Cereal Partners Worldwide (CPW): The No. 2 world player is challenging the No. 1 – Kellogg

On a lovely spring morning in April 2007, while giving her kids some Cheerios, the CEO of Cereal Partners Worldwide S.A. (CPW), Carol Smith thinks about how CPW might expand international sales and/or capture further market shares in the saturated breakfast cereals market. Right now, CPW is the clear No. 2 in the world market for breakfast cereals, but it is a tough competition, primarily with the Kellogg Company, which is the world market leader.

Maybe there would be other ways of gaining new sales in this competitive market? Carol has just read the business bestseller Blue Ocean Strategy and she is fascinated by the thought of moving competition in the cereals breakfast market from the ‘red ocean’ to the ‘blue ocean’. The question is just how?

Maybe it would be better just to take the ‘head-on’ battle with Kellogg Company. After all, CPW has managed to beat Kellogg in several minor international markets (e.g. in Middle and Far East).

The children have finished their Cheerios and it is time to drive them to the kindergarten in Lausanne, Switzerland where CPW has its HQ.

Later that day, Carol has to present the long-term global strategy for CPW, so she hurries to her office, and starts preparing the presentation. One of her marketing managers has prepared a background report about CPW and its position in the world breakfast cereals market. The following shows some important parts of the report.

History of breakfast cereals

Ready-to-eat cereals first appeared during the late 1800s. According to one account, John Kellogg, a doctor who belonged to a vegetarian group, developed wheat and corn flakes to extend the group’s dietary choices. John’s brother, Will Kellogg, saw potential in the innovative grain products and initiated commercial production and marketing. Patients at a Battle Creek, Michigan, sanitarium were among Kellogg’s first customers.

Another cereal producer with roots in the nineteenth century was the Quaker Oats Company. In 1873, the North Star Oatmeal Mill built an oatmeal plant in Cedar Rapids, Iowa. North Star reorganized with other enterprises and together they formed Quaker Oats in 1901.

The Washburn Crosby Company, a predecessor to General Mills, entered the market during the 1920s. The company’s first ready-to-eat cereal, Wheaties, was introduced to the American public in 1924. According to General Mills, Wheaties was developed when a Minneapolis clinician spilled a mixture of gruel that he was making for his patients on a hot stove. Cereal Partners Worldwide (CPW) Cereal Partners Worldwide (CPW) was formed in 1990 as a 50:50 joint venture between Nestlé and General Mills (see Figure 1).
General Mills

General Mills, a leading global manufacturer of consumer food products, operates in more than 30 global markets and exports to over 100 countries. General Mills has 66 production facilities: 34 are located in the United States; 15 in the Asia/Pacific region; six in Canada; five in Europe; five in Latin America and Mexico; and one in South Africa. The company is headquartered in Minneapolis, Minnesota. In financial year 2006 the total net sales were US$11.6 of which 16 per cent came from outside the United States.

In October 2001 General Mills completed the largest acquisition in its history when it purchased The Pillsbury Company from Diageo. The US$10.4 billion deal almost doubled the size of the company, and consequently boosted General Mills’s worldwide ranking, making General Mills one of the world’s largest food companies. However, the company is heavily debt-laden following its Pillsbury acquisition, which will continue to eat into operating and net profits for the next few years.

The company now has more than 100 US consumer brands, including Betty Crocker, Cheerios, Yoplait, Pillsbury Doughboy, Green Giant and Old El Paso.

Integral to the successes of General Mills has been its ability to build and sustain huge brand names and maintain continued net growth. Betty Crocker, originally a pen name invented in 1921 by an employee in the consumer response department, has become an umbrella brand for products as diverse as cookie mixes to ready meals. The Cheerios cereal brand, which grew rapidly in the US post-war generation, remains one of the top cereal brands worldwide.

However, heavy domestic dependence leaves the company vulnerable to variations in that market, such as supermarket price-cutting or sluggish sales in prominent product types such as breakfast cereals.

Internationally, General Mills uses its 50 per cent stake in Cereal Partners Worldwide (CPW) to sell its breakfast cereals abroad. Cereal sales have faced tough competition recently leading to significant drops in sales, particularly tough competition from private labels.

