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2021 Top picks: From recovery to growth

December 2021

2021 Top picks: From recovery to growth

Companies are developing new growth strategies and tools to meet the demands of pandemic recovery in a digitally transformed economy. Here are some of the most promising.

Introduction

As leaders position their businesses for growth and renewal in the coming months, we offer our year end compendium, a curated set of articles around four key trends shaping the growth agenda for CEOs. We start with several perspectives that our leaders have published on growth, starting with how important sustainable, inclusive growth is to the world's recovery. We explore the role of intangibles in driving growth and the importance of purpose, analytics, and creativity. In addition, we've included several articles specific to our current inflationary context, given we have not seen an inflationary surge of this magnitude in four decades.

And as the pandemic continues to shatter brand loyalty, we have included perspectives on the big shifts in consumer and customer behavior, and how business leaders can respond in time. We then dive into how leaders are balancing brand marketing and performance marketing using a 'full-funnel' marketing approach and how they are building stronger customer experience and personalization capabilities. Finally, we share how leaders are improving their e-commerce capabilities by using analytics to improve their marketing and commercial growth.

Many businesses have responded admirably to the current challenges, pushing their rate of innovation and driving scale. Given the continued challenges in front of us, winning the future will require leaders to be even bolder. Leaders will need to enable growth that is sustainable and inclusive, operating at unprecedented speed, acquiring interconnected capabilities, and developing future-ready talent. We hope our work here helps provoke your thinking on how to do so.

From all of us at M&S, here's to a healthy and prosperous New Year. We look forward to continuing to bring you the best of our insights in 2022.

All the best,
Greg Kelly, Brian Gregg, Eric Hazan, Dennis Spillecke, and Bruno Furtado

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Theme 1:

Powering catalytic growth

Getting tangible about intangibles: The future of growth and productivity?

Companies that master the deployment of intangibles investment will be well positioned to outperform their peers.

This article is a collaborative effort by Eric Hazan, Sven Smit, Jonathan Woetzel, Biljana Cvetanovski, Mekala Krishnan, Brian Gregg, Jesko Perrey, and Klemens Hjartar.

June 2021

Investment in intangible assets that underpin the knowledge or learning economy, such as intellectual property (IP), research, technology and software, and human capital, has risen inexorably over the past quarter century, and the COVID-19 pandemic appears to have accelerated this shift toward a dematerialized economy. Are we seeing the start of a new stage in the history of capitalism based on learning, knowledge, and intellectual capital? As economies recover from the pandemic, could a wave of investment in intangible assets breathe new life into productivity and unlock more growth potential?

New research uses sector-level data and the results of a new survey of more than 860 executives that reveal that "top growers"—companies in the top quartile for growth in gross value added, a measure of economic growth—invest 2.6 times more in intangibles than low growers, companies in the bottom two quartiles. The research uses the survey and sector-level data from the INTAN-Invest database to explore the correlation between intangible investment and the productivity of sectors, economies, and firms, and to discover the formula for the effective deployment of intangible assets to drive growth.[1] The research takes the broader definition of intangibles outlined by economists Jonathan Haskel and Stian Westlake, who include economic competencies such as advertising and brands, marketing research, organizational capital, and training. This more expansive definition of intangibles appears more relevant to the role they increasingly play in companies, sectors, and economies.

Over the past 25 years, the investment share of intangibles has increased by 29 percent

Over the past 25 years, the United States and ten European economies achieved 63 percent growth in gross value added (GVA). During this period, the share of total investment of intangibles as defined by the INTAN-Invest database increased by 29 percent (Exhibit 1). Rising investment in intangibles has been linked with increasing total factor productivity of entire economies. This could indicate that the deceleration of productivity growth over the past decade partly reflects a slowdown in investment in intangible assets.

The share of intangibles in total investment has risen steadily even in the face of economic disruptions such as the bursting of the dot-com bubble in the late 1990s, although this shift decelerated in the aftermath of the global financial crisis. During the pandemic, when social distancing necessitated a shift toward remote working and large-scale and much faster digitization, investment in intangible assets accelerated once again. In the United States, for example, intangibles investment (as measured by gross fixed capital formation) as a share of total investment increased by one percentage point between the first three quarters of 2019 and 2020 to reach 29 percent of total investment in 2020. In some European economies, the increase in the intangibles share was larger—2.8 percentage points in France, and 1.9 percentage points in the United Kingdom, according to national statistical agencies.

Investing in intangibles correlates with productivity and sector growth

An intangibles-rich economic model is not the only way for an economy to be successful; there are other ways to promote productivity and growth. Nevertheless, economies that are experiencing growth in intangibles investment are also posting growth in total factor productivity.[2] This suggests that an increase in intangibles investment may trigger an increase in total factor productivity, and therefore long-term economic growth.

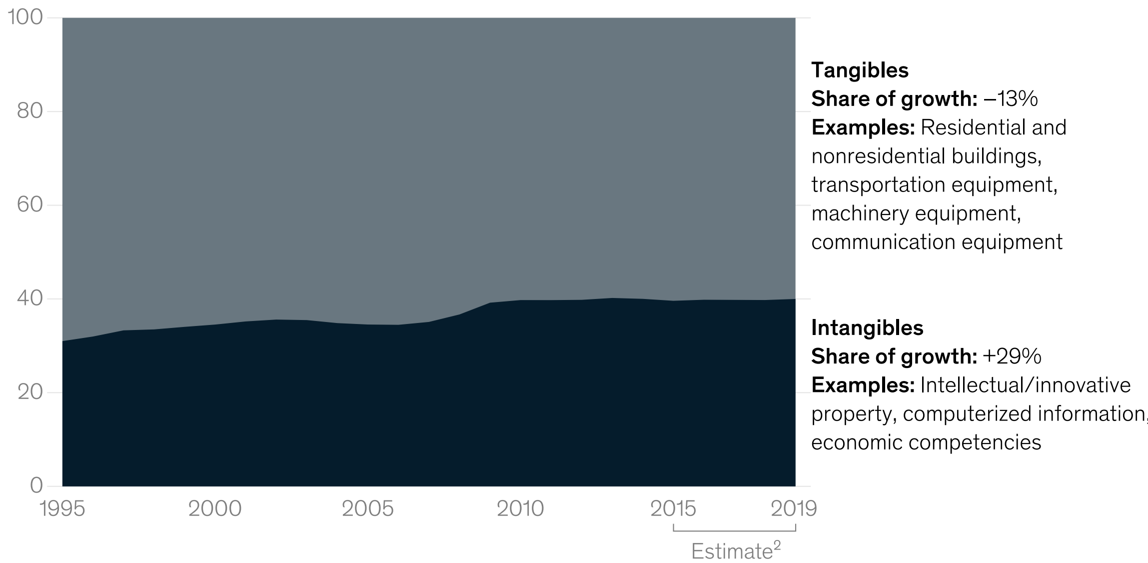
Additionally, there is an observable link between investment in intangibles and GVA growth at the sector level, according to statistics from the INTAN-Invest database. Broad correlations are present across sectors, but the strength of the correlations varies.

Sectors that have invested the most in intangibles—more than 12 percent of their GVA—have achieved higher growth in GVA, at more than 2.7 percent per year, or 28 percent higher than other sectors. Knowledge-intensive services have invested relatively heavily in intangibles at 15 percent of their

Exhibit 1

The investment mix has shifted toward intangibles over the past 25 years.

Investment mix in United States and 10 European countries, %[1]



[1]European countries are Austria, Denmark, Finland, France, Germany, Italy, Netherlands, Spain, Sweden, and United Kingdom.
[2]Data extrapolated for 2015–19 based on 2010–15 average growth.
Source: EU-KLEMS; Eurostat; INTAN-Invest; McKinsey Global Institute analysis

GVA and, on average, achieved above-average GVA growth of 3.0 percent a year. Innovation-driven services including information and communications technology (ICT) on average invested 17.4 percent of their GVA in intangibles and grew at 2.9 percent a year. Most other sectors invested less than 10 percent of their GVA and achieved below-average rates of GVA growth.

Regardless of the sector, companies that invest more in intangibles grow more

In all sectors, there are companies that are outperforming others. One of our key findings is that firms that invest most in intangibles are outperforming their peers. Top growers, defined as companies in the top quartile of growth by sector in 2018–19 (whose median growth was 20 percent) are investing 2.6 times more in intangibles than low growers (3 percent median growth in 2018–19) (Exhibit 2). The gap between them increases to between five and seven times in sectors such as financial services where competitive advantage is anchored on knowledge.

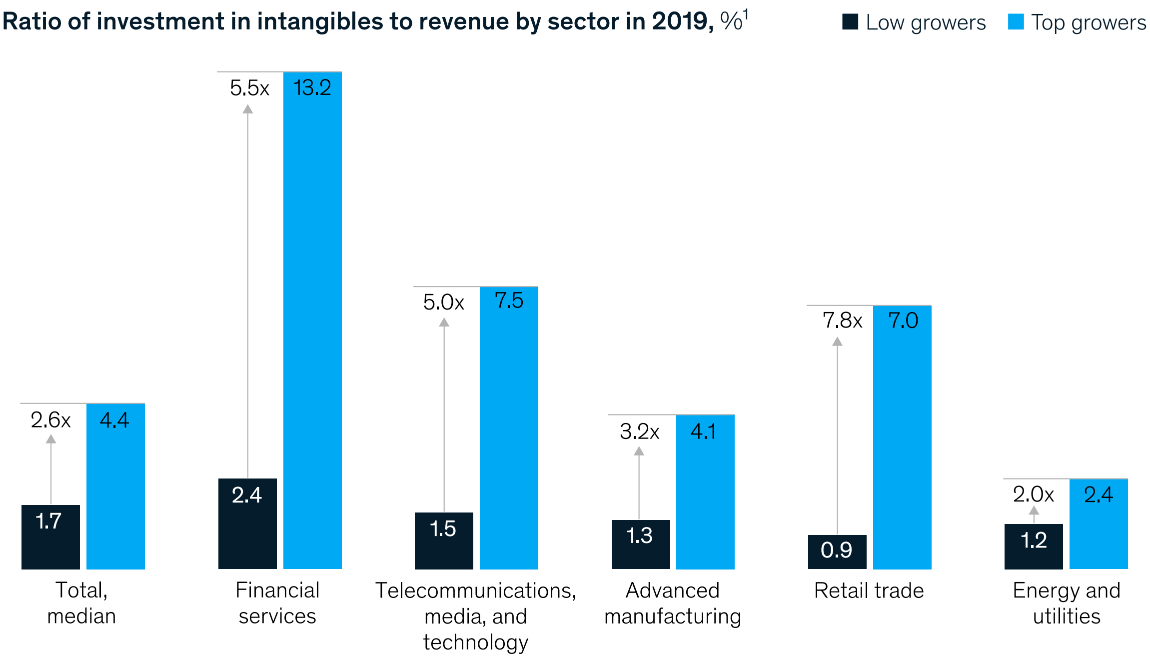
Even in sectors with relatively lower growth such as manufacturing, top growers are using high investment in intangibles to outgrow the market. Some companies that have outperformed their sectors have diversified into “intangible-like” adjacencies. For instance, manufacturing companies in slower-growing industries have used their intangible assets (such as brand) to carve out resilient niches within the industry or find new growth markets.

Top growers in innovation-driven sectors, including telecommunications, media, and technology, invest 5.2 times more than low growers. One leading entertainment industry company today still invests in tangible assets such as roller coasters, land,

Exhibit 2

Top growers invest 2.6 times more in intangibles than low growers across sectors.

Ratio of investment in intangibles to revenue by sector in 2019, %[1]



Note: Figures may not sum to 100% because of rounding.
[1]Median by sector. Survey included other sectors not shown on this exhibit.
Source: McKinsey survey (n = 591); McKinsey Global Institute analysis

and stores, but it is building up its data analytics capability with a team of more than 1,000 people to develop a more personalized customer experience. Similarly, top growers in knowledge-intensive sectors such as financial services invest 5.4 times more than low growers. One major European bank had invested limited amounts in intangible capital and had limited access to data, a shortage of skills, and conflicting data strategies. In response, the bank invested heavily in organizational and managerial capital and deployed an analytics transformation program covering the redesign of its organization, a talent strategy, the modernization of its data architecture, and building analytics capabilities across the organization.

Top growers in retail trade invest 8.0 times more in intangibles than low growers. Again, advanced analytics are part of the story as retailers increasingly shift focus from adding to tangible capital by opening new stores to developing new sources of growth on the back of digital, data, and analytics. One leading US discount retailer used digital and analytics capital to connect partners, acquire companies, and win customers in a single digital platform, embedding machine learning throughout the organization. In parallel, the company worked to improve its brand capital, offering customers a loyalty program with a focus on free delivery, more choice, and a personalized pricing system. The company also developed its human, organizational, and managerial capital, reskilling existing workers and attracting new talent.

Intangibles are interdependent, and companies achieve greater synergies by investing in them all. Companies that have invested across all categories of intangibles are further ahead in their digitization journey, less likely to be disrupted because they are highly innovative, and highly likely to be able to attract top talent and retain it. All of this creates value and, importantly, value that can be defended even amid a deep market and economic disruption. During the COVID-19 pandemic, companies that invested significantly in all four main types of intangible capital—innovation capital, digital and analytics capital, human and relational capital, and brand capital—were able to maintain 2019 levels of growth.

Top growers not only invest more in intangibles but also deploy them in ways that develop new capabilities

Purely investing in intangibles is not sufficient to drive growth. Companies need to think about how those intangibles are deployed and implemented to ultimately build capabilities that create a competitive advantage.

Top growers and low growers both invest in intangible assets—the first more than the second. The survey results suggest that there is considerable agreement among top and low growers across sectors that intangible capabilities are key to delivering growth and competitiveness. About 24 percent of both top and low growers strongly agreed that digital and analytics capital is crucial for building a sustainable competitive advantage, and this finding holds across sectors from telecommunications, media, and technology, where data have been a valuable asset for building ecosystems, to advanced manufacturing as more players digitize their supply chains. The key difference, however, is that top growers take the deployment of intangible capital to the next level and display a detailed understanding of how intangibles can be used to develop the capabilities that are most likely to deliver on growth. When asked to be precise about what delivers disproportionate returns, survey respondents cited specific use cases, rigorous processes, data-driven decision making, and, broadly, using intangible investment to embed data, talent, innovation, and purpose in their day-to-day operations. In short, low growers plan, while top growers do (Exhibit 3).

Looking in more detail at the different types of intangible asset, a clear picture of higher growth driven by effective deployment and use of intangibles emerges (Exhibit 4):

— *Innovation capital.* The share of top growers that reported using data as the basis of decision making was nearly double the share of low growers. Likewise, more than twice the share of top growers said that they have rigorous processes in place to measure the impact of R&D and design, enabling them to build rapidly on successes and abandon failures. Similarly, twice as many top growers are more willing to disrupt their own business models proactively (rather than waiting to be disrupted) and actively search for opportunities to invest in disruptive innovation.

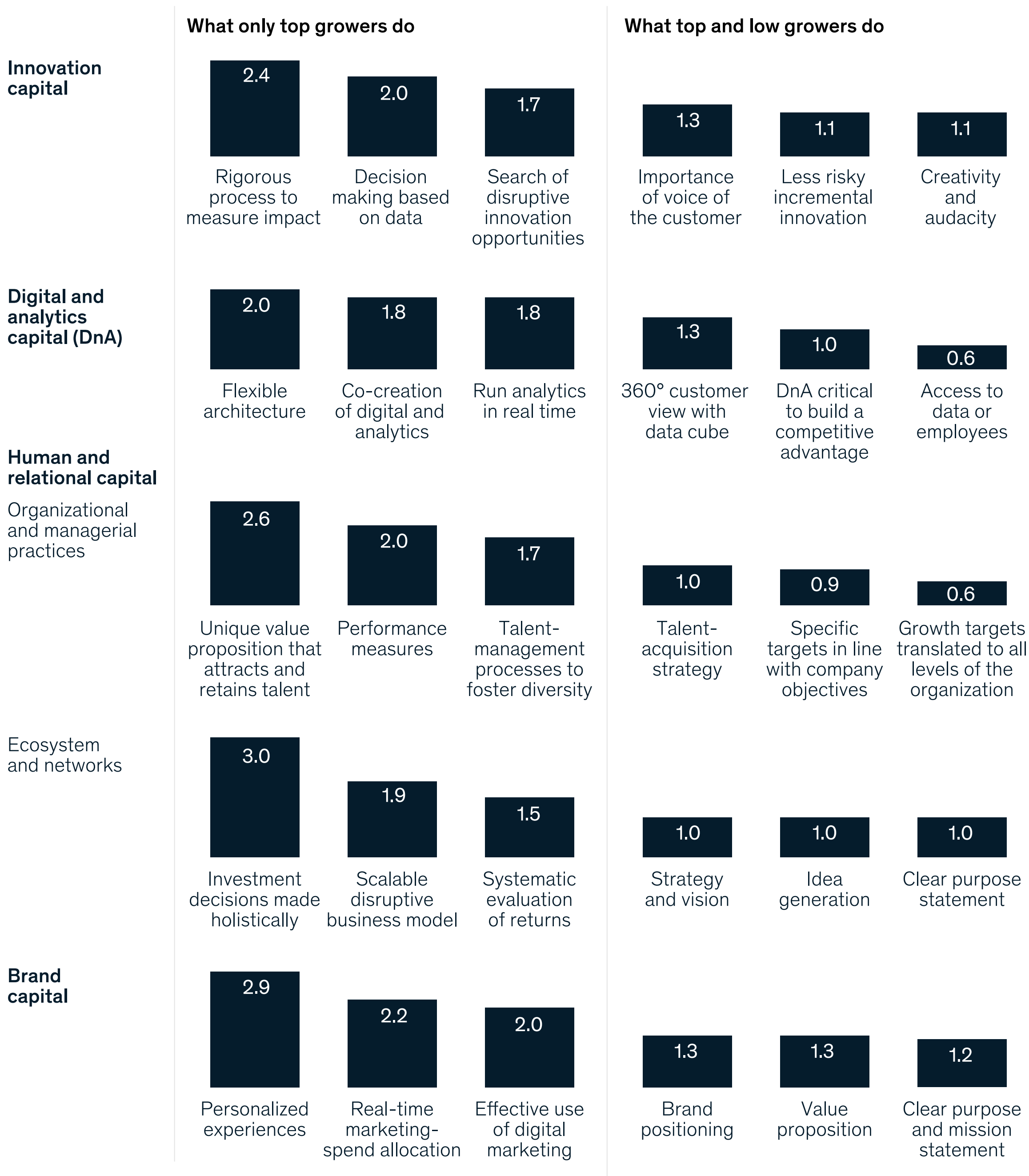
— *Data and analytics capital.* Only top growers say that they have taken the next steps needed to implement their digital strategy, including making effective use of proprietary data, investing in flexible architecture to avoid being held back by legacy systems—so-called tech debt—and ensuring that they can leverage the full power of intangibles through real-time analytics. Top growers are 1.3 times more likely to have proprietary data, 1.8 times more likely to run analytics decisions in real time, and 2.0 times more likely to have a flexible infrastructure.

— *Human and relational capital.* Both top and low growers agree on the importance of attracting talent, but top growers are 2.6 times more likely than low growers to strive to retain that talent by offering a unique value proposition. Top growers are twice as likely to define performance measures for all parts of the organization, and 1.7 times more likely to put in place talent-management processes to foster diversity. Our survey indicates that top growers are 3.0 times more likely to make investment decisions holistically, to do so on a systematic and regular basis, and to maintain agility. Top growers are 1.5 times more likely to make decisions about spending and investment allocation through systematic but agile evaluation of returns. Finally, top growers are twice as likely as low growers to agree strongly that it is important to scale disruptive new business models.

Exhibit 3

Top and low growers recognize the importance of strategy and vision in intangibles, but top growers take concrete steps to implement.

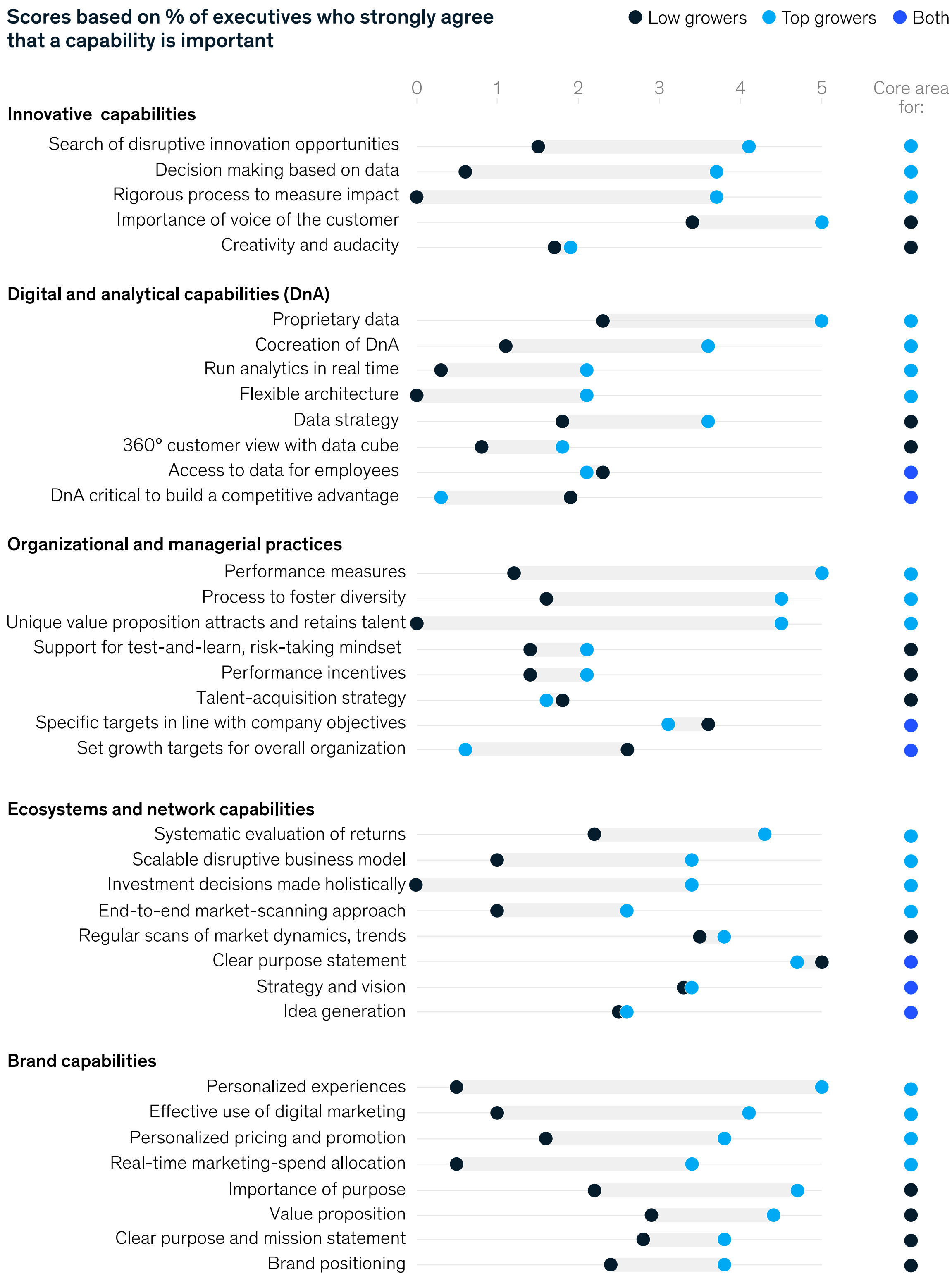
Ratio of top growers to low growers per capability, based on the % of executives who strongly agree on the following capabilities[1]



[1]Survey respondents had the option to comment on more than one capability.
Source: McKinsey survey (n = 591); McKinsey Global Institute analysis

Exhibit 4

Effective deployment and use of intangibles distinguishes top growers from low growers.



Source: McKinsey survey (n = 591); McKinsey Global Institute analysis

— *Brand capital.* Only top growers are already deploying this type of intangible to ensure that they can leverage brands effectively by not only listening to the voice of consumers but listening in a tailored way to serve them with personalized offerings backed by real-time data analytics and tailored pricing and promotion. It is notable that 2.5 times more top growers than low growers regard personalization as the core part of the customer experience, and more than double the share of top growers say that they continuously allocate and reallocate marketing spending in or near real time.

Deploying intangibles is a moving target. As businesses invest, they will need to continually assess not only what is key to success today but what areas they will need to prioritize for growth in the future. Continuous reexamination of the type of intangibles that are most likely to deliver on competitiveness and growth, that can be scaled, and that are most likely to deliver synergies that may create value in other areas of the learning economy will require a high level of visibility. Companies should consider setting up a control tower that monitors the skills the organization needs, what IP will deliver the next slice of competitive advantage, and what area innovation capital should focus on.

Huge value is at stake, and executives and policy makers need to ask themselves what it will take to realize the opportunity

The correlation of investment and deployment of intangibles with growth in GVA is becoming ever clearer, and huge value is at stake. As a thought exercise, consider the potential value that could be created if 10 percent more companies were to attain the share of intangible investment, and the GVA growth, of top growers. This could produce an additional $1 trillion in gross value added or a 2.7 percent increase across sectors in OECD economies. If more companies could capture more of the productivity- and growth-driving power of intangibles, these assets could play a major role in the bounce-back of companies and economies from the COVID-19 crisis.

Executives—and governments—searching for sources of growth should arguably pay more attention to the full range of intangible assets. The formula that top growers have apparently hit upon may help other businesses to understand the best way to invest in intangibles and deploy them, and help policy makers to put in place the right kinds of enabling infrastructure.

For companies, execution is key. Top growers invest 2.6 times more than low growers in intangibles, invest in the four major types of intangible asset, and deploy them effectively with a focus on embedding intangibles in day-to-day business operations to achieve returns. Mindset matters. Investing in intangibles is different from investing in tangibles. Take a supermarket as an example. Investing in a new store is fairly straightforward for a retailer with relatively certain prospects for sales. However, the sales boost from investing in, say, a real-time promotion platform is less certain. In the worst-case scenario, the property may be able to be resold, but an investment in software may not be able to be recovered. This illustrates why investing in intangibles requires a mindset shift toward the test-and-learn, risk-taking approach that is more typical of top growers than low growers. In the survey, 70 percent of top growers agreed with the statement "in order to achieve above market growth, you need to pivot to a mostly test-and-learn, agile culture," compared with 60 percent of low growers.

As the intangible, digitized economy spreads, the imperative to reskill—within companies, and more broadly in society—becomes even more urgent. Digitization, automation, and the deployment of intangibles appears to have accelerated as leading companies responded to the pressures of the COVID-19 pandemic. A December 2020 McKinsey Global Economic Conditions survey of executives found that about 75 percent of respondents in North America and Europe said they expected investment in new technologies including automation to accelerate in 2020–24, up from 55 percent who said they increased such investment in 2014–19. This could put more pressure on low-skill workers who are disproportionately susceptible to being displaced by automation.

Intangibles bring new requirements for knowledge infrastructure. The shift from tangible to intangible assets increases the need for knowledge infrastructure. Policy makers will need to focus on facilitating knowledge infrastructure, including education, as well as communications technology including the internet, urban planning, and public science spending. Increasingly important will be digital infrastructure to store and manage data, the technology needed to support high-speed connectivity to transport data, and powerful high-performance computers to process data. This infrastructure will fully unlock the value of big data and foster scientific and technological innovation that enables firms to achieve their digital and innovation objectives.

The evidence is stacking up in an age increasingly driven by innovation and knowledge that firms and sectors that invest most heavily in intangibles are reinforcing and deepening their competitive advantage and achieving the highest rates of growth in gross value added. Fast-growing companies invest 2.6 times more than slower-growing counterparts. But investment in intangibles is only a starting point. The full potential of these game-changing assets will not be realized unless companies are smart about how they deploy them to create synergies and scale, and enhance a range of capabilities that can deliver on growth.

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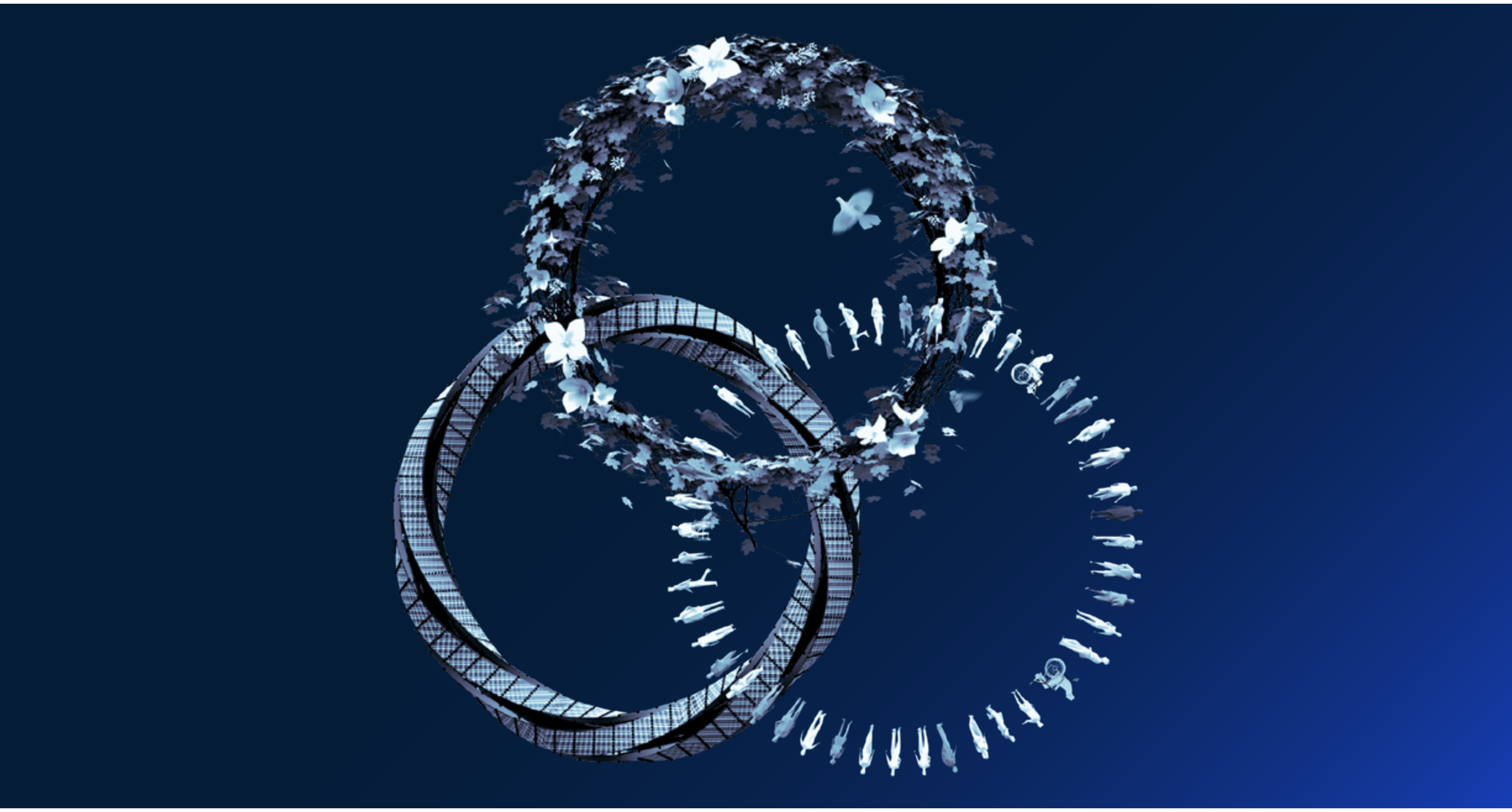
Our future lives and livelihoods: Sustainable *and* inclusive *and* growing

Growth for all, growth for good. Here, we offer a proposal for business, government, and society leaders.

by Bob Sternfels, Tracy Francis, Anu Madgavkar, and Sven Smit



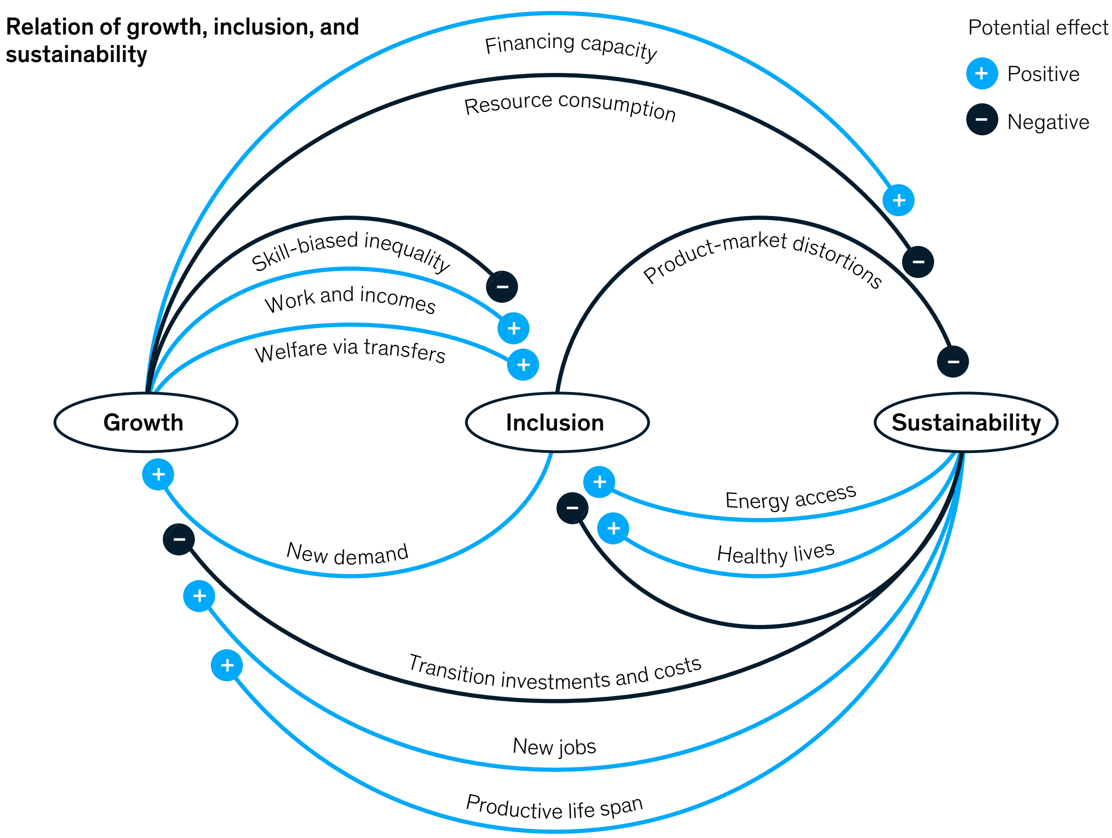
October 2021

As the world economy starts to emerge from the COVID-19 crisis, the time will soon come for leaders to look beyond safeguarding lives and livelihoods and to set their sights on a more profound challenge: bettering them. This societal challenge might be ten times as big as the pandemic and last ten times as long. The three goals we have in mind—growth, sustainability, and inclusion—buttress one another yet don't always pull in the same direction; we see powerful reinforcing as well as counteracting loops among them (exhibit). And so, while many might broadly agree on the aspiration, there's a very tough question lurking in the background: How do we go about building a future that delivers growth *and* sustainability *and* inclusion?

Full disclosure: we're not going to offer an answer. Instead, we propose a way for changemakers in business, government, and society to explore the problem, a mental model that might offer the best chance to reach the answer. It starts with this: we believe the *ands* are crucial and that they are in fact the means to the *end*. The three elements of growth, sustainability, and inclusion are deeply

Exhibit

Sustainable and inclusive growth can be a dynamic, self-reinforcing combination, but achieving it will require addressing counteracting forces.



Growth
Without growth, how will we achieve prosperity and well-being or pay for the transitions needed for a more sustainable and inclusive economy?

Inclusion
Without inclusion—an opportunity for productive work and life satisfaction for all citizens—how will we ensure the demand that propels growth?

Sustainability
Without sustainability, how can we have a long-term, tenable view on growth for this generation and the next?

connected and cannot be viewed as trade-offs. Consider this: without growth, how could we achieve prosperity and well-being or pay for the transitions needed to make the economy more sustainable and inclusive? Without sustainability, how could we fashion growth for the current generation and the ones to follow? Without inclusion—an opportunity for productive work and a satisfying life for all citizens—how could we ensure the demand needed to propel growth? Indeed, getting to *and*—moving to a world in which growth *and* sustainability *and* inclusion form a powerful dynamic—is the imperative for the next era of business.

But before we get to the challenge of *and*, let's face facts: hastening growth, sustainability, and inclusion are incredibly difficult challenges in their own right. Fortunately, thinkers, strategists, activists, and many others around the world—dreamers and doers—are working on it. We are too. In our view, the world will need to confront three problems simultaneously:

— *Growth is elusive.* In the mature G-7 economies, GDP growth has halved to 1 percent per year on average since the 2008 global financial crisis.[1] It's the same story in emerging economies: despite some exceptions, such as China and India, growth in emerging economies overall has been lower recently than in the early 2000s.

— *Poverty is still endemic,* despite the progress made. More than 600 million people still lived in extreme poverty as of 2017. And in 2020, another 100 million or so people joined them as a result of the COVID-19 pandemic. This will persist unless today's leaders create sufficient jobs with decent wages, as well as a robust social contract that ensures access to affordable housing, healthcare, and energy for the bottom one to three quintiles of the population, depending on the country. Meanwhile, a new threat to personal income is mounting: the rise of technology-driven changes in the ways we work, which the pandemic has accelerated. We estimate that more than 100 million people will need to make occupational transitions by 2030 in a set of eight advanced and emerging economies.

— *Ensuring a sustainable future will require massive investment.* For example, the International Energy Agency estimates that net-zero emissions might require investments of almost $5 trillion each year by 2030, and $4.5 trillion per year by 2050.[2] The annual bill equates to about half of global corporate profits in 2019, or about one and a half times the annual increase in public debt over the preceding 15 years. Additional investments needed for decarbonization in agriculture, transportation, and other sectors could nearly double the bill. While many of these investments would produce a return, their financing or pricing is not yet set up.

And that's just the start: as we explain in this article, even if the global economy were to get these three goals notionally right, there are contingencies among them that, if left unresolved, could wreck any progress made.

Here, we seek to frame the debate about achieving sustainable, inclusive growth in a clear-eyed way, laying out the aspiration but also the toughest problems that need to be solved to achieve this growth, with some illustrations as to their size. Good strategy should always start with asking the right questions. For today's leaders, the questions are vast and profound—*and* soluble.

The virtuous cycle starts with growth

What do we mean by sustainable, inclusive growth? There are many ideas associated with these words. We aim for broad rather than narrow interpretations:

— In *growth,* we include the ambition of increased prosperity and well-being, including economic-profit growth for companies, GDP growth

[1] World Economic Outlook Database, October 2021, International Monetary Fund, imf.org.
[2] *Net Zero* by 2050, International Energy Agency, July 2021, iea.org.

for nations—as well as measures such as life satisfaction for citizens—derived in part from dignity of work (while recognizing that measurable definitions of well-being are still evolving).

— In *inclusion,* we consider equality of opportunity and broad-based progress of outcomes for all—especially sufficiency of living standards—and the narrowing of inequalities among genders, ages, ethnicities, family backgrounds, and places of residence.

— In *sustainability,* we aim for environmental resilience, which starts with reducing climate risk but also includes much broader preservation of natural capital as well as intergenerational fairness, all considered in terms of economic and societal costs and benefits.

These three goals are daunting. Fortunately, they can strengthen and reinforce one another:

— *Growth supports inclusion, part 1: Creating meaningful jobs and lifting incomes.* High-growth emerging economies have delivered powerful proof that growth supports inclusion, by reducing the global share of those living in extreme poverty by two-thirds—to less than 10 percent of the world's population—and by welcoming hundreds of millions to the middle class. This applies in advanced economies too: from the early 1990s to 2005, before the global financial crisis, GDP per capita rose by 2 to 4 percent per year and real median household market incomes also rose.

