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White paper

Context Matters: USA

The State of Research & Development Within the Consumer Packaged Goods Industry

by Joseph J. Carideo
Partner

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Overview

The function of Research & Development (R&D) within the Consumer Packaged Goods (CPG) industry has experienced a sea change, like almost no other function. Depending on the company, it may be called R&D, Product Innovation, New Product Development, Product Diversification, etc. What is common, however, among perpetually successful CPG companies is the proactive business platform that R&D has now been given.

No longer just a service organization to marketing groups, R&D is now a vital link in the procreation of ideas that will impact sales and profits. R&D budgets have doubled in the last few years for a number of companies producing food, beverage and household products. This is one manifestation of the importance R&D plays in these companies. It is not atypical to see businesses with sales in the \$10 billion to \$30 billion range with R&D budgets of \$30 million to \$100 million.

Because the function has become so capital-intensive, today's R&D leaders are not just scientists. They are business people, as well. They are well-versed in marketing concepts and financial measurements and may spend as much as 30 to 40% of their time on non-scientific issues. Many, in addition to degrees in science or engineering, have MBAs.

The aphorism, "innovate or die," may be an exaggeration; but innovate or stagnate is not. The successful CPG companies are pushing products from their labs to the marketplace on a consistent basis; and there are defining differences between those who are able to do this and those companies who are struggling with it.

Why Some Companies are More Successful at New Product Development Than Others

There are three common threads in the R&D organizations of companies that are successful in bringing new products to the market:

- Consumer Centric
- Process Driven
- Talent

Consumer Centric

To these companies the consumer is the boss. Successful companies keep the interest of the consumer in mind in determining the priorities of their new product initiatives.

Patents and published papers are nice, but don't necessarily generate revenue for the company. Those companies with an academic bias towards R&D usually find that they cannot get projects to the market, or they are working on projects that do not satisfy a real economic need. As one senior R&D executive put it, "When I got here, we were doing more research than development and there was a bottleneck of projects that were never going to produce significant revenue".

There are several ways these R&D organizations keep the focus on the consumer. Not the least of which is interactive collaboration with the marketing and marketing research organizations, which we will explore in more depth.

Process Driven

An R&D executive of a major CPG company compared the product innovation effort to a golfer. “It’s all about form. Without good form you’ll never consistently hit good golf shots. You might get lucky once in a while, but your effort will never achieve the sustained results you want.”

The same holds true for new product development. Without a well-defined product development process, a company’s R&D efforts will not consistently produce new products that have commercial value.

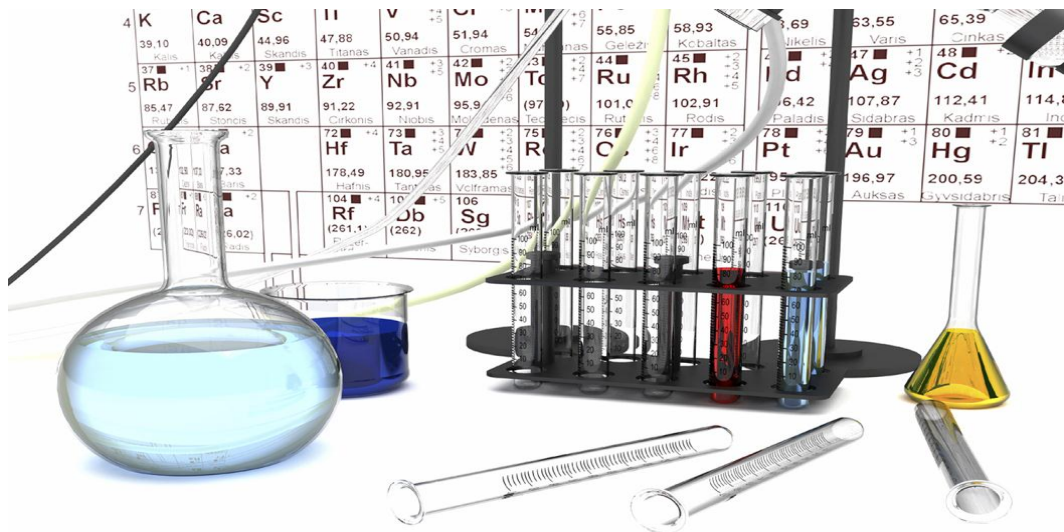
There are typically three key drivers of success within this process:

- Portfolio Management
- Collaboration
- Metrics

Portfolio Management:

It is not unusual for a consumer products company to have 70 to 100 new product development projects in the pipeline at any given time. Never losing the focus on revenue generation, there must be a rationalization of the projects with respect to resource commitment.