Nestlé

Founded in 1866, Nestlé is the world’s largest food and beverage company in terms of sales. The company began in the field of dairy-based products and later diversified to food and beverages in the 1930s. Nestlé is headquartered in Vevey, Switzerland and the company has 500 factories in 83 countries. It has about 406 subsidiaries located across
the world. The company employs 247,000 people around the world, of which 131,000 employees work in factories, while the remaining employees work in administration and sales.

Nestlé’s businesses are classified into six divisions based on product groups, which include Beverages; Milk Products, Nutrition and Ice Cream; Prepared Dishes and Cooking Aids; Chocolate, Confectionery and Biscuits; PetCare; and Pharmaceutical Products. Nestlé’s global brands include Nescafé, Taster’s Choice, Nestlé Pure Life, Perrier, Nestea, Nesquik, Milo, Carnation, Nido, Nestlé, Milkmaid, Sveltesse, Yoco, Mövenpick, Lactogen, Beba, Nestogen, Cerelac, Nestum, PowerBar, Pria, Nutren, Maggi, Buitoni, Toll House, Crunch, Kit-Kat, Polo, Chef, Purina, Alcon, and L’Oréal (equity stake).

Nestlé reported net sales of $83 billion for the fiscal year 2005.

**CPW**

CPW markets cereals in more than 130 countries, except for the United States and Canada, where the two companies market themselves separately. The joint venture was established in 1990 and the agreement also extends to the production of private label cereals in the UK. Volume growth for CPW was 4 per cent in 2005. The company’s cereals are sold under the Nestlé brand, although many originated from General Mills. Brand names manufactured (primarily by General Mills) under the Nestlé name under this agreement include Corn Flakes, Crunch, Fitness, Cheerios and Nesquik. Shredded Wheat and Shreddies were once made by Nabisco, but are now marketed by CPW.

The CPW turnover in 2005 was a little less than US$2 billion.

When CPW was established in 1990 each partner was bringing distinctive competences into the joint venture:

*General Mills:*
- proven cereal marketing expertise;
- technical excellence in products and production processes;
- broad portfolio of successful brand.

*Nestlé:*
- world’s largest food company;
- strong worldwide organization;
- deep marketing and distribution knowledge.

CPW is No. 2 in most international markets, but it is also market leader in some of the smaller breakfast cereal markets like China (80 per cent market share), Poland (70 per cent market share), Turkey (70 per cent market share), East/Central Europe (50 per cent market share) and South East Asia (50 per cent market share).
The world market for breakfast cereals
In the early 2000s breakfast cereal makers were facing stagnant, if not declining, sales. Gone are the days of the family breakfast, of which a bowl of cereal was standard fare. The fast-paced American lifestyle has more and more consumers eating breakfast on the go. Quick-serve restaurants like McDonald’s, ready-to-eat breakfast bars, bagels and muffins offer consumers less labour-intensive alternatives to cereal. Although the value of product shipped by cereal manufacturers has grown in absolute figures, increased revenues came primarily from price hikes rather than market growth.
English-speaking nations represented the largest cereal markets. Consumption in non-English markets was estimated at only one-fourth the amount consumed by English speakers (see Table 1), where the breakfast cereal consumption per capita is 6 kg in UK, but only 1.5 kg in South-west Europe (France, Spain and Portugal). On the European continent, consumption per capita averaged 1.5 kg per year.

Growth in the cereal industry has been slow to nonexistent in this century. The question at hand for the industry is how to remake cereal’s image in light of the new culture. Tinkering with flavourings and offerings, such as the recent trend toward the addition of dried fresh fruit, proves some relief, but with over 150 different choices on store shelves and 20 new offerings added annually, variety has done more to overwhelm than excite consumers. In addition, cereal companies are committing fewer dollars to their marketing budgets.

<table>
<thead>
<tr>
<th>Region</th>
<th>Per capita consumption per year (kg)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sweden</td>
<td>9.0</td>
</tr>
<tr>
<td>Canada</td>
<td>7.0</td>
</tr>
<tr>
<td>UK</td>
<td>6.0</td>
</tr>
<tr>
<td>Australia</td>
<td>6.0</td>
</tr>
<tr>
<td>USA</td>
<td>5.0</td>
</tr>
<tr>
<td>South West Europe</td>
<td>1.5</td>
</tr>
<tr>
<td>(France, Spain)</td>
<td></td>
</tr>
<tr>
<td>South East Asia</td>
<td>0.1</td>
</tr>
<tr>
<td>Russia</td>
<td>0.1</td>
</tr>
</tbody>
</table>

Development in geographical regions

As seen in Table 2, the United States is by far the largest breakfast cereals market in the world. In total North America accounts for 50 per cent of the global sales of $20 billion in 2005. The United States accounts for about 90 per cent of the North American market.