— *Growth supports inclusion, part 2: Correcting labor-market inadequacies.* In growing economies, government transfers and tax policies can help support incomes for large swaths of the population. Research from the McKinsey Global Institute found that real market incomes were flat or fell for just 20 to 25 percent of households, after taxes and transfers; before these transfers, some 60 to 70 percent of households saw incomes decline.[3] During the pandemic, while US median household income dropped 2.9 percent in 2020, the share of people living in poverty declined, after accounting for government aid.[4]

— *Growth enables sustainability by encouraging investment.* Economic growth strengthens consumer confidence, spending, and demand, all vital elements of a healthy investment climate—which the energy transition is going to need. And as our research on outperforming emerging economies has shown, the capital deepening that results from greater investment spurs productivity and, with it, wages and growth.[5]

— *Greater inclusion and sustainability promote growth through new demand and investment opportunities.* Sustainability drives new business opportunities in domains such as clean technologies. India, for example, could more than quadruple its renewable-energy capacity by 2030; we estimate that this could generate some $90 billion in GDP and support about two million jobs in 2030. And inclusion has similarly powerful effects on growth. We estimate that more inclusive access to healthcare could add 0.4 percent to the world's GDP growth by 2040. More broadly, inclusion spurs demand, as a burgeoning middle class is a key driver of consumption. Africa has about 200 million young people of working age and will have close to a billion by 2050. Youth training and development, especially of digital skills, can vault this group into the middle class—and help close skill gaps in the rest of the world.

— *Sustainability reinforces both inclusion and growth through the 'energy prize.'* The energy transition will yield a prize of two cross-cutting benefits: lower costs that make energy more accessible, and more productive lives. Over the past ten years, the cost of electricity from renewables fell about 50 to 85 percent.[6]

[3] "Poorer than their parents? A new perspective on income inequality," McKinsey Global Institute, July 13, 2016, McKinsey.com.
[4] Income, poverty and health insurance coverage in the United States: 2020, US Census Bureau, September 14, 2021, census.gov.
[5] "Outperformers: High-growth emerging economies and the companies that propel them," McKinsey Global Institute, September 11, 2018, McKinsey.com.
[6] "Majority of new renewables undercut cheapest fossil fuel on cost," International Renewable Energy Agency, June 22, 2021, irena.org.

Renewables are now gaining ground in developing economies. In sub-Saharan Africa, a region with the lowest energy-access rate in the world, decentralized renewable solutions such as rooftop solar are taking root.[7] Lower emissions and reduced air pollution can improve health and allow more people to participate productively in the economy. History has some instructive lessons: after passage of the Clean Air Act in the United States, in 1970, reduced pollution increased the labor-force participation rate for affected individuals and had a positive long-run impact on wages.[8]

Squaring the circle

If only each element of the circle of sustainable, inclusive growth created purely positive reinforcements to the others, the way forward would be clear. But the reality is that sustainability, inclusion, and growth also counteract. Squaring this circle means combating three sets of potential counterforces, which could be just as powerful as the reinforcing loops.

Growth's counteractions

Growth imposes two major challenges. First is the persistent rise in inequality, which could worsen with growth. Already, 70 percent of the global population live in countries where inequality is mounting. Second is rising resource consumption and emissions.

— *Growth affects inclusion through skill-biased inequality—and its magnitude is set to rise with trends accelerated by the COVID-19 pandemic.* Growth in the knowledge-based economy has stoked demand for higher-level cognitive, technological, and socioemotional skills—a demand not matched by the supply of workers with such skills. As a result, a skill-biased inequality in many countries has sprung up. In the United States, for example, wages for middle-income jobs grew by 1.1 percent between 2000 and 2018, whereas wages for high-pay and low-pay workers grew much faster, at 7.3 and 5.3 percent, respectively. As the pandemic accelerates digitization and automation, almost all growth in labor demand could occur in high-

The three elements of growth, sustainability, and inclusion are deeply connected and cannot be viewed as trade-offs.

[7] Jan Corfee-Morlot et al., *Achieving clean energy access in sub-Saharan Africa*, Organisation for Economic Co-operation and Development, January 31, 2019, oecd.org.
[8] Adam Isen, Maya Rossin-Slater, and Reed Walker, "Every breath you take, every dollar you'll make: The long-term consequences of the Clean Air Act of 1970," VoxEU, February 19, 2014, voxeu.org.

wage occupations. The number of workers who would need to make occupational transitions by 2030 in order to stay employed would increase by up to 25 percent, including—for the first time—many low-wage workers.

— *Growth counteracts sustainability through greater resource consumption.* The global "material footprint"—that is, the raw materials used to make the goods that we consume—rises in correlation with GDP growth.[9] As growth expands in emerging countries, the problem of an increasing global material footprint could get worse. According to the World Bank, about 10 percent of the world's people still have no access to electricity, and 2.6 billion people lack access to clean cooking solutions.[10] If increased demand from a globally expanding consuming class is not accompanied by improvements in resource efficiency, this will put an even heavier burden on the planet.

Sustainability's counteractions

Trillions in capital are needed for energy investment to achieve the goal of net-zero emissions by 2050. If consumers and businesses shoulder the burden, near-term growth and inclusion could suffer, even though the longer-term benefits are clear. If costs are passed on to consumers, energy prices could rise well before the gains are eventually reaped, and if costs are passed on to businesses, the profitability of whole sectors could suffer.

This dynamic sets up the potential for two counteractions: uneven distribution of impact and a challenge to the goal of inclusion.

— *The energy transition could affect some countries and sectors severely.* Oil- and natural-gas-producing economies could see their annual per capita income from these products fall by about 75 percent by the 2030s, according to the International Energy Agency.[11] Lower-income countries will be disproportionately exposed because they have a higher share of emissions-intensive sectors and will also need to make higher investments relative to their GDP. Those sectors include power, automotive, construction, and others, all of which will be intensely affected, as will supply chains.

— *Lower-income households are disproportionately vulnerable.* In Europe, recent rises in energy prices—the vanguard of the energy transition—are falling heavily on low-income households, prompting some governments, including in Spain, to provide subsidies.[12] And while the transition could lead to some 18 million more jobs in the green economy, according to International Labour Organization estimates, many people, especially lower-income workers, will need to retrain to qualify for these new jobs.[13]

Inclusion's potential counteractions

The positive spillovers of inclusion are indisputable and well documented: greater workforce participation, higher creativity, more capital allocated to children's needs. However, poorly conceived measures to boost inclusion can have unintended negative consequences that can include distorted product markets, reduced investment, or faster environmental depletion. For example, in developing economies, free or highly subsidized nonvolumetric pricing of electricity used to pump water can lead to groundwater depletion.[14] Efforts to achieve equality can also backfire if they become a box-ticking exercise, or a quota-driven program, which may fail to address the root causes of inequality. As a result, the goal of achieving a fairer workplace or society may not be achieved, and outcomes may even worsen for certain groups.

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[9] *The Sustainable Development Goals Report 2019*, United Nations, 2019, unstats.un.org.
[10] "Report: Universal access to sustainable energy will remain elusive without addressing inequalities," World Bank press release, June 7, 2021, worldbank.org.
[11] *Net Zero by 2050*, July 2021.
[12] "Spain targets energy firms as European bills surge," BCC, September 14, 2021, bbc.com.
[13] *Greening with jobs—World Employment and Social Outlook 2018*, International Labour Organization, May 14, 2018, ilo.org.
[14] Bekele Shifraw, "Addressing groundwater depletion: Lessons from India, the world's largest user of groundwater," World Bank Independent Evaluation Group, August 23, 2021, ieg.worldbankgroup.org.

Achieving a future that is sustainable *and* inclusive *and* growing is so compelling an idea that today's leaders owe it to future generations to act immediately.

Starting here, starting now: A proposal

Achieving a future that is sustainable *and* inclusive *and* growing is so compelling an idea that today's leaders owe it to future generations to act immediately. Such a feat cannot be left to enlightened self-interest: if it were that easy, the problem would already have been solved. We see six key challenges that will need to be tackled—with success or failure hinging on how effectively these challenges are met.

1. How to ***unlock growth supported by higher productivity*** of an additional 1.0 to 1.5 percentage points of GDP per year, at a global scale with the same urgency that we have seen during the COVID-19 pandemic?

2. How to ***reduce the transition costs of decarbonization*** by, say, $500 billion to $1 trillion of the $5 trillion in required spending per year through technological innovation and smart-portfolio choices?

3. How to ***finance and smooth the cost of the energy transition***, country by country and sector by sector, in a way that won't stifle growth?

4. How to ***reskill and re-employ*** more than 100 million workers who are in stagnating or shrinking occupations as a result of technological change, including the many millions who will likely be displaced by energy transitions?

5. How to strengthen the social contract by ***achieving basic needs for median households***, including affordable housing, healthcare, and energy—needs that are unmet for many of these families in both advanced and developing countries—in a way that attracts private-sector innovation and supply?

6. How to ***support the most vulnerable population segments***—for example, the poorest one-fifth of the global population—that struggle with access and affordability in areas such as nutrition, water, energy, education, and financial capital?

Answering these six questions would negate the counterforces mentioned earlier and allow the virtuous cycle to flow unimpeded. But important obstacles, linked to incentives, stand in the way. First is what Mark Carney has called "the tragedy of horizons": today's leaders collectively need to take action today for returns that will accrue only over time.[15] Second is the tragedy of the commons: for collective action, especially on environmental sustainability, all invested parties must look past their parochial interests and fight for the common good.

No stakeholder can solve all these problems on their own. A clear road map, with buy-in from others, is paramount, as is a framework of incentives that balance short- and long-term horizons and interests across value-chain elements, economic sectors,

[15] "Breaking the tragedy of the horizon—climate change and financial stability—speech by Mark Carney," Bank of England, September 29, 2015, bankofengland.co.uk.

countries, and regions. As in the case of the pandemic, tackling these challenges successfully will require multiple experiments, unprecedented speed in scaling successful ones, and broad participation across actors.

Governments will need to orchestrate a resilient transition—to manage risks, smooth costs, and avoid cascading crises in response to actions taken. On the business side, more companies and CEOs will need to enter the arena, to engage deeply in the design of policies, and to contribute their market knowledge. They will need to be open and realistic about the challenges, while also setting ambitious goals to create positive impact for their customers, workforces, societies, and the environment. Their capacity for innovation can and must be harnessed to shift the frontier of what's possible and to help achieve what may seem unachievable. If companies don't engage well and honestly, younger generations of workers will hold them accountable.

When it comes to achieving sustainable, inclusive growth, it is crucial first to fully recognize both the reinforcing as well as the counteracting loops. Then the conversation must move from agreeing on the targets—for who would not agree to such a tantalizing vision—to understanding how to solve the tough problems that stand in the way.

For our part, we have put our hypotheses on those problems at the top of our research agenda and look to learn even more from the leaders of the global organizations we work with who are "making a dent in the universe" through sustainable, inclusive growth. We hope that the ways in which we've sketched out the forces and counterforces here contributes to our collective understanding. With that, it may be possible to start to move toward a sustainable *and* inclusive *and* growing global economy.

If we don't focus on the *and*, we won't achieve the end.

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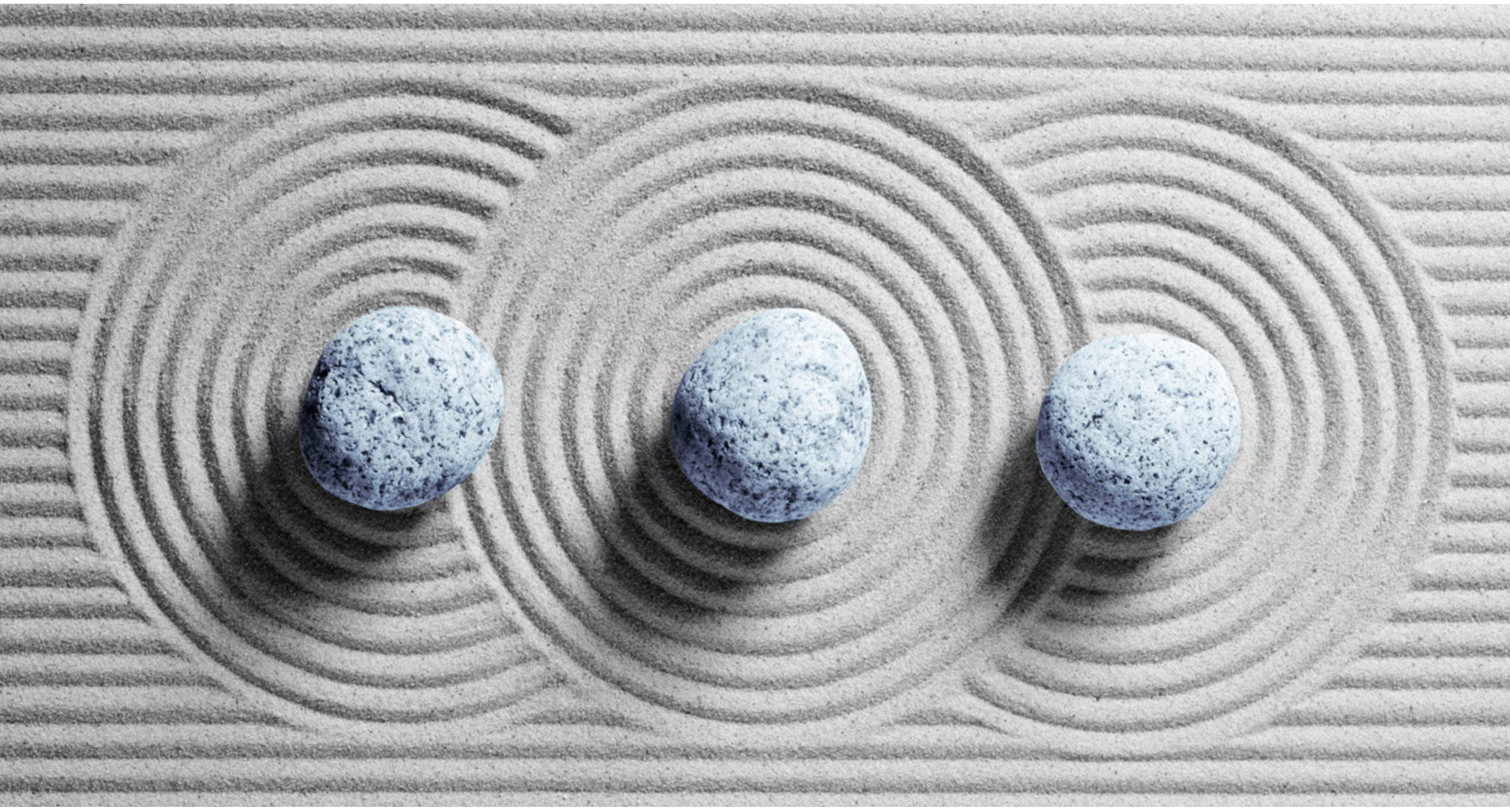
The authors wish to thank Peter Gumbel and Daniel Pacthod for their contributions to this article. This is the first in a series of articles devoted to sustainable and inclusive growth.

Designed by McKinsey Global Publishing

The growth triple play: Creativity, analytics, and purpose

Companies that integrate creativity, analytics, and purpose are delivering at least two times the growth of their peers.

by Biljana Cvetanovski, Brian Gregg, Eric Hazan, Orsi Jojart, and Jesko Perrey



June 2021

Key takeaways

— Only 7 percent of companies are delivering on the growth triple play by unifying creativity, analytics and purpose. They are **driving average revenue growth of 2.3 times versus peers from 2018–19 (which increased to 2.7 times versus peers from 2019–20).**

— In the period 2018–19, companies using just one of the capabilities—either creativity, analytics, or purpose—saw an average growth rate of more than 6 percent. Adding a second component saw growth rates climb to more than seven percent. **For those that employed the full triple play, growth rates climbed to more than 12 percent.**

— CMO's have a once-in-a-generation opportunity to lead growth, as **78 percent of CEOs are now banking on CMOs and marketing leaders to drive growth.**

The next normal is the 'no normal'

The year 2020 was unlike any other, as lives and livelihoods were upended by the pandemic. COVID-19 affected every aspect of our lives, forcing customers and businesses alike to embrace new behaviors, including digital ways of working, shopping, and relaxing. Within a span of a few months, a decade's worth of e-commerce adoption took place as the pandemic raged, leading to many new, digital-first marketplaces. The normal we all knew was gone. In fact, there was no normal at all.

The historic shifts brought on by the pandemic have also fundamentally changed the role of marketing leadership and the chief marketing officer (CMO). According to McKinsey's new research, in these "no normal" times, 78 percent of CEOs are now banking on marketing leaders to drive growth.

We looked at how more than 860 executives across the globe are prioritizing investments and capabilities that help accelerate growth.[1] In the process, we uncovered three elements—creativity, analytics, and purpose—that constitute a "growth triple play" that provides at least two times the growth of peers who don't invest in all three in tandem. Even before the pandemic, companies that had developed all three capabilities were logging double the growth of their industry peers, a margin that only increased once the COVID-19 crisis hit. But even though all three elements are available to most companies, only 7 percent of companies have been able to use them successfully in combination.

To better understand how companies are using the growth triple play of creativity, analytics, and purpose to drive above-market growth, we separated out those that have most successfully integrated all three elements to see what they do differently.

The growth triple play

The companies that use the three elements of the growth triple play together—creativity, analytics, and purpose—achieve dramatically higher average growth rates. The research shows using the full growth triple play can boost average growth rates by 2.3 times compared to companies that don't use any of the three elements. The results were even more dramatic during the pandemic, when the impact of using the full triple play boosted growth rates by 2.7 times.

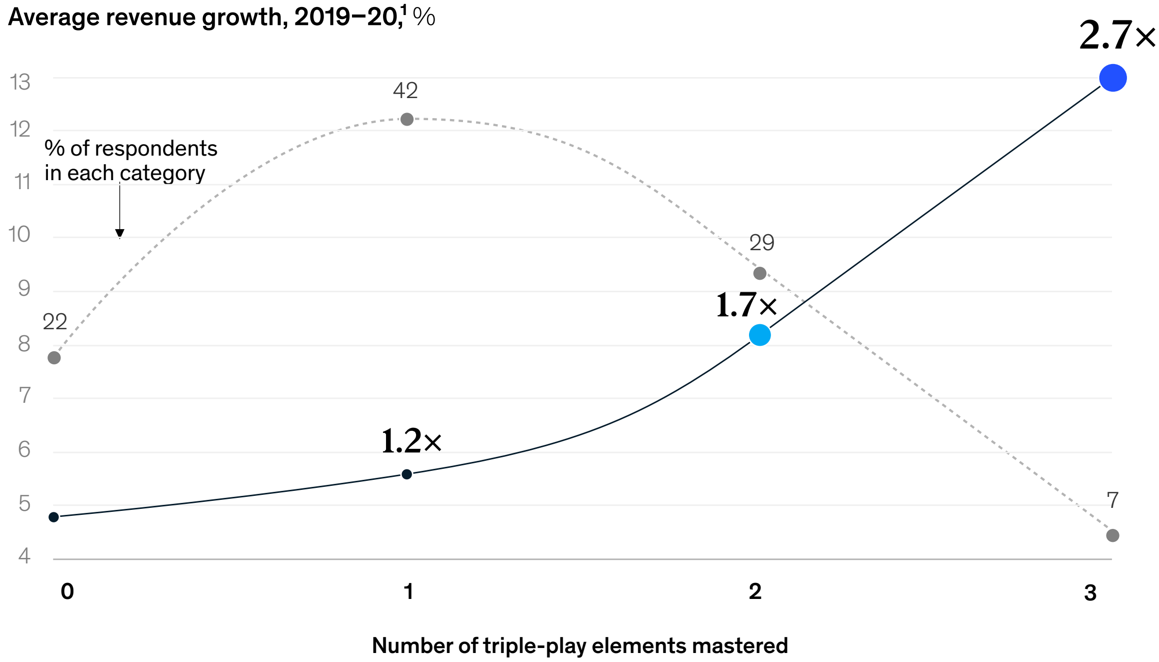
That cumulative impact is striking. In 2018–19, companies that used any one of the capabilities—whether creativity or analytics or purpose—saw an average growth rate of more than 6 percent, for companies that added a second component, growth rates climbed by another 15 percent to more than 7 percent, and for those that employed the full triple play, growth rates shot up by 67 percent to more than 12 percent.

[1] For the full McKinsey Global Institute report, see "Getting tangible about intangibles: The future of growth and productivity?," McKinsey Global Institute, June 2021, on McKinsey.com.

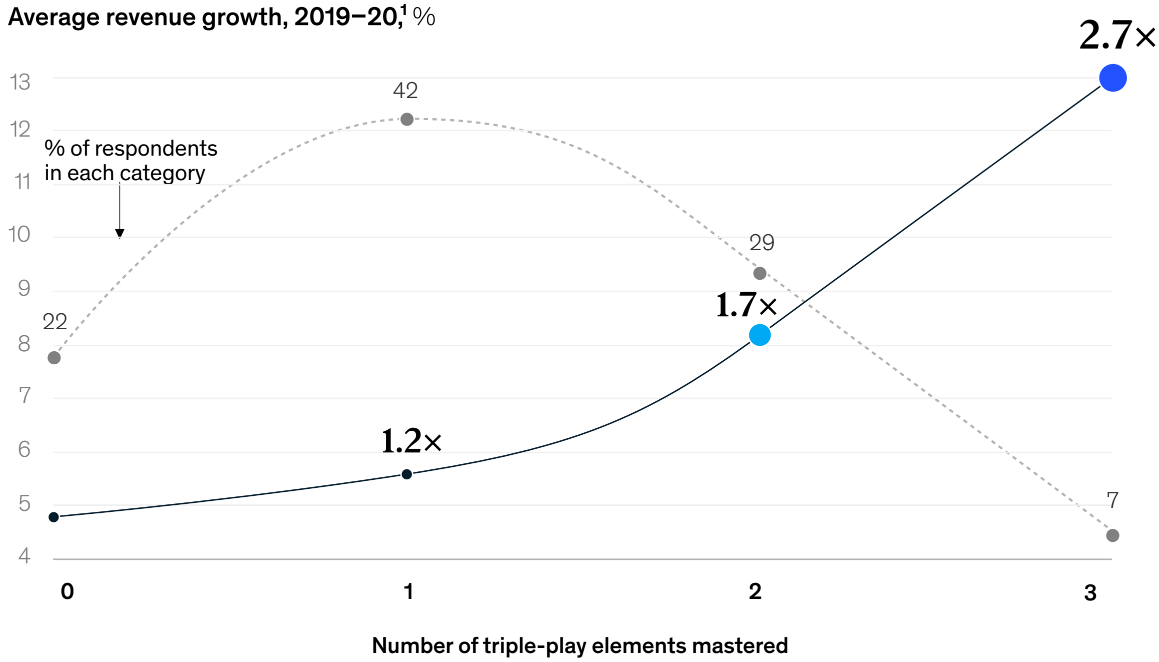
Exhibit 1

The triple play is positively associated with growth, having a further halo effect during the pandemic.

Average revenue growth, 2019–20,[1] %



Average revenue growth, 2019–20,[1] %



Each element of the triple play is critical. Creativity is part of the origin story of marketing. It's in the breakthrough ideas that have always underpinned bold, imaginative campaigns. The last revolution in marketing was all about the fusion of creativity and data analytics. What's new today is partly the addition of purpose, the statement of a goal higher than just ringing up the next transaction. Purpose can vary widely, as long as it is true to what the brand ultimately stands for. Says Ann Mukherjee, CEO North America at Pernod Ricard: "Purpose could be about fun. Purpose could be about indulgence. Purpose could be about being a rebel. Purpose could be about saving the world. But purpose must be intrinsic to what the brand's narrative is."

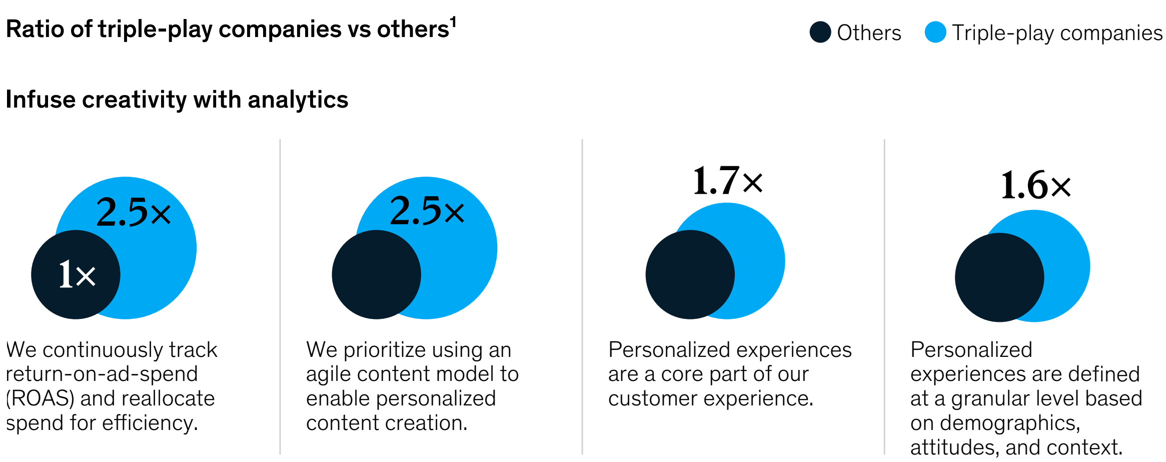
The elements of the triple play turn out to be mutually reinforcing. The speed and granularity delivered by analytics is far more powerful when integrated with innovative, breakthrough creative ideas and programs. Both resonate with customers in a deeper way when they are connected to purpose. Triple-play companies that have learned to integrate all three elements are 1.8 times more likely to be in the top quartile of growth within their sectors. McKinsey's research provides clear insights into exactly how the triple-play companies are deploying the three elements. It is not a theoretical exercise. Those companies take these specific steps to activate the triple play across the full sweep of their marketing practices:

Infuse creativity with analytics

Creativity starts by thinking and dreaming big, by opening the aperture to new ideas and approaches to delight customers. The discipline comes from making sure the customer is always front and center. Triple-play companies take more than a 360-degree view of their customers. Creativity is what gives rise to new campaigns, new products, innovative ways to serve consumers, and more. The addition of granular data and analytics can unleash creativity more effectively to drive deeply personalized customer interactions using iterative, test-and-learn approaches. Analytics help marketers make decisions at a faster clip by using marketing sensors to monitor changes in consumer behavior and make budget reallocations in real time.

Exhibit 2

Companies that utilize the growth triple play infuse creativity with analytics at much higher rates than those who don't.



[1]Ratio of triple-play companies that answered "strongly agree" vs other companies that answered "strongly agree."

From the field: Mars' Sheba brand uses the power of creativity to bring HOPE

Great creativity draws people in, engages them, and ultimately inspires them to take action, whether it's buying a product or embracing a cause. Jane Wakely, lead CMO of Mars, Incorporated, explains how the Sheba Hope Reef project builds on Mars's purpose with science while embracing creativity: "Purpose is our guiding light at Mars; we want to make a meaningful and measurable difference in the world. Sustainable fishing is close to our heart because pet parents love their pets to sometimes enjoy fish. Our goal, working with WWF over the past decade, has been to sustainably source 100 percent of the fish used in our pet food recipes. But we wanted to do more; scientists tell us that by 2043, 90 percent of the world's coral reefs will in fact be gone and 25 percent of all marine biodiversity will be lost. Since 2008, the Mars Coral Reef Restoration Program has installed over 19,000 Reef Stars, incorporating more than 300,000 coral fragments to help restore ocean health.

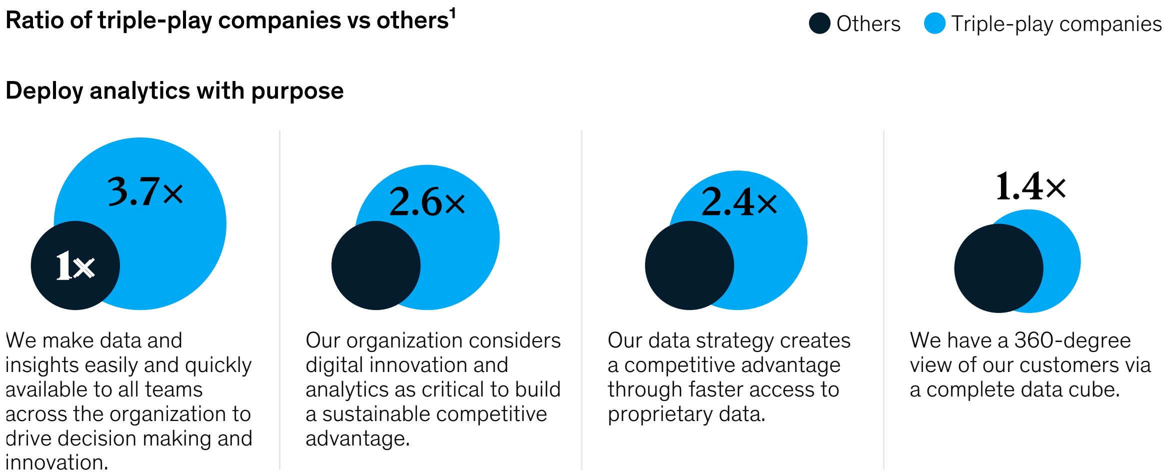
We believe that more coral today means more fish for tomorrow. This purpose, in turn, inspires creativity. By involving our creative partners, we have built a coral reef which simply spells out the word 'H-O-P-E.' HOPE Reef is so large it can be seen from space. We want to grab people's attention in a cluttered world, and then drive them to a collection of content that educates them about coral restoration and galvanizes them to join the effort to restore ocean health. "It's a magical way to open people's minds, but also their hearts and get them on board to drive a movement that makes a meaningful and measurable difference," said Wakely.

Creativity is what gives rise to new campaigns, new products, innovative ways to serve consumers, and more.

Deploy analytics with purpose
Creating moments that are meaningful for customers requires analytical horsepower and precision to discover customer intentions, interests, and unmet needs. At a time when companies are generating massive quantities of data, however, purpose serves as the anchor for marketers to determine which insights matter most and to focus their efforts there. That's why triple-play companies prioritize flexibility in their analytics and data architecture to not only co-create strategy with the C-suite but also to share those insights across the organization.

Exhibit 3

Deploying analytics with purpose is another feature of the growth triple play that companies who outperform their peers focus on.



[1]Ratio of triple-play companies that answered "strongly agree" vs other companies that answered "strongly agree."

Triple-play companies prioritize flexibility in their analytics and data architecture to not only co-create strategy with the C-suite but also to share those insights across the organization.

From the field: How Salesforce is organizing entirely around the customer

Brian Solis, global innovation evangelist at Salesforce and eight-time best-selling author, says technology has conditioned today's consumers to expect that they can get whatever they want, wherever they want it, within minutes. Meeting that high bar is simply not possible without analytics and an unwavering focus on the customer. This also includes organizational transformation. "We've become a customer-360 company, because we're helping customers organize and digitally transform entirely around the customer and customer insights to deliver that real-time value, throughout the customer journey. The goal is to create connected, intuitive, and personal 'ignite moments,' that moment when you have someone's attention and you know their intention, and you can deliver the best, most personalized, efficient, convenient, and 'wow' experience possible. Analytics help companies understand those wants in real time; AI and automation can even help them deliver against them ahead of time."

Focus on the purpose

Purpose acts as a North Star, guiding the overall direction as CMOs and marketers make crucial decisions that shape long-term growth. Linking purpose to creativity and analytics helps companies recognize the opportunities that are going to resonate most deeply with customers. CMOs and marketers understand the power of purpose and weave it into the culture, creating a recognizable sense of mission for customers, employees, prospective employees, and other stakeholders.

Purpose acts as a North Star, guiding the overall direction as CMOs and marketers make crucial decisions that shape long-term growth.

Exhibit 4

Finding power in purpose is the final element that companies who employ the growth triple play focus on.

Ratio of triple-play companies vs others[1]

Others | Triple-play companies

Find power in purpose

We have a unique value proposition to encourage talented people to join and stay with the company.

My company has a clear purpose and mission statement that allow us to assess what we do and don't do with respect to growth opportunities.

My company has a powerful, winning value proposition and brand positioning.

Our purpose is at the core of how we think and talk about our brand(s).

[1]Ratio of triple-play companies that answered “strongly agree” vs other companies that answered “strongly agree.”

From the field: How Oatly finds purpose in a more resilient food system

It’s not hard for John Schoolcraft, chief creative officer of Oatly, a global alternative dairy company based in Sweden, to explain his company’s purpose. Oatly aims to drive a systemic shift towards a sustainable, resilient food system where people don’t have to trade taste against the future of the planet. “Just talking about sustainability is useless. We want to prove to people that the things we are doing are having a positive impact on the world. For example, we have programs where we work with farmers on sustainable farming initiatives, such as more diverse crop rotation, which allow farmers to lower their use of fertilizers and herbicides, improve long-term soil health, and diversify incomes. We’re trying to create change, to gain the trust of our consumers through action instead of just talking. If you were to go back and analyze our creative work for the past nine years, you would see this approach in almost everything.”

Winning in the next-normal world

Marketing leaders have a once-in-a-generation opportunity to lead, shape, and drive the growth agenda. They can take advantage of this opportunity by integrating creativity, analytics, and purpose—the growth triple play—across the full spectrum of marketing activities. Already, the most successful CMOs are deftly using the precision and rigor of analytics to anticipate and satisfy customer needs, guided by purpose and energized with creative approaches.

On a practical level, winning in this next-normal world means orchestrating functions, across the organization and partnerships in the extended ecosystem, based on a richer understanding of customer wants and needs. In most companies, only the CMO is positioned to take this on with both internal and external relationships. Indeed, CEOs are increasingly depending on their marketing leaders to deliver growth. As marketers take on this expanded growth mandate, the most successful are willing to make fundamental changes to position themselves and their organizations to thrive in the post-pandemic environment. Success will be defined by how well those CMOs execute on the following three imperatives:

One: Lead from the front as a unifier

The CMO is now more than ever viewed as the CEO's "go-to" growth partner. Standing at the frontier where customer needs meet organizational capabilities, the CMO is uniquely positioned to draw on all functions across the organization. The ability to deliver on the growth agenda and demonstrate tangible impact will depend heavily on the strength of the collaborative alliances the CMO can forge across the C-suite and beyond.

Climb in the cockpit—you're the copilot now. Unleashing the full power of the triple play won't be possible without a strong relationship with the CEO. It's important to be bound together with a common vision and a strong foundation of trust. For example, while CEOs need no convincing on the importance of creativity in driving growth—77 percent of CEOs, COOs and board members already believe that creativity is a crucial growth driver in the post-COVID-19 era—only half of them believe it can be integrated with technology. Marketing leaders will need to draw on their full power as unifiers to bridge this gap, bringing together the creative and analytical branches of the organization, driven by purpose to create the solutions that can ignite and sustain growth over the long term.

Pernod Ricard North America CEO Ann Mukherjee sees the CMO as the Rosetta stone for the organization, from the finance department to the CTO. "The CMO has to be a jack-of-all-trades. They don't have to be a perfect expert when it comes to technology but must understand technology to stand side by side with the CTO and understand data architecture. In today's world of analytics, the delivery of mass-personalized content requires the CMO to understand martech, to understand how data flows in the company and how to deliver that across multiple systems. The CMO has to do the same thing with the finance organization to help them understand what value creation for a brand is, and to understand how that drives pricing or promotion. So all the things that typically were marketing are still important. But, today, the organization needs every function to be rowing in the same direction for you to deliver growth. That's why the CMO has to be a unifier."

Build alliances, not partnerships. To achieve that kind of unity of purpose across the organization, CMOs and marketers must lead from the front as unifiers as they work to build those critical relationships. Successful unifiers become strategic integrators sitting at the intersection of talent, technology, strategy, and communications. But forging that level of collaboration may not be easy. While most CEOs, COOs, and boards agree that marketing should be driving growth, there is much less consensus about the role of the CMO among the rest of the C-suite. Only 44 percent of CFOs and 62 percent of tech leaders agree that growth belongs to the CMO. The ability to create strategic alliances across the entire C-suite will be a critical skill in the next normal.

Be an ecosystem maestro. Speed of action only goes so far if other players in the ecosystem fail to move as quickly or are not aligned to a company's values and goals. To achieve extraordinary impact, orchestrating ecosystems and partnerships will be key in dealing with the new pace of change, complexity, and disruptions. Top CMOs and marketing leaders are thoughtful about what skills they need in house and which are better left to outside specialists who become part of a networked team of resources, there when marketing leaders need them but willing to recede when they don't. Triple-play companies in our survey were 1.9 times more likely to say they worked with agencies that lead in a certain capability area—even if that meant the company needed to manage more agencies.

Two: Inspire a better outcome with purpose
In the next normal, decision making happens fast and is pushed deep into the organization. A clearly defined and articulated purpose is what keeps the organization moving together in the same direction as one cohesive unit.

Rally stakeholders with purpose and vision. A clear purpose acts as a beacon, signaling to both internal and external stakeholders that the company knows who they are and what they stand for. Team members on the frontlines draw on that sense of purpose as they set priorities and make rapid-fire decisions. They know intuitively where they have permission to operate—and where they do not. That beacon is just as important for external stakeholders. Ecosystem partners know where the lines are drawn, investors understand the strategic priorities, and customers can measure how closely the organization synchs with their personal values.

Purpose is especially important when it comes to the critical task of recruiting and retaining talent. A clear purpose helps companies attract in-demand workers—especially important for companies located far from Silicon Valley that are competing for digital stars. Once the hiring agreements have been signed, that sense of purpose helps companies allocate critical talent to the most important value-driving roles. Triple-play companies are twice as likely to have a more robust talent-acquisition strategy than other companies. These savvy companies understand that attracting and retaining the right talent is more important to achieving and maintaining above-market growth than investments of capital.

Shape the portfolio with purpose. A well-defined purpose can also help marketers sculpt the product and brand portfolio, providing a guide for adapting and growing brands. Values will vary from organization to organization, but brands should serve both the organization and the customer, and in many cases a higher purpose. At Mars, Wakely calls this "building brands for mutual value." "We believe that brands should be driving transformative, sustainable growth for their category. Through our 'building brands for mutual value' vision we are reimagining the whole concept of brand-building and the value they can bring to the next generation. By harnessing the power of key brands to drive real change on key social and environmental issues, we can deliver mutual value for pets, the people who own them, the partners we work with, and the planet we all live on. This is at the heart of our vision and why our brands like Sheba are sparking action on issues such as biodiversity loss." That level of clarity helps organizations continuously refine their growth agendas. Triple-play companies are 1.6 times as likely to regularly review and refine their brand strategy to maximize growth and three times more likely than peers to discard brands, products, or activities that don't drive growth or detract from growth—even if they are part of the company legacy.

Three: Fire up the full growth triple play
There's a reason only 7 percent of companies have been able to deploy the full growth triple play: it's very hard to do. Only those that have developed the necessary capabilities are able to integrate creativity, analytics, and purpose.

Make the triple play core to company culture. Creativity is so fundamental to the marketing discipline, going back to its very roots, that every CMO and marketer should have a firm grip on the building blocks of visual representation, messaging, and media. But creativity also includes the ability to bring novel and disruptive new ideas to the surface, where those ideas can be refined, tested, and either scaled or discarded. That last part, however, is heavily dependent on the strategic analytical muscle, especially the ability to collect proprietary data and use it to generate insights that can drive value. Purpose helps set the overall direction, ensuring that every product or service, no matter how disruptive or surprising, is true to the brand identity and recognizable as such by customers.