Most of the companies we have dealt with have a risk-adjusted portfolio which gives them a balance of low-to-high-risk projects under development.



Typically, companies will create three levels within their risk portfolio:

- Low risk projects are based on existing knowledge and capabilities and have a quick turnaround to the market; product extensions would fall into this category.
- Medium risk projects have a basis of knowledge relative to the product but the company's experience with aspects of production or distribution may be light or non-existent.
- High risk projects are the "game changers." These are the new product development opportunities that can create a new category of business for a company. There is typically a lot of white space in these projects and their time to market is clearly longer, but their revenue potential can have a material impact on a company.

Collaboration:

Cross-functional collaboration is critical to maintaining a rational review of pipeline projects. At different stages of development executives from marketing, operations, finance, technology, legal, etc. will join the team, headed-up by R&D, to bring their expertise to the process. The debate that goes on in these meetings is critical to the decision of committing further resources to a project. While new product development is still a technical model, this collaboration integrates a strong business influence into this process.

Metrics:

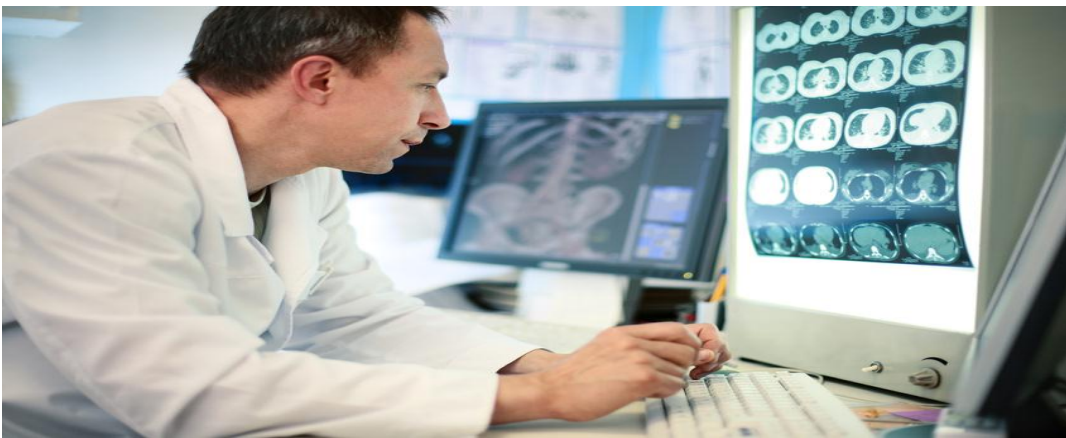
Clearly defined and measurable benchmarks are stated upfront by companies in terms of what they expect from a new product initiative. At any point in time, a project can be eliminated from the pipeline if it is believed that it will no longer meet the company's metrics for success. Some of the metrics companies use are: net present value of future cash flows, ROI, time-to-shelf, break-even point, all-in-cost vs. payout. Some companies will go as far as stating the objective of one game-changing new product (i.e., non-derivative revenue of at least \$100 million annually) from R&D every two years. The key is to have a process which ensures that no one falls in love with an idea that cannot be monetized.

Talent

As previously stated, the successful R&D leaders we have encountered within this industry have been business people, as well as, scientists.

They are great communicators who can translate science into terms easily understood by business leaders.

These R&D leaders may have climbed the career ladder through their lab work, but they developed great project management skills along the way. They know how to set priorities and manage many projects at the same time. Their decision making skills are superb, always keeping in mind the corporation's ultimate objective.



These executives have a good blend of both strategic and tactical outlooks. They understand the importance of “blue sky” exploration because of the product breakthroughs that can come from it; but they are keenly aware of the need to build on the success of getting products to the market quickly. They also maintain a high level of rationality in their organization to defend against falling in love with a product that no longer meets the metrics developed for the NPD process.

Finally, these R&D leaders are great motivators. Their enthusiasm is contagious and they are successful in translating their vision of NPD for their management, peers and subordinates.

In short, the R&D leaders of highly successful Consumer Product Companies are leaders of scientists but, more than that, they are business leaders.

No Walls R&D

Open innovation is increasingly being practiced by CPG companies. No longer fearful of proprietary infringements, companies are teaming with suppliers, universities, other companies and a host of third-party contractors. One major CPG company invites entrepreneurs to present their ideas to a team of evaluators, on a quarterly basis; and at least one game-changing product has been developed from this process.