The European region accounts for 30 per cent of global sales, at US$6 billion in 2005. By far the largest market is the UK, contributing nearly 40 per cent of the regional total, with France and Germany other key, if notably smaller, players. Eastern Europe is a minor breakfast cereal market, reflecting the product’s generally new status in the region. It contributed just 3 per cent of world sales in 2005. However, the market is vibrant as new lifestyles born from growing urbanization and westernization – key themes in
emerging market development – have fuelled steady sales growth. Despite its low level of per capita spending, Russia is the largest market in Eastern Europe, accounting for over 40 per cent of regional sales in 2005. The continued steady growth of this market underpinned overall regional development over the review period. Cereals remain a niche market in Russia, as they do across the region, with the product benefiting from a perception of novelty. A key target for manufacturers has been children and young women, at which advertising has been aimed.

The Australasian breakfast cereals sector, like Western Europe and North America, dominated by a single nation, Australia, is becoming increasingly polarized. In common with the key US and UK markets, breakfast cereals in Australia are suffering from a high degree of maturity, with annual growth at a low single-digit level.

The Latin American breakfast cereals sector is the third largest in the world, but at US$2 billion in 2005, it is notably overshadowed by the vastly larger North American and Western European markets. However, in common with these developed regions, one country plays a dominant role in the regional make-up, Mexico, accounting for nearly 60 per cent of the overall breakfast cereal markets in Latin America.

In common with Eastern Europe, breakfast cereal sales, whilst small in Africa and the Middle East, have displayed marked growth in recent years as a direct result of greater urbanization and a growing trend (in some areas) towards westernization. Given the overriding influence of this factor on market development, sales are largely concentrated in the more developed regional markets, such as Israel and South Africa, where the investment by multinationals has been at its highest.

In Asia the concept of breakfast cereals is relatively new, with the growing influence of Western culture fostering a notable increase in consumption in major urban cities. Market development has been rapid in China, reflecting the overall rate of industry expansion in the country, with breakfast cereals sales rising by 19 per cent in 2005. In the region’s developed markets, in particular Japan, market performance is broadly similar, although the key growth driver is different, in that it is health. Overall, in both developed and developing markets, breakfast cereals are in their infancy.

**Health trend**

With regards to health, breakfast cereals have been hurt by the rise of fad diets such as Atkins and South Beach, which have heaped much scorn on carbohydrate-based products. The influence of these diets is on the wane but their footprint remains highly visible on national eating trends. In addition, the high sugar content of children’s cereals has come under intense scrutiny, which caused a downturn in this sector, although the industry is now coming back with a range of ‘better for you’ variants.

Regarding convenience, this trend, once a growth driver for breakfast cereals, has now become a threat, with an increasing number of consumers opting to skip breakfast. Portability has become a key facet of convenience, a development that has fed the emergence and expansion of breakfast bars at the expense of traditional foods, such as breakfast cereals. In an increasingly cash-rich, time-poor society, consumers are opting to abandon a formal breakfast meal and instead are relying on an ‘on-the-go’ solution, such as breakfast bars or pastries. These latter products, in particular breakfast bars, are taking share from cereals, a trend that looks set to gather pace in the short term.
**Trends in product development**
Consumer awareness of health and nutrition also played a major part in shaping the industry in recent years. Cereal manufacturers began to tout the benefits of eating breakfast cereal right on the package – vitaminfortified, low in fat, and a good source of fibre. Another trend, begun in the 1990s and picking up steam in the 2000s, is adding dehydrated whole fruits to cereal, which provides colour, flavour, and nutritional value. Yet touting health benefits to adults and marketing film characters to children have not been sufficient to reinvigorate this mature industry.