Build a suite of growth enablers. Top marketers understand what motivates customers at a deeper level and can identify changes in customer behavior almost before they manifest. To achieve that level of customer knowledge, companies will need to develop insights that can help identify changes in demand markers based on when, where, and how fast customers are moving. This requires a suite of additional skills and practices to ensure rapid value creation and sustainable growth. The most important include the following:

— *Allocate resources*—by the week, the day, and the hour. Marketers should look to invest in a brand-building measurement ecosystem, including addressable TV analytics, "brand lift" studies geared for analysis, and geo-specific attribution and testing. This way, marketers have the flexibility to collect detailed insights on how exactly their campaigns are impacting consumer behavior and to track brand, reach, and frequency metrics. This new wave of data and performance metrics allows marketers to quickly adjust and reallocate resources and budget, by the week, the day, and the hour. Triple-play companies are 1.6 times more likely to continuously allocate and reallocate marketing spend in real time (or near-real time) to the most effective spend channels.

— *Know your customer like you're in the room.* The ability to serve up exactly what the customers want, when they want it, and in their choice of channel, is rapidly becoming a baseline customer expectation. It requires real-time data and analytics to create customized pricing and promotion. Triple-play companies go even further: they are 2.1 times more likely to have their brand positioning fit to clearly defined target groups. Some leading companies are developing new levels of understanding by building systems that can pool and analyze structured and unstructured data, algorithms that can identify behavioral patterns and customer propensity, and analytics capabilities to feed that information into dashboards. Those companies' customer-data platforms can connect a single customer across devices, cookies, and ad networks, and enable real-time campaign execution across touchpoints and channels.

— *Find new ways of working to boost the metabolic rate.* Without flexible architecture, developers will be slowed by dependencies across teams, the need to stabilize or integrate codebases after their development, and a lack of team-level ownership and accountability. Triple-play companies understand this and are allocating significant investment to modernizing their architecture. They are 2.8 times more likely to run analytics decisions in real time, and 2.1 times more likely to have a flexible infrastructure.

Seizing the big moment

Even in the most volatile of times, there are companies that are driving growth that is twice as high as their peers' through creativity, analytics, and purpose. By drawing on the full power of the growth triple play, CMOs and marketers can increase their odds of success, elevating their profile and their organization to new heights, and creating impact along the way.

For those that get it right, it can be the start of a new era where marketing is ascendant, and Marketing and the CMO is at the heart of decision-making. But to do so, they must act on new ideas, rigorous data-bound execution, and an unerring sense of purpose at the core.

The most resolute CMOs and marketers can rise above the chaos to lead the charge, inspiring their organization and their customers along the way.

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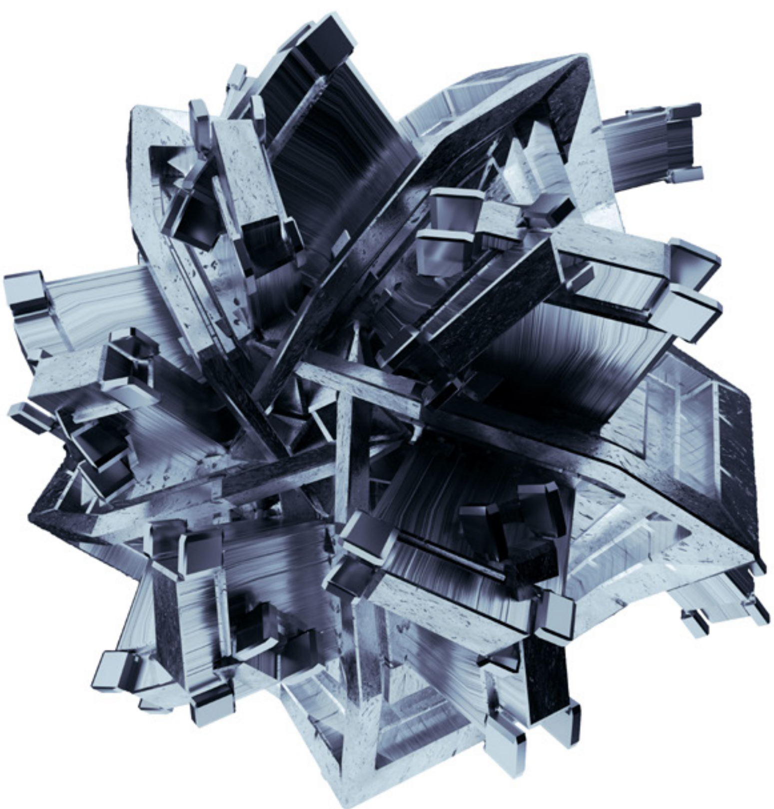
Marketing & Sales Practice

Seven principles for achieving transformational growth

Dogged persistence and nimble execution underscore a set of proven ground rules for growth.

by Michael Betz, Joy Chen, Rock Khanna, and Duncan Miller



April 2021

Growth creates value: companies that outperform their peers on growth post 30 percent higher total returns to shareholders.[1] Growth also benefits organizations and their customers, opening up new opportunities for employees and creating additional resources for innovation. It's hardly surprising, then, that growth is at the top of the agenda for almost every business. In the wake of COVID-19, many companies are looking to growth to help them quickly recover revenues and steady their business. For others, growth is a way to gain market share, capitalize on disruptions in consumer behavior, or lay the foundation for sustained success in the post-pandemic era.

As any executive will tell you, however, achieving and sustaining growth is hard—and it's not for lack of will or effort. Many companies have pushed well-developed and well-executed programs on a range of initiatives, from customer experience to sales effectiveness, that have shown clear success in delivering revenue. The issue, however, is that these promising results often stall out or deliver only a small portion of the company's full growth potential.

Delivering transformative growth requires the whole enterprise to act in concert—from the marketing-and-sales teams that drive customer acquisition, to the product and service leaders who deliver the customer experience, to the customer-service staff who help ensure customer satisfaction and loyalty. Because market conditions, competitive threats, and customer sentiments change often, such growth requires a mixture of doggedly persistent and nimble execution.

Over the past few years, we've worked with a wide range of organizations on comprehensive transformation programs to drive meaningful and sustainable revenue growth. Based on these experiences, we've identified seven principles that help leaders break historical patterns and achieve their growth objectives.

1. Look past the myths

Though growth transformations present significant challenges, executives can sometimes be deterred from attempting them by a few persistent myths.

One such myth is that pursuing growth during a crisis is a distraction from the issues at hand. On the contrary: McKinsey analysis shows that investing in growth during a downturn delivers the best results for organizations with healthy cash positions and balance sheets.[2] While it's important for businesses to focus on short-term issues related to a downturn, waiting for the economy to recover could mean missing chances to gain a competitive edge. There's no perfect time to embark on transformational growth, so waiting serves no purpose. The companies we work with tell us they wish they had started sooner, not waited longer.

Another myth we often hear is that a growth transformation will take too long and cost too much. To be sure, growth transformations do require

[1] Yuval Atsmon and Sven Smit, "Why it's still a world of 'grow or go'," McKinsey Quarterly, October 2015, McKinsey.com.
[2] Rebecca Doherty and Anna Koivuniemi, "Rev up your growth engine: Lessons from through-cycle outperformers," May 2020, McKinsey.com.

Because market conditions, competitive threats, and customer sentiments change often, such growth requires a mixture of doggedly persistent and nimble executivion.

investment, and the full payoff may not come until year two. However, disciplined organizations are able to quickly unlock significant efficiencies (for example, by improving efficiency of direct response channels such as paid search) and capture short-term revenue wins (for example, by adjusting prices).

Yet another myth is that growth isn't something leaders can control; it's the result of market forces, competitive dynamics, customer preferences, or sheer luck. True, external factors and good fortune play their part, but it's equally true that almost every business can improve its growth position. In fact, McKinsey analysis has identified a significant spread in growth performance among companies in almost every sector, indicating there is ample room for growth.[3]

2. Cleansheet a bold growth goal

The all-too-familiar approach to setting growth targets—taking last year's figures and adding or subtracting a few percentage points based on experience or gut feeling—has always been counterproductive. Now, when the pandemic has rendered year-on-year comparisons meaningless, it is sheer folly. The acceleration of the mass migration to digital triggered by COVID-19 requires leaders to cast a skeptical eye on trend lines and historical precedents and set goals that reflect the new landscape's potential. That means starting from scratch with a zero-based approach to growth planning. Time and again, we've seen leaders using this approach set and meet goals 40 percent higher than they achieved with their traditional strategies.

A zero-based approach to cost planning is well understood, but how does it work for growth? Top-performing companies start by breaking down the business into its components: customer journeys, brands, product lines, commercial activities. They then set a peak-performance goal for each revenue driver along each journey: generating demand, converting demand to sales, retaining customers, and expanding customer relationships over time. When setting these goals, they look for examples from top-performing units inside the organization and gather external benchmarks from market leaders, experts, and innovators in other sectors. They are guided by curiosity and an open mind, examining how new technologies can support more ambitious goals, challenging institutional norms, and refusing to blame external factors for past performance problems.

For one large retailer, adopting a zero-based approach to growth overturned long-held assumptions that its core brick-and-mortar business could not grow. While its stores had endured years of dwindling revenues, its much smaller online business had been growing at a double-digit pace. Prior forecasts predicted continuing decline for in-store business and a gradual slowing of growth in e-commerce. But leaders set aside these trend lines and their gut feelings about the company's likely trajectory and looked afresh at marketing strategy, sales-team performance, customer loyalty programs, and potential synergies between the physical and virtual sides of the business. Armed with this wider perspective, leaders reset their ambition: a double-digit improvement in the company's overall growth rate. Twelve months later, they had achieved it. *For more, see "How absolute zero (-based budgeting) can heat up growth."*[4]

3. Drive big impact from multiple moves

Rarely does growth come in one big bang; in our experience, targeting a comprehensive set of seemingly modest increments is a better strategy. We regularly see companies drive double-digit impact by identifying a few key revenue drivers, applying best practices to each one, and stacking up a series of small wins.

Although "breaking down the opportunity" into smaller wins is more manageable, many executives are still unsure how to proceed. There is, however, a body of empirical evidence on how businesses

[3] Kabir Ahuja, Abhinav Goel, and Kate Siegel, "Debunking four myths of organic growth," May 2019, McKinsey.com.
[4] Ronald Falcon, Kyle Hawke, Matthew Maloney, and Mita Sen, "How absolute zero (-based budgeting) can heat up growth," January 2018, McKinsey.com.

Leaders using this zero-based approch set and meet goals 40 percent higher than they achieved with their traditional strategies.

can drive commercial excellence, from boosting marketing effectiveness, to motivating sales teams, or testing and scaling pricing innovations. The challenge is not to invent new ways to improve performance, but to take the time to look outside your organization for proven methods and emerging solutions and apply them with discipline and rigor to the drivers that genuinely push the needle on growth.

When one educational-services company reviewed its marketing effectiveness, it found it had neglected brand awareness and overemphasized performance-marketing tactics. Drawing on empirical evidence and bottom-up analysis, the company reset its marketing budget and reallocated investments, boosting high-conversion inquiries by 24 percent. Working along the customer journey, the team then enhanced the website's user experience to increase inquiry flow; intensified coaching and adopted performance-management "nudges" to improve frontline sales; and introduced multichannel communications and peer-mentorship programs to support student success. Together, these efforts reversed five years of sales decline, propelling the company to double-digit growth in new sales in less than a year. *For more, see "Commercial excellence: Your path to growth."*[5]

4. Deliver a constant flow of growth

As one executive wryly observed, "Focus is overrated." What he meant was that sustained growth comes from creating and replenishing a pipeline of promising initiatives that deliver a constant flow of growth over time. Successful growth transformations strike a balance between quick wins (within three months), midterm operational improvements (three to nine months), and long-term strategic advantage (up to three years). They identify a comprehensive set of growth opportunities using the zero-based approach described above and then constantly review, reprioritize, and renew the mix of initiatives as the transformation progresses and its impact becomes apparent.

Quick wins are particularly important because they can generate savings or revenue to fund the growth program. For example, cutting spend on nonworking media or low-ROI trade shows could release funding for effective new digital-marketing campaigns. In addition, quick wins provide visible proof that the transformation is working, which can boost confidence, motivation, and momentum for longer-term efforts.

One multinational payments company kickstarted its growth transformation by analyzing price points across multiple products and services. Where it found room for growth, such as in high principal payments, it quickly lowered prices to gain share. In the medium term, it used granular geographic analytics to improve yield, reducing prices at locations with competitors nearby and raising them where competitors were more distant. The new pricing model delivered $100 million in incremental revenue as measured against comparable locations using the old model. To capture long-term growth, the company is now exploring more

[5] Russell Groves, Kun Lueck, and Stefano Redaelli, "Commercial excellence: Your path to growth," October 2018, McKinsey.com.

radical changes, such as moving from transaction fees to subscription-based pricing. *For more, see "Building an engine for growth that funds itself."*[6]

5. Execute with rigor

Even with the most promising ideas, strategies, and market conditions, a growth transformation won't deliver the goods unless it is implemented effectively. Given the need to develop and orchestrate a broad set of initiatives over time, impact depends on having a powerful execution engine. Yet excellence seems to be the exception, not the rule: only 37 percent of executives taking part in a recent McKinsey survey reported that their company's transformation had been implemented successfully.[7]

We find that companies that are successful at large-scale performance improvements apply the same rigor to growth transformations as they would to operational or cost-efficiency programs. Leaders translate ideas and goals into plans with detailed forecasts, KPIs, and milestones, and establish a weekly cadence for making cross-functional decisions and fine-tuning initiatives in real time. They communicate compellingly about the need for growth in order to motivate employees and foster accountability, and they involve middle management and frontline staff in driving change so as to go faster, do more, and build organization-wide support.

The leaders of a private-equity-owned business, for example, sought to reverse years of declining sales. Aware that the company's culture often led to paralysis by analysis, leaders appointed a chief growth officer to lead major initiatives in marketing strategy, sales-team performance, and customer experience. Within a year, the company had achieved double-digit growth in new sales. Looking back, the head of marketing credited this success to rigorous execution: "By adopting a weekly cadence of tracking progress, making decisions, and driving accountability, we were able to implement far more than we thought and at a much more rapid pace. It was the quality of our execution as much as the quality of our ideas that allowed us to meet and exceed our growth goals." *For more, see "Executive quick take: A guide to implementing marketing-and-sales transformations that unlock sustainable growth."*[8]

6. Turn measurement into a competitive advantage

As a military strategist once observed, "No plan survives contact with the enemy." Similarly, no growth transformation unfolds precisely as intended. Because changes in customer sentiment, competitor behavior, or market conditions will inevitably threaten to throw plans off course, having the means to measure progress systematically—and the stomach to act decisively—is a major asset. Such measurement yields insights that help leaders double down on successes, ditch failures, and adjust implementation for maximum impact.

Measuring growth is no easy task, however. Multiple variables are in play, and quantifying the impact of critical growth drivers such as brand building and sales force effectiveness are notoriously difficult. To tackle this challenge, companies can apply new digital metrics, such as share of branded search, to assess the impact of marketing campaigns, and apply advanced analytics to compile operational and survey data to link customer-experience improvements to hard-dollar revenue gains.

Tracking what matters. Having mapped customer decision journeys, identified revenue drivers, and developed initiatives, leaders then determine which metric to track—lead volume, win rate, deal size—to assess the progress of each initiative. One industrial company used account penetration, new product growth, and new-market entry as its key metrics and linked them to Customer Relationship Management (CRM) and Enterprise Resource Planning (ERP) systems to provide real-time visibility and performance updates for each driver and set of initiatives. Transformation leaders evaluated data from these systems in monthly progress reviews to

[6] Kabir Ahuja, Biljana Cvetanovski, Liz Hilton Segel, and Jesko Perrey, "Building an engine for growth that funds itself," May 2018, McKinsey.com.
[7] "How the implementation of organizational change is evolving," February 2018, McKinsey.com.
[8] Ralph Breuer, Kedar Naik, Bogdan Toma, and Martina Yanni, "Executive quick take: A guide to implementing marketing-and-sales transformations that unlock sustainable growth," September 2019, McKinsey.com.

Only 37 percent of executives taking part in a recent McKinsey survey reported that their company's transformation had been implemented successfully.

decide when and where to reallocate resources. The effort paid off with incremental revenue growth of 4.5 percent in a declining market.

Applying innovative metrics and predictive analytics. With growth drivers that are difficult to pin down or slow to change, like brand awareness or customer experience, companies can use new concepts, such as share of branded search, to measure progress. They can also take advantage of the increasing power of advanced analytics to build predictive models that highlight the relationships between customer behaviors and sales. One wellness company calculated how customer lifetime value correlated with satisfaction scores, number of guest services, and interaction with personalized nudges. Armed with insights from this analysis, it made changes in its stores and CRM tactics that increased average customer lifetime value by more than 8 percent.

Running multivariate experiments to assess impact and reduce risk. One of the thorniest challenges in measuring growth comes in weighing multiple metrics for multiple initiatives. Brand building can drive more web traffic that yields more sales, for instance, but it can also increase sales conversion rates on performance-marketing channels, such as paid search. An accurate way of tracking impact is to compare the results from an integrated package of changes in a given country or customer segment with the results from a control group. One online job-search company ran a matched-market experiment to assess the effectiveness of a new marketing campaign that combined investments in brand media with efforts to optimize performance-marketing channels. After the test showed a strong ROI, the company launched the campaign nationally.

Advanced measurement techniques help leaders not only to quantify impact but also to nurture a collaborative, data-driven culture focused on metrics and test results, not on anecdotes and finger-pointing. Because these methods capture the impact of factors that take longer to play out, such as improvements in product or service experience, they also help leaders balance their set of initiatives to drive sustained growth. *For more, see "Performance branding and how it is reinventing marketing ROI" and "Four ways to shape customer-experience measurement for impact."*[9]

7. Make capability building a priority, not an afterthought

Success in a digital world demands specialist expertise and analytical capabilities in activities from dynamic pricing to multichannel sales to digital marketing. Smart companies start to build those capabilities by conducting a comprehensive diagnostic of growth-related skills in marketing, business development, sales, pricing, and customer experience to act as a basis for personalized

[9]Thomas Bauer, Julien Boudet, Michael Lamb, and Kelsey Robinson, "Performance branding and how it is reinventing marketing ROI," June 2020, McKinsey.com; Victoria Bough, Ralph Breuer, Harald Fanderl, and Kevin Neher, "Four ways to shape customer-experience measurement for impact," April 2017, McKinsey.com.

development plans. They then execute on the plans with the same care and determination they apply to the transformation itself by nominating an executive sponsor and workstream leader to drive the effort and set milestones, identifying KPIs, and tracking progress.

Courses and training naturally have their place, but the best learning comes from doing: sitting next to an expert, observing, and then practicing a new skill. With the difficulties of face-to-face contact during COVID-19, best practices are emerging for sharing expertise remotely. Short and frequent video calls are proving to be more motivating than occasional long sessions—half an hour twice a week, say, rather than half a day once a month.

It's worth noting that tackling too many skill gaps at once saps energy and focus. A better approach is to take each function in turn and isolate a set of capabilities that directly link it to value creation. Then it's a matter of practicing, repeating, reinforcing, and role modeling the new skills. To make them second nature, smart companies introduce daily performance huddles, set aside one-to-one coaching time, and hold high-profile celebrations of small wins.

At one leading B2B technology company, a redesign of the sales organization was coupled with a program to reinforce managers' everyday coaching skills. The program was customized to meet the needs of different roles and reinforced through changes in performance indicators and incentives. After a pilot among 30 sales reps exceeded its revenue target by over 20 percent, the company began rolling out the program across its entire inside sales team. *For more, see "The five things sale-growth winners do to invest in their people."*[10]

Transformations are uncertain in the best of times, and growth transformations are the most challenging of all. Following the seven principles outlined above can't guarantee success, but it should help tilt the odds in your favor.

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The authors would like to thank Michael Harney, Steven Lubow, Lindsey Padrino, and Shreya Thacker for their contributions to this article.

[10] Matt Deimund, Michael Drory, Daniel Law, and Maria Valdivieso, "The five things sales-growth winners do to invest in their people," October 2018, McKinsey.com.

Revenue growth management: The time is now

Market challenges and legacy decisions are forcing consumer-packaged-goods companies to rethink their strategies for revenue growth management.

This article was a collaborative effort by Kevin Bright, Mher Panossian, Pieter Reynders, Ankit Sood, and Roman Steiner, all with McKinsey's Marketing & Sales Practice.

August 2021

Key takeaways

— The pandemic has unleashed a wave of additional complications for consumer-packaged-goods (CPG) industry leaders to understand and resolve.

— Input costs for many products have jumped, and consumer behavior has shifted significantly, intensifying the pressure to rethink revenue growth management (RGM).

— CPGs need a differentiated, three-step approach to become best-in-class. But their window for taking action is narrow.

Three fundamental challenges for CPGs

Consumer-packaged-goods leaders have faced difficult and constrained times over the past decade. Even before the pandemic, growth in the consumer industry was challenging, and margins were sustained primarily through productivity gains to offset the effect of price compression. In this context, CPGs needed to build new capabilities to capture more value from RGM. While 2020 brought volume growth for some CPG categories thanks to pandemic-driven consumption growth, the overarching issues have been exacerbated by the inability to sufficiently leverage RGM. Now, as CPGs look ahead, they are facing three major challenges: to relieve P&L pressure from commodity inflation at a level not seen in over a decade, to address consumer and shopper shifts, and ultimately to develop repeatable ways to align prices with or beyond the consumer price index (CPI).

While the pandemic provided a pause—RGM was understandably not a priority for companies in the past year—it also unleashed a wave of new challenges.

First, there is the return of inflation. Many commodity prices are spiking and are expected to remain high, driven by everything from global supply-chain disruptions when the pandemic hit to the more recent strong rebound in consumer demand with limited capacity to meet it (exhibit). These factors are significantly raising input costs for CPG companies, resulting in greater than double-digit increases in cost of goods sold (COGS) in some situations. Given the extent of inflation, multiple retailers have publicly expressed an expectation for higher CPG prices.

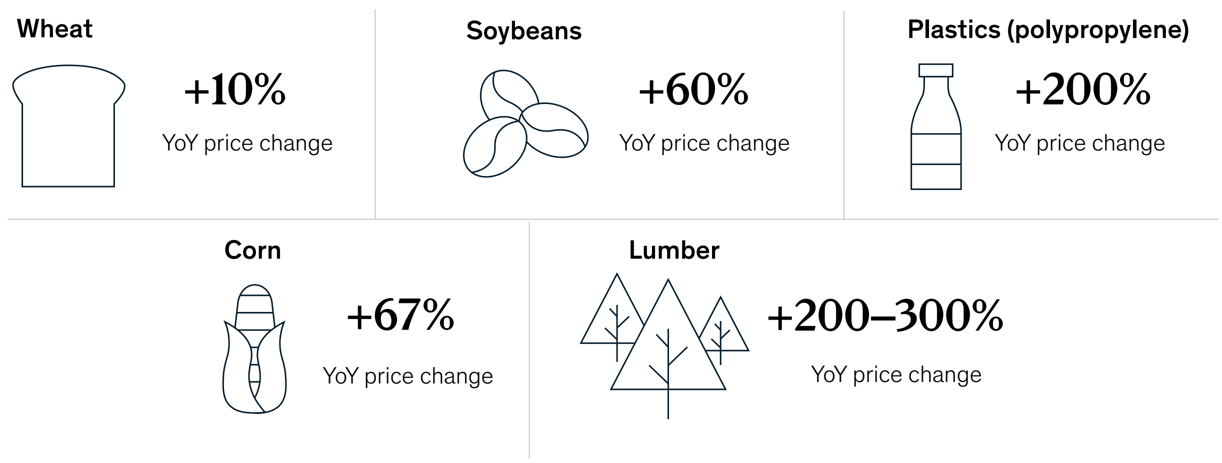
Secondly, there have been unprecedented changes in consumer behavior, shopping habits, and channel dynamics in the past 18 months, which are likely to influence all categories for years to come:

Consumer behavior: declining brand loyalty, increasing at-home needs, and a K-shaped recovery. Across markets, 25 to 40 percent[1] of consumers have tried different brands since COVID-19 started, highlighting the importance of promotions to attract brand switchers. Second, demand has spiked for categories like health and wellness and “at-home” needs, a trend that is expected to persist in the next normal. Third, while our analysis indicates a recovery in consumption, it also anticipates sharp differences geographically and across income segments. In the United States, consumption from high-income households, which accounted for two-thirds of the pandemic-driven consumption drop, will likely determine the economic recovery’s magnitude and pace. The demand recovery is thus expected to be K-shaped: rising consumption for high-income households and slower consumption recovery for low-income households, whose incomes have been affected

[1] Tamara Charm, Anne Grimmelt, Hyunjin Kim, Nancy Lu, Mayank, Mianne Ortega, Kelsey Robinson, Yvonne Staack, and Naomi Yamakawa, “Consumer sentiment and behavior continue to reflect the uncertainty of the COVID-19 crisis,” October 2020, McKinsey.com.

Exhibit

Prices of select commodities have increased in the past year.



disproportionately by the pandemic. In Europe, extensive government support has limited the impact on employment and thus disposable income. However, the resulting higher savings rate has been more elevated among high-income households, and the outlook for low-income-household consumption can be negatively impacted by the labor market.[2] In Asia, the largest drivers of growth are expected to remain the increasing incomes and spend of low-to-mid-income households.[3]

Shopping habits: bigger baskets, fewer trips, and changing preferences. We see shoppers doing more stock-up and fill-in buying than impulse purchasing, although there are important nuances. Additionally, our research[4] shows the shopper base has divided even further. For example, 19 percent of Europeans have already traded down in 2020 and plan to continue doing so.

Channel dynamics: dramatic shift toward online retail and "at-home" channels. Online retail has grown by more than 50 percent in some categories, accelerating a long-term trend, with a high share of consumers expected to continue shopping online. Second, "out-of-home" channels, historically often more profitable for CPGs, have materially shrunk, presenting additional complications. Finally, B2B marketplaces have grown to serve fragmented small grocers, impacting traditional distributors (especially in China, India, and Brazil).

The final factor challenging revenue growth management for CPGs concerns pricing. Historically,

[2] For the full McKinsey Global Institute report, see "The consumer demand recovery and lasting effects of COVID-19," McKinsey Global Institute, March 2021, on McKinsey.com.
[3] Homi Kharas, "Who gained from global growth last decade—and who will benefit by 2030?" Brookings Institute, January 16, 2020, brookings.com.
[4] Claus Gerckens, Franck Laizet, Daniel Läubli, Jean-Albert Nyssens, and Eugen Zgraggen, "The path forward for European grocery retailers," March 2021, McKinsey.com.
[5] Annie Gasparro and Dave Sebastian, "Shoppers start to see effect of higher commodity costs," *Wall Street Journal*, March 31, 2021, wsj.com; Sharon Terlep, "Procter & Gamble will raise prices in September," *Wall Street Journal*, April 20, 2121, wsj.com; Amelia Lucas, "Coca-Cola CEO says company will raise prices to offset higher commodity costs," CNBC, April 19, 2021, cnbc.com.

CPG pricing has trailed inflation, creating margin pressures. For example, US consumer price index (CPI) data show the price of packaged foods increased 12 percent from January 2012 to January 2020, less than the 17 percent increase for all items excluding food and energy. In Europe, pressures on retailers have made net price reductions the norm rather than the exception. CPGs now find themselves needing to catch up to compensate for both the past 18 months and for longer-term behavior.

Driving growth through a differentiated approach

While the outlook remains unclear, we see CPGs shifting from simply meeting demand—the stance for many during the past 18 months—to pursuing margin and growth in this new context. Indeed, companies from food to household and personal care have announced price increases for 2021 in the mid- to high-single-digit range.[5]

While inflationary pressures often cause CPGs to use pricing to support margins (and this is also happening), companies that have successfully navigated such circumstances in the past consider near-term pricing actions strategically, defining a multiyear journey to realize their pricing objectives through a mix of RGM levers, rather than simply using headline pricing across the board.

Indeed, shifting dynamics and the inflationary environment call for an even more comprehensive assessment of the levers available to companies to meet their pricing objectives. CPG leaders need to rethink RGM's main elements— pricing, trade and promotion investment, assortment —and how to combine them to create the necessary "muscle."

— *Pricing.* While it is tempting to move fast to cover 2021 input-cost inflation, CPGs need to set pricing strategy for the long term. It's critical to take a nuanced approach, informed by volume, simulations of the impact of price moves on profits, and measurement of net elasticities, for example. Given the macro-economic dynamics at play, such as the K-shaped recovery in the United States, it will also be important to assess the impact of pricing decisions, across price tiers and income segments, on the affordability concerns of consumers. Taken together, these actions facilitate surgical rather than flat price increases across the portfolio or even in micro-geographies, balancing revenue and profits against volume, penetration, and market share. Finally, it will be important for CPGs to understand the full implications of the evolution to online buying and increased transparency and to adjust their pricing actions appropriately.

— *Trade and promotion investments.* While there may likely be competitive pressure and a tendency to simply revert to 2019 levels over coming months, the 2020 promotion reductions enable re-baselining and "retraining" shoppers. Resetting in the right way requires a clear view of the impact of new consumer behavior during promotions and of the short- and long-term impact of promos. In Europe, the focus on net price management means some reductions will likely need to be shifted to other conditional trade terms to compensate. In the United States, we could see a significant shift to pay-for-performance structures and more conditional trade terms. In growing emerging markets, there's demand for new trade-investment approaches, such as leveraging digital B2B marketplaces. In Asia, a shift in 2020 to modern trade in some markets, at the expense of fragmented trade, requires CPGs, who have historically focused more on route-to-market excellence, to shift toward structured trade investment and promotions. Finally, CPGs need to ensure they are effective in the growing online channels, including personalized promotions.

— *Assortment.* Equally important is resetting the assortment based on true incrementality and cost of complexity. CPGs seek to address the challenges of changing their product mix

[5] Annie Gasparro and Dave Sebastian, "Shoppers start to see effect of higher commodity costs," *Wall Street Journal*, March 31, 2021, wsj.com; Sharon Terlep, "Procter & Gamble will raise prices in September," *Wall Street Journal*, April 20, 2121, wsj.com; Amelia Lucas, "Coca-Cola CEO says company will raise prices to offset higher commodity costs," CNBC, April 19, 2021, cnbc.com.

to offset margin pressure, retail demands for portfolio simplification, and new shopper behaviors. While not returning to the 2019 level of SKU proliferation, CPG companies need to mindfully introduce “good complexity” by selecting innovations and SKUs that are truly incremental.

Additionally, as a result of shifting consumer habits, micropockets of consumer growth (such as shopper type, income level, location preferences) have shifted. Identifying these micropockets and acting on them through a superior understanding of markets and consumers has thus become even more important, and the key to winning them could be getting the above RGM actions right.

Implementing these measures requires solid RGM analytics. The fluid nature of shopper behavior and the supply shortages in 2020 have created noise in the historical data and are making it more challenging to identify relevant data trends. This calls for RGM teams to adapt their data-and-analytics approach to incorporate different consumer-insight sources. These include sentiment surveys to get updates on behavior shifts in time to react, data-set partitioning to isolate temporary effects and train analytical models accordingly, and an increased frequency of data-set updates to be able to monitor changes.

How to approach the opportunity

That’s why 2021 is such an important year for RGM in the consumer sector. We recommend three actions best-in-class CPGs should take during the second half of this year as they plan for 2022:

1. *Undertake a comprehensive clean-slate review of RGM.* Given the dramatic shifts in consumer behavior and commodity price pressure, it’s time to reevaluate underlying assumptions and rebuild plans thoroughly, based on the differentiated approach described above. It’s also an opportunity to “clean the slate” and remediate such historical RGM fundamentals as channel conflicts, poor-performing promotions, everyday low price/cost (EDLP/EDLC) funding, underperforming trade investments, and price points stuck at given thresholds.

2. *Embrace new, granular data sources and advanced analytics to drive consumer-centricity.* The boom in consumer-level data for CPGs can present new possibilities, if CPGs become adept at understanding their consumers and shoppers at granular levels and at translating those insights to tactical execution guidelines. For example, CPGs are now leveraging advanced analytics to tailor their store-level assortment to fragmented trade, often building multiple store segments based on their shopper profiles. This segmentation can be built on consumer traffic and demographics data through geospatial capture and store-shelf data captured automatically through sales-rep handhelds. This enables tailoring assortment and in-store execution to microlocal consumer preferences.

3. *Rebuild your RGM tech for the next normal.* The complexity and increased importance of omnichannel execution, the plethora of data sources, and the ever-faster pace of market change makes rapid and user-friendly RGM tech a critical enabler of effective RGM. We have accordingly seen multiple CPGs advance their tools and analytics suite to support decision making, in particular with automated data-ingestion pipelines, automated visibility tooling, and more integrated, predictive price-promo-pack action simulations, enabling faster and more precise RGM action. These capabilities demand a step up in analytics infrastructure, talent, partnerships, and governance. Typically, it takes companies at least 18 to 24 months—and for some, a multiyear transformation journey—to develop the capabilities required for success.

Market and consumer changes are challenging CPGs to rethink their RGM strategies. Hence, the next normal presents an opportunity for a step-change in RGM's impact. But the window may be narrow, and any delay in mobilization risks leaving CPGs out of the game, failing to keep up with consumer and market dynamics that are fundamentally—and rapidly—changing.

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The authors wish to thank Pedro Fernandes, Simon Land, Sheldon Lyn, and Joel Saa-Seoane for their contributions to this article.

Defying cost volatility: A strategic pricing response

While input cost increases and volatility are challenging, they present an opportunity to improve pricing and institutionalize best practices—but margins will likely suffer if these are not executed in a strategic way.

by Alex Abdelnour, Arnau Bages-Amat, Stephen Moss, and Manish Prabhu

August 2021

Key takeaways

— The ongoing input cost increases and volatility, while representing a difficult challenge, provide an opportunity to improve pricing through adoption of best practices.

— Organizations that adopt a strategic approach to pricing actions can significantly minimize margin leakage during a pricing action.

— Our four-step approach can put your organization on a path to pricing excellence, allowing you to recover cost increases and minimize negative impacts to financial performance in a responsible, transparent, and customer-centric manner.

The impact of the global pandemic on demand and pricing varied across industries. While demand initially fell significantly for segments such as luxury retail and food service, others such as consumer building products saw demand spike as people invested in their homes. The pandemic also disrupted supplier operations and supply chains, leading to significant availability issues across products and geographies.

Not surprisingly, most companies during the past 18 months focused on meeting customer demand and managing profitability through targeted cost savings. Pricing remained an afterthought. And while many upstream players have begun to increase prices in response to cost increases, downstream organizations have balked. Many have left prices largely unchanged or have implemented only minor increases, especially during mid- to late 2020, concerned about the impact on communities when lives and livelihoods are at risk.

Yet the business environment in recent months has been very different. In the United States, the consumer price index jumped 5.4 percent in June, its biggest monthly gain since August 2008.[1] Raw-material costs have also been increasing steadily since July 2020 (Exhibit 1). As a result, several manufacturers and distributors have implemented price increases to keep up with rising costs and minimize impact on financial performance.

The decision to implement price changes in an atmosphere still heavily impacted by a global pandemic is not easy. Pricing strategies grounded in advanced data analytics, informed by value created for customers, and supported by well-planned price execution can help put a check on the degradation of financial performance, potentially narrowing the gap between supply and demand. It may also position companies for improved financial performance when business returns to postpandemic normalcy. Yet price changes are not simple and can carry risks: our analysis shows poor management of pricing actions can wipe 66 cents off every dollar of potential price improvement (Exhibit 2).

As companies imagine the postpandemic economy, leaders ready to invest in pricing to counter inflation and to build strong foundations for growth may want to carefully consider four steps:

1. building an analytical fact base
2. setting a value-based dynamic pricing strategy
3. creating conviction among the sales force
4. governing and carefully tracking execution and results

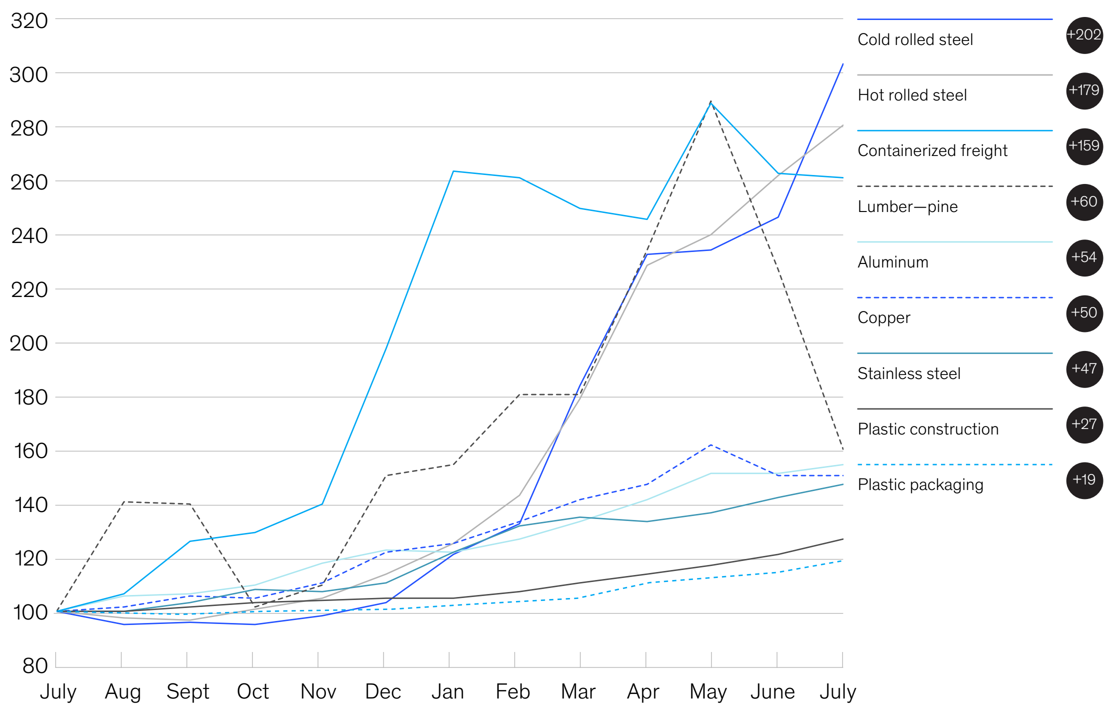
By strategically and systematically implementing price changes, companies could effectively pass on input-driven cost increases (or decreases) in a value-based way while potentially creating healthier pricing practices and stronger customer relationships that will endure.

[1] Agence France Presse, "US Annual CPI Jumps 5.4% In June, Biggest Since 2008: Govt," Barron's, July 13, 2021, barrons.com.

Exhibit 1

Manufacturers and distributors must adjust their pricing strategies to account for rising costs of raw materials.

Select raw-material costs indexed to July 2020, %



Source: Drewry; ITC; Metal Bulletin; Nasdaq; SBB; US Bureau of Labor Statistics

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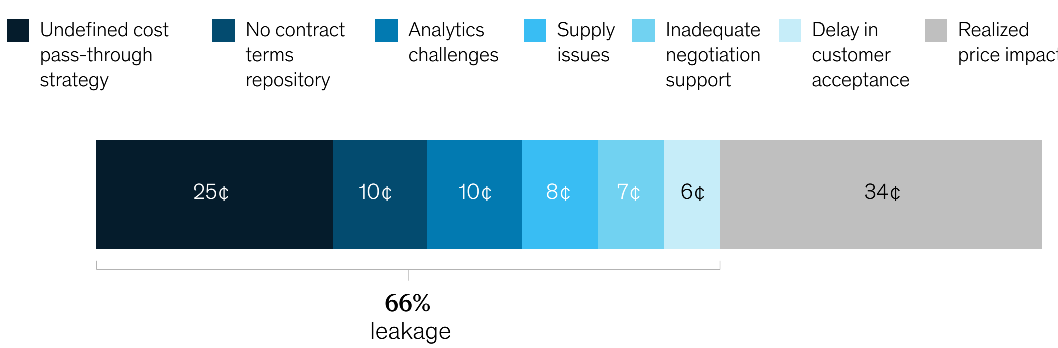
Exhibit 2

Two-thirds of potential price improvements tend to leak out because of inadequate strategy, policy, and process support.

Distribution of one dollar in price improvement, cents



Source: McKinsey analysis

Many commercial leaders have hesitated, reluctant to reflect the impact of input cost increases in their product prices.

