hours sewing 70 pairs of black loafers by hand for a wage of 120 pesos, or about \$11. When she wants to wash her hair, she walks to her local *tiendita*, or "small store," to buy a 0.34 ounce, single-use packet of Procter & Gamble Co.'s Head & Shoulders shampoo. The price: two pesos, or about 19 cents. "That I usually can afford," she says.

Shoppers like Ms. Díaz factor heavily into P&G's plan to conquer more of the globe. The consumer-products giant has a goal of increasing total sales by 5% to 7% annually over the next three years. As part of that mission, it is looking to tap roughly one billion additional consumers -- most of them very poor women who live in developing countries.

Reaching these customers isn't easy. In emerging markets, P&G estimates that 80% of people buy their wares from mom-and-pop stores no bigger than a closet. Crammed with food and a hodgepodge of household items, these retailers serve as the pantries of the world's poorest consumers for whom both money and space are tight.

Rather than stock up on full-size goods, which cost more per item, they buy small portions of soap, laundry detergent, and single diapers as they need them -- even though the smaller sizes are usually sold at a premium. In Mexico City, for instance, a full-size bottle of Head & Shoulders that lasts roughly 70 shampoos costs half as much, per ounce, as a single-use sachet.

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Martina Perez Diaz

CORNER STORE

• **The Situation:** P&G sees growth potential in an unusual market: the tiny neighborhood stores of

P&G calls such locally owned bodegas, stalls and kiosks "high-frequency stores," because of the multiple times shoppers visit them during a single day or week.

developing countries.

- **The Background:** In emerging markets, P&G estimates as many as 80% of people buy their wares from such mom-and-pop stores.
- **Next Step:** Getting better shelf space in the shops.

Though most are rudimentary, usually operating out of the owner's home, these shops are a vital route into developing markets, executives believe. But while P&G estimates there to be about 20 million high-frequency stores world-wide, so far just 2.5 million carry their

products.

Over the past six years, P&G has been deploying its armies of researchers, product developers and merchandising wizards to better understand both high-frequency-store shoppers, owners and the haphazard distributor networks that stock them.

For P&G the stakes are high. Sales of P&G products in developing markets currently total \$20 billion, up from \$8 billion five years ago. In recent years, emerging markets have contributed about 40% of the company's "organic" sales growth, which excludes gains from acquisitions. The company still lags other consumer-product rivals. Last year P&G derived 26% of sales in these regions -- a far cry from Unilever and **Colgate-Palmolive Co.**, which manage to snag about 40% of their business in developing markets.

Many industry observers initially believed that these independently owned shops would die out as major retailers such as **Wal-Mart Stores Inc.** and United Kingdom-based **Tesco PLC** expanded their reach into developing markets. Instead, P&G saw the opposite happen. Today, high-frequency stores, considered in aggregate, are P&G's largest customer, with Wal-Mart coming in second.

As these countries' economies have grown, more tiny stores have popped up to serve their customers' rising fortunes. The buy-in-bulk mentality which had made mass-merchants roll over smaller stores in the U.S. simply didn't apply. "That was a paradigm shift for us," says P&G Chief Operating Officer Robert McDonald. "We'll be in those big-box stores, but we've also got to be in the small ones."

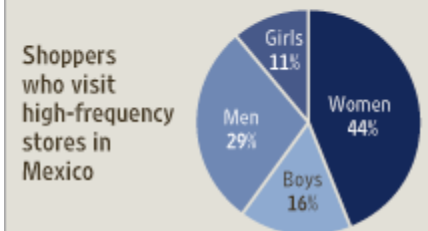
Though Mexico is one of Wal-Mart's most successful markets, high-frequency stores are still regularly visited by 70% of the population, P&G estimates. By the company's count, Mexico has 620,000 high-frequency stores. In most villages and cities there is one approximately every one-and-a-half blocks. Though the average shopper spends just 23 pesos, or \$2.14, a day in high-frequency stores, annual sales total about \$16 billion.

Selling products through these stores requires a special set of skills.