Under the difficult market conditions, cereal packaging is receiving new attention. Packaging was a secondary consideration, other than throwing in special offers to tempt kids. But these days, with meal occasions boiled down to their bare essentials, packaging and delivery have emerged as key weapons in the cereal marketer’s arsenal. New ideas circulating in the industry usually include doing away with the traditional cereal box, which has undergone little change in its lifetime. Alternatives range from clear plastic containers to a return of the small variety six-packs.

**Trends in distribution**
Supermarkets tend to be the dominant distribution format for breakfast cereals. The discounter format is dominated by mass merchandisers, the most famous example of which is Wal-Mart in the United States. This discounter format tends to favour shelf-stable, packaged products and as a result they are increasingly viewed as direct competitors to supermarkets.

Independent food stores have suffered a decline during the past years. They have been at a competitive disadvantage compared to their larger and better resourced chained competitors.

**Trends in advertising**
Advertising expenditures of most cereal companies were down in recent years due to decreases in consumer spending. However there are still a lot of marketing activities going on.

General Mills has a comprehensive marketing programme for each of its core brands, from traditional television and print advertisements to in-store promotions, coupons and free gifts. In 2002, the company teamed up with US publisher Simon & Schuster to include books or audio CDs with the purchase of its Oatmeal Crisp Raisin and Basic 4 cereals.

Other promotions have included free Hasbro computer games included in boxes, promotion of new millennium pennies and golden dollars in 2000, and the inclusion of scale models of the Cheerios-sponsored NASCAR.

In response to Kellogg’s 2001 launch of Special K Red Berries, General Mills countered with the introduction of freeze dried fruit in Cheerios, with Berry Burst and Triple Berry Burst product extensions from February 2003. The introduction is a response to the need for the packaging to communicate the inclusion of real berries in the box and not just flavouring. Consequently, the chosen designs consisted of vibrant red and purple boxes, each featuring a spoonful of Cheerios and fruit splashing in milk. Since freeze-dried fruit tends to absorb moisture, the company was also compelled to develop a more moisture-resistant package liner.
The introduction of Berry Burst Cheerios was supported by a US$40 million advertising and promotional campaign that included TV advertising, consumer couponing, outdoor advertising, in-store sampling and merchandising.

**Celebrity glamour**

Celebrity endorsements continue to play a critical part of General Mills’s marketing strategies, in particular its association with sporting personalities dating back to the 1930s with baseball sponsorship. One of the main lines of celebrity endorsement involves Wheaties boxes and a long line of sports people have appeared on the box since the 1930s. In 2001, Tiger Woods, spokesman for the Wheaties brand, appeared on special edition packaging for Wheaties to commemorate his victory of four Grand Slam golf titles.

**Distribution**

General Mills distributes the majority of its products directly through its own sales organization to retailers, cooperatives and wholesalers. In Europe and Asia-Pacific the company licenses products for local production, but it also exports to over 100 different countries.

**New products, new channels**

New products and new product innovations have helped create new distribution channels for General Mills recently. The success of General Mills’s snack products has helped create a large demand for products in convenience stores and the company has actively developed products to meet the demands of the convenience store consumer such as its healthy Chex Mex range. A new chocolate-flavoured Chex Mex was added to the product line in 2005.

The development of cereal-in-a-bowl range has helped create new outlets for General Mills’s products in college cafeterias and hotel restaurants. This may see the development of additional products to compliment these channels.

**Traditional channels**

Traditional retailers such as supermarkets continue to play a major role in the distribution of General Mills’s products, and the company has an extensive number of cereal, snack, meal and yoghurt brands to maintain shelf space in major retail outlets.

**Private label competition intensifies**

Across many categories, rising costs have led to price increases in branded products which have not been matched by any pricing actions taken in private labels. As a result, the price gaps between branded and private label products have increased dramatically and in some cases can be as much as 30 per cent.

This creates intense competitive environments for branded products, particularly in categories such as cereals which is one of General Mills’s biggest markets, as consumers have started to focus more on price than brand identity. This shift in focus is partly the result of private labels’ increased quality as they compete for consumer loyalty and confidence in their label products.
Competitors

Kellogg’s

The company that makes breakfast foods and snacks for millions began with only 25 employees in Battle Creek in 1906. Today, Kellogg Company employs more than 25,000 people, manufactures in 17 countries and sells its products in more than 180 countries. Kellogg was the first American company to enter the foreign market for ready-to-eat breakfast cereals. Company founder Will Keith (W.K.)