A (new) world of cost volatility

After the upheaval of the past year, demand has begun to stabilize at a new level—often very different than before the COVID-19 pandemic. Supply chains are adjusting to the next normal, and prices of raw materials are increasing rapidly, primarily trending upward across categories. To accommodate this shift in input costs, manufacturers and distributors may have to adjust their pricing strategies. Yet many commercial leaders have hesitated, reluctant to reflect the impact of input cost increases in their product prices. This hesitation may be driven primarily by the fear that being the “first mover” in their segment could potentially hurt customer relationships in a way that is only worsened by the pandemic (for example, significant volume loss). Yet we believe there are few alternatives to passing on (at least partially) input cost increases.

In our experience, being reactive about a price increase often leads to last-minute, generic, broad-brush price hikes that lower customer satisfaction and worsen any systematic pricing or margin strategies companies may have in place. For example, in a previous article we shared the story of a packaging company that delayed changing its prices for a few quarters before being compelled to pass through a sweeping price increase to mitigate the impact of a 20 percent yearly rise in raw-material costs.[2] The move wasn't aligned with its overall pricing strategy, and the organization hadn't prepared its sales force to respond to customers' concerns and questions. Within three months, it lost double-digit market share and had to roll back a portion of the price changes.

A four-step approach to pricing success

Companies should consider investing in a careful and strongly executed plan both to maintain margins and to create stronger customer relationships and healthier pricing practices. To carry this out, most decision makers can adopt a four-step approach to pricing discipline:

1. *Build the analytical fact base.* Compile transactional data down to contribution margin for the past two to three years and create transparency on all key contracts. Assess historic cost pass-through performance and current cost pass-through policies (if there are any in place). Evaluate contractual obligations and opportunities for renegotiation in a systematic way. In parallel, revamp standard, actual, and forecast costing processes to ensure the true impact of input cost changes is reflected in the cost of goods sold. Assess forecasting accuracy of cost, and supply and demand. Building the analytical fact base that shows the impact of expected cost increase, as well as planned and potential pricing actions on future profitability, allows for the development of a future pricing strategy based on insights rather than gut feel. This helps remove abstraction—especially when input costs haven't been tracked historically—and provides the logic and language business leaders and sales teams need to credibly and transparently communicate with customers. In addition to a more long-term pricing strategy, the transactional and contractual transparency allows for the rapid identification of quick wins, such as outdated,

[2] Alex Abdelnour, Christopher Angevine, and Jeremy Seeley, “The commercial response to cost volatility: How to protect margins against inflation and tariffs,” June 2019, McKinsey.com.

margin-bleeding contracts that should be renegotiated right away.

2. *Set your dynamic pricing strategy.* A key objective of any good pricing strategy needs to be the protection of margins. But the approach to achieving that needs to be tailored to the business and economic situation. For a price-sensitive commodity business that is highly affected by select raw materials, the focus needs to be on rapid and full cost pass-through. This is often achieved by linking prices to commodity indexes. This approach is reactive, and often leads to delayed cost pass-through and consequently margin loss. While effective for a commodity business, the same approach could be damaging for a business selling specialized, differentiated products and services. Leading organizations have used advanced analytics to forecast changes in raw-material costs and imbalances between supply and demand, as well as prices in their end markets, and built capabilities to proactively change their pricing and contracting approaches. Depending on the situation, a value-based treatment of price changes (where the value is quantified and priced in relation to competitive products) or a more steady, measured price increase—to ensure margins are protected when raw-material cost increases pass through production, inventory, and finally to goods sold—could be the right approach. In addition, organizations can look for remediations that are related to the purchasing or manufacturing of the products, such as switching contracts to alternative suppliers, changing product content to lower the impact of raw-material cost without compromising product quality, updating standard cost processes to build in latency and accuracy, and matching customer contract duration to supplier contract duration.

3. *Create conviction in the sales force.* Provide appropriate training so sales teams can gain confidence in holding effective price-change conversations with customers, manufacturers, and distributors. Commercial leaders need to anticipate buyers' questions so that sales representatives and managers are comfortable discussing price with procurement organizations—we find that an effective preparation is for sales teams to role-play customer conversations in a variety of scenarios. Many organizations institute a comprehensive performance-management system, including training, value-selling, updated incentives, and key performance indicators, along with rollout of cutting-edge analytical pricing tools. All of these are in service of building sales confidence and conviction. In fact, many leading sales organizations find that the price-change conversation is an opportunity to discuss other ways the supplier can create value with the customer. If the supplier is viewed more as a partner and less as a vendor, the price-increase conversation could be seen as a win–win for both sides.

4. *Implement governance and impact tracking.* Establish clear escalation processes for pricing approvals, and delineate performance-management processes specifying how customer concerns are handled, what information and approvals are required to make exceptions to a planned increase, and how quickly information and answers will be provided to the decision maker on the account team. Standard pricing processes and performance reviews are often too slow to manage rapid change in a magnitude that has not been seen in a long time. Management must be able to quickly and easily monitor which customers have been contacted, which are at risk, what price levels have been approved, and whether the business is on track to achieve its target. This can mean tracking results at a customer-item level on a weekly or even daily basis to gain an understanding of where to increase focus. Depending on the nature of the change (temporary versus sustained), this could require a temporary short-circuiting of standard processes or long-term, structural change of key processes.

While these four steps feel intuitively accurate and simple, the real challenge organizations face is their ability to execute them with enough granularity, accuracy, and speed to make them effective and actionable. In our experience, organizations may avoid taking action because of a perception that they lack sufficient data and analytic talent to make progress. The reality is that most organizations have adequate data within existing systems to undertake basic analyses and straightforward actions.

Those realizing value with this approach can then begin to invest further in their systems, especially dynamic pricing systems, as well as in acquiring analytic talent to uncover future pricing opportunities. Coupled with a focused change-management effort across the organization, these organizations put themselves on a road to achieving the cross-functional collaboration necessary to deal with cost increases, price volatility, and any other challenge that might arise. It's a path to pricing excellence: organizations can potentially recover cost increases and minimize negative impacts to financial performance in a responsible, transparent, and customer-centric manner.

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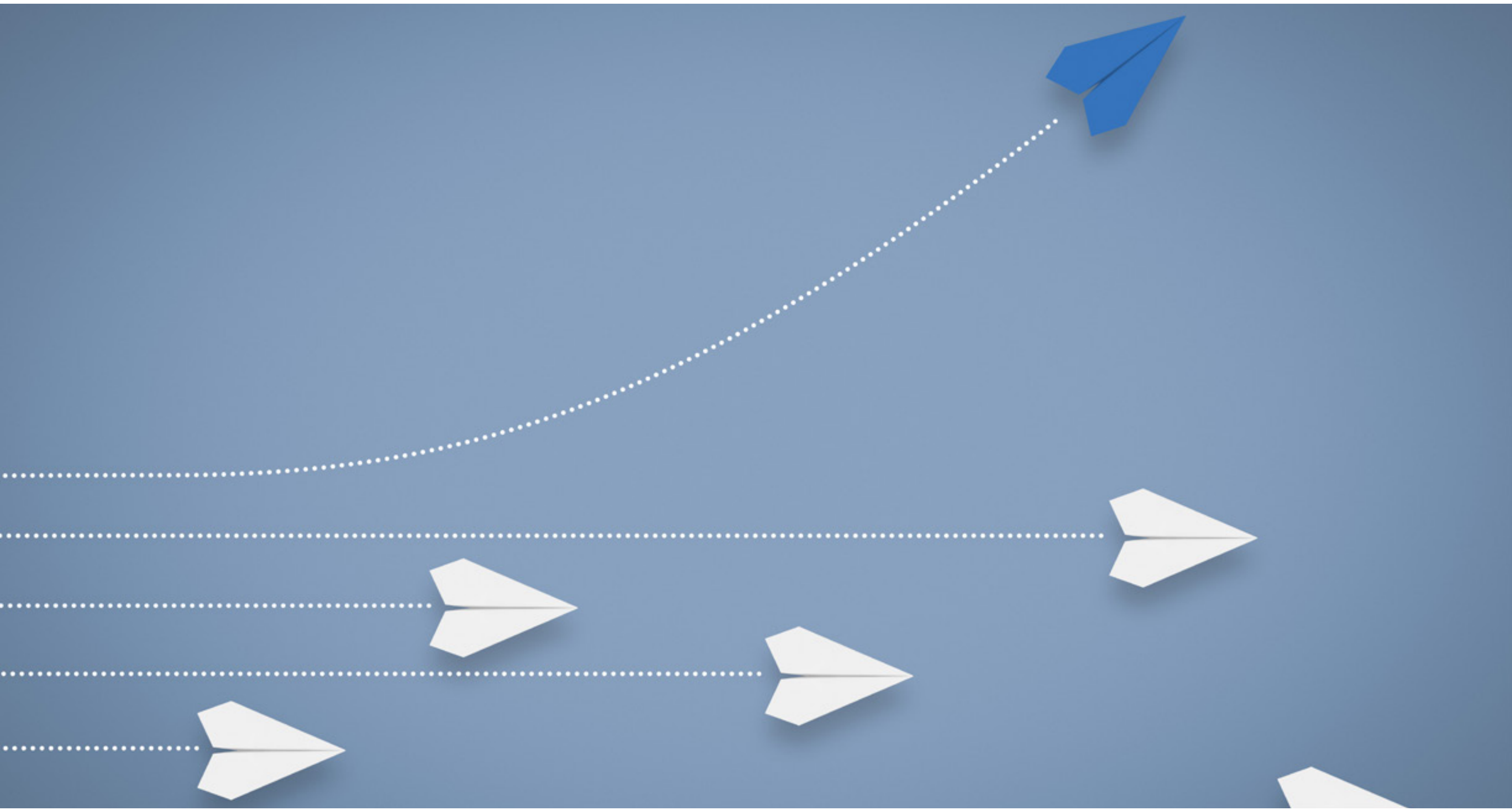
The authors wish to thank Rohan Maini and Dean Pugachev for their contributions to this article.

Designed by McKinsey Global Publishing

By the numbers: What drives sales-growth outperformance

New data reveals that outperformers are ahead of the pack where it matters in insights, agility, talent, and tech

by Boudewijn Driedonks, Sinem Hostetter, and Ryan Paulowsky



April 2021

Insight, agility, talent, and technology continue to be the four most important dimensions in next-generation sales growth. But excellence in each of these areas looks far different today than it did five years ago. A McKinsey global survey of 2,500 B2B companies across industry found that those willing to shake up their sales models and embrace next-generation capabilities are growing revenue at twice the rate of GDP.

In each dimension, top performers nail the basics, then move quickly to levers that drive exponential gains. For insights, that's predictive data and analytics. For agility, that's speed in customer responsiveness and cross-functional teaming. Collectively, it's a capability and mindset shift that leads to always-on innovation—and above-average growth.

Outperforming B2Bs zero in on specific dimensions, then go all in generating outsized advantage.

In insights, leaders gain a 2 to5 percent bump in sales as a result of data-driven decision making. In agility, cross-functional coordination and teaming drive a 5 to 10 percent increase in sales. In talent, behavioral science and analytics shape training and development, leading to a 10 to 20 percent improvement in productivity. And in technology, the right digital enablers and processes set the foundation for continued growth and innovation.

Driving sales-growth outperformance

Four dimensions

Insights
Embracing analytics and data to make rapid proactive decisions through the customer journey.

Agility
Organizing the commercial function to bring the best of the organization to every customer interaction.

Talent
Using behavioral science and analytics to hire and develop world-class sales talent.

Technology
Having the right systems, tools and, processes to make it work, seamlessly

Driving sales-growth outperformance

Take action

Insights

Basics: Core pipeline and pricing metrics

Outperformers add: Predictive analytics focused on growth pools

Agility

Basics: Organized to support multichannel

Outperformers add: Organized to scale solution selling, account reprioritization & omnichannel

Talent

Basics: Strong in universal sales skills

Outperformers add: Tailored coaching, continually adapted training

Technology

Basics: CRM & backbone tools

Outperformers add: Advanced, seller-friendly tools

Total impact:

5–10% higher sales

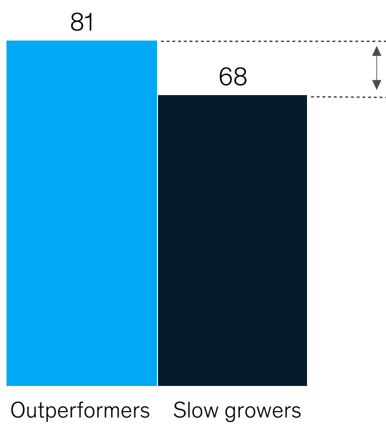
10–20% higher productivity

Fast growers scale insights by centralizing analytics

Eight in ten fast growers cluster data science, engineering, workflow integration, and other cross-functional skill sets into a centralized hub to build critical mass. Close coordination lets teams design new use cases, iterate and deploy them faster, and build scale. Sales leaders that use centers of excellence report greater confidence in their ability to harness the potential of data and analytics than companies that don't.

Insights

% of B2B companies that have an analytics center of excellence



Outperformers invest in an analytics center of excellence

19%

more than slow growers

Companies with an analytics center of excellence are

1.4x

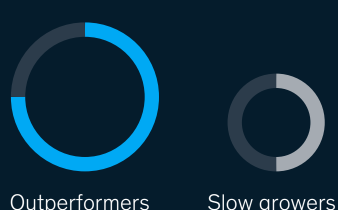
more likely to be outperformers

They move beyond table stakes and apply analytics use cases

Outperformers make data and analytics a strategic asset and invest heavily in building foundational skills. The results pay off: 72 percent of the fastest-growing B2Bs say their analytics are effective in helping them with sales planning, compared to 50 percent of the slowest-growers.

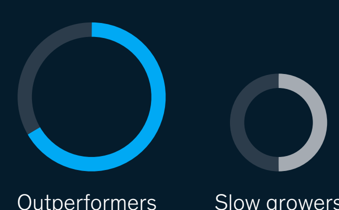
Having mastered the basics, leaders look for "spikes" that give them a customer and scale advantage. From web-crawling to sentiment analysis, outperformers use specialized analytics to dig into individual deals, propensity to buy, and lifetime profitability with greater precision than the average B2B. Two-thirds or more generate deal-level insights, account-level intelligence, and customer-specific sales opportunities. Only about half of slow growers say the same.

Insights



3 out of 4

outperformers apply tables stakes analytics such as sales planning **(vs half of slow growers)**



2 out of 3

outperformers apply analytics use cases to be more granular on deal and account level opportunities **(vs half of slow growers)**

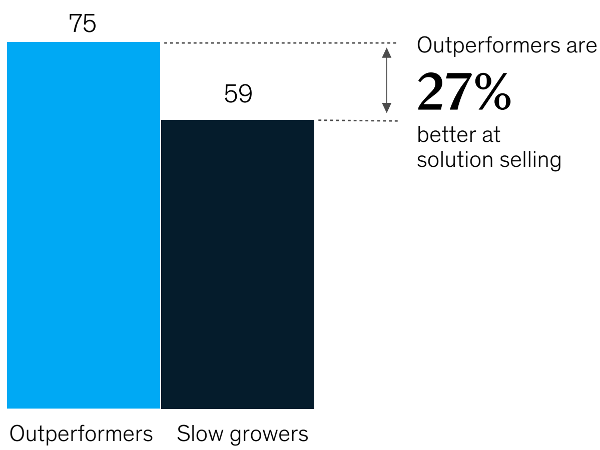
Top sales organizations turn "outside-in" from aspiration to operational discipline

Outperforming B2Bs are more aggressive in making adaptations that put the customer first.

For example, 75 percent are solution sellers, compared to 68 percent for the overall sample and 59 percent for slow growers. Many establish dedicated application marketing and engineering teams, staffed with experts who work across product lines to help customers find best-fit solutions.

Agility

% of B2B companies effective at solution selling



Companies strongly or moderately effective at solution selling are

1.5x

more likely to be outperformers

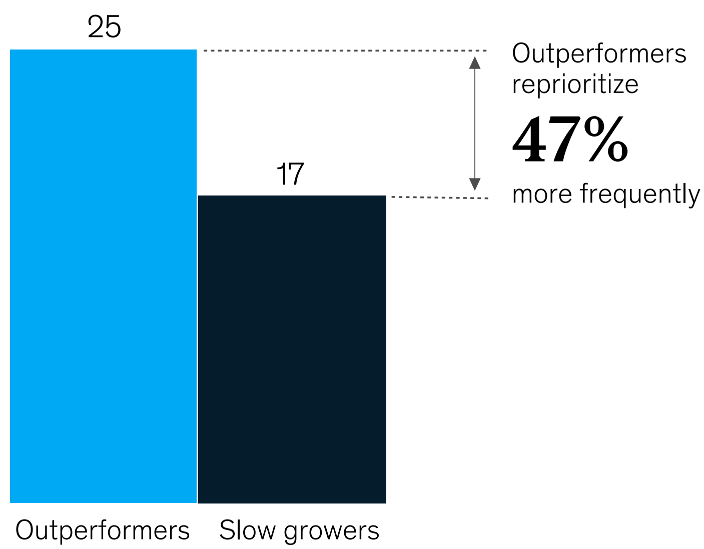
Outperformers update account priorities more frequently

Instead of reviewing and reallocating coverage once a year as is typical of many B2Bs, outperformers are 50 percent more likely than slow growers to adjust their accounts monthly (25 percent versus 17 percent, respectively). That continual realignment allows growth leaders to assign resources toward the highest-value opportunities.

The shift to more frequent reviews is likely to become more widespread—even outperformers have room to improve—enabled by analytics that surface key triggers, such as end-of-life product cycles and insights into particular investments that customers have planned.

Agility

% of companies with account coverage reprioritization happening at least monthly



Leaders go where their customers are—and that's increasingly online

Outperformers fast track omnichannel capabilities, with an emphasis on digital. They have more digital interactions, sell more through digital channels, and offer a more seamless experience across digital and in-person touchpoints. Others are likely to follow: 80 percent of B2B decision makers say that omnichannel sales are as effective or more so than traditional models. Buyers also intend to stick with omnichannel interactions. They see remote and digital self-serve channels as on a par with face-to-face interactions.

Agility

Outperformers interact and sell digitally, in line with developing customer expectations

32%

of outperfomers have more than half their customer interactions through digital channels **(vs 20% for slow growers)**

42%

of outperfomers generate more than half their revenue through digital channels **(vs 25% for slow growers)**

68%

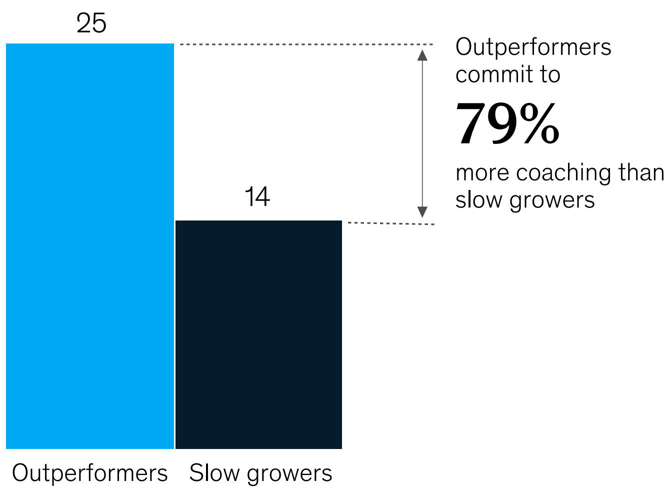
of outperfomers combine traditional and digital channels in the customer journey **(vs 56% for slow growers)**

Outperformers lean into talent development

In elevating the most successful sellers to management roles, B2Bs reward accomplishment. But they sometimes neglect to reinforce the responsibilities that come with the role—namely, to cultivate the next generation of sales stars. Outperformers do things differently. They ensure that top managers are top coaches, with structures and incentives that make this possible. Examples include weekly coaching and giving must-win deals additional executive and team support, backstopped with analytics that track time spent on individual and team development. The result is a virtuous cycle that drives sales growth.

Talent

% of companies where sales managers spend more than 50% of their time coaching



Companies where sales managers spend more than 50% of their time coaching are

1.4x

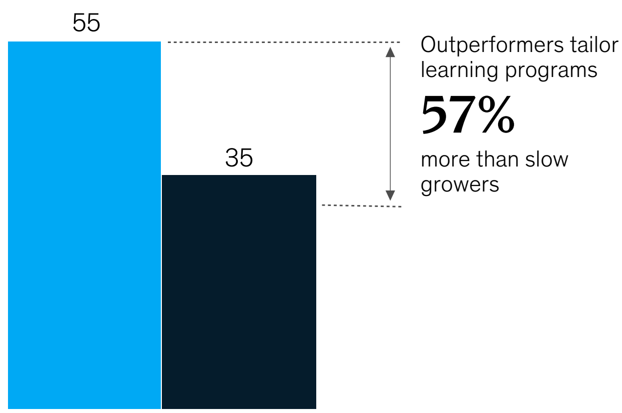
more likely to be outperformers

Sales outperformers eschew one-size-fits-all training

Top B2Bs train for their most pressing needs and adapt learning programs continuously. In addition to tailoring learning journeys for their sales teams, outperformers drill down to the individual, with training tied to the seller's objectives and skills deployed against real opportunities. The experiential learning combined with ongoing coaching empowers sellers to be more effective. Outperformers are 57 percent more likely to tailor their learning programs and 1.3 times more likely to outperform their peers in revenue growth.

Talent

% of companies that tailor learning programs for the sales team



Companies where sales managers always tailor learning programs based on observed strengths are

1.3x

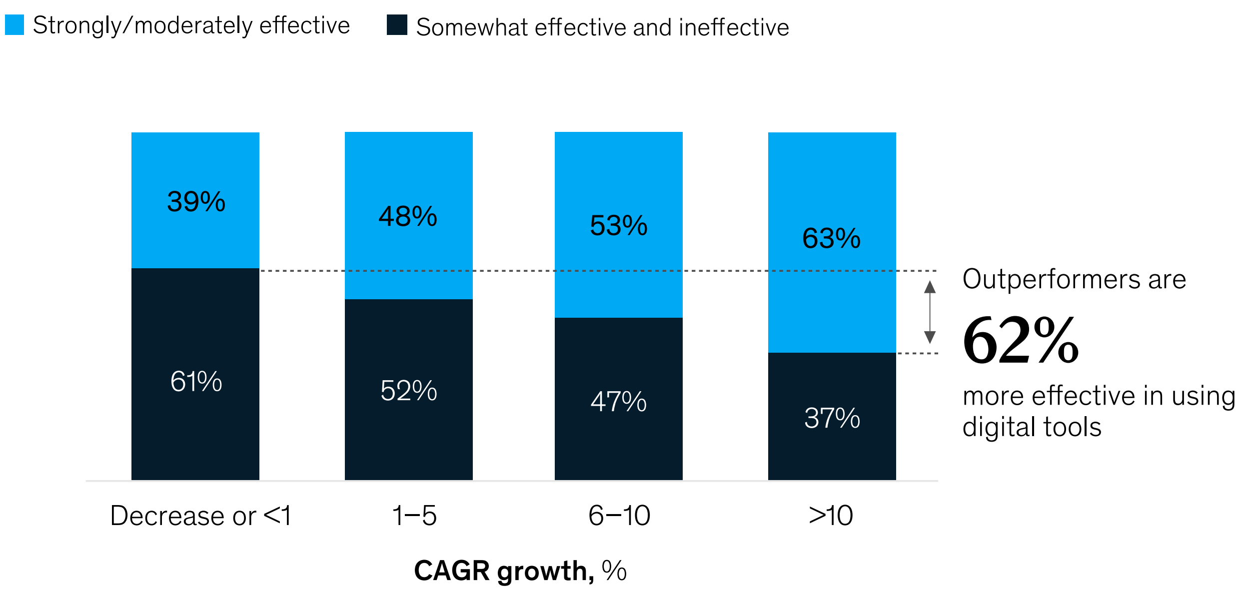
more likely to be outperformers

With technology, leaders create smart tools—and ensure sellers use them

Most sales organizations have plenty of digital tools. The problem is that their reps ignore them. Poor user interfaces, unclear use cases, or confusing recommendations condemn many would-be enablers to the trash heap. Sales leaders emphasize digital tool building. But they place equal focus on adoption—involving sellers in the design to build trust in the system, creating solutions that address key seller pain points, and making those tools intuitive and easy to use. The combination of smart tools and strong adoption translates to higher sales.

Technology

% of B2B companies effective at using digital tools & capabilities to support sales

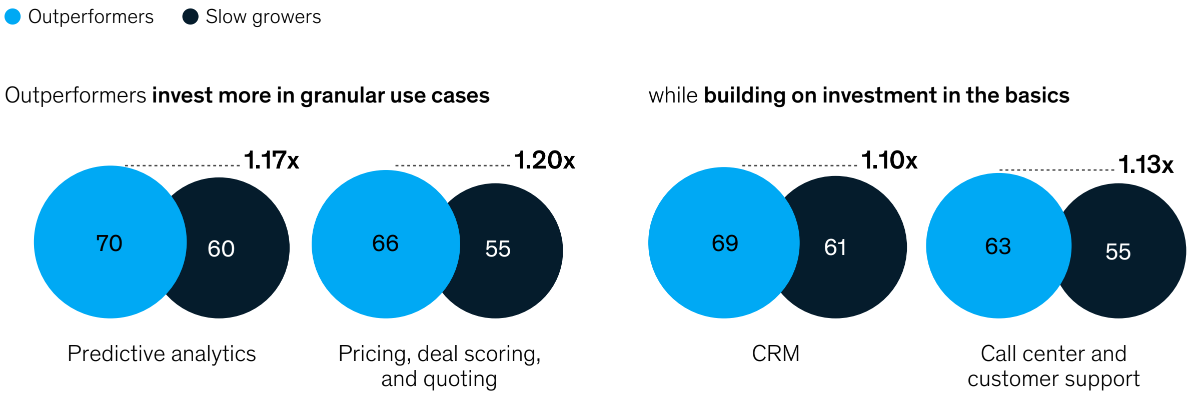


Outperformers invest in advanced digital enablers

Outperformers are widening the investment gap in granular use cases vs. versus basic use cases. Leading B2Bs plan to invest more across digital use cases. Topping the priority list are actionable granular analytics such as pricing and deal scoring, and predictive analytics such as churn prevention, propensity to buy and next product to buy. Starting with their already-strong base, these investments could widen the gap between digital sales leaders and the rest of the field.

Technology

Share of companies that plan to increase investments per use case



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The authors would like to thank Callie Blumenfeld and Bastiaan Dillmann for their contributions.

Theme 2:

Winning the loyalty battle

B2B sales: Omnichannel everywhere, every time

Our latest B2B Pulse research shows how the shift to omnichannel has permanently changed sales and suggests what companies can do to adjust.

by Liz Harrison, Candace Lun Plotkin, Steve Reis, and Jennifer Stanley

December 2021

The COVID-19 pandemic has dramatically accelerated the already-changing dynamics of how work gets done between buyers and sellers. We've been tracking the trends since 2016, when we began to ask B2B decision makers about how they find new suppliers, build and foster relationships with them, and choose what and how to buy and reorder. We wanted to understand the landscape of B2B sales and learn more about preferences at a time when omnichannel selling was emerging and customers were increasingly demanding more digital, consumer-like interactions with suppliers.

When COVID-19 emerged in early 2020, customer behaviors began to shift dramatically, favoring video conference interactions with sales reps and e-commerce. This pressured B2B sales to digitize more quickly; it had already begun to transform, but lagged behind B2C sales. The pandemic accelerated the move already under way to omnichannel and e-commerce, and survey respondents indicated that the change was here to stay.

Our latest B2B Pulse Survey asked hundreds of questions to US-based B2B decision makers—defined as customers who are responsible for making product or service decisions for their company—across dozens of industries.1 We asked decision makers to share their current behavior and preferences for interacting with suppliers. We also asked these same respondents to tell us what sales and marketing changes are happening at their own companies. In short, this research reveals that B2B selling has truly changed much faster and more dramatically than many would have imagined. For example:

— **Ninety-four percent** of respondents view today's B2B omnichannel reality—in which customers buy face-to-face, remotely, and online—as being as effective or more than before COVID-19.

— B2B customers now regularly use **ten or more channels** to interact with suppliers (up from just five in 2016).

— Buyers are more willing than ever before to spend big through remote or online sales channels, with **35 percent** willing to spend $500,000 or more in a single transaction (up from 27 percent in February 2021). Seventy-seven percent of B2B customers are also willing to spend $50,000 or more.

— Suppliers will have to fight hard to retain loyalty if customer needs are not met: for example, **eight in ten** B2B decision makers say they will actively look for a new supplier if performance guarantees (eg, a full refund if a certain level of performance is not met) are not offered.

As businesses gear up for yet another year of potential uncertainty and disruption, we found one thing to be sure: B2B sales are now resolutely omnichannel, with e-commerce, face-to-face, and remote videoconference sales all a necessary part of buyers' experience. But buyers' move to omnichannel hasn't been a matter of simply shifting more transactions online. What B2B customers want is nuanced, and so are their views about the most effective way to reach them.

The 'rule of thirds' for omnichannel B2B sales is now standard

B2B leaders are embracing the new normal of omnichannel sales. Customers use different sales channels—for example, face-to-face, videoconferencing, online chat, or online marketplaces—at different stages of the buying journey. A "rule of thirds" has emerged: customers employ a roughly even mix of traditional sales (eg, in-person meetings), remote (eg, videoconferencing and phone discussions), and self-service (eg, e-commerce and digital portals) at each stage of the sales process (Exhibit 1).

When we share the rule of thirds, we often hear, "But my industry (or customers or company) is different." That assertion conflicts with our survey data: the rule of thirds describes responses from B2B decision makers across all major industries, at all company sizes, in every country. Naturally, some nuances exist, but the similarities far outweigh unique results.

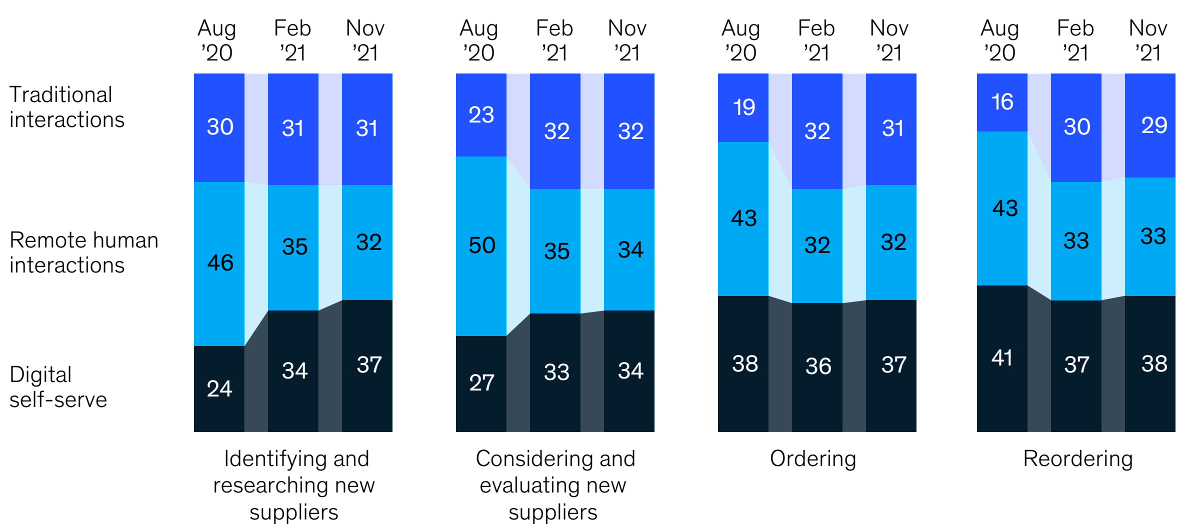
Implication: B2B suppliers cannot solve the needs of an entire segment of customers through one channel, nor can they ignore e-commerce as a channel. The option to engage via face-to-face, remote, and self-service should be available to all customers, from small to medium-size enterprises (SMEs) up to the largest organizations.

Exhibit 1

B2B buyers have settled into using an evenly divided mix of sales channels.

Current way of interacting with suppliers' sales reps,[1] by stage of process[2]

% of respondents, US only



~2/3

of buyers opt for remote human interactions or digital self-service

[1] Q: *Currently, how do you split your time with sales reps from your company's suppliers during the following stages of interactions?*
[2] Traditional includes in-person meetings, direct mail, fax, etc. Remote includes phone calls, video conference calls, emails, etc. Digital includes company websites, e-commerce, chat bots, internet searches, mobile apps, etc.
Source: McKinsey & Company Global B2B Pulse, Aug 2020, n = 602; Feb 2021, n = 562; Nov 2021, n = 602

Omnichannel sales are more effective than ever

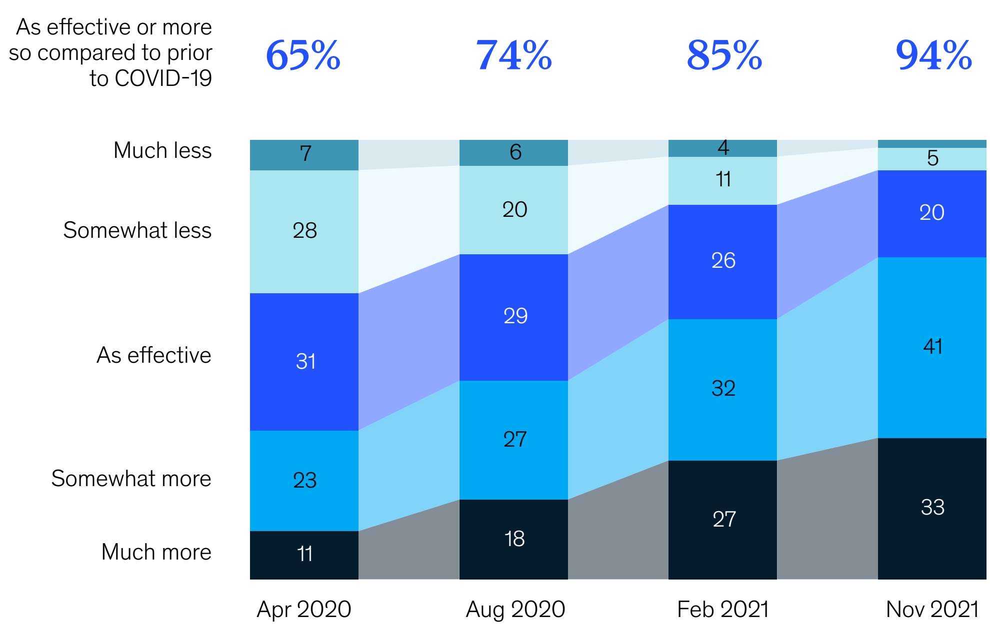
Doubters have become believers. Today, 94 percent of B2B decision makers say the new omnichannel sales model is as effective or more compared to the sales model they used before the pandemic (Exhibit 2). The percentage holding these views has climbed every time we've asked over the past 18 months. In April 2020, only 65 percent of respondents thought the new way of selling was as effective as the model used pre-COVID-19.

Implication: B2B suppliers must continue to adapt to meet this new omnichannel reality. Undoubtedly, shifting to a more varied selling approach is not a straightforward process. But selling organizations can take confidence from the increasing comfort that many of their peers (and their customers) have with omnichannel as an effective way of doing business.

Exhibit 2

Confidence in the effectiveness of new sales models continues to climb.

Effectiveness of new sales models in reaching and serving customers, % of respondents, US only[1]



[1] Q: *Overall, how effective is your company's new sales model at reaching and serving customers?*
Source: McKinsey & Company Global B2B Pulse, Apr 2020, n = 607; Aug 2020, n = 602; Feb 2021, n = 562; Nov 2021, n = 602

Customers are using more channels than ever before

Omnichannel truly involves many channels. The number of channels that B2B customers use has doubled in the past five years. B2B customers say they are now interacting with suppliers via ten or more channels, up from five in 2016 (Exhibit 3).

Exhibit 3

B2B decision makers are using more channels than ever before to interact with suppliers.

Number of distinct channels that B2B customers use during their decision journey,[1] US only

2016	2019	2021
5 channels	**7.5** channels	**10** channels

[1] Q: *What type of research have you used to research suppliers? Which of the following methods have you used to evaluate suppliers and products at this stage? How do you go typically go about submitting a new purchase order? How do you typically submit your re-order?* Count of distinct channels used across the entire buying journey (research, supplier evaluation, ordering, reordering).
Source: McKinsey & Company Global B2B Pulse, 2016, n = 648; 2019, n = 605; Nov 2021. n = 602

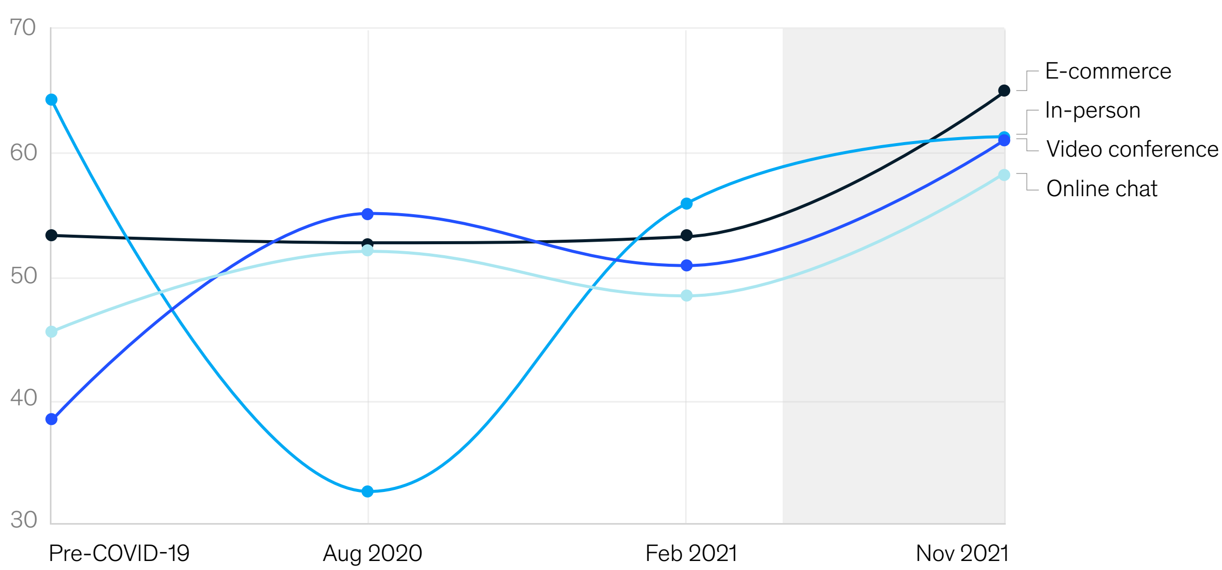
Part of the reason customers are engaging in a wider array of channels is that suppliers are finally catching up to the demand. While in-person selling rebounded to pre-COVID-19 levels during 2021, more companies than ever before also began offering e-commerce as a sales channel (Exhibit 4). We now see a tipping point, with e-commerce surpassing in-person selling as a sales channel, at 65 percent, versus 53 percent earlier this year. Videoconferencing and online chat also rose during the year.

When it comes to how effective these channels are, 32 percent of respondents now rank e-commerce as the single most effective channel, compared to in-person transactions at 23 percent: a swap from eight months ago (Exhibit 5).

Exhibit 4

For the first time, B2B sellers are more likely to odder e-commerce channels than in-person selling.

