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MMS - III (common)

Roll No.:
No. of Pages : 12; including this 13
No of questions 4
Maximum Marks: 50
Duration : 3 Hrs.

PM 03

Questions:

Please go through the case titled Procter & Gamble. Answer the following questions:

a. **Case facts (15 marks)**
b. **Case Analysis (15 marks)**
c. **Problem areas (05 marks)**
d. **Solutions based on resources and capabilities (15 marks)**

case | 10

Procter & Gamble: Organization 2005 and Beyond

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ICFAI Knowledge Center

In September 1998 Procter & Gamble (P&G) announced a corporate restructuring program called Organization 2005. The set of far-reaching initiatives involved comprehensive changes in organizational structure, work processes, and culture to make employees stretch themselves and speed up innovation. Organization 2005 also sought to leverage P&G's global presence. The program was intended to boost sales and profits by introducing new products, closing plants, and eliminating jobs. Spearheaded by Durk Jager, who became P&G's CEO in 1999, this initiative was to be a six-year, $1.9 billion effort. Jager believed that rapid restructuring was necessary to create new growth opportunities for P&G. While launching the program he expressed his optimism:

> Success is defined first and foremost in terms of growth. Unless a company grows at an acceptable rate—year in, year out—it can't sustain its organization. Success also means growing profitably. Otherwise, it can't produce the resources and capability to invest, take risks, or seize new opportunities. The program we lay out here today is designed to deliver that growth, at a consistently higher level. Just come back in a couple of years and take a look. I believe that the best way to accelerate growth is to innovate bigger and move faster consistently and across the entire company.[1]

Jager indicated that the cultural changes he planned to introduce would create an environment that produced bolder goals and plans, bigger innovations and greater speed. As part of the exercise, Jager redesigned the reward system to strengthen the link between executive compensation and results.

BUSINESS SEGMENTS

P&G was one of the best-known consumer goods companies in the world. For the year ended June 30, 2002, P&G reported revenues of $40.2 billion. The company was in the Fortune Global 50 list. It owned several well-known brands that were sold in over 140 countries to nearly 5 billion consumers (see Exhibit 1). P&G had operations in North America, Europe, the Middle East, Africa, Asia, and Latin America. Exhibits 2 and 3 highlight the company's recent financial performance.

P&G had five main business segments: Fabric and Home Care; Baby, Feminine, and Family Care; Beauty Care; Health Care; and Food and Beverage:

- Fabric and Homecare was the most important segment, accounting for nearly a third of P&G's total sales. The division dealt with cleaning products for clothes, surfaces, and dishes. Key brands included Bold and Tide laundry detergents, and Cascade dishwasher powder.
- The Baby, Feminine, and Family Care segment produced tissues and paper towels, feminine protection products, diapers, and baby wipes. Well-known brands in this category were Bounty paper towels and Tampax tampons.
- Beauty Care products included deodorants such as Old Spice, Sure, Cover Girl, and Max Factor cos-

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[1] "Organization 2005 Drive for Accelerated Growth Enters Next Phase," P&G press release, June 9, 1999.

exhibit 1 **P&G Brands around the World**

Region	Shaving Products	Skin Care	Cleansing	Cosmetics
United States	Noxema Old Spice	Noxema Olay	Camay Ivory Moisture Care Olay Safeguard Zest	Cover Girl Max Factor Olay
Latin America	Old Spice	Noxema Olay	Camay Ivory Olay Old Spice Safeguard Zest	Cover Girl Max Factor
Europe, Middle East, Africa	Old Spice	Noxema Olay Roge Cavailles	Infasil Ivory Safeguard Zest	Cover Girl Ellen Betrix Max Factor
Asia		Olay	Camay Ivory Muse Safeguard Zest	Cover Girl Max Factor SK-II

Source: Collected from various sources.

metics. The segment also produced fragrances, shaving products, and shampoos such as the Head & Shoulders and Pantene brands.