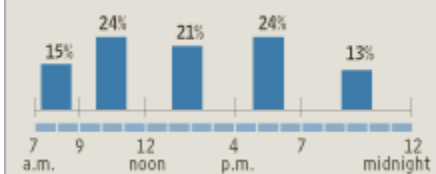
Product visibility, for instance, is one of the biggest challenges to selling in high-frequency stores. Shops tend to be poorly lit and in Latin America average just 250 square feet in size, P&G found. To store owners, displaying P&G staples like

### Smaller Scale

P&G has been tracking the poor consumers in developing markets who visit small, rudimentary shops daily.



### Percentage of visitors, by time of day



Source: Procter & Gamble

household cleaners, bath soaps and shampoos isn't a priority.

Those types of products typically represent just 10% of their sales, while food brings in 35%, and soda brings in 25%. To maximize space, shopkeepers often store laundry detergent, toilet-paper rolls and shampoo packets beneath the counter, handing them to shoppers only upon request.

So P&G began lobbying for better shelf space, one tiny store at a time, by offering them special perks that rivals do not. P&G-employed merchandisers visit the stores about every two weeks to tidy the shelves of their products, post signs with the items' prices and hand out promotional items, including posters. Also, sales representatives deliver inventory to stores themselves, often sparing owners a trip to the local distributor.

P&G touts other advantages, too: Household cleaners and beauty products bring a higher profit margin than food, candy and soda. And when products are arranged as P&G suggests, sales of those items increases 29%, the company claims to owners.



High-frequency stores in Asia, including this one in the Philippines, often hang products from the ceiling; this fall, P&G will try such arrangements in Latin America.

Five years ago, it launched a "golden store" program to encourage owners to display P&G products more prominently. As part of the initiative, representatives visit the stores to spruce up the shelves and display marketing materials -- small touches store owners say they like. To be considered a golden store in Mexico, retailers must agree to carry 40 or so P&G products -- displayed together rather than next to competing brands. So far, about 220,000 have the designation.

To prompt even more sales of its products, P&G began distributing a magazine called "Tu Negocio," or "Your Business." Reserved for golden store owners, the publication explains the benefits of the company's products. It also offers basic business-management tips, including how to calculate profit margins on the items the stores sell.

Recently, José Ramón Riestra, P&G's director of high-frequency stores in Latin America, dropped by a golden store in León. Immediately, he noticed that several P&G products, including Pampers diapers and Camay soap, were placed along a side wall -- on shelves below waist-level inside a glass case. Since most shoppers tend to linger for less than 60 seconds, they likely wouldn't notice the goods.

Smiling as he introduced himself to Rocío Vazquez, a shy 19-year-old at the counter, Mr. Riestra complimented her on her family's store. Ms. Vazquez estimates about 90 people from the neighborhood shop there every day, often two or three times. After inquiring generally about sales, Mr. Riestra got to the real business at hand. "Why are our products so far away, over there?" he asked, pointing to a side wall. "Why not put them behind you?"

P&G calls space nearest the cashier the "hot zone," and considers it the most valuable real estate in these small stores. Since more than 60% of customers already know what they're going to buy,

P&G figures, little time is spent browsing. But P&G researchers found that shoppers tend to gaze at the cashier's area for a precious five seconds as they wait for the owner to hand them a product or get their change -- a prime opportunity to influence future purchases.

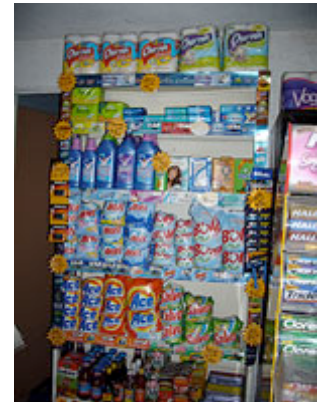
Despite Mr. Riestra's request for better placement, Ms. Vazquez didn't budge. "We're known locally as a food store," she says, pointing to the potato chips, candy and a bowl of Hershey's Kisses, priced two for a peso, or about nine cents, that occupied the space that Mr. Riestra wanted.