Channels offered by B2B sellers,[1] % of respondents, US only



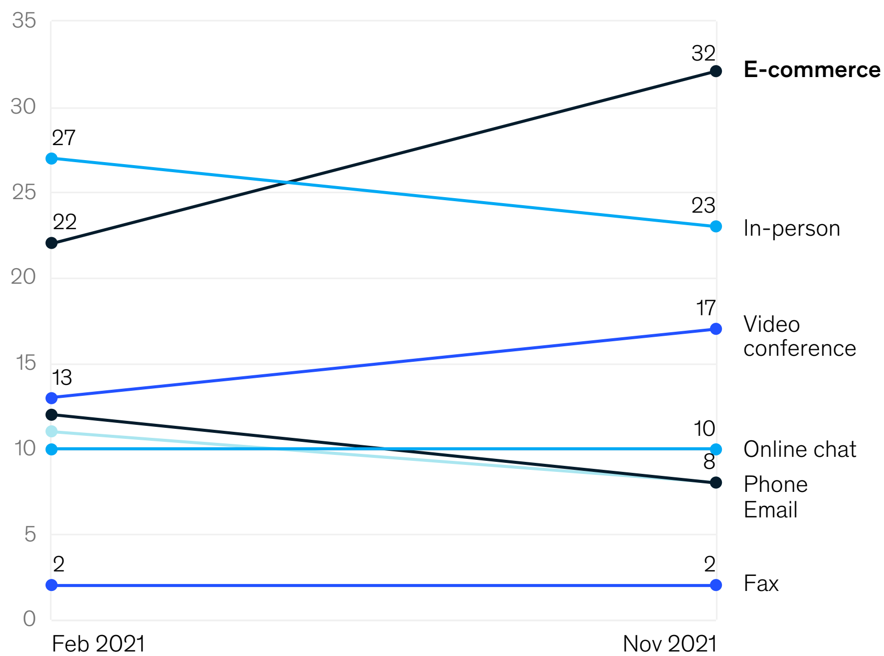
[1] Q: *In what ways is your company's product or service sold today?* Phone and email channels not shown (each flat at ~50%).
Source: McKinsey & Company Global B2B Pulse, Jan 2019–Nov 2021

Implication: Increased opportunities to engage in different ways involves increased complexity. To equip customers to navigate this complex omnichannel ecosystem, sales professionals will increasingly need to become "journey orchestrators," directing customers to different types of channels for experiences that sellers in the past might have completed themselves.

Exhibit 5

E-commerce is the most effective channel for a plurality of B2Bs.

Effectiveness of sales channels, % of respondents who identified channel as their most effective, US only[1]



E-commerce has now surpassed in-person as the single most effective channel

[1] Q: *How effective are each of these sales channels for your company?* Responses are % who ranked the given channel *"1,"* indicatingthat it is the most effective of any channels the respondent's company sells through.
Source: McKinsey & Company Global B2B Pulse, Feb 2021, n = 562; Nov 2021, n = 602

Channel preferences shift depending on the stage or type of purchase

While the overall "rule of thirds" holds throughout the stages of a transaction, some shifts in channel usage occur, depending on the purchase stage and type of purchase. Buyers are more likely to stick with in-person selling for first-time, complex, or high-value sales (Exhibit 6). When the transaction is lower in value or less complex, self-serve is a more attractive channel. But overall, the rule of thirds still holds, with between 30 percent and 40 percent of respondents saying they use each channel type in each purchase situation.

Implication: Although conventional wisdom might dictate otherwise, every type of transaction needs the support of all three channel types: traditional, remote, and self-serve. Businesses should prepare to shift resources toward more in-person sales for higher-value or complex purchases, but other channels remain important. Similarly, self-service sales may dominate lower-value or less complex transactions, but some buyers are likely to opt for in-person sales, so the channel still matters.

Exhibit 6

Preferences swing between traditional and self-serve. But remote remains consistent.

Preferred use of channel by type of purchase situation,[1]

% time communicating with suppliers, US only

The pendulum swings to traditional for first time, high value, and complex purchases, while shifting to self-serve for lower-value, less-complex purchases.

	First time	Lower value	Higher value	Less complex	More complex
Traditional	40	32	37	31	38
Remote	30	31	30	30	31
Self-serve	30	37	33	39	31

[1] Q: *What percentage of the time would you prefer to use traditional vs. remote human vs. digital "self-serve" for each of the following situations?*
Source: McKinsey & Company Global B2B Pulse, Nov 2021, n = 602

Loyalty erodes as customer expectations spike

During the pandemic, an unprecedented share of consumers began changing brands or retailers, and signs suggest that B2B customers could follow suit. The majority of B2B customers we surveyed say they will actively look for another supplier if their main needs are not met. More than 80 percent say that a performance guarantee—including a full refund if a certain performance level is not met—is critical for brand loyalty (Exhibit 7). Purchasers are almost as likely to want real-time customer service, transparency online about product availability and pricing, and a consistent purchasing experience across multiple channels.

Implication: The good news about waning loyalty is that there has never been a better time to attract new customers and retain existing ones. Suppliers who are already committed to quickly innovating and investing to deliver a better omnichannel experience will appeal to customers who would otherwise flee elsewhere.

Exhibit 7

B2Bs are very clear about what they want from suppliers overall, and very willing to consider switching if 'must haves' are not offered.

Experiences required for customer loyalty, % of respondents that will actively look for another supplier if given experience is not present, US only[1]

Tier 1: Must do

Performance guarantee (full refund): **82%**

Product availability shown online: **81%**

Ability to purchase from any channel: **80%**

Prices available online: **80%**

Real-time/always-on customer service: **80%**

Consistent experience across channels: **80%**

Tier 2: Very important, but start on these once tier 1 is done

Outcomes-based pricing: **77%**

Readily available customer reviews: **76%**

Easy-to-place orders via mobile: **73%**

Ability to view products in person if needed: **71%**

Tier 3: Start after tiers 1 and 2 are up and running (unless very easy to start or fix)

Free shipping available on all orders: **69%**

3-D/virtual product demos: **68%**

Single log-in/password for all supplier sites: **68%**

Delivery within 2 days: **67%**

Loyalty program granting points/other rewards: **64%**

[1] Q: *For each of the follow elements, please tell us how essential you believe it is that a supplier offers this to you/your company.* Possible answers: "*1 = Not important/not a part of my decision-making criteria*"; "*3 = I expect this, but it is not a requirement*"; "*5 = Essential, I will look for another supplier if this is not offered.*"

Personal relationships are paramount, regardless of channel

Although online interactions, both remote and self-serve, are here to stay, in-person sales reps are as important as ever. Customers don't want to give up face-to-face visits altogether. Seventy-six percent of respondents describe them as a sign of how much a supplier values a relationship. Critically, 59 percent of customers say they will buy from a supplier only if they've met in person at least once before.

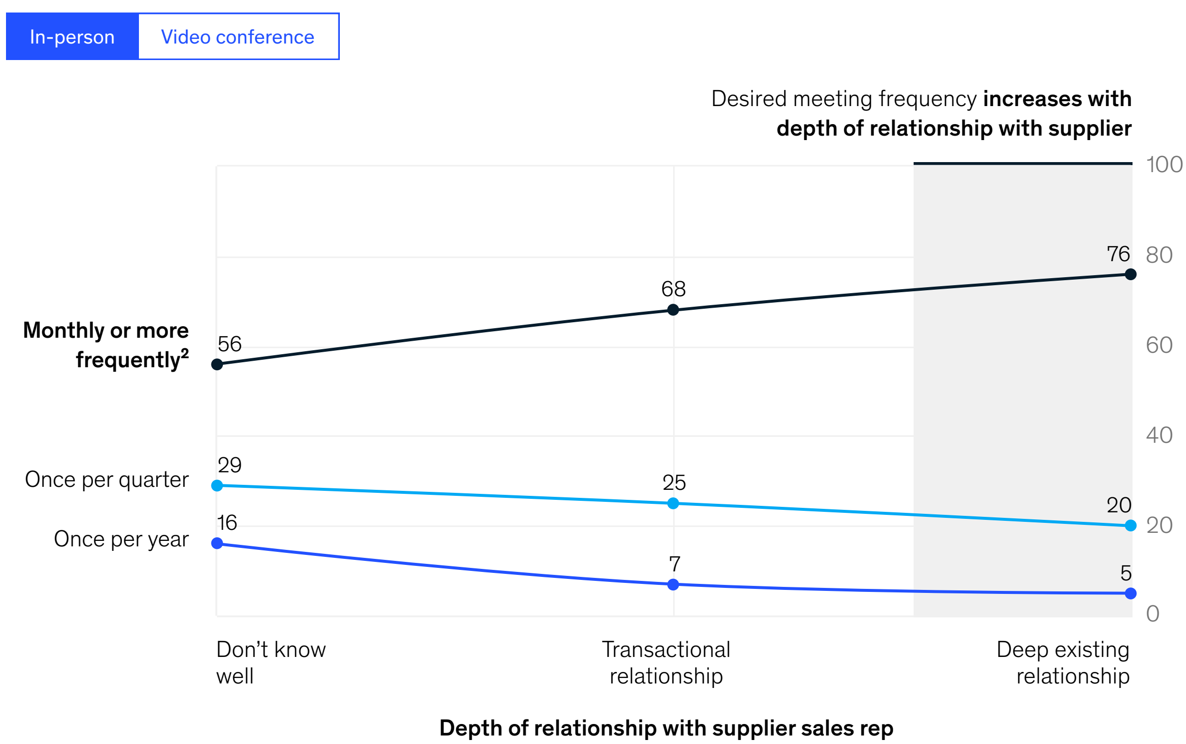
Interestingly, although respondents say they want the in-person touch, they also admit that it's not critical. Seventy-two percent say they get as much value from meeting with sales reps via videoconferencing as they do in person. Further, 69 percent say virtual social activities can be a good substitute for in-person interactions to build trust.

Implication: Salespeople are as relevant as ever, and suppliers should take care not to jettison face-to-face meetings. In particular, businesses should make a point of visiting important customers they haven't yet met in person.

Exhibit 8

In Person and video conference visits from suppliers to B2Bs remain desired and need to be even more frequent with established relationships.

Preferred frequency of in-person and video conference interactions by type of relationship with sales representative,[1] % of respondents, US only



[1] Q: *How frequently do you want to meet different types of sales reps from your suppliers in person? How frequently do you want to meet different types of sales reps from your suppliers via video conference?*
[2] "Monthly or more frequently" includes "Monthly" and "Weekly" responses.
Source: McKinsey & Company Global B2B Pulse, Nov 2021, n = 602

Customers are more willing than ever before to spend big online

Digital spending is not just for low-value purchases. Over one-third (35 percent) of B2B decision makers say they are willing to spend $500,000 or more on a single interaction on remote or self-service channels, up from just 27 percent earlier this year (Exhibit 9). Seventy-seven percent also indicate willingness to spend at least $50,000.

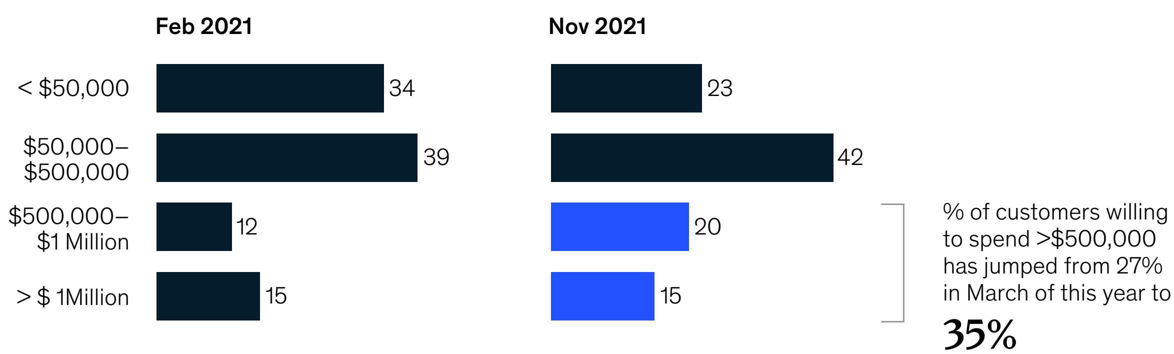
To match this increased comfort with spending big online, companies have continued investing in remote and online sales channels. Sixty-nine percent, for example, say they increased their e-commerce budget over the past year.

Implication: Along with reordering and low-ticket purchases, complex, high-value transactions can and should be available to all customers on digital self-serve and remote channels. This means that many suppliers may need to shift their online product mix and potentially launch new pricing processes to streamline quoting and approvals for large-value purchases.

Exhibit 9

Remote and self-service are not just for low-value purchases; a majority willing to spend $50,000 or more.

Maximum order value through digital self-service and remote human interactions for a new product or service,[1] % of respondents, US Only[2]



[1] Q: *What is the maximum order value that you would purchase through end-to-end digital self-serve and remote human interactions for a new product or service category?*
[2] <1% of respondents selected "Don't know" or "Would not."
Source: McKinsey & Company Global B2B Pulse, Feb 2021, n = 562; Nov 2021, n = 602

Lean into channel conflict

While e-commerce is growing faster than ever, some suppliers remain hesitant. Within companies, self-serve e-commerce is viewed "in competition" with other sales channels. For example, 54 percent say in-person sales competes with e-commerce, and 47 percent say inside sales—fully remote transactions, often conducted by phone only—does the same (Exhibit 10).

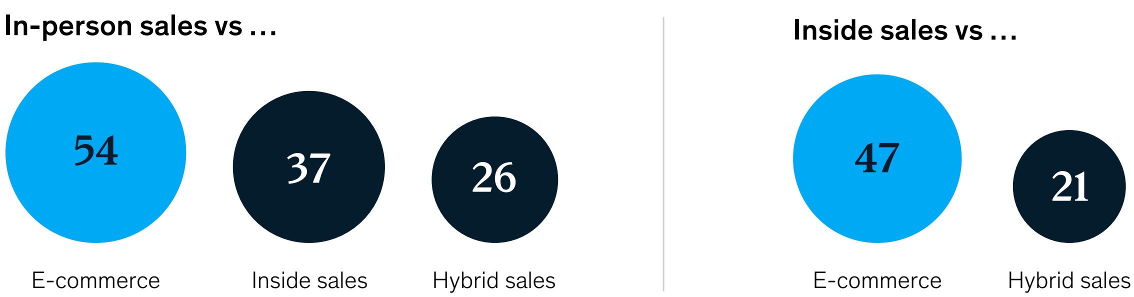
As companies think about making their next move in e-commerce, they will also need to be aware of nuanced customer preferences. For example, 64 percent of B2B decision makers have the greatest comfort with making an online transaction on a supplier website that is behind a paywall. There's slightly less comfort with purchasing a supplier's product or service on a third-party site (60 percent), or from a supplier site with no paywall (56 percent).

Implication: Many companies have found that managing channel conflict requires rethinking sales team incentives, redesigning sales territories, and an overall change management effort. While channel conflict is a challenge, companies that outperform their peers in gaining market share invest more in e-commerce. Their success suggests they are getting value and ROI out of wrestling with the channel conflict.

Exhibit 10

While e-commerce is growing faster than ever before, multiple barriers to usage remain.

Where suppliers experience channel competition,[1,2] % of respondents, US only



37% of respondents believe risk of channel conflict is a barrier to overall growth of e-commerce at their company[2]

[1] Q: *In your company, which of the following channels are experiencing channel competition with each other?*
[2] Q: *What are the barriers contributing to overall e-commerce usage at your company?*
Source: McKinsey & Company Global B2B Pulse, Nov 2021, n = 602

Omnichannel requires diversification in sales roles

With the emergence of more sales channels, companies would do well to recognize that traditional sales roles, like field sales and inside sales, have evolved and settled into an overall hybrid role. A hybrid seller has the same set of responsibilities as a field rep, but hybrid sellers use videoconferences, online chats, and the support of e-commerce to close deals, while field sellers often work in person.

According to survey respondents, their companies are actively focused on growing hybrid and digital sales teams. A net 70 percent of companies increased hybrid sales team resources in 2021 (76 percent grew their hybrid teams; 6 percent shrank them). A net 64 percent added to their digital sales teams (70 percent grew their digital teams; 6 percent shrank them). These changes outpaced growth in more traditional sales roles, like inside and field sellers (Exhibit 11). Companies also expect these trends to continue into 2022 and beyond.

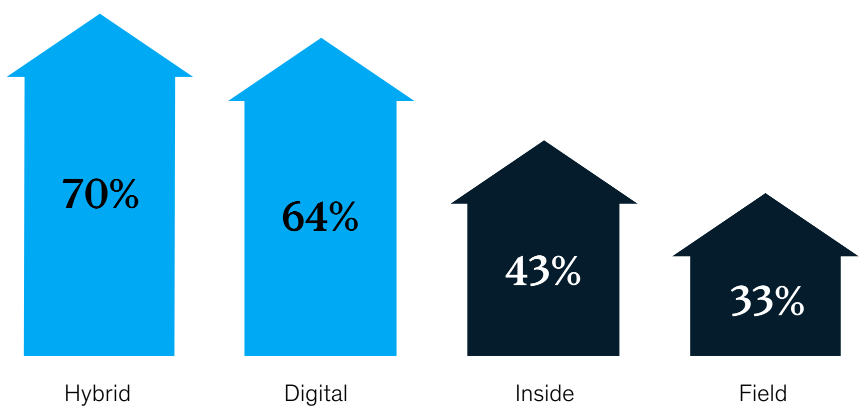
Across the board for our respondents, these sales role changes have been beneficial. Respondents report improvements in cost of sales (sales cost as a percentage of total revenue), with 52 percent reporting a positive trajectory in the past year.

Implication: With the rapid evolution in sales team composition, organizations will need to ramp up hiring, training, and capability building to ensure they are not only bringing in net new hybrid sellers, but also equipping their existing field and inside sales reps to transition to this new role.

Exhibit 11

Hybrid and digital are the fastest-growing sales roles.

Net change in sales roles,[1] % of respondents, US only



[1] Q: *Over the past year, how has the size of your company's sales force in the following areas changed?*
Source: McKinsey & Company Global B2B Pulse, Nov 2021, n = 602

How sales and marketing can deliver higher impact together

Increasing demands from customers, the proliferation of sales channels, increase in data availability, and need to personalize content have driven the need for sales and marketing teams to work as one. In fact, 89 percent of respondents now say that marketing and sales need to work closely together, more so than ever before.

To help enable and drive increased sales, marketing teams have been busy. Fifty-two percent of respondents say their companies have conducted extensive primary research to improve customer experience. Another 51 percent have invested in new capabilities to enable personalized marketing, while 45 percent say their companies have recently reevaluated the role of marketing in their organization overall.

While great progress has been made, there is still a long way to go to ensure marketing and sales teams work together effectively. For example, 57 percent of respondents report that their sales teams still do not fully utilize (and often ignore) content created by marketing.

Implication: Now is the time to ensure that your sales and marketing teams can work together to improve overall customer experience. For example, ensure that your most senior sales and marketing leaders (eg, chief sales officers and chief marketing officers) have a strong relationship. Consider a rotational program to place sales leaders in marketing functions (and vice versa) to build empathy and understanding of the roles.

The next normal for B2B sales is here, and there's no looking back. Businesses are no longer cautiously testing the waters, incrementally (and sometimes reluctantly) inching their way online. The pressures from COVID-19 have accelerated the shift, and the rule of thirds for B2B sales—one-third in-person, one-third remote, and one-third online self-serve—has firmed up. Further, there are nuances within the rule of thirds, and customer loyalty is waning. To stay ahead, businesses will have to remain flexible and dynamic to satisfy the needs of their customers.

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The authors would like to thank David Greenawalt and Kate Piwonski for their contributions to this article.

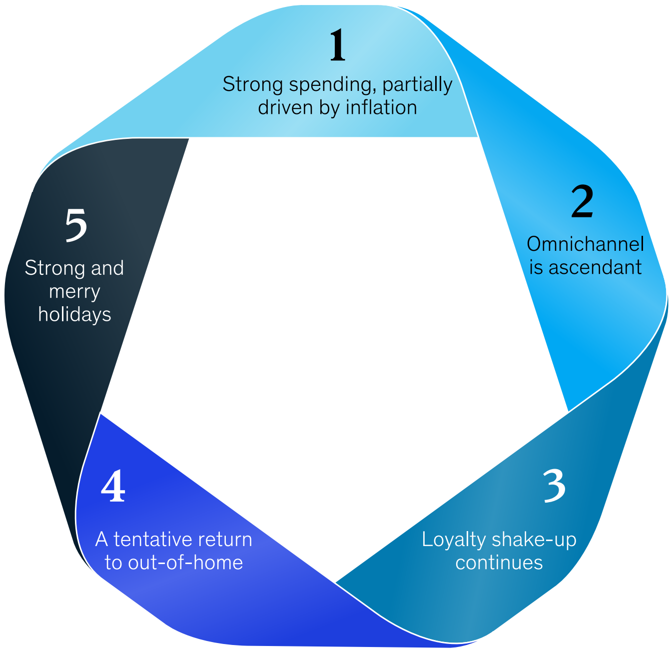
US consumer sentiment and behaviors during the coronavirus crisis

US consumers exhibited strong optimism and spend in October, driven by consumers across the age and income spectrum.

This article was a collaborative effort by Tamara Charm, Janette Hwang, Jackie Laird, Andrea Leon, Nancy Lu, Anirvan Maiti, Jason Rico Saavedra, Kelsey Robinson, Daniela Sancho Mazzara, and Tom Skiles.

December 2021

Five consumer themes emerged in October 2021.



1. Year-over-year growth[1] at 11% vs pre-COVID-19 growth trajectory; millennials show greatest increase in spend (18%)
2. 60–70% of consumers are shopping an omnichannel way; social media is t new window shopping
3. In the past 3 months, over 60% of consumers faced out-of-stocks; only 13% of them waited for the item to co back in stock
4. Almost 50% of consumers are engagi in “normal” out-of-home activities; investment in home continues
5. A strong holiday season is expected, with overall spend expected to grow 7

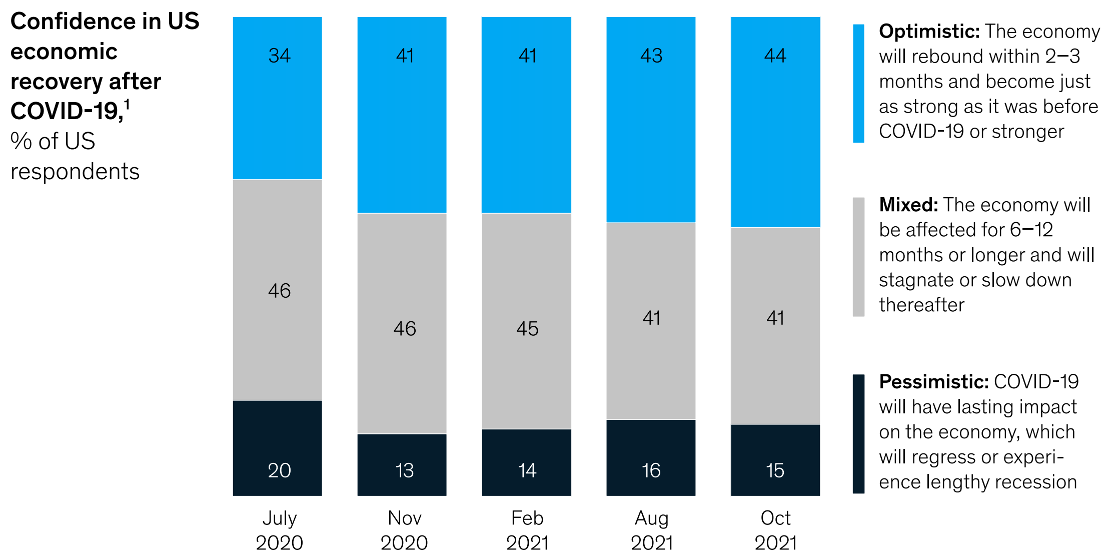
[1]Year-over-year growth for Mar–Sept 2021 relative to estimate of Mar–Sept 2020 growth if COVID-19 had not occurred.
Source: Based on 3rd-party data Feb 2019–Sept 2021, as well as longitudinal surveys conducted Mar 2020–Oct 2021 in the United States

Consumer optimism and spending have remained strong

Overall optimism and spend remained strong with 44 percent of US consumers feeling optimistic and spend increasing 11 percent year on year. High-income consumers are the most optimistic (61 percent) but all income groups contribute to the spend growth. Similarly, all generations are contributing to the growth even though millennials are most optimistic (62 percent). This growth is driven by both the intent to splurge which has been strong since February as well as elevated inflation, especially in the latter half of 2021.

Trend 1

Overall optimism on economic recovery following the COVID-19 pandemic continues to slowly increase in 2021.

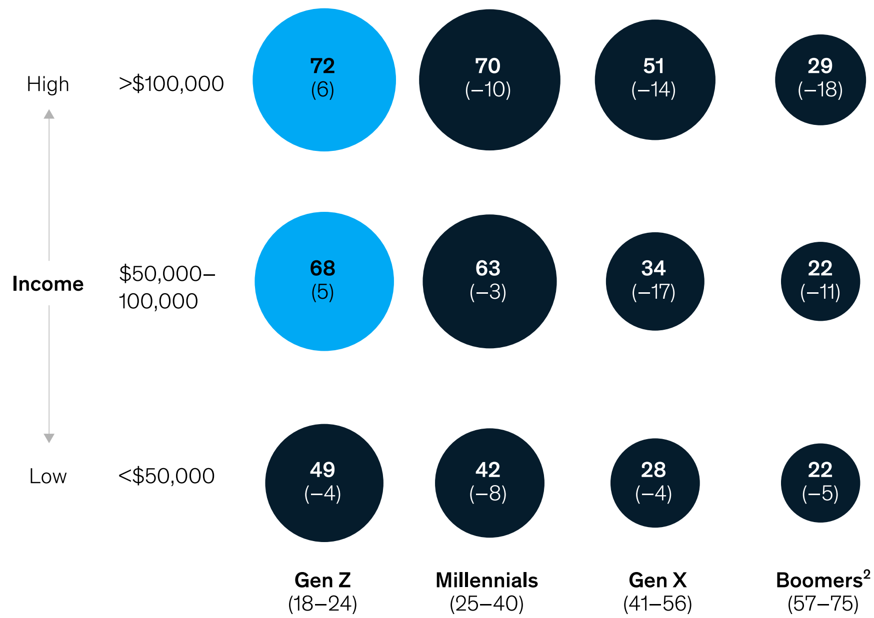


[1]Question: "What is your overall confidence level surrounding economic conditions after the coronavirus (COVID-19) crisis subsides (ie, once there is herd immunity)?" Rated from 1, "very optimistic," to 6, "very pessimistic."
Source: McKinsey COVID-19 US Consumer Pulse Survey, Oct 2021 (n = 2,095), Feb 2021 (n = 2,076), Nov 2020 (n = 2,024), July 2020 (n = 2,024)

Trend 1 cont.

More younger and higher-income consumers plan to splurge on spending.

Expected leisure spending by generation and by household annual income, 2021[1]
% who plan to treat themselves or splurge (percentage change since Feb 2021)

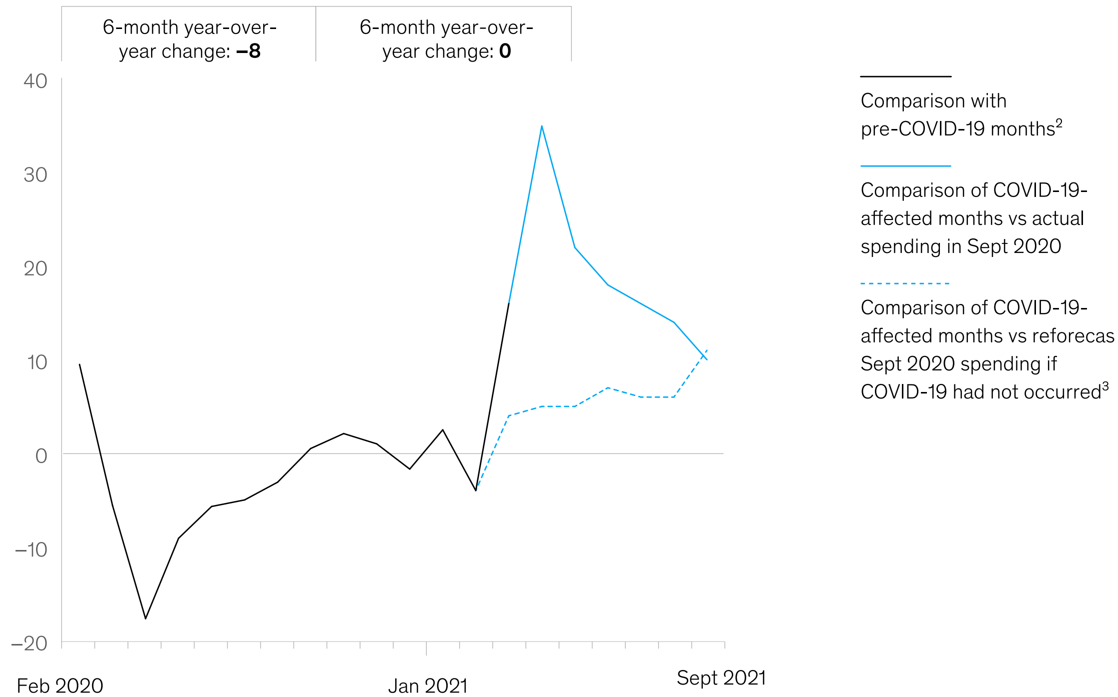


[1]Question: "With regard to products and services you will spend money on, do you plan to splurge/treat yourself in 2021? For example, are there categories of products or services you have spent less on over the last year and a half which you feel you will spend more on now?"
[2]Gen Z are people under 25 years old, millennials are 25–44 years old, Gen X are 45–54 years old, and baby boomers are 55 years old and above. Baby boomers includes silent generation.
Source: McKinsey COVID-19 US Consumer Pulse Survey, Oct 2021 (n = 2,095), Feb 2021 (n = 2,076), sampled and weighted to match the US general population 18+ years

Trend 1 cont.

Spending has been strong so far this year, with September showing an uptick potentially due to an earlier start on holiday spending.

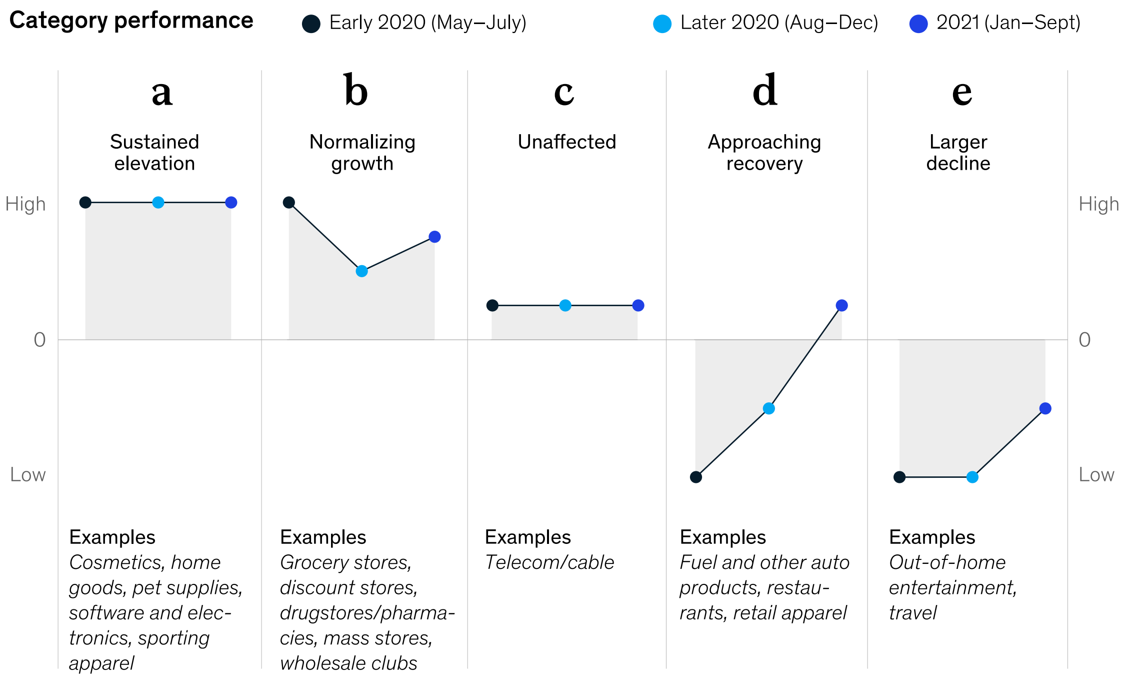
Year-over-year growth in credit-card spending,[1] %



[1]Includes credit-card and some debit-card spending data among banked consumers. While card spending represents only a part of overall consumer spending (housing, utilities, and other major categories are excluded from credit-card spending), the changes in card data closely track changes in official consumption figures reported by the US Bureau of Economic Analysis, because the share of unaffected categories in card spending is comparable to the share of categorie: not affected negatively by COVID-19 in overall consumption (which includes housing). Year-over-year growth in monthly sales during the current period (Feb 2020–Sept 2021) are compared with monthly sales in prior period (Feb 2019–Sept 2020).
[2]Year-over-year spending Mar–Sept 2020 decreased by 8% compared with same period in previous year, whereas Sept 2020–Feb 2021 remained flat compared with same period in previous year.
[3]Re-forecasted Mar–Sept 2020 spend calculated by growing Feb–Sept 2020 spend by the same 1-month growth rate observed between Feb and Sept 2019.
Source: Affinity Solutions credit-card spending data for Feb 2019–Sept 2021

Trend 1 cont.

Five different types of channel and category performance have evolved over the course of the COVID-19 pandemic.



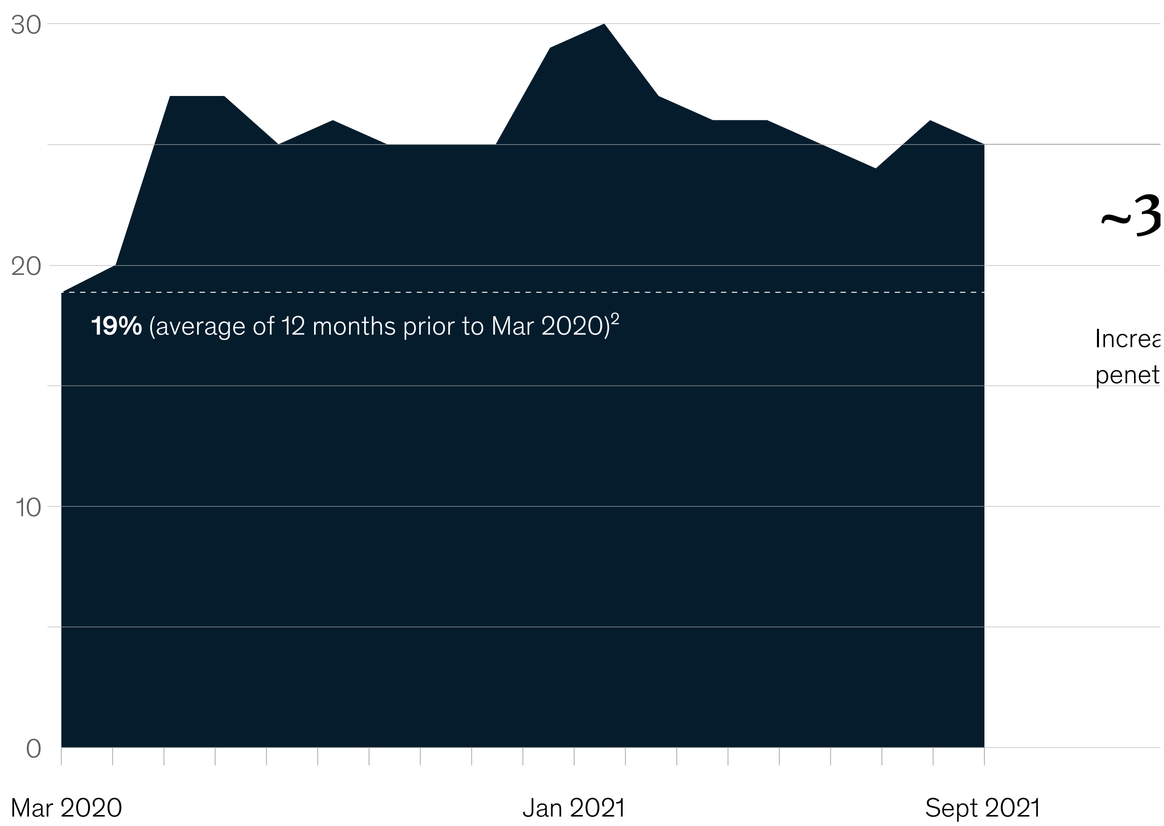
Omnichannel is ascendant and here to stay

Consumer spend in stores continued to recover with 10 percent year-on-year growth in September following stable 5 to 6 percent growth in March through August this year. Simultaneously, e-commerce sales also continued to experience strong growth, rising by about 35 percent year over year, and online penetration remains about 30 percent higher than pre-COVID-19 levels. Omnichannel shopping is ascendant, with about 60 to 70 percent of consumers researching and purchasing both in-store and online across categories. Not surprisingly, social media influence is heaviest among younger consumers but influences all age groups, most commonly in categories including jewelry, accessories, fitness/sports, and cosmetics.

Trend 2

Online penetration holds steady at about 30 percent above pre-C

Retail-oriented online credit-card and debit-card spending, % of total[1]

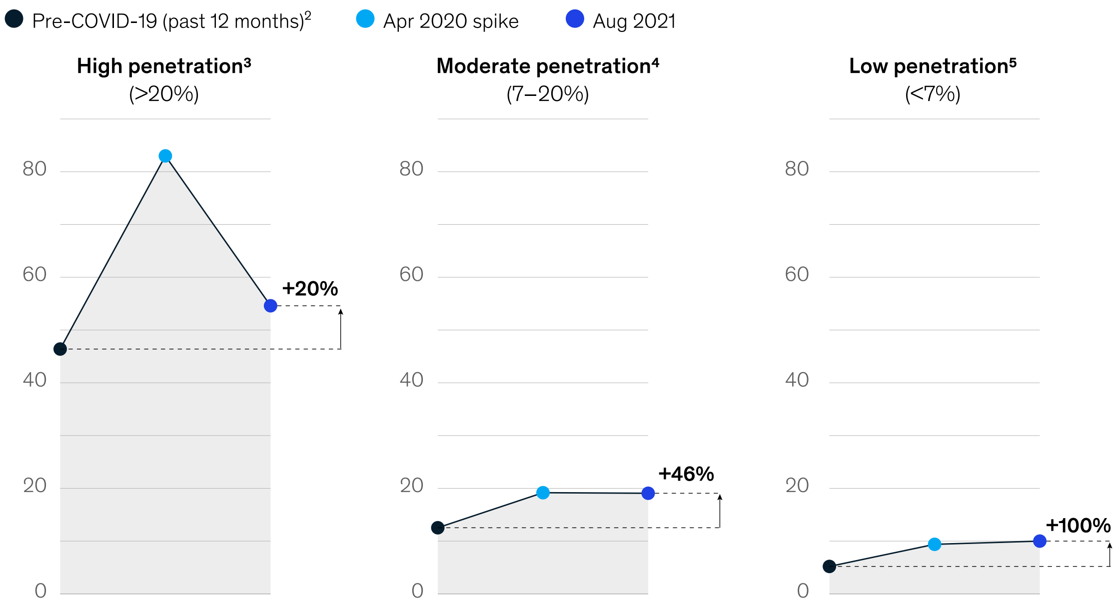


[1]Includes the following retailer categories: Amazon, apparel, software and electronics, cosmetic stores, pet supplies, home stores,
restaurants, grocery stores, drugstores, discount stores.
[2]Last 12 months, Mar 2019–Feb 2020.
Source: Affinity Solutions credit-card and debit-card spend data for Feb 2019–Sept 2021; Facteus debit-card spend data for Feb
Stackline Amazon spend data for Feb 2019–Sept 2021

Trend 2 cont.

The trajectory of e-commerce penetration differs by category and remains elevated compared with pre-COVID-19 levels.