- Health Care products ranged from prescription drugs to toothpastes such as Crest, over-the-counter remedies such as Pepto-Bismol, and pet foods.
- Food and Beverage produced cooking oil, Pringles snacks, and peanut butter. It also offered drinks like Sunny Delight and Folgers coffee.

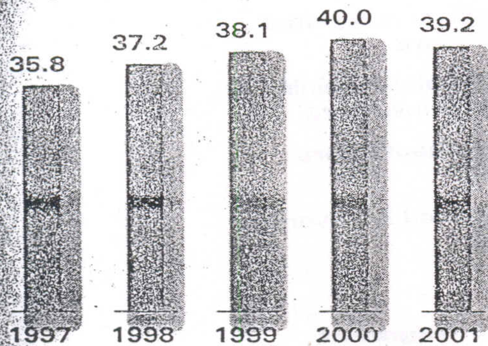
Exhibits 4 and 5 show recent earnings growth of these five groups, and Exhibit 6 presents each group's sales, profitability, and major brands.

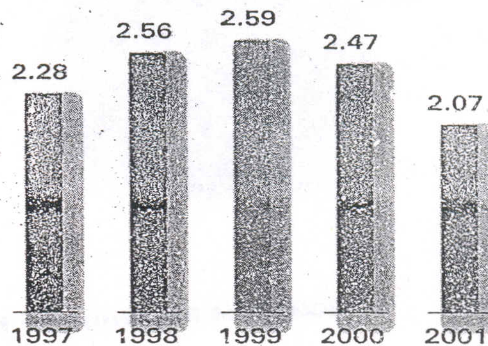
CORPORATE HISTORY

William Procter and James Gamble founded P&G as a partnership in 1837 in Cincinnati, Ohio, by merging Procter's candle-making company with Gamble's soap business. The company grew to $1 million in sales by 1859. P&G's initial foray into branding was the Moon and Stars, a trademark that appeared on all company products starting in the early 1860s. In 1887, P&G became one of the first companies in the United States to offer a profit-sharing program for its employees. In 1924, P&G was one of the first companies to create a market research department to study consumer preferences and behavior. The company's marketing organization and brand management system began to evolve in the early 1930s. In 1933, P&G's Oxydol soap powder sponsored a serial radio program.

P&G had been a late globalizer. But after World War II, P&G began its international expansion in earnest. In 1948, it established an overseas division while setting up its first Latin American subsidiary in Mexico. P&G entered Europe in 1954, Saudi Arabia in 1961, and Japan in 1973. By 1980, P&G was operating in 23 countries and reporting over $10 billion in annual sales. By the mid-1990s over half of the company's sales came from outside the United States. As its global expansion progressed, P&G continued to modify its

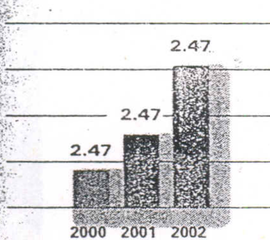
Exhibit 2 Summary of P&G's Financial Performance, 1997–2001

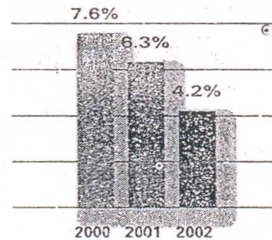


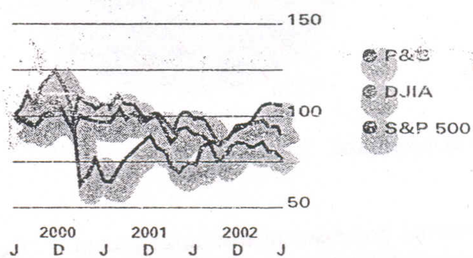


Source: P&G annual report, 2002.