Kellogg was an early believer in the potential of international growth and began establishing Kellogg’s as a global brand with the introduction of Kellogg’s Corn Flakes® in Canada in 1914. As success followed and demand grew, Kellogg Company continued to build manufacturing facilities around the world, including Sydney, Australia (1924), Manchester, England (1938), Queretaro, Mexico (1951), Takasaki, Japan (1963), Bombay, India (1994) and Toluca, Mexico (2004).

Kellogg Company is the leader among global breakfast cereal manufacturers with 2005 sales revenue of $10.2 billion (net earnings were $980 million). Wal- Mart Stores, Inc. and its affiliates, accounted for approximately 17 per cent of consolidated net sales during 2005.

Established in 1906, Kellogg Company was the world’s market leader in ready-to-eat cereals throughout most of the twentieth century. In 2005, Kellogg had 30 per cent of the world market share for breakfast cereals (see Table 3). Canada, the United Kingdom, and Australia represented Kellogg’s three largest overseas markets.

A few well-known Kellogg products are Corn Flakes, Frosted Mini-Wheats, Corn Pops, and Fruit Loops.

<table>
<thead>
<tr>
<th>Manufacturer</th>
<th>Germany</th>
<th>UK</th>
<th>USA</th>
<th>World</th>
</tr>
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<tbody>
<tr>
<td>Kellogg Company</td>
<td>27%</td>
<td>30%</td>
<td>30%</td>
<td>30%</td>
</tr>
<tr>
<td>CPW (General Mills + Nestlé)</td>
<td>12%</td>
<td>15%</td>
<td>30%</td>
<td>20%</td>
</tr>
<tr>
<td>PepsiCo (Quaker)</td>
<td>6%</td>
<td>14%</td>
<td>10%</td>
<td>10%</td>
</tr>
<tr>
<td>Weetabix</td>
<td>–</td>
<td>10%</td>
<td>–</td>
<td>5%</td>
</tr>
<tr>
<td>Private label</td>
<td>35%</td>
<td>15%</td>
<td>10%</td>
<td>15%</td>
</tr>
<tr>
<td>Others</td>
<td>26%</td>
<td>24%</td>
<td>16%</td>
<td>20%</td>
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<tr>
<td>Total</td>
<td>100%</td>
<td>100%</td>
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<td>100%</td>
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</tbody>
</table>

1 In the United States General Mills and Nestlé market each of their breakfast cereal products independently, because the CPW only covers international markets outside the United States.

PepsiCo

In August 2001, PepsiCo merged with Quaker Foods, thereby expanding its existing portfolio. Quaker’s family of brands includes Quaker Oatmeal, Cap’n Crunch and Life
cereals, Rice-A-Roni and Near East side dishes, and Aunt Jemima pancake mixes and syrups.

The Quaker Food’s first puffed product, ‘Puffed Rice’, was introduced in 1905. In 1992, Quaker Oats held an 8.9 per cent share of the ready-to-eat cereal market, and its principal product was Cap’n Crunch. Within the smaller hot cereal segment, however, the company held approximately 60 per cent of the market. In addition to cereal products, Quaker Oats produced Aunt Jemima Pancake mix and Gatorade sports drinks.

The PepsiCo brands in the breakfast cereal sector include Cap’n Crunch, Puffed Wheat, Crunchy Bran, Frosted Mini Wheats and Quaker.

Despite recent moves to extend its presence into new markets, PepsiCo tends to focus on its North American operations.

**Weetabix**

Weetabix is an UK manufacturer, with a relatively high market share (10 per cent) in United Kingdom. The company is owned by a private investment group – Lion Capital. The company sells its cereals in over 80 countries and has a product line that includes Weetabix, Weetos, and Alpen. Weetabix is headquartered in Northamptonshire, UK. In 2005 Weetabix has an estimated turnover of US$1 billion.


**Questions**

Carol has heard that you are the new global marketing specialist so you are called in as a ‘last-minute’ consultant before the presentation to the board of directors. You are confronted with the following questions, which you are supposed to answer as best you can.

1. How can General Mills and Nestlé create international competitiveness by joining forces in CPW?
2. Evaluate the international competitiveness of CPW compared to the Kellogg Company.
3. Suggest how CPW can create a blue ocean strategy.
4. Where and how can CPW create further international sales growth?