Online sales as % of overall sales for credit-card and debit-card spend,[1] by level of pre-COVID-19 penetration



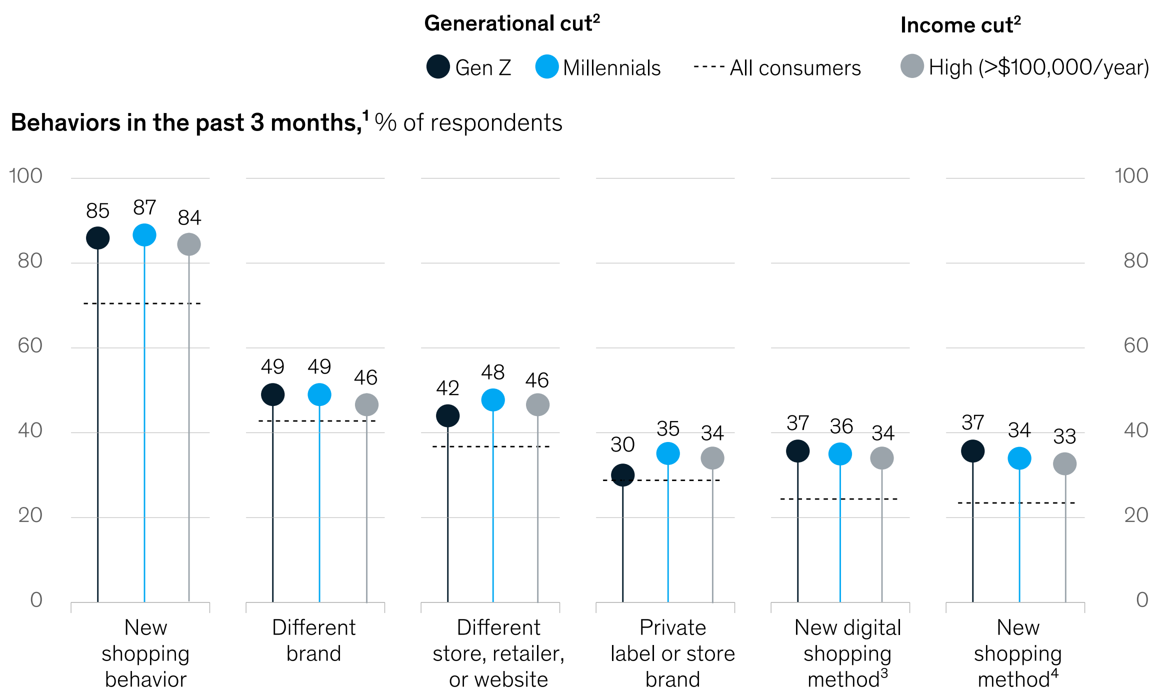
[1]Reforecasted Mar–Sept 2020 spend calculated by growing Feb–Sept 2020 spend by the same 1-month growth rate observed for Feb–Sept 2019.
[2]Online penetration from Mar 2019 to Feb 2020.
[3]High-online-penetration retail categories include those with >20% pre-COVID-19 internet penetration: apparel, software and electronics, cosmetics, pet supplies.
[4]Medium-online-penetration retail categories include those with 7–20% pre-COVID-19 internet penetration: home stores, mass stores, club stores.
[5]Low-online-penetration retail categories include those with <7% pre-COVID-19 internet penetration: restaurants, grocery stores, drugstores, discount stores.
Source: Affinity Solutions credit-card and debit-card spend data for Feb 2019–Sept 2019; Facteus debit-card spend data for Feb 2019–Sept 2019; Stackline Amazon spend data for Feb 2019-Sept 2019

Loyalty shake-up continues

Over 60 percent of US consumers have experienced out-of-stock items in the last three months, and when this happened, only 13 percent waited for the item to come back in stock versus the 39 percent who switched brand or products and the 32 percent who switched retailers. Additionally, we see both increased trading down across income groups with trading up increasing as well among higher income groups.

Trend 3

Changes in consumer behavior have been more extensive among younger and high-income consumers.



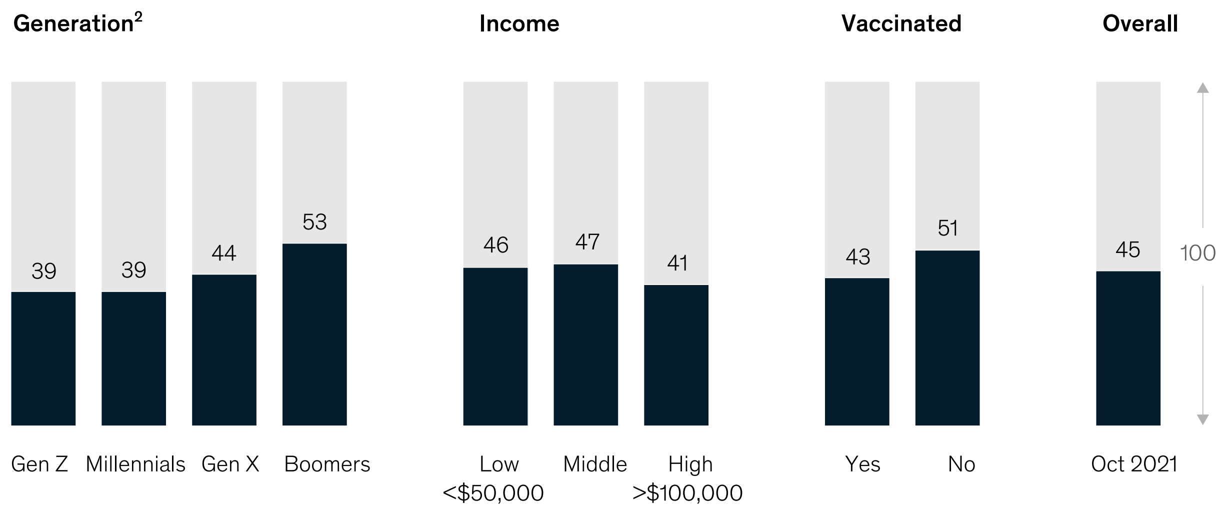
[1]Question: "Over the past 3 months, which of the following have you done?" 28% replied "None of these."
[2]Gen Z are people under 25 years old, millennials are 25–44 years old, Gen X are 45–54 years old, and baby boomers are 55 years old and above.
[3]"New digital shopping method" includes downloaded a new app, signed up for a new subscription service.
[4]"New shopping method" includes curbside pickup and delivery apps.
Source: McKinsey COVID-19 US Consumer Pulse Survey, 10/9–10/15/2021, n = 2,095, sampled and weighted to match the US general population 18+ years.

Increased out-of-home activity for some, while investment in home continues

Almost half of US consumers are engaging out-of-home (for example, dining, shopping), compared to a third of US consumers in February. While engaging in certain out-of-home activities such as work, shopping, social activities, and indoor dining is becoming more common (over half of consumers state doing in the past two weeks), consumers continue to invest in their homes.

Trend 4

Consumers engaging in normal out-of-home activities,[1] % of respondents

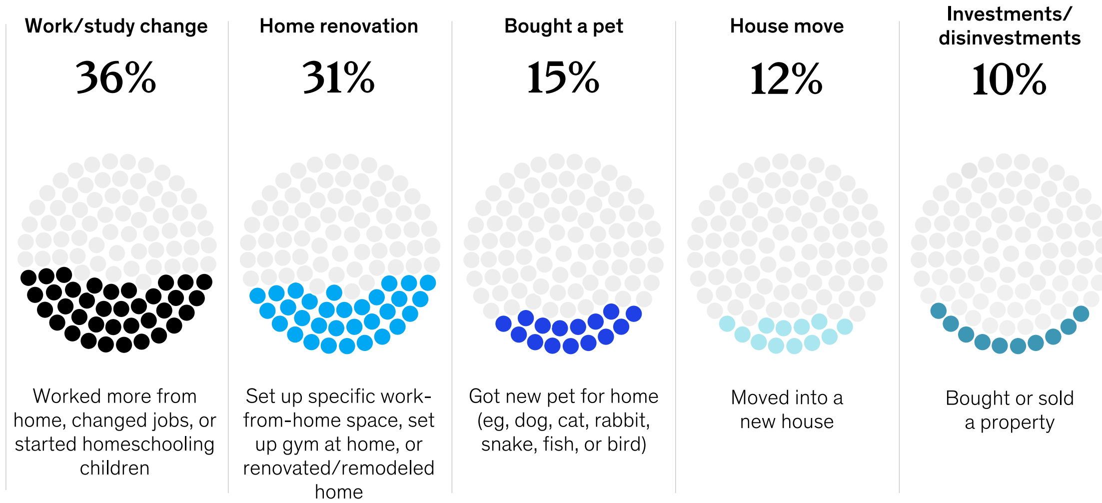


[1]Question: "Which best describes when you will regularly return to stores, restaurants, and other out-of-home activities?" Chart shows those already participating in these activities.
[2]Gen Z, under 25 years old; millennials, 25–44 years old; Gen X, 45–54 years old; baby boomers, 55 years old and above.
Source: McKinsey COVID-19 US Consumer Pulse Survey, 10/9–10/15/2021, n = 2,095, sampled and weighted to match the US general population 18+ years

Trend 4 cont.

Investment in homebody economy continues to be strong.

Changes made in past 12 months as a result of COVID-19,[1] % of respondents[2]



[1]Question: "Which of the following have you done in the last 12 months as a result of the COVID-19 crisis?"
[2]Total percentage of people who choose option(s) in the category.
Source: McKinsey COVID-19 US Consumer Pulse Survey, 10/9–10/15/2021, n = 2,095, sampled and weighted to match the US general population 18+ years

Strong and merry holiday season

Consumer demand is likely to be strong (fourth quarter estimated 7 percent growth versus 2020) particularly in discretionary, travel, and entertainment categories. High-income and millennial consumers are most excited about the holiday season (50 percent of high-income consumers are excited, compared to 25 percent of low-income consumers). Social media will have outsized influence across consumer purchases, particularly for younger generations, with Facebook, Instagram, YouTube, and TikTok expected to be the most influential platforms. Between 40 to 50 percent of consumers plan to shop early this year due to COVID-19 driven supply chain challenges as well as excitement for the holiday season.

Tamara Charm is a senior expert in McKinsey's Boston office; **Janette Hwang** is a consultant in the New Jersey office; **Jackie Laird** is an associate partner in the New York office, where **Nancy Lu** is a consultant and **Jason Rico Saavedra** is a solution associate; **Andrea Leon** and **Daniela Sancho Mazzara** are capabilities and insights analysts in the San Jose office; **Anirvan Maiti** is a data analyst in the Waltham office; **Kelsey Robinson** is a partner in the San Francisco office; and **Tom Skiles** is a capabilities and insights expert in the Chicago office.

Next in loyalty: Eight levers to turn customers into fans

How do top-performing companies maximize the impact of their loyalty programs in the next normal? By focusing on customer behavior, segment by segment.

by José Carluccio, Oren Eizenman , and Phyllis Rothschild

© Blue Planet Studio / Getty Images

October 2021

Key takeaways

- More than three-quarters of consumers have changed their buying habits in the past 18 months—and are increasingly willing to change brands.
- Loyalty programs, properly designed and managed, can unlock significant value.
- The key to a loyalty program's success is having the right data to measure it.

Since the onset of the pandemic, more than 75 percent of consumers have changed their buying habits. In a historic shift in brand loyalty, 39 percent have either changed brands or retailers, and 79 percent of those intend to continue exploring their options in the next normal.[1] Shoppers are increasingly voting with their wallets based on a new set of concerns, according to our consumer research conducted throughout the pandemic. In addition to value and convenience, purpose now drives their decisions. And, unlike pre-pandemic days, consumers across all income groups are willing to trade down to get what they want.

Loyalty programs are an often overlooked area for performance improvement that can help offset the ongoing willingness among consumers to try new brands and retailers. Our research has found that top-performing loyalty programs can boost revenue from customers who redeem points by 15 to 25 percent annually, by increasing either their purchase frequency or basket size or both.

However, we have observed that around two-thirds of established loyalty programs fail to deliver value, with many actually *eroding* value. Yet enlarging loyalty-program participation can be a critical key to increasing company-wide sales, while creating the data foundation for other valuable initiatives such as data-driven marketing, and also improving the customer experience. Getting more out of a loyalty program, or indeed turning one around, doesn't have to involve a complete redesign however.

Eight drivers of loyalty-program value

Understanding the following eight levers that significantly impact the performance of loyalty programs—regardless of geography, industry, or customer segment—can enable companies to extract the most from their investments in relationship and membership programs.

1. Take advantage of redemption elasticity

Many companies fear that offering incentives to redeem loyalty points "devalues" their program currencies. But lowering the price of redemptions can create a significant sales boost, incrementally spiking revenue by activating previously dormant customer loyalty without any negative long-term impact.

In addition, companies that promote deeply earn deeper engagement among a special few brand-loyal customers over time. Often executives will

[1] "US consumer sentiment and behaviors during the coronavirus crisis," August 2021, McKinsey.com.

overestimate the negative impact of deep cuts on top- and bottom-line performance, but what may be lost in a single transaction can be more than made up for in repeat visits and greater frequency among those cherishing the original "memorable redemption" (and among consumers in their influence group).

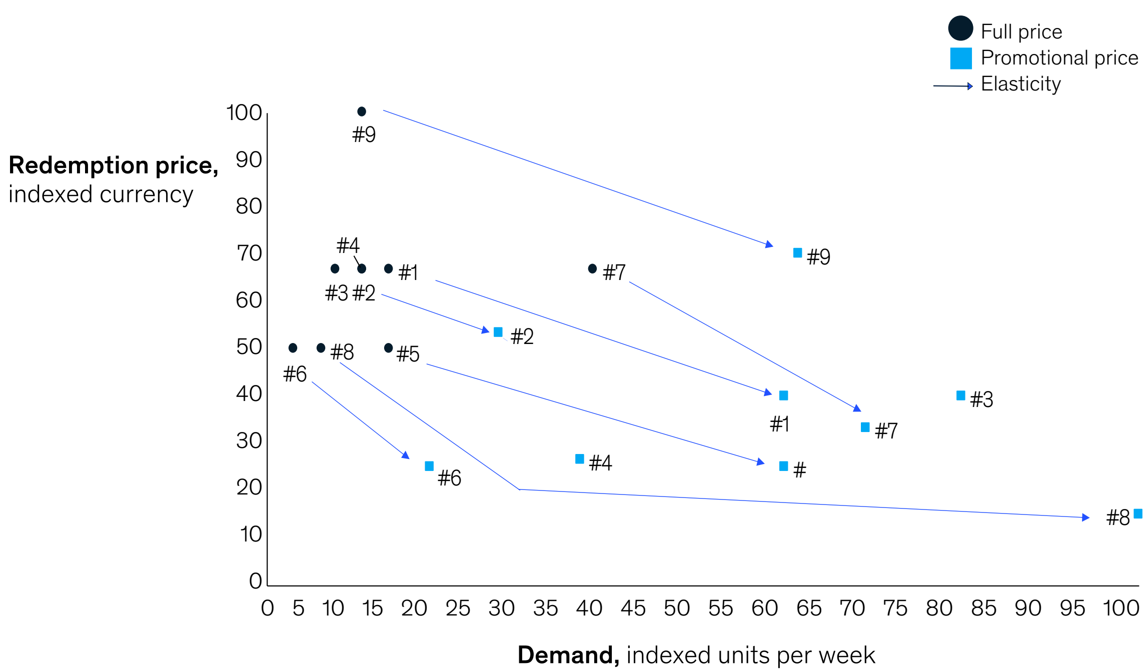
Exhibit 1 illustrates the effect of a small reduction in redemption points on demand for an airline company's round-trip flights. The response was –2 for promotional prices, compared with full-price elasticity ranging from –0.2 to –0.5.

2. Measure 'breakage' by high-value segments
All loyalty programs have members who don't redeem points or don't even know they exist, and as a result, their points eventually expire. This "breakage" reduces a program's balance-sheet liability in most cases, which sounds positive for program economics. But that's not the complete story. Reasons for breakage can include issues with redeeming points, members forgetting they're enrolled in a program, unappealing or less relevant rewards, and unachievable or expensive reward thresholds. Whatever the cause, however, breakage represents lost business opportunities, because inactive customers are at its root.

The best loyalty programs achieve their full value potential by reinvigorating members to participate in them, not by depending on breakage to make their economics look successful. The secret is to measure breakage by customer segment to ensure

Exhibit 1

Loyalty-program redemption prices affect airline flight demand in unexpected ways.



Source: McKinsey analysis

that the programs aren't alienating any particular group and that high-value segments aren't breaking too badly.

In parallel, leading companies also do the following:

— make point redemption simple and facilitate the process

— enhance loyalty programs with special features, challenges, bonuses, and games to increase earning

— remind customers of their point balances with targeted communications

— give customers more options to redeem points, such as donating their points to a charity

— connect core-business promotions and revenue-management initiatives to loyalty mechanisms

— introduce points-plus-cash options to facilitate access to big-ticket rewards

3. Enlist partners to enhance offers and rewards
Partnerships are an effective way to monetize a loyalty program and bolster its value, particularly in highly competitive markets. Alliances can provide access to new consumers or markets, expand benefits, access additional data, increase brand awareness and positive brand halo effects based on the partner, and provide greater earning options that increase both engagement and value.

But partnerships can also backfire in the absence of clear governance around key decisions and a jointly shaped value proposition, creating the following loyalty-program pitfalls:

— redemption catalogs with products or services of no value to customers

— benefits or discounts that are more readily attainable through other channels

— a clunky redemption process resulting in customer frustration and disappointment

— unbalanced perceptions of value delivered by the brand, creating "misplaced loyalty" among valuable customers toward that brand

Avoiding these pitfalls requires establishing clear alliance conditions from the outset, transparently detailing the terms, redemption process, economics, and value exchange. It's also important to recognize the benefit of this specific partnership in light of other offers in the program to ensure a consistent experience, taking time to understand how customers will interact with a new partnership to ensure the desired impact.

4. Offer points-plus-cash options to make a real difference
Many customers are enticed by exciting rewards and benefits in a loyalty program but lack the amount of program currency, or points, to access them. This sense that the rewards are "unattainable" can even discourage them from continuing to accrue points, since the cost of rewards is so high. That's where offering points plus cash is so powerful. Allowing members to pay with a combination of their points and cash reduces the redemption threshold and increases the program's attractiveness, which can motivate inactive customers. The reduced redemption ticket is also a way to create additional price discrimination for loyal customers. When companies provide a points-plus-cash option, redemptions sometimes increase by 20 to 25 percent. When correctly accounted for, it can be a game changer for overall program profitability.

5. Measure success based on engagement, not just accruals
Most loyalty programs are keen to share numbers on their program memberships or spend by members: these are a good reflection of the broad potential universe of members and comparing non-members to members. Members are generally a heterogeneous group that can be split into segments: enrolled, active (based on whatever

definition fits best), and redeemers. The most valuable metric to track is redeemers, or fans. While a typical active loyalty-program member spends 10 percent more than someone who is enrolled but not active, redeemer members spend 25 percent more than enrolled but inactive members (Exhibit 2). Currency or point redemption accelerates the virtuous loyalty loop as the customer achieves the reward or benefit and mobilizes to accrue more. That's why tracking and focusing on increasing redeemers can trigger much greater sales uplift than simply measuring the number of members.

6. Segment customers into groups you can handle

Loyalty programs provide unique and valuable data about customers, regardless of the channel through which they engage, the frequency of their interaction, or their specific needs. Leveraging these data to create meaningful, actionable segments that drive a world-class customer experience and maximize the value of all customers has become critical to optimizing a loyalty program. It's expensive, though, so businesses need to get it right. Segmenting by behavior rather than needs, value, or demographics, ensures that the specific interventions directed to each customer segment are not only rooted in customers' current behavior, but drive toward the behavior desired from them in the future. Done correctly, a behavioral segmentation becomes the foundation for creating personalized customer experiences. We have seen such initiatives yield increases of 10 to 20 percent in customer acquisition, 10 to 15 percent in long-term value and retention, and 20 to 30 percent in satisfaction and engagement.

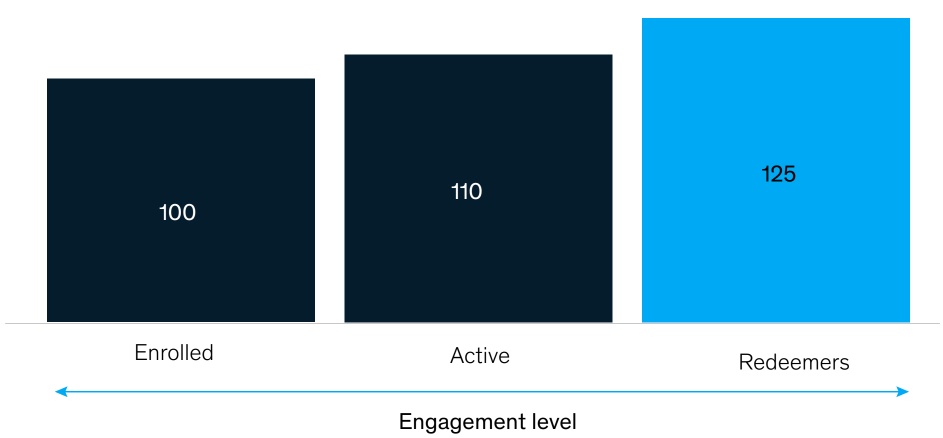
7. Personalize test-and-learn across such segments

We know loyalty data can create granular segments of customers. Building a rapid A/B testing capability is critical to fully leveraging those groups, allowing marketing organizations to experiment with new ideas, quickly discard those that don't work, and scale those that add value. A great example is email marketing. It's not only marketers' most-used

Exhibit 2

Redeemers can unlock disproportionate sales.

Customer revenue per engagement level, indexed



Source: McKinsey analysis

vehicle—88 percent of companies employ it—but it has one of the highest returns on investment, generating an average of $38 for every $1 spent, whether that's by getting members to redeem, making them aware of new benefits, highlighting partners, or acknowledging recent activity.[3] Yet 39 percent of companies don't apply A/B testing to different segments—a huge missed opportunity. We've found that personalized A/B testing elements, such as email tone and language, timing of sending, and imagery, can increase conversion and click-through rates by 15 to 30 percent.[4]

8. Create a standalone P&L for transparency on returns

Accurately measuring the incremental impact of loyalty programs is one of the most difficult challenges for organizations. Unclear key performance indicators (KPIs), complicated ROI calculations, and the need to account for the balance-sheet impact of liabilities all make tracking toward a healthy and sustainable program complex. To top it off, many loyalty programs' profit-and-loss (P&L) statements are rolled in with other company programs, further complicating measurement.

We've found measuring performance around a program-specific P&L assessment helps executives in all areas drive performance, whether they're in agile marketing teams looking at average basket size or members of the finance function examining the impact of breakage on liabilities. Measuring a baseline P&L is usually the first step, helping an organization to understand its starting point in order to identify its potential paths forward. Whether the option chosen—a series of campaigns, a new approach to segmentation, or an alliance with a retail partner—connecting it to a single P&L statement and its key levers lays the foundation for performance discussions and adequate budget allocations.

The battle for customer loyalty has only intensified in the past year. As the journeys consumers take to make purchasing decisions shift and previous purchase equations implode, it becomes more and more important to build effective customer relationships and membership programs. Loyalty programs face challenges and must prove their worth. But by understanding the levers that move them forward and how their value is optimized,

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The authors wish to thank Gabriel Bolaños, Francisco Elmiger, and Sebastián Martinez for their contributions to this article.

[2] Julien Boudet, Jason Cherok, Michele Choi, Marilyne Crepeau, Lars Fiedler, Michelle Fradin, Tobias Haefele, Ninghang Hu, Holger Hurtgen, David Kalman, Joey LaRose, Wei Wei Liu, Kathryn Rathje, Kelsey Robinson, Gustavo Schuler, Boudhayan Sen, Eli Stein, Sergio Velasquez-Terjesen, Alexis Wolfer, *CustomerOne Consumer CXO*, September 2021, McKinsey.com.
[3] "A/B test your email campaigns," Campaign Monitor, April 2019, campaignmonitor.com.
[4] Ibid

Theme 3:

Creating a customer-centric growth model

Why every business needs a full-funnel marketing strategy

Full-funnel marketing is not just a campaign strategy; it's a total shift in how marketing works.

by Jacob Ader, Julien Boudet, Marc Brodherson, and Kelsey Robinson

February 2021

You could say that marketing has a split personality. On one side is traditional brand building, driven by TV ads and other broad-reach vehicles. Many old-guard marketers who have risen through the ranks excel at this. The other side is performance marketing, or the data-driven measure of online activity. The young guns of marketing who have grown up in the digital age dominate this discipline.

For many companies, this split is inhibiting growth aspirations. Budget and impact conversations often become contentious: performance marketers tout their ability to drive clicks while brand builders argue for longer-term investments, although they often struggle to demonstrate the near-term value their teams generate. In recent conversations with two dozen top marketing executives, less than a fifth report having a very strong understanding of how their brand-building campaigns are performing. “It’s tough to measure either the short-term or long-term impacts of brand campaigns,” says one marketing executive. “We attribute increases in sales to them because of correlation, not necessarily causation.” This is troubling for CMOs because 83 percent of CEOs look to marketing as a growth engine for the business.

Brand building’s measurement problem has obscured its importance. As a result, many CMOs shift too much of their marketing spend toward the easy-to-justify capture of customers at the bottom of the funnel at the expense of the less tangible generation of customer demand and attention at the top. This skew toward bottom-of-the-funnel campaigns has significant implications for long-term value: long-term value: data from three large marketers in media and apparel retail industries indicate that customers who have an emotional connection to a brand tend to be more loyal and valuable over time than those who arrive at a site because of a generic keyword search or social media ad.

To redress this imbalance, leading organizations are moving toward “full-funnel” marketing, an approach that combines the power of both brand building and performance marketing through linked teams, measurement systems, and key performance indicators (KPIs). By adopting full-funnel marketing, companies can become more relevant to their customers, develop a fuller and more accurate picture of marketing’s overall effectiveness, and generate more value without having to spend additional marketing dollars. This approach isn’t just about doing more across each stage of the funnel. It’s about understanding how each of the stages impacts the others for a complete customer experience—how media spend on addressable TV, for example, can boost the impact of personalized emails, or how social-media ad campaigns can drive online and in-store visits.

In our experience, a thoughtful and data-driven full-funnel marketing strategy can drive significant value. By shifting greater media allocation to areas with higher returns and employing test-and-learn optimization for demand-generation campaigns, marketers can achieve a 15 to 20 percent lift in marketing ROI. Additionally, many marketers have found that incorporating both brand building and performance elements in a campaign often increases the overall return on ad spend compared with spending on performance channels alone.

Why now

While the idea of full-funnel marketing has been around for years, most companies have been unable to overcome the organizational and technological barriers to actually implementing it effectively. There are several reasons why now is a critical time for marketers to lean into full-funnel marketing. For one, performance-marketing returns have recently plateaued or declined, thanks to inflation in digital-media costs and customer saturation in some highly targeted ad markets.[1] In addition, widely available automation tools have commoditized the

[1]eMarketer Forecast Database, eMarketer, February 11, 2021, emarketer.com.

execution of performance marketing, making it difficult to secure a significant competitive advantage.

Driving full-funnel marketing is particularly necessary given the dramatic changes in customer behavior seen during the COVID-19 pandemic. This year, more than 60 percent of consumers tried a new shopping behavior in response to economic pressures, store closings, or changing priorities, one-third of whom experimented with a different brand of product. Our data make clear that customers' expectations of brands are shifting, with many citing a brand's purpose as a key reason for buying. This wave of data on new behaviors has provided marketers with a windfall in terms of developing a better understanding of what their customers want and how they make decisions across the entire funnel, offering an opportunity to both win new customers and ensure the loyalty of existing ones.

Four essentials of full-funnel marketing

The contours of a full-funnel marketing program will be different for different marketers across the spectrum. But whether CMOs are launching a new product or brand, repositioning a legacy brand, or simply trying to drive in-quarter sales, they will want to embrace four common and essential elements:

1. Brand-building measurement

Traditional TV ads, the backbone of many brand-building campaigns, have long suffered from a tracking problem. They offer the potential to reach large numbers of consumers and elicit powerful emotional responses, but their inflexibility prevents marketers from collecting detailed insights on how exactly the campaigns are impacting consumer behavior.

This is starting to change. Consumers are increasingly moving toward internet TV and digital streaming services, including audio. These options allow marketers far greater visibility into who is seeing their ads and allows them to show different ads to different households that are watching or listening to the same program. This trend has accelerated during the pandemic. Some 33 percent of consumers in Europe and 41 percent in the United States say they have begun or increased their usage of online streaming channels this year.[1]

In addition, many new measurement approaches to brand campaigns have taken off in recent years, allowing marketers to move beyond such coarse methodologies as brand trackers and reach/frequency metrics:

— *Addressable TV and audio.* Even for linear TV viewing, set-top boxes and smart TVs can now provide visibility into who has viewed particular ads, via content-recognition technology that works with unique IP addresses. This enables advertisers to establish a much more direct link between ad exposure and consumer actions.

— *Digital 'brand lift' surveys.* Unlike traditional brand trackers, these surveys, often on mobile devices, allow marketers to measure upper-funnel metrics, such as brand awareness and favorability, on a near-real-time basis and tie them to specific ad exposure at scale. They can also isolate the impact of ads by separating recently exposed populations from unexposed groups.

— *Attribution tools.* Using ad logs, these tools correlate the specific time and location in which a cohort of consumers sees an ad with the actions those consumers take. For instance, in the minutes after a TV spot airs in a particular geography or is seen by a particular demographic, do search queries, website visits, or social-media mentions increase? Unlike qualitative surveys, these "correlated outcomes" don't suffer from discrepancies between consumers' stated and actual behavior.

[2]McKinsey & Company COVID-19 Europe Consumer Pulse Survey 6/18–6/21/2020, n = 5,645, across Italy, France, Germany, Spain, UK, and Portugal, sampled and weighted to match European general population 18+ years; McKinsey & Company COVID-19 US Consumer Pulse Survey 7/30–8/2/2020, n = 2,024, sampled and weighted to match the US general population 18+ years.

2. A unified set of KPIs

Linking KPIs between channels and stages of the funnel to actual business results, such as conversions or leads, allows companies to better understand the real impact of their marketing and then create messages that will elicit the best responses. For instance, if unaided brand awareness is increasing, what effect, if any, is that having on website traffic or digital purchases? Are brand-building efforts leading more consumers to make branded search queries, which have a lower cost per click than generic product-category searches?

This unified view also helps marketers figure out how different touchpoints throughout the funnel affect each other and to identify the metrics that matter most. If brand-building campaigns, for example, are leading to more website conversions or branded search queries, these are clear signs that investing in more brand building will likely pay off. Only when marketers have linked KPIs can they identify the interactions most tightly tied to business value and start making smart decisions to adjust or rebalance their marketing spend.

3. An updated media mix model for integrated spending

Many marketers now rely on media mix models (MMM) to measure the impact of their campaigns and determine how much money they should spend on different types of advertising and marketing. While MMMs have proven useful for making allocation decisions, they fall short in a number of ways. Because they require long look-back periods to estimate the impact of each type of spend, they aren't responsive to short-term changes, such as shifts in campaign performance, or changes in shopping behavior due to external factors, such as those we are seeing today. They also don't get very granular in their spending recommendations and can fail to capture the nuances of actual channel behavior. For example, a model may recommend spending increases for paid search ads on branded search terms even though a brand is already showing up in close to 100 percent of results.

MMMs also don't offer granular data on which channels or platforms should get credit for customer conversions. Some 30 percent of marketers admit to being held back by these difficulties, including those with budgets of more than $500 million.

To make MMMs more reliable and better suited to a full-funnel marketing strategy, organizations need to modernize them with additional inputs, such as those from incrementality tests and multitouch attribution (MTA) models. Doing regular incrementality tests, which involve running a structured experiment with a control group of consumers who aren't shown ads, can provide a cleaner verification of a particular channel's performance, as well as insights that are closer to real-time and more granular data on campaigns. This helps marketers assess the true impact of their efforts and adjust the attribution for a channel accordingly. Recent technology and analytics advances have made such incrementality tests simple and inexpensive, although they are time consuming to run at scale across channels.

Advances in analytics have also helped improve the process of determining where credit for a customer conversion should go in MTA models. Combining this with audience-propensity scoring helps further define how valuable a particular channel or tactic is. If a campaign on a particular social-media platform, for instance, converts consumers who already have a high propensity to purchase, that channel would be assigned a lower "incrementality multiplier."

4. A full-funnel operating model

Full-funnel marketing requires a complete top-to-bottom integration of the function; it can't simply be tacked onto existing daily processes. That starts with rethinking how work gets done across functions. While the transformation of an operating model requires changes across almost all elements of the marketing function, four areas are the most important to get right:

— *Incentives for full-funnel performance.* To help make measurement rigor a core part of marketing's culture, marketers should be held accountable and rewarded for their ability to deliver on well-defined engagement or revenue goals. These should be based on both a unified set of KPIs tied to full-funnel performance, such as total brand awareness and total visitor traffic, and KPIs that measure incremental value, such as extra traffic coming from A/B testing or additional revenue driven by brand campaigns according to the MMM.

— *Cross-functional collaboration.* Full-funnel marketing can't be done effectively without close collaboration among all stakeholders, including brand managers, performance-marketing leaders, analytics marketers, and finance. To ensure productive interaction, some companies have created weekly huddles, where insights are shared from across the funnel and decisions are made jointly on everything, including KPIs, spending levels, and which audiences to target.

— *Deeper collaboration between media agency and partner.* Marketers often have an incomplete understanding of what their agencies actually do and what value they are accountable for. Correcting this involves not just more active agency management but also closer collaboration. This includes ensuring that the marketers, not the agency, own their user-level data, insisting on collaboration for rapid testing and iteration, and pushing media companies to create integrated ad buys that leverage their brand-building and performance-marketing channels.

— *Adoption of test-and-learn capabilities by brand marketers.* The dynamic, rapid test-and-learn capabilities common to performance-marketing teams need to be extended to mid- and upper-funnel teams. Brand marketers can use these methodologies to rapidly test personalized creative and to optimize the videos or other consumer content ads that are delivered alongside, a tactic shown to be highly effective.

Full-funnel marketing is not just a campaign strategy; it's a total shift in how marketing works. It demands close team collaboration to harness the complete range of marketing capabilities to increase the impact from all campaigns. Most importantly, it allows the CMO to provide the C-suite with a much richer and more complete picture of how exactly marketing is driving growth.

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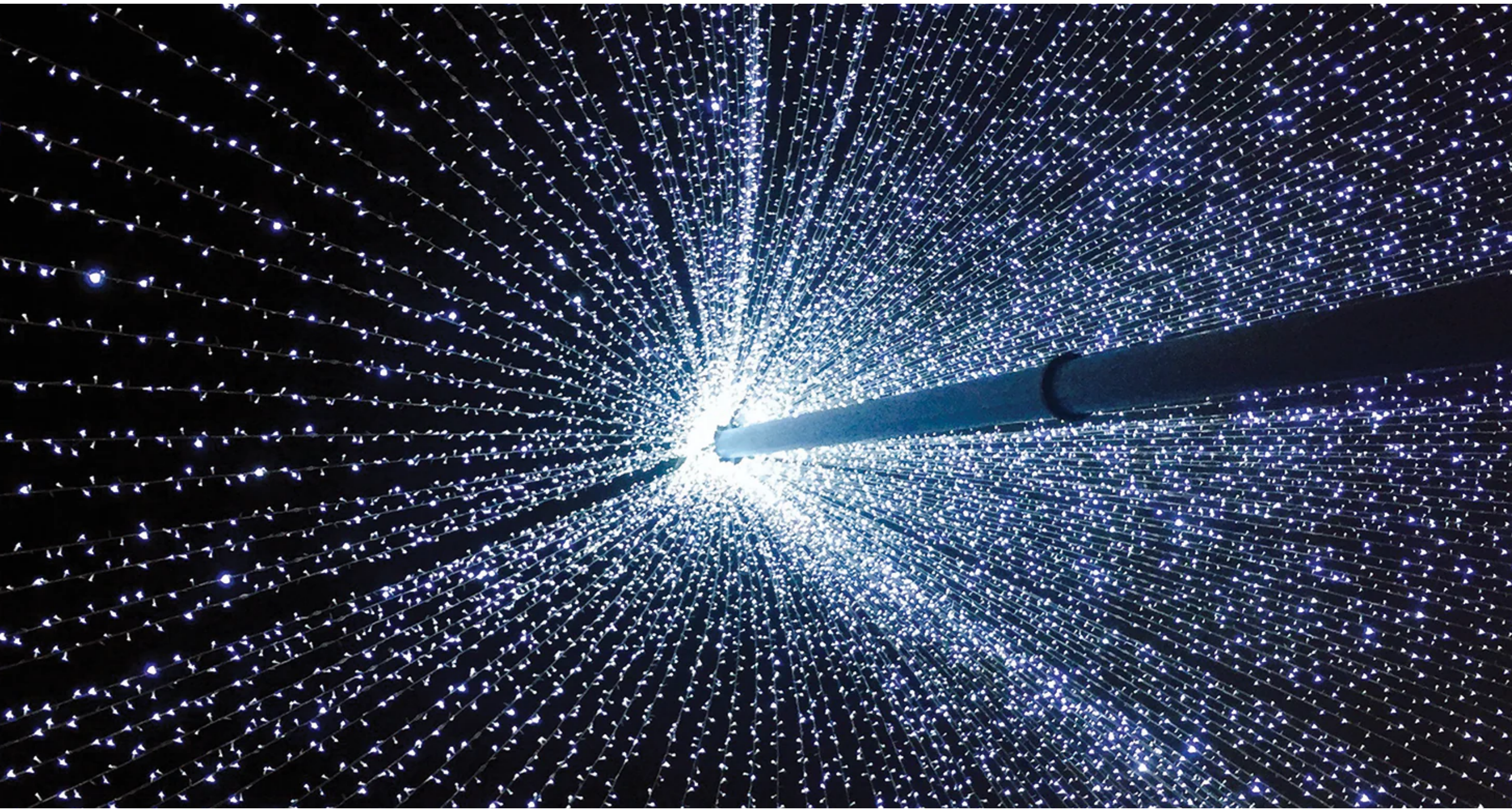
Prediction: The future of CX

Designing great customer experiences is getting easier with the rise of predictive analytics.

This article was a collaborative effort by Rachel Diebner, David Malfara, Kevin Neher, Mike Thompson, and Maxence Vancauwenberghe, representing views from McKinsey's Marketing & Sales and Operations practices.



February 2021

Companies of all stripes have invested heavily in tools and technologies to help them understand their customers more deeply and to gain the advantages of superior customer experience (CX). Yet as leaders strive to form a more complete picture of customer preferences and behaviors, they continue to rely on aging survey-based measurement systems that for decades have formed the backbone of CX efforts. Companies use these systems to track CX performance through brand or relationship surveys, "close the loop" on customer feedback via post-transaction surveys, and even plot strategic moves by attempting to mine the feedback from their regular surveys over time. Entire teams dedicate themselves to managing questionnaires and boosting response rates—and the resulting metrics can shape everything from employee bonuses and executive compensation to strategic investment decisions.

The trouble is, executives increasingly recognize that survey-based measurement systems fail to meet their companies' CX needs—although surveys themselves are an important tool for conducting research. In fact, this article draws on our recent survey of more than 260 CX leaders from US-based companies of all sizes.[1] Ninety-three percent of these respondents reported using a survey-based metric (such as Customer Satisfaction Score or Customer Effort Score) as their primary means of measuring CX performance, but only 15 percent of leaders said they were fully satisfied with how their company was measuring CX—and only 6 percent expressed confidence that their measurement system enables both strategic and tactical decision making. Leaders pointed to low response rates, data lags, ambiguity about performance drivers, and the lack of a clear link to financial value as critical shortcomings.

A few leading companies are pioneering a better approach that takes full advantage of the wealth of data now available. Today, companies can regularly, lawfully, and seamlessly collect smartphone and interaction data from across their customer, financial, and operations systems, yielding deep insights about their customers. Those with an eye toward the future are boosting their data and analytics capabilities and harnessing predictive insights to connect more closely with their customers, anticipate behaviors, and identify CX issues and opportunities in real time. These companies can better understand their interactions with customers and even preempt problems in customer journeys. Their customers are reaping benefits: think quick compensation for a flight delay, or outreach from an insurance company when a patient is having trouble resolving a problem. These benefits extend far beyond the people typically thought of as "customers"—to members, clients, patients, guests, and intermediaries. Early movers in the world of customer-experience analytics herald a fundamental shift in how companies evaluate and shape customer experiences.