Exhibit 3 P&G's Performance in 2002

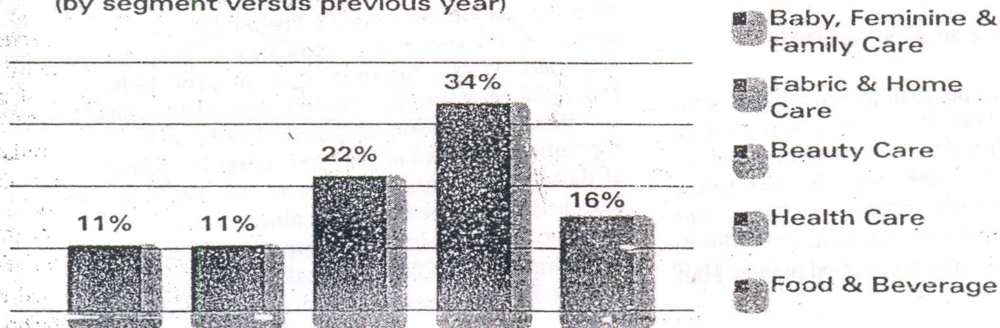






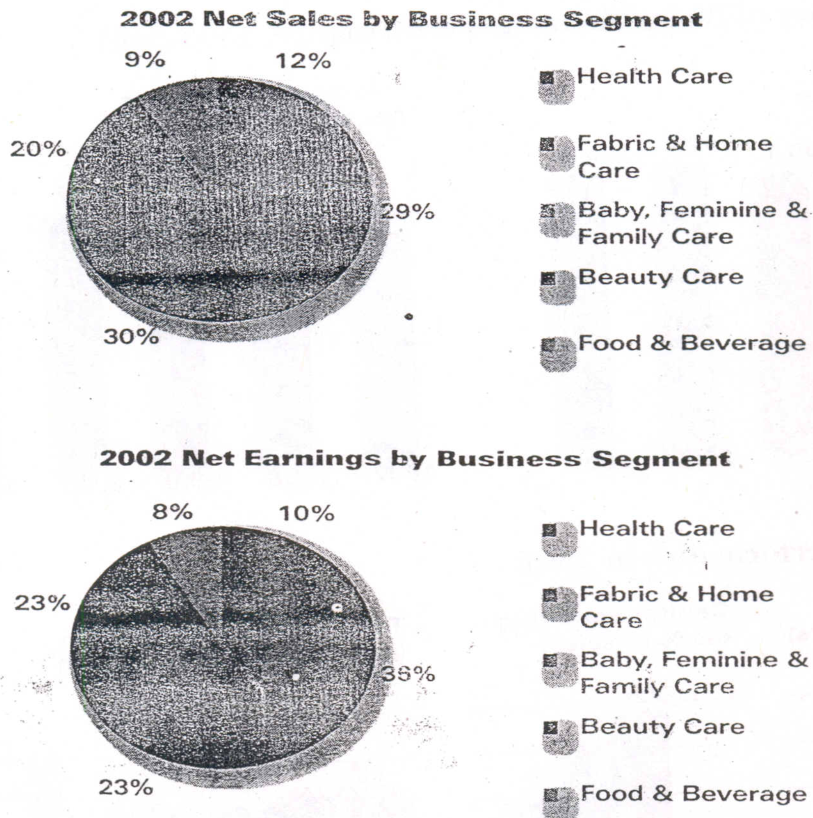
Source: P&G annual report, 2002.

Exhibit 4 P&G's Earnings Growth from Different Segments



Source: P&G annual report, 2002.

exhibit 5 P&G Net Sales and Net Earnings by Segment



Source: P&G annual report, 2002.

structure and internal processes to maximize global leverage. Various initiatives were launched to facilitate exchange of knowledge and best practices across the company.

Exhibits 7 and 8 provide additional background on the company.

ORGANIZATION 2005

In 1998, P&G's earnings per share (EPS) fell below the 14 to 15 percent that Wall Street had gotten used to. Revenue growth, which had varied between 1.4 and 5.5 percent between 1995 and 1999, was also well below P&G's internal target of 7 percent. Revenue growth was slowing down, particularly in developed markets, due to the maturity of the company's established brands. Half the brands were generating the bulk of the growth while the rest were lagging behind. In a retail world increasingly populated by private-label goods, P&G's premium products were having difficulty competing. More nimble competitors were beating P&G to the market by launching new products, by executing marketing plans better, and by increasing innovation speeds. There was also speculation that P&G's profitability was being eroded by the increasing dominance of retailers like Wal-Mart. With a turnover of about $160 billion in 1999, Wal-Mart was a particularly formidable player.