Next, Mr. Riestra and a P&G sales representative tried to persuade Ms. Vazquez to carry an additional version of Ace detergent, called Ace Natural. Containing aloe, the detergent promises to make washing clothes by hand gentler on skin. Usually high-frequency stores carry just one or two brands of detergent, so persuading shopkeepers to take on an additional version of a brand they already sell is difficult.

"Tell your customers this will be better for their hands," Mr. Riestra says, pointing to the Ace bag's illustration of an aloe plant. He also noted that the price, 4.50 pesos, or 42 cents, is a peso less than the regular version of Ace she already carries.

On this score he had better luck. Ms. Vazquez agreed to carry a few packages of the new detergent.

Initially, P&G had its own exclusive sales force in Mexico to supply store owners with its products. Then, two years ago, the company decided that it lacked the scale and resources to maximize distribution -- especially in far-flung regions. P&G began offering basic sales training to independent agents and encouraged them to build their own teams. Today, the company is experimenting with allowing agents and their workers to earn commissions from markups on products sold to stores.



Procter & Gamble

Mexican high-frequency store, showing a 'golden store' arrangement of P&G products.

By relying on local agents, P&G is also able to strengthen its ties to store owners. This is especially important, since owners can be very influential in the brands their customers choose.

Though the agents' jobs can be lucrative, the barriers to entry are high. Each must buy his or her own inventory up front, paying in cash. To purchase his first supply of P&G products last year, Luis Mosqueda says he sold nearly all of his family's furniture, his car, his children's toys and his mother's gold jewelry. Now, he says he earns about \$24,000 a year -- an income that makes him relatively affluent. Twelve sales representatives work for him, including two of his brothers.

In marketing goods to low-income shoppers, P&G tries to keep in mind their budget constraints and even the coins they carry. Because they are often paid a daily wage, Mexican customers generally carry five- and 10-peso coins. "If you want to sell to low-income consumers, you have to know what's in their pockets," Mr. Riestra says. "It doesn't make sense to have something cost 11 or 12 pesos."

To ensure satisfactory profit margins, P&G uses what it calls "reverse engineering." Rather than create an item, and then assign a price to it -- as in most developed markets -- the company first considers what consumers can afford. From there, it adjusts the features and manufacturing processes to meet various pricing targets. To hold down the cost of its Ace Natural detergent, used to hand-wash clothes, P&G reduced the amount of enzymes in the product. The result: a product that costs a peso less than regular Ace and is gentler on skin.

P&G says that reverse engineering helps to keep the company's after-tax margins "comparable" to those in wealthier, developed countries.

Internally, P&G emphasizes to its employees that products developed for emerging markets must "delight, not dilute." Quality, executives say, is still critical. "You cannot trick a low-income consumer, because they can't afford to buy products that don't work," says Mr. Riestra. If a product doesn't perform, "they won't ever buy you again, and they'll tell everyone they know about it, too."

The company has addressed this point in several ways. Running water, for example, is in short supply for many low-income Mexican consumers. In response, P&G developed a fabric softener, Downy Single Rinse. It can be added to a load of laundry along with detergent to eliminate an entire rinse cycle in the semiautomatic machines typically used here.

Other observations of the crowded quarters in which many poor Mexican people reside have led to lucrative insights about feminine-hygiene products. With women usually lacking the money and privacy to change their pads frequently, P&G developed Naturella, a low-priced, extra-absorbent cotton pad scented with chamomile, which has soothing and feminine connotations in Latin America.

Driven by strong sales in high-frequency stores, Naturella propelled P&G to take the lead in feminine care in Mexico, and is now sold in other developing markets, including Russia, Poland and the Balkans.

This September, P&G plans to bring to Latin America a merchandising technique common in the tiny shops of Asia: hanging products from the ceiling. Finding that dangling items can catch shoppers' attention more than products sitting on shelves, Mariano Martin, P&G's global customer business development officer, issued a directive to his team: "Own the air."

"The ceiling is still a very virgin location," says Christiane Rizk, a research specialist for high-frequency stores. "We have to get there before someone else does."

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