In this article, we explore how data and analytics are beginning to transform the art and science of customer experience. We present new research that brings clarity and a fact base to the shortcomings of survey-based measurement systems. We then examine how a few leaders have implemented data-driven CX systems and in turn reduced churn, boosted revenue, and lowered cost to serve. We end with insight on how to get started, including four key steps for CX leaders as they transition toward data-driven insight and action.

The benefits are not automatic. Those just starting out will face stumbling blocks and organizational resistance. But with commitment, even companies with rudimentary CX systems, limited data, and a shortage of data scientists can begin laying the groundwork to transform their CX programs and their customers' experiences.

The CX programs of the future will be holistic, predictive, precise, and clearly tied to business outcomes. Evidence suggests that the advantages will be substantial for companies that start building the capabilities, talent, and organizational structure needed for this transition. Those that stick with the traditional systems will be forced to play catch-up in the years to come.

‘Survey says’: The shortcomings of traditional CX measurement

While surveys themselves are a valid means of gathering customer insight, they fall short as a management tool for measuring CX performance and identifying and acting on CX opportunities. For organizations to lead from a customer-centric position, they increasingly need a comprehensive view of the full customer journey, as well as the ability to obtain deep, granular insight on what is driving customer experience. They need immediate and individual signals in order to take action “in the moment” and to create relevant experiences for each customer, and they need to demonstrate that the experience enhancements they would like to invest in will result in positive ROI. Survey-based systems have four major flaws that make those critical tasks nearly impossible (exhibit).

1. *Limited:* The typical CX survey samples only 7 percent of a company’s customers, providing an extremely limited view of what customers experience and value. In fact, only 13 percent of the CX leaders we surveyed expressed full confidence that their CX measurement system provides a representative view of their customer base.

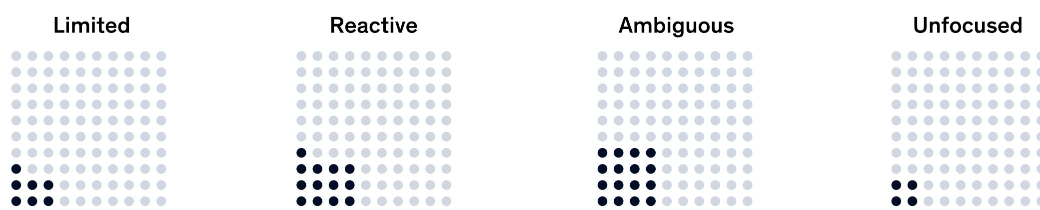
2. *Reactive:* Surveys are a backward-looking tool in a world where customers expect their concerns to be resolved increasingly quickly. Nearly two-thirds of respondents ranked the ability to act on CX issues in near real time as among their top three priorities, but only 13 percent of leaders expressed certainty that their organizations could achieve this level of rapid insight through existing systems.

3. *Ambiguous:* Surveys often fail to reveal the root causes of customer sentiment. In fact, scores can vary based on many outside factors, including geographical bias and industry shocks, making it difficult to perform reliable root-cause analysis using surveys alone. Only 16 percent of CX leaders said that surveys provide them with granular-enough data to address the root causes of CX performance.

Exhibit 1

Survey-based systems can no longer meet the demands of today’s companies.

Four flaws with today’s survey-based customer-experience (CX) measurement systems



Limited	Reactive	Ambiguous	Unfocused
Only **7%** of the customer voice is shared with CX leaders	Only **13%** of CX leaders are confident that their organization can take action on CX issues in near real time	Only **16%** of CX leaders think that surveys allow them to address the root causes of performance	Only **4%** of CX leaders believe their CX measurement system enables them to calculate a decision’s return on investment

Source: 2020 McKinsey Customer Experience Survey, conducted in collaboration with AlphaSights and Gerson Lehrman Group

4. *Unfocused:* As one executive at a large financial-services company put it, “The association between survey-based scores and business outcomes is not well understood, and, as a result, many parts of the organization simply claim a business impact from their CX initiatives with no real evidence.” Several companies have recently come under fire for basing investment decisions on a survey-based score alone. Remarkably, of the CX leaders we surveyed, only 4 percent said that their system lets them calculate the ROI of CX decisions.

Predictive customer insight is the future

Since survey-based systems became ubiquitous, the world of insight generation has transformed through impressive advances in the ability to generate, aggregate, and analyze data. Companies now have access to a broad array of data sets: internal data on customer interactions (both digital and analog), transactions, and profiles; widely available third-party data sets that cover customer attitudes, purchase behaviors and preferences, and digital behaviors, including social-media activity; and new data sets on customer health, sentiment, and location (in stores, for example) generated by the Internet of Things (IoT). Other business disciplines, including marketing and revenue management, have already transformed through the aggregation and analysis of these vast data sets. The contrast is stark: Why use a survey to ask customers about their experiences when data about customer interactions can be used to predict both satisfaction and the likelihood that a customer will remain loyal, bolt, or even increase business?

Why use a survey to ask customers about their experiences when data about customer interactions can be used to predict satisfaction?

Some CX leaders have taken the plunge and have begun making use of the data on offer, drawing valuable insights that can prompt alerts and guide swift action to improve customer experiences. While the specifics may vary across companies and industries, this approach centers on a predictive customer-experience platform that consists of three key elements:

1. *Customer-level data lake*

First, the company gathers customer, financial, and operational data—both aggregate data and data on individual customers.[2] The company processes these data and stores them in a cloud-based platform. Comprehensive, connected, and dynamic customer-level data sets allow the organization to map and track customer behavior across interactions, transactions, and operations. Whereas surveys reflect the views of a subset of customers at a single point in the past, these rich data sets encompass the full customer base and span the customer journey, thereby shedding light on the root causes of performance.

The data lake serves as the foundation for developing a rigorous understanding of customer experiences. The platform should be reliable throughout the organization, with clear and consistent mapping across all data sources and unique identifiers for customers, product lines, and other critical business input.

2. *Predictive customer scores*

The company develops analytics—often using several types of machine-learning algorithms—to understand and track what is influencing customer satisfaction and business performance, and to detect specific events in customer journeys.

The algorithms generate predictive scores for each customer based on journey features. These scores allow the company to predict individual customer satisfaction and value outcomes such as revenue, loyalty, and cost to serve. More broadly, they allow CX leaders to assess the ROI for particular CX investments and directly tie CX initiatives to business outcomes.

3. *Action and insight engine*

Information, insights, and suggestions are shared with a broad set of employees (including frontline agents) and tools (such as customer-relationship-management platforms) through an application-programming-interface (API) layer. For example, agents can receive alerts and notifications about the actions they should take to personalize customer experiences and improve CX outcomes. The API layer serves as a single source of truth, fueling recommendation engines based on both the data lake and customer scores. Importantly, the predictive platform, unlike survey-based systems, delivers timely insights and spurs swift action, both by employees and through digital interfaces.

Predictive CX platforms allow companies to better measure and manage their CX performance; they also inform and improve strategic decision making. These systems make it possible for CX leaders to create an accurate and quantified view of the factors that are propelling customer experience and business performance, and they become the foundation to link CX to value and to build clear business cases for CX improvement. They also create a holistic view of the satisfaction and value potential of every customer that can be acted upon in near real time. Leaders who have built such systems are creating substantial value through a wide array of applications across performance management, strategic planning, and real-time customer engagement.

Predictive CX platforms become the foundation to link CX to value and to build clear business cases for CX improvement.

One leading credit-card company wanted to adopt a more omnichannel strategy and boost its performance in digital channels. It focused on building a CX data and analytics stack to systematically identify, improve, and track the factors influencing customer satisfaction and business performance across 13 priority journeys. It started by gathering interaction, transaction, and customer-profile data with a journey analytics platform to identify drivers of satisfaction for each journey, as well as areas where it could improve. The platform included data on repeat interactions, lead times, and how often customers hopped from one channel to another. It also encompassed more subtle factors, such as whether the company effectively handled negative outcomes and what communications took place at various points in time.

This analytics-driven approach gave the company a quantified and systematic view into the problems, opportunity areas, and channel interactions across millions of customers, enabling the organization to support a systematic journey-improvement cycle. The team used the analytics platform to focus its investments and operational efforts on the journeys and specific moments that made a difference for customers, and it ultimately reduced its interaction and operational costs by 10 to 25 percent as a result of the CX and digital transformation.

Prioritizing CX efforts through intentional strategic planning is another promising use case for data-driven systems that allow CX leaders to understand which operational, customer, and financial factors are creating systemic issues or opportunities over time. One US healthcare payer, for example, built a “journey lake” to determine how to improve its customer care. The journey lake syncs four billion records across nine systems, spanning marketing, operations, sales, digital, and IoT. The resulting holistic customer view enabled the organization to identify operational break points—thresholds where patients often ask to speak with a supervisor or move to another channel to resolve an issue—and proactively reach out to patients through the website, emails, and outbound calls to settle the problem. It also used the data to develop a smarter digital migration strategy, targeting customers who had minimal engagement on digital channels and coaching them to use more self-service functions. The organization substantially increased digital adoption by focusing on the most significant pain points, such as prescription renewals; it reduced its costs by decreasing (by more than a quarter) the frequency with which customers turned to other channels after starting with digital.

Finally, thanks to the near-real-time nature of analytical insights, these new systems create a platform for proactive daily customer engagement. One leading airline built a machine-learning system based on 1,500 customer, operations, and financial variables to measure both satisfaction and predicted revenue for its more than 100 million customers every day. The system allowed the airline to identify and prioritize those customers whose relationships were most at risk because of a delay or cancellation and offer them personalized compensation to save the relationship and reduce customer defection on high-priority routes. A combined team of about 12 to 15 data scientists, CX experts, and external partners worked together for about three months to build the system and lead this first application, which resulted in an 800 percent uplift in satisfaction and a 60 percent reduction in churn for priority customers.

How to turn data into insight and action

The transition to predictive insight will not take place overnight. As our research shows, most organizations still rely on surveys to gauge customer sentiment. Leaders now have the opportunity to take their CX programs to the next level—starting from where their organizations are now. Based on our research on organizations that have successfully made the transition, we have identified four key steps to jump-start such CX transformations.

1. Work on changing mindsets: The transition will inevitably involve challenges, not least of which will be a mindset shift for both teams and CX executives. Leaders may feel that predictive systems are outside their purview, the domain of the IT department or a data-science team. But times are changing, and today's CX leaders need to focus on data as they once zeroed in on a single CX score. Some may point to the fact that their organization has already done regression analysis on a few key performance indicators. It's time to think bigger and bolder, and to build a system—not dabble in data.

The role of the CX leader is evolving, which means that executives will need to reposition themselves within their organizations. When asked about the biggest challenge with the current system, one chief experience officer responded: "People associate CX with marketing, not technology." That is changing as more and more companies take up predictive analytics, and it's up to CX leaders to help encourage the change in perception.

The CX team should define direction and strategy, but ensuring buy-in and excitement among the affected stakeholders will be key to scaling impact.

2. Break down silos and build cross-functional teams: CX functions often fall into the trap of creating their own silos within a company. To begin the transition, CX leaders need to better integrate with the rest of the organization.
Data owners will inevitably span operations, marketing, finance, and technology functions, so convening across senior leadership will be vital to ensure efficient data access and management. (And, of course, data scientists—not CX professionals—will be the ones writing the algorithms.) The CX team should define direction and strategy, but ensuring buy-in and excitement among the affected stakeholders will be key to scaling impact.

One travel-industry client, for example, began its data-driven system with a focus on delivering real-time enhancements to its customer-service operation because the CX team had a strong partnership with the service organization and could prove value quickly. The initial effort involved close collaboration: CX acted as the business owner, the data-science team developed the product, and the customer-service organization acted as the first recipient of an initial minimum viable product. Outside the core team, an advisory board including the COO, CFO, and chief marketing officer stayed informed of the progress and advised on future use cases so that when the initial pilot was successful, the COO was already on board for an additional use case in his organization. Even in the case of smaller-scale initiatives—for example, where an organization hires contractors rather than standing up an in-house data-science team—these strong, cross-functional relationships at both the development and steering-committee level will be vital to creating and scaling the CX insight engines of the future.

3. Start with a core journey data set and build to improve accuracy: Most organizations face challenges with data quality and availability—and without data, this transition is a nonstarter. The good news is that organizations can get started with basic customer-level data, even if the data are not perfect. The first step is to collect individual customer-level operational and financial data. A combination of customer profiles, along with digital and analog interactions, is usually a solid jumping-off point.

Teams should create a detailed journey taxonomy, including all the potential drivers of satisfaction for their customer base. The taxonomy can be used for hypothesis generation, leading to new measurable attributes for inclusion in the predictive model. These attributes—called data features in machine learning—can range from numeric properties, such as a customer's annual spend, to binary properties, such as whether the customer purchased a product online or in a store. Over time, understanding which features are significant in the machine-learning model—and comparing those with the team's hypotheses—can help organizations to recognize where data may be inaccurate or incomplete and to adapt their data-acquisition strategy accordingly. If data for certain features do not exist, teams can explore options to acquire new data sets (for example, credit-agency data) or apply new instrumentation to generate required features (for example, IoT sensors to map customer interaction points in physical environments). As the machine-learning algorithm ingests more data and generates its own insights, the data sets will become more robust—proving useful across multiple enterprise applications.

Ultimately, companies can look to integrate data from sources across the customer journey, including chat, calls, emails, social media, apps, and IoT devices. Regardless of the source, all data collection, storage, and use should follow privacy and cybersecurity best practices. (Notably, our colleagues have found that customer-data protection can serve as a source of competitive advantage as consumers become more careful about sharing data and avoid or stop doing business with companies whose data-security practices they don't trust.) Organizations should follow regional data regulations and remove any variables related to protected classes, such as race and religion. All identifying information should be encrypted and anonymized before it is analyzed. Finally, regular risk reviews can help detect algorithmic bias in CX systems. CX leaders are responsible for knowing what their organizations are doing to protect customer data, mitigate bias, and promote fairness in their predictive systems.

In the early days, it is important to have a clear view for how the insights will be applied and to focus on a few specific use cases that will create immediate return.

4. Focus first on the use cases that can drive quick value: Data-driven, predictive systems offer CX organizations a unique opportunity to tie CX strategies to tangible business value. In the early days, it is important to have a clear view for how the insights will be applied and to focus on a few specific use cases that will create immediate return. As a simple framework, organizations can review major sources of opportunity, pain points, or both across existing customer journeys and think through how a predictive system might create new solutions or enhance existing ones that may have a direct impact on loyalty, cost to serve, cross-sell, and up-sell behaviors.

For example, one company applied its predictive system to its issue-resolution journey after realizing that its contingency funds—which had previously been allocated uniformly across customers—could be applied more strategically. The company developed an algorithm that could identify high-priority customers as measured by lifetime value and recent experiences (such as the extent of delayed service the customer had experienced in the past month), and it used the algorithm to allocate contingency funds toward dissatisfied, high-value customers. This first use case proved successful, saving the organization more than 25 percent of its planned budget and paving the way for future applications. Leaders should ask themselves what use cases present a clear opportunity to drive value through a proof of concept so they can build momentum and gain support.

After years of serving as the benchmark for defining and refining a company's customer-experience performance, survey-based systems are heading toward their twilight. The future of superior customer-experience performance is moving to data-driven, predictive systems, and competitive advantages are in store for companies that can better understand what their customers want and need.

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The authors wish to thank Victoria Bough, Harald Fanderl, Abhishek Gupta, Oliver Jakubiec, Marc Levesque, Nicolas Maechler, Evelyn Milde, Iwan Tanuwidjaja, Kelly Ungerman, and Elsa Yan for their contributions to this article.

The value of getting personalization right—or wrong—is multiplying

Next in Personalization 2021 Report reveals that companies who excel at demonstrating customer intimacy generate faster rates of revenue growth than their peers. And the closer organizations get to the consumer, the bigger the gains.

This article was a collaborative effort by Nidhi Arora, Daniel Ensslen, Lars Fiedler, Wei Wei Liu, Kelsey Robinson, Eli Stein, and Gustavo Schüler

November 2021

Key takeaways

- Personalization matters more than ever, with COVID-19 and the surge in digital behaviors raising the bar. Three-quarters of consumers switched to a new store, product, or buying method during the pandemic.

- Seventy-one percent of consumers expect companies to deliver personalized interactions. And seventy-six percent get frustrated when this doesn't happen.

- Personalization drives performance and better customer outcomes. Companies that grow faster drive 40 percent more of their revenue from personalization than their slower-growing counterparts.

Personalization is not only a crucial capability, it's one that punches above its weight, no matter whether the company is a digital native, a brick-and-mortar player, or a behind-the-scenes producer or supplier.

Consumers don't just want personalization, they demand it. With store and product loyalty more elusive, getting it right matters. Roughly 75 percent of consumers tried a shopping behavior in the last 18 months, and more than 80 percent of those intend to continue with new behaviors.

Furthermore, our research found that companies that excel at personalization generate 40 percent more revenue from those activities than average players. Across US industries, shifting to top-quartile performance in personalization would generate over $1 trillion in value. Players who are leaders in personalization achieve outcomes by tailoring offerings and outreach to the right individual at the right moment with the right experiences.

These seven charts show how consumer attitudes around personalization are changing and what outperforming companies are doing to grow customer lifetime value at scale.

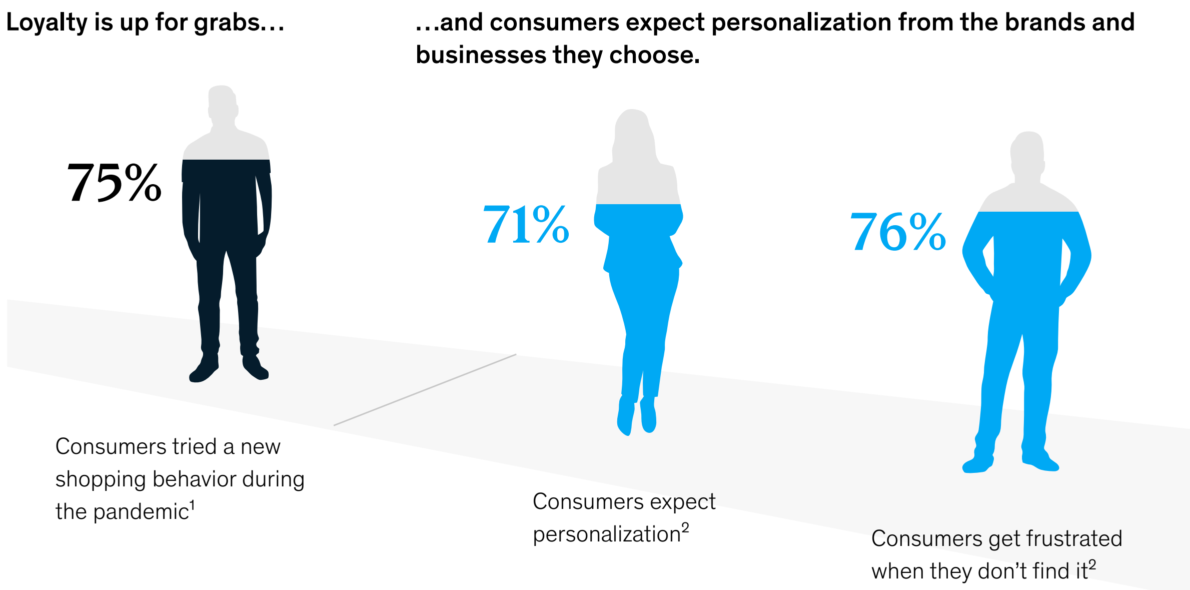
Personalization matters more than ever before

The surge in online interactions since the onset of the pandemic escalated expectations—giving consumers more exposure to the personalization practices of e-commerce leaders and raising the bar for everyone else. From web to mobile and in-person interactions, consumers now view personalization as the default standard for engagement.

Our research shows that 71 percent of consumers expect companies to deliver personalized interactions. And 76 percent get frustrated when this doesn't happen. Ratcheting up the pressure on companies, if consumers don't like the experience they receive, it's easier than ever for them to choose something different. Three-quarters of consumers switched to a new store, product, or buying method during the pandemic.

Exhibit 1

Nonpersonalized communications pose a business risk in a low-loyalty environment.



[1] Question: "Since the coronavirus (COVID-19) crisis started, which of the following have you done?" 25% of consumers selected "none of these." Possible answers: "new shopping methods"; "different brand"; "different store, retailer, or website"; "private label or store brand"; "new digital shopping method."

[2] Question: "Please indicate how much you agree or disagree with the statements below when it comes to personalized communications and products/services from brands/businesses: I expect personalized communications and products/services tailored to my needs from the brands/businesses that I buy from. It is frustrating when a brand/business shows or recommends me things that are not relevant to me." Possible answers: "strongly disagree"; "disagree"; "somewhat disagree"; "somewhat agree"; "agree"; "strongly agree." Numbers shown indicate respondents that selected "somewhat agree"; "agree"; and "strongly agree."

Source: McKinsey Next in Personalization 2021 consumer survey 9/7–9/8/2021 (n = 1,013), sampled and weighted to match the US general population 18+ years; McKinsey Consumer Pulse Survey 8/25–8/31/2021 (n = 2,094) and 2/18–2/22/2021 (n = 2,076), sampled and weighted to match the US general population 18+ years.

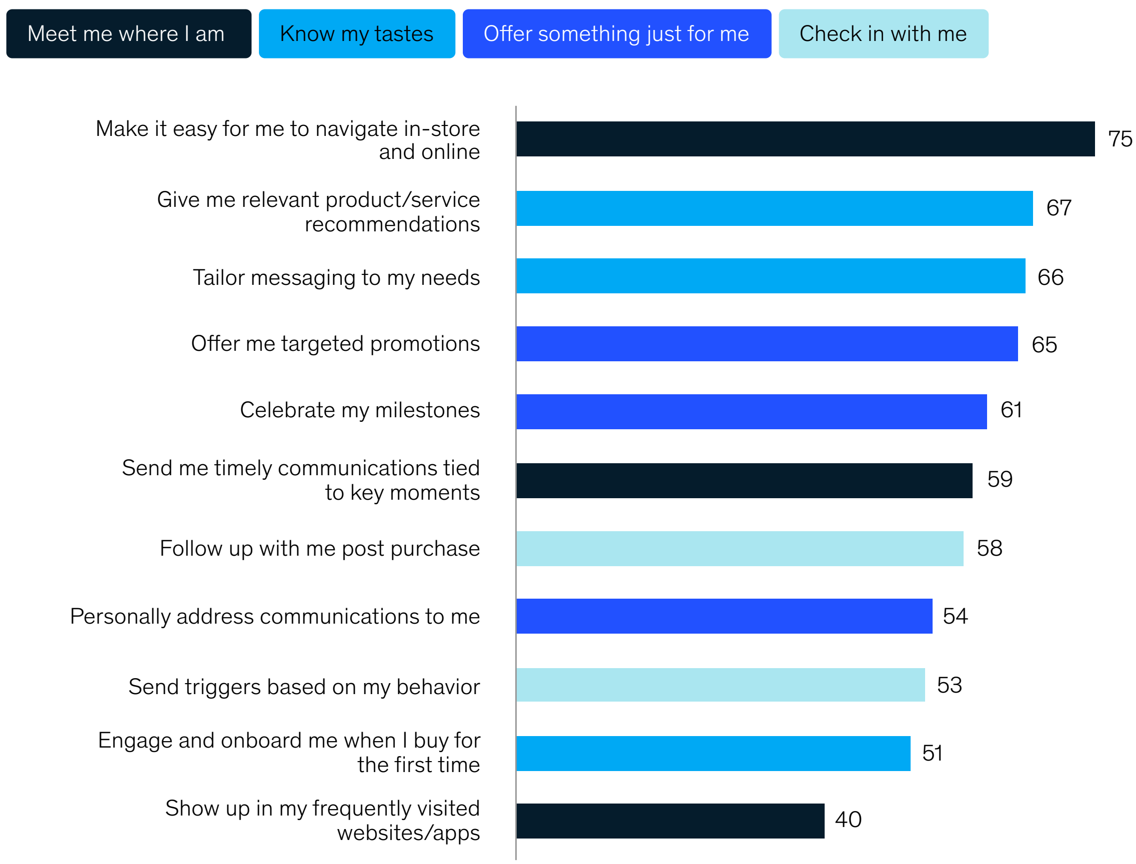
Research shows shoppers have a strong point of view on personalization

Seventy-two percent said they expect the businesses they buy from to recognize them as individuals and know their interests. When asked to define personalization, consumers associate it with positive experiences of being made to feel special. They respond positively when brands demonstrate their investment in the relationship, not just the transaction. Thoughtful touchpoints such as checking in post-purchase, sending a how-to video or asking consumers to write a review generate positive brand perceptions.

Exhibit 2

Consumers expect brands to demonstrate they know them on a personal level.

Importance of personalization actions for consumers purchasing for the first time, % of respondents[1]



[1] Question: "We would like to know how each of these aspects influences your decision to buy from a brand/business for the first time. For that brand/business, please indicate how important each of the following aspects is." Possible answers: "not at all important"; "somewhat important"; "important"; "very important"; "extremely important." Numbers shown indicate respondents that selected "important"; "very important"; and "extremely important."
Source: McKinsey Next in Personalization 2021 consumer survey 9/7–9/8/2021 (n = 1,013), sampled and weighted to match the US general population 18+ years

…And consumers reward those that get it right

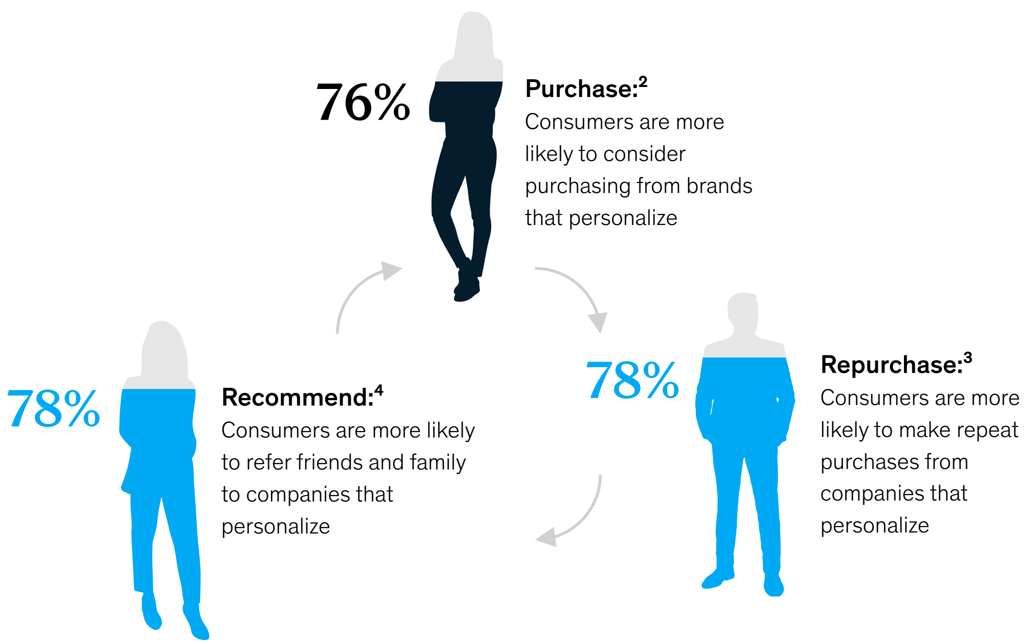
Over three-quarters of consumers (76 percent) said that receiving personalized communications was a key factor in prompting their consideration of a brand, and 78 percent said such content made them more likely to repurchase.

Personalization is especially effective at driving repeat engagement and loyalty over time. Recurring interactions create more data from which brands can design ever-more relevant experiences—creating a flywheel effect that generates strong, long-term customer lifetime value and loyalty.

Exhibit 3

Personalization directly influences buying behavior across the customer life cycle.

Likelihood to purchase, recommend, and repurchase depending on personalization, % of respondents[1]



[1] Question: "Please indicate how much you agree or disagree with the statements below when it comes to personalized communications and products/services from brands/businesses."
[2] Purchase: "I am more likely to consider buying from brands/businesses that engage with me in a personalized and tailored way."
[3] Repurchase: "I am more likely to repurchase from brands/businesses that offer personalized communications and products/services."
[4] Recommend: "I am more likely to recommend brands/businesses to my friends and family that offer personalized communications and products/services."
Possible answers: "strongly disagree"; "disagree"; "somewhat disagree"; "somewhat agree"; "agree"; "strongly agree." Numbers shown indicate respondents that selected "somewhat agree"; "agree"; and "strongly agree."
Source: McKinsey Next in Personalization 2021 consumer survey 9/7–9/8/2021 (n = 1,013), sampled and weighted to match the US general population 18+ years

Performance propels outperformance

Research shows that personalization most often drives 10 to 15 percent revenue lift (with company-specific lift spanning 5 to 25 percent, driven by sector and ability to execute). The more skillful a company becomes in applying data to grow customer knowledge and intimacy, the greater the returns. For digitally native companies that forge a data-backed, direct-to-consumer model, personalization isn't just how they market, it's how they operate.

Exhibit 4

Digitally native companies drive more revenue from personalization than other company archetypes.

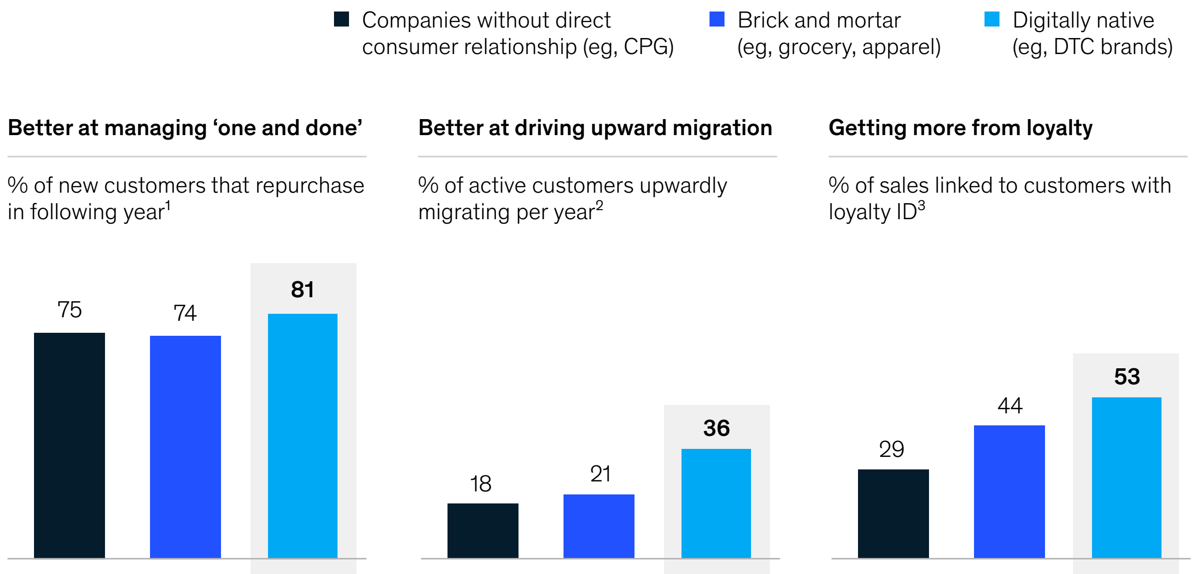
Company archetype	Companies without direct relationship (eg, CPG)	Brick and mortar (eg, grocery, apparel)	**Digitally native (eg, DTC brands)**
Strength of customer relationship	**Low**	**Medium**	**High**
	• Typically does not own customer transaction • Limited access to or use of 1st-party data	• Owns customer transaction, not always product development • 1st-party data captured but mixed	• Owns customer transaction and product development • 1st-party data at heart of decision making
% of revenue driven by personalization[1]	~5–10%	~10–20%	~25%

[1] Question: "What percentage of your revenue comes from personalized marketing actions/or tactics?" Possible responses: values from 0 to 100%.
Source: McKinsey Next in Personalization 2021 benchmarking survey, 2/7–2/14/2021 (n = 100) sampled among consumer businesses

Those leading the charge in personalization also have better customer outcomes. Their focus on the relationship and long-term value leads to better upward migration, retention, and loyalty.

Exhibit 5

Companies that drive greater revenue impact from personalization (eg, digitally native) have better customer outcomes.

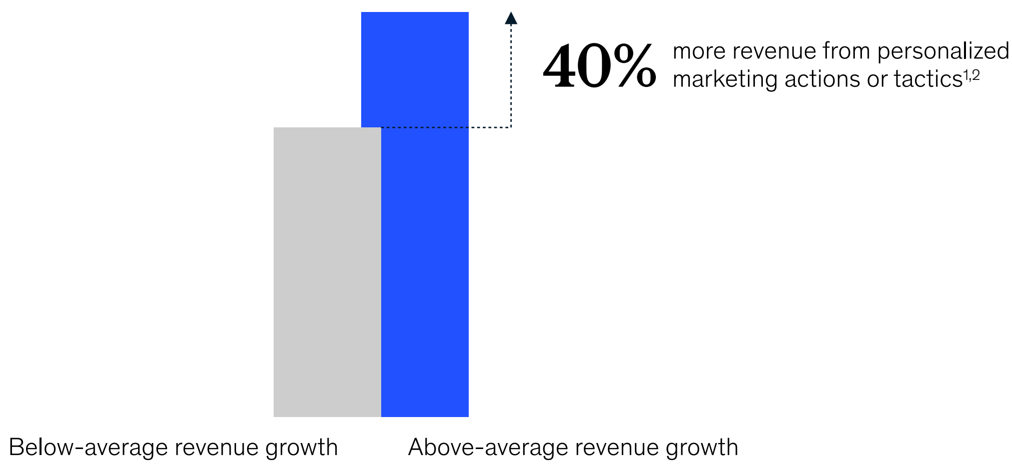


[1] Question: "What percentage of new customers repurchase in the following year?"
[2] Question: "What percentage of your active customers (any customer who made at least one purchase in a given year) are upwardly migrating per year (ie, spending more this year than last year)?"
[3] Question: "What percentage of revenue is tied to customers that are part of your company loyalty program (eg, 80% of sales are tagged with loyalty ID)?"
Possible responses: values from 0 to 100%.
Source: Source: McKinsey Next in Personalization 2021 benchmarking survey, 2/7–2/14/2021 (n = 100) sampled among consumer businesses

Personalization can also be a revenue accelerator even for businesses that typically lack direct access to customers such as companies in the consumer packaged goods segment. Among these companies, those with the fastest rates of revenue growth were far more likely to prioritize personalization than slower growers. The research suggests that even small shifts in improving customer intimacy create competitive advantage—and these benefits grow with maturity.

Exhibit 6

Companies that capture more value from personalization grow faster.



[1] Companies divided into two groups based off past-year revenue growth; top half classified as higher growth and bottom half as lower growth.
[2] Question: “What % of your revenue comes from personalized marketing actions/or tactics?” Possible responses: values from 0 to 100%.
Source: McKinsey Next in Personalization 2021 benchmarking survey, 2/7–2/14/2021 (n = 20) sampled among consumer companies without direct consumer relationship (eg, CPG)

Outperformers organize their business around personalization

Companies that achieve the best results from personalization approach it differently. Rather than seeing personalization solely as a marketing or analytics problem, they view it as an organization-wide opportunity. Rather than focusing solely on short-term wins, they look for long-term drivers of growth and emphasize customer lifetime value.

Here are the five things outperformers can do to accelerate personalization and create value:

— *They lean into data and analytics to identify opportunities.* Looking across the customer life cycle, leaders build a granular view of where there is the most value. They leverage customer segments and microsegments, and factor in behavioral, transactional, and engagement trends. They use those insights to define and quantify their personalization objectives and ground their efforts in customer-centric key performance indicators (KPIs).

— *They invest in rapid activation capabilities powered by advanced analytics.* Leaders develop at-scale content creation and AI-driven decisioning capabilities so they can respond to customer signals in real-time. They leverage predictive analytics and models to determine what content and messages to serve which customers (for example, propensity models, or predictive next-best-action algorithms). They also establish robust measurement processes that track the impact of customer interventions and feed that information back to their systems and teams. These processes help them deliver the right content through the right channels at the right moments in a consumer's journey.

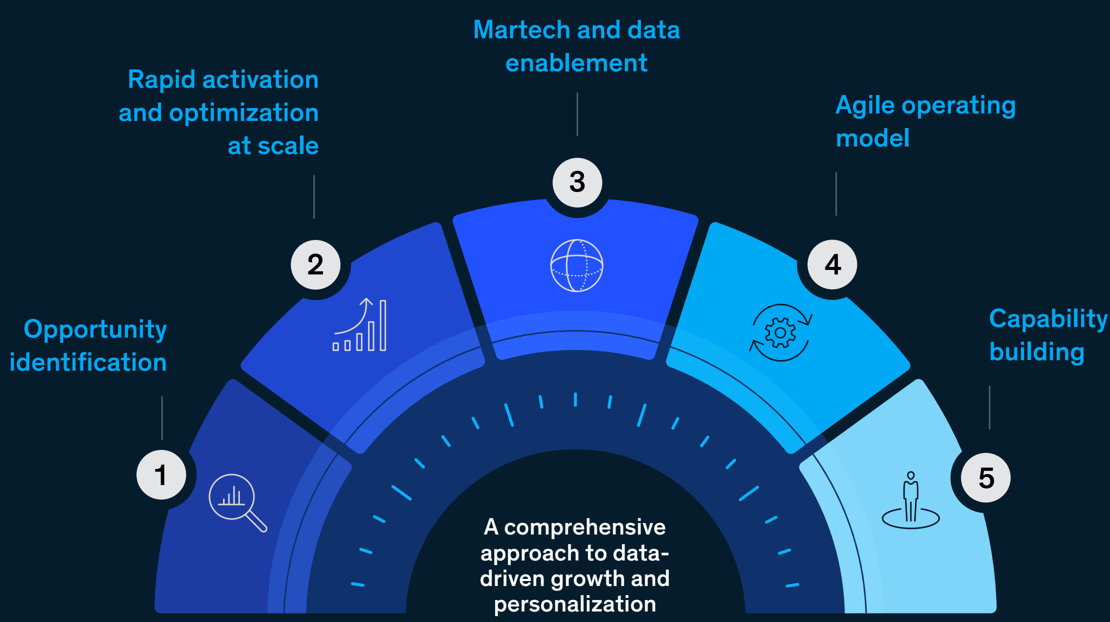
— *They invest in fit-for-purpose martech and data.* Rather than letting a "thousand flowers bloom," personalization leaders target a specific set of customer outcomes and use cases that support them. They align organizational resources around these use cases and work back from the desired outcomes to build the data and martech road map and identify the enablers and investments needed to deliver.

— *They commit to an agile operating model.* Businesses that succeed in scaling personalization create teams that cut across marketing, product, analytics, and technology, using a hub-and-spoke approach. Each hub owns specific elements of the personalization journey, with each spoke empowered to build underlying use cases. Together, these teams run hundreds of tests per year, enabled by advanced data analytics and test-and-learn techniques.

— T*hey invest in talent and training to refine capabilities.* Leaders bring a similarly data-driven approach to building their teams and organizational capabilities. They focus in on the skills needed to support personalization at scale (for instance, digital and e-commerce acumen, advanced analytics, product management, or performance marketing). Then they map these capabilities against their current talent base, using the results to inform hiring, training, and upskilling. This approach allows companies to anticipate the expertise and tools they need as their personalization program advances.

Exhibit 7

There are five ingredients in our CustomerOne approach.



1.

Opportunity identification

Granular growth across the customer life cycle, including where to focus and how to start

2.

Rapid activation and optimization at scale

AI-driven decisioning, dynamic content and measurement to enable activation across channels and touchpoints

3.

Martech and data enablement

Technical talent, partnershipsm and enablement across major platforms to power consumer-backed use cases

4.