P&G's innovation track record had also been disappointing. New brands had the ability to add billions of dollars in incremental revenue, but P&G had not launched a major new brand in almost a decade.

The need to reinvigorate growth led P&G to conceive Organization 2005. The goal of the program was to improve P&G's competitive position and generate oper-

exhibit 6 **P&G's Business Lineup in 2002**

Baby, Feminine, and Family Care	
Sales*	$12 billion (flat)
Profits†	$1.9 billion (up 10%)
$Billion brands	Always, Pampers, Charmin, Bounty
New developments	Brand extensions Bounty napkins, Charmin Fresh Mates, and Tampax Compak were all performing well. Ailing feminine brands moved to Beauty Care in July 2002.
Fabric and Home Care	
Sales*	$11.8 billion (up 1%)
Profits†	$2.7 billion (up 12%)
$Billion brands	Tide, Ariel, Downy
New developments	Swiffer WetJet revolutionized cleaning in 2000 with disposable mop-and-cleanser-in-one. New scents like Tide Clean Breeze and Downy Clean Breeze helped freshen old brands.
Beauty Care	
Sales*	$8 billion (up 10%)
Profits†	$1.6 billion (up 13%)
$Billion brands	Pantene
New developments	Hugo Boss fragrance sales grew 47% in latest quarter. Ohm by Olay, P&G's first line of body care products, arrived in July 2002. Sales of Olay were likely to exceed $1 billion in 2003.
Health and Oral Care	
Sales*	$5 billion (up 14%)
Profits†	$742 million (up 27%)
$Billion brands	Crest, Iams
New developments	Acquired in 1999, Iams pet food sales tripled with new products like Eukanuba Dental Diet (using Crest know-how). Heartburn drug Prilosec is going o-t-c this year, pending FDA approval.
Food and Beverage	
Sales*	$3.9 billion (down 5%)
Profits†	$596 million (up 9%)
$Billion brands	Folgers, Pringles
New developments	The company dumped Crisco and Jif but was trying to save Sunny Delight. A bright spot was tortilla chips, with sales up 33% since November 2001 following the introduction of Pringles sibling Torengos.

*Sales: Estimated for fiscal year ending June 30, 2002.

†Profits: Pretax estimate for fiscal 2002.

Source: Luisa Kroll, "A Fresh Face," *Forbes,* July 8, 2002.

exhibit 7 P&G's Simplification Drive in the 1990s

Standardizing	Product formulas and packages
Reducing trade promotions	Fewer discounts and rebates
Easing up on coupons	Issuing fewer coupons
Getting rid of marginal brands and cutting product lines	Cutting extra sizes, flavors and other variants to make it easier for customers to find what they were looking for
Reapplying strategies that work	Extending successful strategies to other parts of the world.

Source: A. V. Vedpuriswar, *The Global CEO: Lessons from the World's Leading Corporations* (New Delhi: Vision Books, 2001)

exhibit 8 P&G: Chronology of Recent Events

September 9, 1998	P&G taps Durk Jager as CEO
June 9, 1999	P&G says it will lay off 15,000 workers as part of Organization 2005 program
July 29, 1999	P&G posts fiscal fourth-quarter profits well below those of the prior year
January 19, 2000	Warner-Lambert, American Home Products disclose they are in merger talks with P&G
January 23, 2000	P&G investors sell stock, causing a 10% drop in the share price
January 25, 2000	Stock price falls more than $2 after the company warns of lower-than-expected third-quarter results
March 7, 2000	P&G warns that it expects third-quarter profits to be down 10% to 11% from a year ago.

ating efficiencies through more ambitious goals, nurturing greater innovation, and reducing time-to-market. This was to be accomplished by substantially redesigning the company's organizational structure, work processes, culture, and pay structures.