Open innovation is a way for companies to short-cut their NPD objectives, while spreading the risk and the cost. It is also a way to avoid getting stuck in conventional wisdom. Like portfolio management, however, it must be reviewed periodically by the team in a cold, objective manner.

“Today, and in the future, open innovation will be the difference between successful and unsuccessful companies. However, No Walls R&D is a better description since collaboration and executing projects externally are not only about innovation as related to new products, but also about cost savings, extending the R&D resources, etc., which in the ultimate are also forms of innovation.”

Structure of R&D

There is some truth to the adage “any structure could work with the right people in place”. But there appears to be certain commonalities in CPG companies relative to the organizational structure of R&D. Some of these observations are:

- The SVP/EVP of R&D is a member of the operating or executive committee for the corporation and reports to the CEO or business unit head.
- Some companies have raised the profile of NPD by creating a board-level committee for innovation.
- In multi-divisional companies each business unit has its own R&D group, but the corporate R&D group is also very involved in creating synergies between them and helping them find resources.
- While we have seen any number of variations of functions under R&D (e.g., Q.C., Regulatory & Compliance, Engineering, Packaging, among others) the one that appears to be gaining consensus on its criticality to the NPD effort is Consumer Insight. Traditionally viewed as an element of marketing research, a growing number of CPG companies are creating Consumer Insight groups within R&D to help keep their scientists on a consumer-centric bent.

It is clear that the NPD efforts within CPG companies have elevated the traditional position of R&D from a “cost” center to a “revenue” center. The continued success of these companies is clearly linked to new products, processes and formulas coming out of R&D’s pipeline.

“This is great and clearly emphasizes the importance of transitioning ‘traditional’ R&D to a ‘new’ and proactive business partner responsible for sustainable revenue generation. I couldn’t agree more with all your statements and specifically like the part on talent development and career paths. Well done!!!”

Dr. Heidi Kleinback-Sauter
SVP, R&D Global Foods
PepsiCo, Inc.

Succession Planning

Where will the head of R&D come from? Most likely from within the R&D structure, either within the company or recruited from outside. Because of the quick turnaround required in going-to-market in the CPG industry, it is unlikely that executives who have only worked within the pharmaceutical or technology industries, or industries where product development and revenues have a flatter curve, will have the requisite experience to lead the NPD effort.

The real question for the future is where can the head of R&D go within these companies. It is our belief, based on the executives we have met over the years, that you will see the CEOs of CPG companies coming from the ranks of R&D in the future. These are extremely bright and well-balanced business executives who can speak on a variety of business issues, beyond science and technology. They are every bit as critical to the success of these companies as marketing, sales, finance or operations. The fact that there have not been more examples of this taking place is somewhat surprising, but we are confident that, in the future, corporate boards will see the wellspring of talent that they have in the heads of R&D.



"I think you captured the essence of New Product Development in successful companies and I fully agree that there should be more elevation of R&D executives into the top ranks of management, but probably won't happen because they are viewed as specialists."

Dr. Victoria Spadaro-Grant
Senior Vice President, R&D
Cadbury Schweppes
Formerly SVP, R&D, Pepsi Foods

About the Author



Joseph J. Carideo
Partner

Battalia Winston
New York, NY

T (212) 308-8080

F (212) 355-7146

E jcarideo@battaliawinston.com

W www.battaliawinston.com

Joe Carideo is a Partner in charge of the Firm's retail and consumer products practice. Prior to joining Battalia Winston, Joe worked at Thorndike Deland Associates for 20 years as Senior Partner in Charge of Retail and Consumer Products. Prior to joining Thorndike Deland, Joe was Vice President for Organizational Development and Staffing at American Express, and Director of Corporate Staffing at R.J. Reynolds Industries.

Joe conducts senior-level searches for a broad spectrum of retail companies as well as consumer products companies in both the fashion and packaged goods arenas. Joe works with the boards of large retail organizations to recruit Chief Executive Officers and Chief Operating Officers. Venture capital firms have retained him to find leadership for small to medium sized retail investments. The White House has consulted with him concerning the retail businesses of the U.S. Armed Forces. Joe's practice also includes boards of directors and functional heads for both line and staff positions.

Joe holds an M.A. in Organizational Psychology from Fairleigh Dickinson University, and a B.S. in Psychology from Saint Joseph's University.

Joe is married with two children and is a member of the Union League Club.