Agile operating model

Rapid test & learn engine with the right roles, cross-functional talent, and ways of working to drive omnichannel impact (eg, across digital, physical, assisted channels)

5.

Capability building

Talent development to sustain impact over time (eg, digital acumen, agile, analytics skillsets)

Personalization is a force multiplier—and business necessity—one that more than 70 percent of consumers now consider a basic expectation. Organizations able to build and activate the capability at scale can put customer lifetime value on a new trajectory—driving double-digit revenue growth, superior retention, and richer, more nurturing long-term relationships.

Nidhi Arora is a consultant in McKinsey's San Francisco office, where **Wei Wei Liu** is an associate partner, and **Kelsey Robinson** and **Eli Stein** are partners; **Daniel Ensslen** is a consultant in the Boston office; **Lars Fiedler** is a partner in the Hamburg office; and **Gustavo Schüler** is a partner in the Southern California office.

Theme 4:

Harnessing the digital surge

McKinsey & Company

Marketing & Sales Practice

Five traps to avoid: The long game of DTC and e-commerce

Simply selling online is relatively easy. But unless you plan from day one to build a sustainable e-commerce business, you risk crippling your ability to scale over time.

This article was a collaborative effort by Karel Dörner, Dianne Esber, Jason Shangkuan, Bernardo Sichel, and Amy Tong, all with McKinsey's Marketing & Sales Practice.

September 2021

Key takeaways

— The pandemic has only accelerated consumer demand for the ability to buy online.

— Merely selling online is very different from building a sustainable e-commerce business.

— Companies need to avoid five traps when launching direct-to-consumer operations.

It happened so quickly it almost felt miraculous: companies around the world pivoted to e-commerce in response to the COVID-19 pandemic. Seemingly overnight, online ordering and delivery was available from restaurants and grocery stores, coffee shops, and traditional retailers. It was a triumph of business ingenuity as companies sought to keep their doors open in the face of an unforeseen challenge.

For many, it worked. E-commerce sales penetration in the United States more than doubled to about 35 percent in 2020 from around 16 percent the previous year, the equivalent of roughly ten years of growth within a few months.[1] Companies that successfully captured the business of consumers who were purchasing more online saw e-commerce climb to almost 50 percent of their overall revenue, a level expected to persist or increase as consumers continue to demand greater buying flexibility. This shift is expected to be durable: around 55 percent of Chinese consumers are likely to continue buying groceries online after the peak of the crisis.[2]

The challenge? Even if it felt as though *everyone* was buying *everything* online, large retailers were the primary beneficiaries, as they had invested in e-commerce capabilities for years and could therefore adapt quickly to the changed consumer behavior. Small and medium-size retailers (those with less than $5 billion in annual revenue) and brand manufacturers, such as consumer packaged goods and apparel companies, still realize a much smaller portion of revenue from e-commerce. These companies have a long way to go to build successful e-commerce businesses, and as parts of the world move toward the next normal, cracks are appearing in e-commerce operations that companies rushed to launch.

Getting e-commerce right

Investing in e-commerce can be costly, but those who do it well enjoy a significant return on investment. A recent survey of 800 executives revealed that companies got better revenue growth from launching a new business than they did from traditional growth efforts, such as new products and services.[3] The tricky part is execution: 30 percent of consumers who have a bad experience with a brand don't return, and that rises to more than 70 percent if consumers have three bad experiences.

At a time when brand loyalty remains shaky with 75 percent of consumers trying new digital

[1] "Five Fifty: The quickening," *McKinsey Quarterly*, July 2020, McKinsey.com.
[2] Antonio Achille, Caleb Balloch, Lambert Bu, Cherry Chen, Guang Chen, Lucille Chen, Will Enger, Johnny Ho, Xin Huang, Daniel Hui, Dymfke Kuijpers, Nick Leung, Lavonda Li, Joanna Mak, Joe Ngai, Felix Poh, David Pountney, Alex Sawaya, Steve Saxon , Jeongmin Seong, Sha Sha, Kay Tu, Jonathan Woetzel, Chenan Xia, Lei Xu, Hai Ye, Jackey Yu, Stefano Zerbi, Cherie Zhang, Jia Zhou, and Daniel Zipser, "Understanding Chinese Consumers: Growth Engine of the World," November 2020, McKinsey.com.
[3] Shaun Collins, Ralf Dreischmeier, Ari Libarikian, and Upasana Unni, "Why business building is the new priority for growth," *McKinsey Quarterly*, December 2020, McKinsey.com.

behaviors, it's critical from day one to think about how decisions will impact your ability to scale.[4] Companies trying to move fast to launch an e-commerce business or a minimum viable product (MVP) often make short-term decisions that hamper their ability to scale six to 12 months later. That's when it gets hard, and the right foundation becomes essential: only 24 percent of new businesses launched in the past ten years have become viable large-scale enterprises (see sidebar, "What great direct-to-consumer looks like").[5]

We've identified five short-term traps that often hamper companies' ability to successfully grow over the long term.

1. Leading with tech focus

Companies often take a sequential approach to building their e-commerce business, focusing first on technology and development while deferring focus and investment in areas such as operations and channel management.

A $2 billion consumer-products company launching its direct-to-consumer (DTC) business was laser-focused on its website, heavily investing in development and design to keep pace with the desired launch timeline. Indeed, successful site launch was a key success metric for its IT and DTC leaders. The site went live on schedule, but the DTC business constantly lacked inventory: some key stock-keeping units (SKUs) driving more than 15 percent of revenue had out-of-stock rates of more than 40 percent. The problem? Sales and operations leaders didn't have the same objectives and success metrics as the IT and DTC teams. Operations hadn't built the proper stock-management and planning processes needed to support the new business, and the company's sales teams allocated products to wholesale customers rather than DTC.

2. Building a directionless tech stack

Companies often architect and make technology, design, or ecosystem decisions for quick launch. But the wrong technology platform, architecture, or partners will create significant technical debt, hampering efforts to scale, and adding cost, complexity, and delays to unwind and rebuild.

A midsize European retailer with more than 500 retail stores selected a seemingly turnkey e-commerce partner to rapidly launch its online sales site. It worked—in the short term. But when the retailer sought to scale the business, it ran into significant challenges. One was high ongoing costs—since many turnkey e-commerce platforms are best designed and optimized for simpler businesses, the retailer's technology costs doubled as it sought to expand to multiple geographies and brands. Another was slow feature updates. Developers copied and pasted code as a shortcut for speed, but this created challenges when making updates or adding new features. Rather than changing code once, a change in one place had to be individually changed everywhere.

3. Underinvesting funds and capabilities

Companies often seek to mitigate the risks of launching e-commerce businesses by spending as little as possible, borrowing resources and talent from other parts of the organization and expecting an immediate ROI for every dollar spent.

A consumer-services company launching an e-commerce business took only a six-month view of the expected ROI, barely dedicating enough funding for launch. The problem? First, although it had hired an e-commerce leader, it relied heavily on personnel borrowed from other functions, such as IT and operations, for all other roles. At one point, only three of its 15 e-commerce employees were dedicated to and hired for that business, and it hadn't begun building a pipeline of candidates for other positions filled by borrowed resources. After launch, the company couldn't scale beyond its first market. Using borrowed resources had stalled needed recruiting, and the opportunity to hire and train new talent was lost when the borrowed employees returned to their primary responsibilities. Second, the company expected a positive return on

[4] "US consumer sentiment and behaviors during the coronavirus crisis," August 2021, McKinsey.com.
[5] Ibid.

advertising spend for any marketing efforts, leading the marketing team to take a conservative approach to acquiring traffic: it spent around 3 percent of revenue on digital marketing, compared with up to five times that amount allocated by other companies in start-up growth mode. After two months, site traffic for the company's e-commerce business had barely moved.

4. Learning the economics on the fly
Companies often don't fully understand what unit economics look like, and they make short-term decisions that stifle growth, or they implement a business model that needs to be redesigned and slows down forward momentum.

A large national food distributor building an e-commerce and DTC business believed it could deliver and manage its supply chain for e-commerce by leveraging the scale of its existing operations. Yet after launching and delivering to customers, it discovered that the existing operations model was inadequate to profitably scale the business. The company's warehouse network was optimized for B2B, not for fulfillment and shipping, and the cost of adding those services for e-commerce and DTC was equal to 20 percent of revenue, making it the primary driver of their unprofitability.

5. Building the new business too close to the core
Corporate business-building activities are often hampered by certain challenges associated with working in a legacy organization. In a survey of executives involved with corporate venture capital (CVC) incubators and accelerators, almost half of the respondents said internal policies had slowed the development of new businesses. Fewer than 10 percent said their companies had given start-ups full freedom to operate.

A leading consumer-products company struggled to launch its new digital business without the right digital talent. As a well-known consumer company, they had no problem finding candidates, but technical talent, such as developer and product managers, found the new business lacking in the advantages they perceived in start-ups. For example, they would be required to work at corporate locations, such as Austin, San Francisco, or New York, which were far away from where they lived. Additionally, the recruiting process took months due to chains of approval required for headcount and aligning schedules. This gave candidates used to fast-paced start-ups the impression that this was a company where they couldn't move fast.

What you can do to avoid these traps

If any of these traps sound like something your company might be doing today or could fall into, the good news is there are some key actions that can be taken to avoid them. Critical to each is keeping the customer experience at the forefront. Taking these actions without having the customer in mind is likely to have little or no impact.

Growth trap 1: Leading with tech focus
Make e-commerce a priority and tie performance goals to outcomes for all cross-functional leaders. If you're thinking about launching a DTC or e-commerce channel, prioritize that aspiration for all functional leaders, then design and build all elements of the business in parallel.

For example, before 2020, Nike set a goal of deriving 30 percent of total revenue from e-commerce sales by 2023. Nike hit that goal three years early but had set itself up for success years before. In 2017, Nike aligned objectives across the business to prioritize its DTC business setting a goal of three milestones, "2X Innovation, 2X Speed, 2X Direct."[6] Now, the company is on track to break 50 percent of total revenue from e-commerce.[7]

Growth trap 2: Building a directionless tech stack
Define the longer-term architecture and build your minimum viable product (MVP) as a stepping-stone toward the target state. An MVP is critical to prove business value and validate design decisions. Therefore, the MVP design and ultimate state should be based on target-state considerations such as desired customer journey, geographic and brand footprint, flexibility to add new features, and ROI.

[6] Mark Parker, "Letter to shareholders," Nike, July 20, 2017, nike.com.
[7] Lauren Thomas, "Nike's online business is booming – 'digital is here to stay,' CEO says," CNBC, September 23, 2020, cnbc.com.

What great direct-to-consumer looks like

At a leading consumer-products company in 2020, DTC revenue more than doubled to account for more than 25 percent of total revenue and the majority of the company's incremental growth. Yet this success didn't happen overnight. The company's online journey started in 2018 with a number of key decisions made at the outset that prepared it to scale its business in response to the rapid customer shift to online buying. Those decisions helped the company avoid the five traps that often hinder companies' DTC efforts, in the following ways:

— *Avoiding trap 1: Shifted leadership goals from top-line focus to a balance of sales and profit growth.* Previously, with performance incentives tied to sales growth, regional sales leaders focused their efforts on growing revenue with wholesale accounts. To spur greater focus on DTC, the company changed performance incentives to give equal weighting to both sales growth and profit growth. This new focus drove regional sales leaders to focus resources on DTC, since it was 25 percent more profitable than the wholesale channel. Local marketing, operations, and technology teams subsequently made decisions that supported growth for the DTC channel.

— *Avoiding trap 2: Replatformed and re-architected its technology platform specifically for DTC.* At the outset, the company aspired to scale DTC globally. But it wanted to ensure a consistent brand experience without sacrificing localized content and messaging. When selecting and designing its tech platform, the company ensured it could support the expected traffic and designed common site templates to be deployed globally. At the same time, it enabled local marketing teams to customize and control content for local markets.

— *Avoiding trap 3: Set marketing budgets based on revenue targets and performance.* To avoid multiple drawn-out approvals for marketing investment, the DTC business had permission to invest as long as it reached a minimum ROI for every dollar spent, with spending capped at a set percentage of target revenue. If it hit this cap without reaching ROI targets, the DTC team would then have to reconsider any additional funding requests. This up-front agreement freed it to move quickly, unencumbered by corporate approval processes.

— *Avoiding trap 4: Utilized A/B testing to understand profitability drivers.* The company had provided same-day delivery and home installation to DTC customers, assuming it was necessary to compete with retail channels. Yet A/B testing revealed it instead led to lower conversion. When the company switched to standard delivery and removed home installation, not only did the profitability increase (thanks to lower delivery costs) but conversion rate did too.

— *Avoiding trap 5: Separated DTC with its own P&L from the retail business.* Unlike the retail business—which relied on closing two or three strategic relationships—DTC adopted an agile continuous delivery model focused on deploying hundreds on small changes to acquire and convert customers. This resulted in building a deeper knowledge of customers and ability to drive greater customer LTV through the direct customer relationships.

For example, Williams-Sonoma's e-commerce revenue penetration rose to 70 percent in 2020 from 58 percent a year earlier, attributable in part to its investment in building a scalable, modern e-commerce platform. Williams-Sonoma comprises multiple brands beyond its namesake, such as a Pottery Barn, Pottery Barn Kids, and West Elm. Its single platform allows it to create a different look and feel across all properties while at the same time testing new capabilities that can quickly and readily scale across all.[8]

[8] Peter High, "How Williams-Sonoma Became The World's Largest Digital-First, Design-Led And Sustainable Home Retailer," *Forbes*, July 2021, forbes.com.

Growth trap 3: Underinvesting dollars and capabilities
Create a "learning buffer" in your budget. As a promising business starts to scale, it's important to acknowledge that there will be setbacks. They are a reality of building a business and necessary, in fact, to learning and progress. That reality needs to be reflected in budgets. A learning buffer doesn't mean providing the new business with infinite funding. The best enterprises release funding as the new business hits set targets. That money, however, needs to be ready to go to avoid endless rounds of approvals, which blunt the new business's momentum.

A US consumer-products company continuously invested in online marketing as long as the investment broke even. The DTC business aligned this with finance to continually allocate marketing dollars in six-month increments so long as it achieved this metric. This allowed it to learn and refine its campaigns and algorithms to the point that by the end of six months, the DTC business could predictably achieve a fivefold return on marketing spend.

Growth trap 4: Learning the economics on the fly
Understand the key drivers of growth and profitability through the lens of profit and loss. A deep understanding of unit economics can help identify where you need to invest, further determine where to build or partner, or define the right revenue model for a scalable, profitable business.

A leading consumer electronics company with more than $10 billion in revenue increased its e-commerce earnings before interest and tax (EBIT) by 50 percent through two strategic decisions: first, it outsourced its warehouses, and second, the company reinvested the savings into its technology platform to focus on customer experience and personalization. It realized it could not operate a supply-chain network as efficiently as much larger players, and outsourcing reduced its supply-chain costs by half. On the other hand, the company realized its DTC conversion rate lagged competitors, and focusing investments on personalization and marketing drove EBIT growth by increasing conversion rates even as traffic increased.

Growth trap 5: Building the new business too close to the core
Create physical virtual distance between the new e-commerce and core businesses. Physical separation allows companies to establish new centers to attract expertise and entrepreneurial talent who collaborate with more agile ways of working. Companies can also create virtual separation by minimizing obligations to the legacy features of the parent company such as giving freedom for financial pressure, from red tape, and to source talent.

In the United States, Walmart opened Silicon Valley offices to attract top tech and entrepreneurial talent to accelerate its technology and e-commerce ambitions. In 2014, Walmart employed approximately 1,000 tech employees, and today is one of the largest tech employers in Silicon Valley with over 10,000 software engineers, data scientists, and machine learning engineers. Walmart has taken these learnings to grow a tech community at its headquarters in Bentonville, Arkansas, and even influence its core DNA.

The desire to launch e-commerce capabilities rapidly is understandable—and important, given the changes in consumer behavior. But ensuring that decisions are considered carefully from day one is critical to building a foundation for long-term success.

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B2B commercial analytics: What outperformers do

B2B companies that successfully apply commercial analytics are uncommon—and more likely to achieve uncommon success. Outperformers share four behaviors.

by Warren Davis, Ryan Gavin, Sinem Hostetter, and Wilson McCrory

December 2021

Key takeaways

— Companies that effectively use analytics in service of marketing and sales performance are 1.5 more likely to achieve above-average growth rates than their peers.

— B2B companies historically lag behind their B2C counterparts in adopting and deploying commercial analytics, but the ones who engage with the tools already outperform their peers; their return on sales are up to five percentage points higher than that of their counterparts.

— B2B companies are increasingly ready to invest in—and execute on—analytics. They should learn from the outperformers.

If outsized growth is the holy grail, adept use of commercial analytics is one clear way to get there, fast. Our research shows that B2B companies that effectively harness analytics in service to marketing and sales performance are 1.5 times more likely to achieve above-average growth rates than their competitors.[1] Other B2B companies have taken notice.

Many business leaders seek to harness analytics to grow their businesses. But B2B companies have historically lagged behind their B2C counterparts in adopting and effectively employing commercial analytics. However, those that use the technology more effectively outperform their peers, using many techniques of B2C sales to engage prospects and customers and increase the lifetime value of each customer relationship (Exhibit 1). These outperformers also achieved up to five percentage points higher return on sales, a common measure of how efficiently companies convert sales into profits.

We have found that outperformers not only distinguish themselves by their methods, but by their consistency and clarity in strategizing for the challenges of the transition from the very beginning. Companies ready to invest in the pursuit of outsized growth would do well to take a page from the outperformers' playbook by investing in these four critical areas.

The hurdles of analytics

B2B outperformers succeed at translating commercial analytics into profitable growth even as many B2B sectors are under threat from B2C companies, such as e-commerce companies with more advanced and sometimes superior e-commerce and analytics capabilities that have begun to encroach on B2B territory by offering industrial supplies.

B2B companies and their leaders realize that analytics are important. In a 2021 McKinsey survey of more than 2,500 respondents in six countries and more than ten industries, 64 percent of B2B companies indicated that they expect to increase their spending on predictive analytics. But they tend to fall short when it comes to applying the right resources throughout the entire overhaul of their commercial operations.

The problems start at the beginning of the process, when many companies struggle to identify goals for their analytics programs, such as preventing churn or increasing cross-sells. As a result, while every company has significant volumes of data, many B2B companies lack the capabilities to translate data into relevant, usable insights that help them to sell more effectively by improving their understanding of their customers' experiences, needs, and triggers.

[1] Boudewijn Driedonks, Sinem Hostetter, and Ryan Paulowsky, "By the numbers: What drives sales-growth outperformance," April 2021, McKinsey.com.

Exhibit 1

Companies that are investing in their analytics are seeing much faster growth than their peers.

Companies that expect to increase spend on predictive analytics (most of any marketing and sales capability)

Companies that have strong analytics are 1.5x more likely to be faster growers than their peers

Companies that believe they are making effective use of analytics vs 43% just five years ago

Efforts to boost commercial performance also often fall flat if frontline sales teams do not buy into new sales-support tools or incorporate them into the regular habits and cadences of their work. In short, many companies fail to plan for and execute on the ways analytics will create end-to-end changes in their commercial operations.

Four behaviors for commercial analytics success

Our study of B2B outperformers' commercial analytics programs revealed four common behaviors. Before launching a program, they create internal agreement on the sources of commercial value for their organizations. From there, they assemble or develop the right analytics workforce. They facilitate the work of the analytics team by bringing together the right data tools to facilitate faster decision making and to foster capabilities and execution. Although many companies put similar efforts in place, the key to outperformance is effective, coordinated execution in all four areas.

Build consensus on sources of value

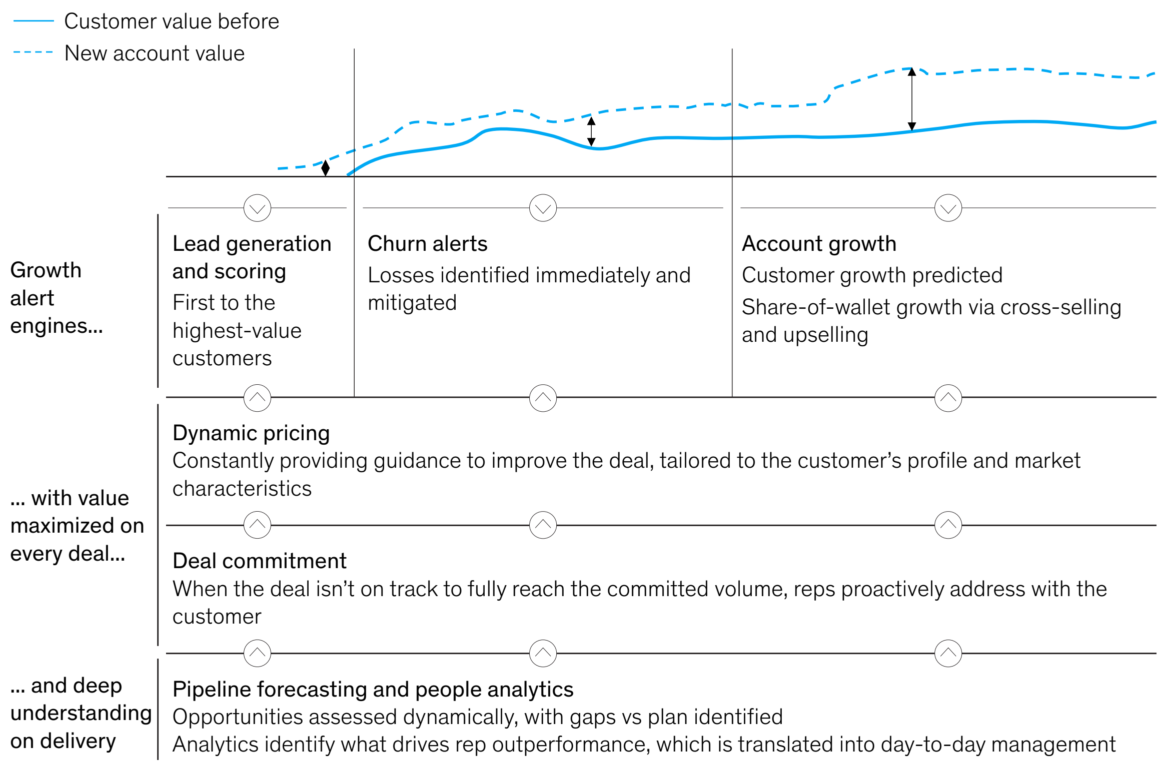
Analytics can do a lot if used effectively. But without agreement on what analytics to pursue, companies can waste resources and energy on programs that do not deliver value. Before embarking on a commercial analytics program, cross-functional teams should collaborate to figure out where the greatest value is, then work with commercial leaders to shift resources and effort to focus on those areas. Crucially, leadership should expect to iteratively improve their approach to analytics. For instance, not every use case, tool, or model is a good fit for every situation, but quick experimentation and decision making—in other words, failing quickly and investing in demonstrably viable use cases—can maximize learning and minimize waste.

A review of the customer lifecycle—acquisition, product-customer fit, pricing, and retention or reacquisition—can yield significant insight into the most important sources of value (Exhibit 2).

The most promising use cases can get sponsorship from at least one executive whose team can benefit from it relatively soon, can generate value quickly, and—particularly in larger companies—are clearly scalable. For example, a distributor realized that it had a significant churn problem. It lost customers who accounted for up to 30 percent of its sales every year, enough to offset its new-customer acquisition. The organization's leaders decided to invest in decreasing churn before addressing

Exhibit 2

Outperformers apply comprehensive tools and analytics across the customer lifecycle.



other issues. This focused application of analytics resulted in an additional $30 million of run rate (annualized revenue) in eight months.

Assemble the right analytics talent

Top analytics talent produces outsized returns: the best data scientists and engineers are ten to 50 times more productive than average performers.[2] As a result, analytics talent is in demand in almost every sector. However, B2B companies can attract and retain the right talent by making their value proposition as employers clear. This proposition will vary for each company. For instance, companies whose analytics functions are less mature might highlight the opportunity to build a high-performing analytics team. While not all analytical problems are glamorous, many data scientists and engineers are interested in gaining industry-specific knowledge. One energy and materials company discovered that the data scientists and data engineers it attracted were keen to learn more about the industry, so it provided opportunities for the analytics workforce to develop a sense of connection to the company and industry through bootcamps and workshops. Another conglomerate initially failed to attract candidates to a far-flung office, but the number of applications skyrocketed when it moved the analytics hub to a major city.

To build an analytics team, companies should begin by hiring an analytics leader who can anchor the function and attract other analytics talent. Senior academics and analytics leaders from major tech companies are good candidates.[3] The focus should

[2] Drew Hansen, "This LinkedIn data scientist suggests 10 ways to excel in her field," *Forbes*, Nov 29, 2016, forbes.com.
[3] For more on anchor hires, see Matthias Daub, Ranja Reda Kouba, Kate Smaje, and Anna Wiesinger, "How companies can win in the seven tech-talent battlegrounds," October 2020, McKinsey.com.

initially be on hiring the right people instead of filling as many roles as possible. In addition to data scientists, companies should recruit strong data engineers and analytics translators to build the data foundation.[4]

While most B2B companies have in-house recruiters, decision makers should not hesitate to engage outside recruiters for the sake of finding the right people in a timely manner. For instance, one logistics company worked with recruiters who were familiar with data and analytics and used automated assessments to cut the hiring time for data engineers from ten months to three weeks in one quarter.

Working in the same location is often helpful in building and reinforcing team cultures. Companies should therefore ensure that the analytics team has the structure needed to work in an agile way in the first few years, even if not everyone is co-located (Exhibit 3).[5]

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[4]For more on analytics translators, see Nicolaus Henke, Jordan Levine, and Paul McInerney, “Analytics translator: The new must-have role,” February 2018, McKinsey.com.

[5]For more on building an analytics team, see Gloria Macías-Lizaso Miranda, “Building an effective analytics organization,” October 2018, McKinsey.com; Matt Ariker, Tim McGuire, and Jesko Perrey, “Five roles you need on your big data team,” July 2013, McKinsey.com; and Oliver Fleming, Tim Fountaine, Nicolaus Henke, and Tamim Saleh, “Ten red flags signaling your analytics program will fail,” May 2018, McKinsey.com. For more on agile work in a hybrid or remote environment, see Quentin Jadoul, André Nascimento, Olli Salo, and Renato Willi, “Agility in the time of COVID-19: Changing your operating model in an age of turbulence,” November 2020, McKinsey.com.

Exhibit 3

Here’s how the investment in analytics comes together.

Front-end quoting tools and CRMs
- CRM systems
- Order entry & quoting tools
- Digital tools
- E-commerce

Reporting and analysis dashboards
- Performance dashboards
- Data visualization and analysis
- Microreports and notifications (email, text, app notifications)

Analytics-ingestion API

Algorithms

Growth accelerators
- Propensity to buy
- NPTB/bundling
- Micro-segmentation
- Lead prioritization
- Churn analytics

Margin accelerators
- Dynamic pricing
- Deal scoring
- Rules-based pricing
- Contract performance

Aftermarket and services attach
- Predictive maintenance
- Service attach prompter
- Warranty analytics

Data lake
- Transactional data
- Customer master
- Product master
- Market research
- Vendor master
- D&B data
- Features
- Sourcing data
- SPAs and special pricing
- Contract information
- Sales headcount and location
- Service calls and information

Data-ingestion layer
- Data cleansing
- Data engineering
- Data optimization
- Feature generation

Ingestion API

External data
- Total available market (TAM)
- External factors

Complex fragmented legacy enterprise resource planning (ERP) with sales and pricing data
- ERP 1
- ERP 2
- ERP 3
- ERP 4

Use flexible data architecture, algorithms, and tools

Effective data architecture, algorithms, and tools are already standard at companies that are successfully using analytics. The key is for companies just starting analytics work to move decisively with the data they have to begin gleaning insights as soon as possible and avoid the trap of sinking into a lengthy IT project.

For beginners, perfect is the enemy of the good. Almost all companies complain about their data quality. But in our experience, almost all companies also have good-enough internal data that can be immediately put to use in a minimum-viable-product version of a data lake. Companies typically only use only a small portion of their available data, but the new insights lie in the other 90 percent. Data such as inbound inquiries, on-time shipments, and call center notes can generate significant insights if they are properly linked. One organization had planned on a two-year data-lake project that would eventually support its work on alleviating global hunger. However, an initial analysis revealed that the organization really needed something that would support its initial set of analytics models. Readying the required data only took a month and allowed the preliminary models to run in 30 minutes at a cost of $2. In the meantime, the data-lake overhaul, an investment in infrastructure, proceeded in parallel.

Finally, any insights from analytics models should be paired with business judgment. In a cross-functional team, this input should come from a business-function leader who has direct responsibility for the commercial outcomes related to a customer, region, or group. This person should consult any other experts as needed. Having the voice of the business on the team can ensure that any insights are logical and ultimately understandable and actionable for the sales team.

Use change management to boost front-line execution

Analytics programs' ultimate test is whether they are accepted by front-line sales teams, which makes the difference between boosting the company's performance and having its efforts wither.

In our experience, even highly predictive models can be rejected by the front line if a tool they had not heard of until they were instructed to use it generates an incorrect recommendation. In those cases, the model's failure is often a reason for sales teams to abandon a model that they find no reason to trust. The remedy for this pitfall is to involve front-line teams in the development of analytics tools. This approach builds trust in the tool and yields insight into the needs of both front-line teams and their customers.

Once tools are ready, front-line leaders and high performers should model and champion their use to reinforce sales teams' knowledge of the tools' efficacy. One company gathered its sales managers for a two-day training summit each time it launched new analytics tools for use cases such as pricing, churn, and cross-selling. This methodical approach helped the company grow its earnings before interest, taxes, depreciation, and amortization (EBITDA) by more than 10 percent for several consecutive years.

Once tools are past the pilot stage, integrating them into the company's roster of standard tools with which reps are familiar make them more acceptable to the front line. Indeed, an integrated insights dashboard has an air of permanence compared with the spreadsheets and ad hoc dashboards commonly used during pilots.

However effective or beneficial new tools are, it may be difficult for the salesforce to form new habits, especially when old habits are comfortable. Weekly routines can help frontline reps integrate new analytics tools into their working cadence. One company implemented a set of weekly reviews designed to integrate analytics insights into the sales function's work. Another company rewards and praises its sales reps based on the frequency with which they use their analytics tools. The sales reps who consistently used the tools achieved better results over time, which accelerated the adoption of those tools.

Companies should also use insights to personalize rep-specific targets. For example, one company used pricing analytics to set specific price-increase targets for each rep. The reps didn't have to implement every new insight to hit their targets, so they retained a sense of control.

Finally, new insights tools can reveal opportunities for cross-functional collaborations. Insights often have implications for nonsales teams. For instance, one company that built a tool to analyze churn found that 50 percent of its open service issues remained unresolved, a significant failure that contributed to customer defections. In response, leaders organized weekly district reviews of the customers that most at risk of churn. Supply chain, sales, and customer service all participated in rectifying the situation. The use cases identified in the first six months were worth $20 million to $30 million.

The timely and effective adoption of commercial analytics tools and techniques offers B2B companies undeniable strategic advantages. By learning from the outperformers, others in the sector can improve their performance and even build defensible advantages.

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The big reset: Data-driven marketing in the next normal

Savvy marketers are rethinking their tech and data strategies to double down on precision marketing following COVID-19.

by Chase Bibby, Jonathan Gordon, Gustavo Schüler, and Eli Stein

March 2021

Between March and August 2020, one in five consumers switched brands, and seven in ten tried new digital shopping channels. The retail sector experienced ten years of growth in digital penetration in a matter of months. But the resulting surge in data has not provided marketers with substantially better understanding of their customers, because their companies' outdated data modeling isn't able to capture these shifts with the necessary granularity and speed.

Rather than using the data to try to better target customers and tailor messages, many marketers have reverted to mass communications and promotions. As one CMO told us, "I've largely retreated to mass marketing instead of data-driven marketing because customer behavior is changing so fast I can't trust my historical data and models."

But some marketers are accepting the data for the bounty it is and, rather than stepping back from precision marketing, are doubling down. A consumer-goods company, for example, anticipated that sales of beauty products would spike as communities eased out of lockdown. Marketing teams tracked reopenings on a county basis, using epidemiological statistics, municipal reporting, and traffic data to determine where to focus their media spend. These tactics drove a double-digit increase in sales.

Similar insights helped a business service provider get a jump on another emerging trend. Business registration and employment data showed that small healthcare providers in major metropolitan areas were growing at a much faster rate than other small and midsize businesses. Armed with that insight, the company created healthcare-specific product bundles and has launched paid media ads to target those businesses and locales. These moves, combined with other, similarly data-driven campaigns, are poised to increase sales in a core product by more than 10 percent.

Companies that hone their precision marketing in these ways can drive significant customer acquisition during periods of convulsive change. Capturing this opportunity, however, will require brands to update their modeling—from pulling in new sorts of data to retraining algorithms—in order to both keep pace with changing needs and expectations as well as anticipate shifts in customer behavior.

New challenges to account for

Precision-marketing models are trained to recognize and draw inferences from behavioral patterns. An algorithm might learn, for instance, that customers who make more than two visits to a store's website within a two-week period are 30 percent more likely to make a purchase. Such indicators can trigger tailored offers to convert browsers into buyers, allowing marketers to direct their acquisition efforts and spend toward the most profitable segments.

But buyer behavior has changed significantly since the pandemic began, rendering the relationship rules baked into many existing data models invalid. Externalities that once seemed incidental, such as customer mobility, now have outsize importance. Is visitation down because customers can't get to the store or because they no longer wish to shop there? Many marketing teams simply don't know. A Fortune 100 CMO said, "The indicators for the new opportunities we face are not contained in our own data."

In addition, while patterns exist, they are harder to discern—and even when discerned, they can feel ephemeral, such as communities opening up only to lock down again. To tease out salient behavioral indicators in time to act on them, marketers need continually refreshed data from a variety of sources and at a far more detailed level—looking as deeply as the city-block level in some cases. However, many companies tend to rely on internally derived customer data, using modeling tools that were not built to handle large volumes of data.

Two other issues compound the challenges facing marketers. McKinsey data show that marketing budgets have been slashed for most companies, with six of ten marketers reporting major cuts. "My budget has evaporated," said one senior marketer. "We have barely enough to execute our 'must do' marketing, let alone experiment with new tactics."

The other issue is the rapid, large-scale shift to remote working. Data-driven marketing works best in agile settings, where teams can test and iterate in sprints. But with nearly two-thirds of employees working from home, marketing leaders have found it difficult to create an effective cadence. “In the past we used to go all in on marketing opportunities by having a command-center-like war room,” said one Fortune 100 CMO, “but with everyone working remotely, we haven’t been able to react as fast as we have in the past.”

How to make modeling more precise when everything else is in flux

While other organizations may have retreated to mass marketing, those that upgrade their modeling can be far more effective in generating revenue. Here’s what they need to do:

Tap new (and better) data. Precision marketing is only as good as the data behind it. New models with old data are still likely to provide inaccurate results. To hone their insights, leaders in the new normal will take a wide-angle approach to data collection by gathering not only behavioral trends and location-based insights but also third-party analytics on their business, customers, and competitors to complement their in-house customer data. Companies starting this journey are finding the most value in incorporating epidemiological data from government sources and customer-mobility and sales data from third-party providers into their models. Companies that extend their data gathering in these ways can identify upticks in demand and where new customers are coming from, as well as assess which customers in their existing base have increased spending and where lapsed customers have gone.

Before it updated its modeling approach, for example, a retail chain could only tell how many customers it was gaining or losing. The company then decided to pull in cell-phone data to scan changes in their competitors’ net traffic. That analysis showed that many of the customers they were gaining during the pandemic were coming from more expensive, specialty players, while those they were losing were heading to cheaper, larger-format players. On the basis of this information, the retailer transformed its onboard and churn-prevention campaigns. They sent emails advertising higher-end offerings to customers transitioning from specialty stores while touting bargain-oriented products to value-oriented customers at risk of churn.

In another example, a business-services provider tapped into new third-party data sources that identify key moments in the small-business life cycle. In one such effort, the provider aggregated data sources that indicated, with a lag of only one day, when new companies were being launched during the turbulence of COVID-19. Their salespeople reached out immediately with products and messages tailored to the needs of newly formed companies, such as systems tools. These collective efforts increased sales productivity by more than 25 percent.

Robust data can also allow companies to generate better competitor insights. By comparing third-party assortment, sales, and promotional data to their own figures, for instance, marketers can evaluate the strength of different value propositions and see which elements resonate with different groups of customers. They can then provide these groups with tailored messaging, content, and offers.

Invest in tech that learns at scale. The increased uncertainty in the new normal requires marketers to get better at testing and faster at reacting. A more agile operating model is a key element in this, but it is also increasingly necessary to work with technology that learns at scale. This requires developing technology capabilities that can read and interpret signals of consumer intent and consumer responses to marketing messages and then feed them back into the marketing engine so it can learn what works and what doesn’t.

Marketers who really push the limits are using artificial intelligence (AI) to monitor campaigns and interrogate responses at a detailed level, to learn not only what works and what doesn’t but for which segments, at what times, and over which channels—and then to adjust their strategy based on those insights. Deriving those specific insights using standard analytics might take the average marketing organization several days. But AI-enabled monitoring can do this in minutes, sometimes seconds.

For example, a consumer services company launched consumer-retention campaigns as communities came out of lockdown. Their customary analytics, which could only assess campaigns in the aggregate, was only marginally effective. However, the organization piloted a new AI engine that could look deeply enough to evaluate responses at the core base statistical area (CBSA), which showed that the campaign was highly effective in specific niches with similar economic and epidemiological profiles. This AI engine will identify how the campaign's performance patterns evolve, allowing marketers to configure the system so that nightly AI-driven analytics feed directly into the campaign's targeting logic. This and similar campaigns are a crucial element in a broader data-driven marketing program that has helped the company increase its rate of testing more than fivefold.

Two keys to success: Investing savings and being agile

In order to derive value from these upgraded models, two actions are crucial:

Generate savings to invest in tech. While some companies are simply cutting budgets and retrenching across the board, others are finding it can be more beneficial to reduce spend in unproductive areas and reallocate the savings—as much as 10 to 20 percent of the overall budget, in some cases—into analytics. This requires a thorough but fast reevaluation of all marketing spend to see how the COVID-19 environment has affected ROI. Event sponsorships, traditional TV advertising, and programmatic display based on outdated terms are just a few areas where marketing performance is likely to have shifted significantly. One apparel retailer, for instance, found that the effectiveness of paid search has diminished sharply during the crisis, while social-media activity has been far more productive. Marketing leaders can free additional investment by also reusing and repurposing existing assets. The savings can then be redeployed to fund data-driven growth programs.

Deploy agile marketing in a remote setting. Agile practices are effective in allowing marketing teams to test consumer behaviors and react quickly to changes. While traditionally, agile teams were thought to perform best when working in the same place, the exigencies of the pandemic have required this approach to be rewired for remote work. Leading companies are converting physical war rooms into virtual ones, creating additional points of contact to support adherence to agile protocols (such as sprint check-ins by video, for example) and the use of collaboration tools. The best companies have gone a step further by integrating some of their vendor teams into their remote practices, including working with IT to create shared tools and compatibility guidelines to account for vendors' different technologies.

Companies that get it right are showing impressive results. For example, a North American telco created a virtual war room that featured online work spaces and digital scrum boards for task and performance management. Sprint planning was conducted using rounds of progressive voting, with each vote spurring active debates on the merits of each test idea. They also held ceremonies using video stand-ups. The virtual war room not only improved test results but helped the team launch tests more than three times faster than their traditional, in-person setup.

Budgeting and operating practices need to be continually reviewed to support this remote agile model. Instead of quarterly or semi-annual planning sessions, marketing leaders should assess performance monthly to ensure that funding and resources are aligned with the biggest opportunities.

Organizations that prioritize their precision-marketing efforts can turn the COVID-19 crisis into a time of transformation. By capturing new data, searching for new behavioral relationships, and enabling rapid experimentation, marketers can seize granular growth opportunities and enter the recovery with significantly greater ROI and resilience.

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December 2021

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