P&G estimated that Organization 2005 would accelerate annual sales growth to 6–8 percent and annual earnings growth to 13–15 percent.

Organization 2005 envisaged the transformation of P&G's organizational structure from one based on geography to one based on global product lines. The program had five key elements:

1. *Global business units (GBUs):* P&G moved from four business units based on geographical regions to seven GBUs based on global product lines. By putting the responsibility for strategy and profit on brands, instead of geographic regions, P&G hoped to spur greater innovation and speed.
2. *Market development organizations (MDOs):* P&G established eight MDOs whose objective was to tailor global marketing programs to local markets.
3. *Global business services (GBS):* Overhead functions such as human resources, accounting, order management, and information technology were consolidated from separate geographic regions to one corporate organization—the GBS—that would serve all GBUs.
4. *Corporate functions:* Most of the corporate staff were transferred to one of the new business units.
5. *Company culture:* P&G redesigned reward systems and training programs to improve result orientation among employees.

Organization 2005 involved substantial costs. Of the approximately $1.9 billion in costs, approximately $400 million were planned for 1999, approximately $1.0 billion over the next two fiscal years, and the balance during fiscal years 2002–2004. However, these costs were expected to be more than offset by savings from the program. The company expected to increase its after-tax profits by approximately $600–$700 million annually by fiscal year 2003–04 and $900 million by fiscal 2004. P&G would eliminate 10,000 positions through fiscal 2001, with a further 5,000 cuts after 2001. Approximately 42 percent of the total workforce reduction would occur in Europe, the Middle East, and Africa; 29 percent in North America; 16 percent in Latin America; and 13 percent in Asia.

Despite the substantial retrenchment, Durk Jager remained confident that employee morale would not be

exhibit 9 **Organization 2005: The Costs of Restructuring, 2001–2003 (in millions)**

	Years Ended June 30		
	2002	2001	2000
Separations	$393	$ 341	$153
Accelerated depreciation	135	276	386
Asset write-downs	208	731	64
Other	222	502	211
Total (before tax)	958	1,850	814
Total (after tax)	706	1,475	688

Source: P&G annual report, 2002.

exhibit 10 **Organization 2005 Program Impact**

	Total	Fiscal Years 1998, 1999–2000, 2001	Fiscal Years 2001, 2002–2003, 2004
Estimated costs (after-tax)	$1.9 billion	$1.4 billion	$0.5 billion
Estimated job impact	15,000	10,000	5,000

Estimated Job Impact by Item

	Product Supply	GBS	Other
Job impact	6,700	3,900	4,400

Estimated Job Impact by Region

	Job Impact	Expressed as %
Europe, Middle East, Africa	6,250	42
North America	4,300	29
Latin America	2,450	16
Asia	2,000	13
Total	15,000	100%

Source: P&G annual report, 1999.

affected. He believed that Organization 2005 was about accelerating growth, not cutting jobs:

> These job reductions are principally an outgrowth of changes, such as standardizing global manufacturing platforms, to drive innovation and faster speed to market, as always, we have considered these decisions very carefully with deep concern for the impact on our people. We would carry out the changes with maximum respect and attention to the welfare and future of our employees.[2]

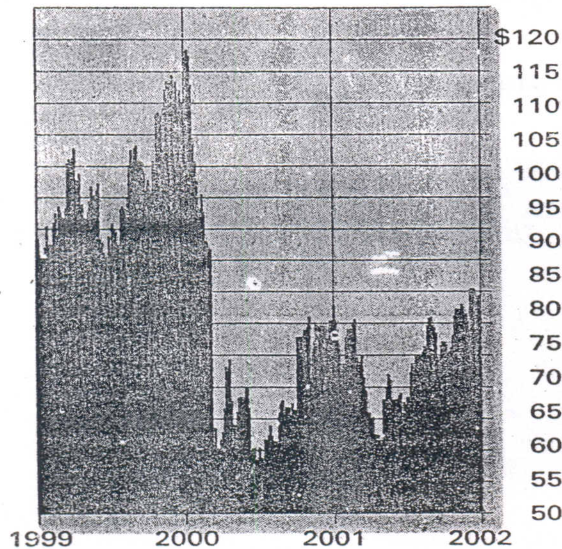
P&G announced it would make full use of normal attrition and retirements, hiring reductions, relocations, job retraining, and voluntary separations to help reduce the number of potential involuntary separations. In cases of involuntary separations, P&G would offer employees financial assistance to help them in their new careers. Exhibits 9 and 10 provide additional information on P&G's Organization 2005 initiative.

JAGER'S RESIGNATION

Soon after it was introduced, Organization 2005 ran into various problems. After reaching $117 per share in

[2] Ibid.

exhibit 11 **Procter & Gamble's Share Price, 1999–2002**



Source: www.aol.com.

January 2000, P&G's stock price fell below $90 per share in February. On March 7, 2000, P&G warned that its earnings would drop by 10 to 11 percent rather than rise 7 to 9 percent as previously expected. Among the reasons P&G cited for the drop in earnings were higher raw materials costs, lower realization, and increasing competition from many generic brands that produced cheaper versions of many of its core products. The news sent the company's stock to its lowest level since the mid-1990s. The stock price plunged to less than $60 per share, wiping out $40 billion in market value in one day (see Exhibit 11). Then in April 2000, P&G posted an 18 percent decline in third-quarter profit, its first decline in eight years. It also announced that fourth-quarter results would fall short of estimates. Jager accepted responsibility for the company's problems and resigned. But he maintained:

> I am proud of the vision we set out to achieve with Organization 2005, and we've made important progress. It's unfortunate our progress in stepping up top-line sales growth resulted in earnings disappointments.[3]

Analysts speculated on the reasons behind Jager's failure. It was said Jager had tried to put too much pressure on P&G managers to bring products to market faster. Major moves such as the dual acquisition of Warner-Lambert and American Home Products had turned out to be futile—none improved P&G's performance. Jager's exhortations also did not fit well with P&G's cautious corporate culture. His plan had been too aggressive. He had introduced new products recklessly in the hope of finding the next billion-dollar product. He had also decided arbitrarily that P&G would sell its products under the same name all around the world—so in Germany, the name of P&G's dishwashing liquid suddenly changed from Fairy to Dawn, the name under which it sold in the United States; but since Dawn was unknown in Germany, sales plummeted.

There had also been problems related to people. Managers had become critical of Jager's confrontational style. As employees felt they were being pushed, there was significant disenchantment. In Europe, about 2,000 people were suddenly transferred to Geneva. About 200 employees were asked to relocate from various parts of Asia to Singapore. Besides transfers, the program had also led to various behavioral problems. As a result of the Organization 2005 program, some food and beverage managers, based in Cincinnati, were asked to report to a president in Caracas, Venezuela. Managers in the laundry and household cleaning business reported to Brussels.

ORGANIZATION 2005 UNDER LAFLEY

Alan George Lafley, a 23-year P&G veteran, replaced Jager as president and CEO in mid-2000 when the company's stock price was $57. Lafley announced he would improve operations and profitability and rebuild the management team. The heads of P&G's operating businesses and corporate functions hailed from 13 different countries. The new faces included Deb Henretta, head of global baby care; Jim Stengel, global marketing officer; and Fabrizio Freda, head of the global snacks business. Overall, the average age of the Global Leadership Council (GLC) was only 49, compared to 54 three years earlier (see Exhibit 12). Unlike Jager, who focused on taking new initiatives in underdeveloped markets, Lafley decided to concentrate more on big countries and big products. He decided to increase sales of Tide and Pampers in Western Europe before

[3] "P&G CEO Quits Amid Woes," *CNN Money*, June 8, 2000.

Exhibit 12 Procter & Gamble's Global Leadership Council, June 1999 and June 2002

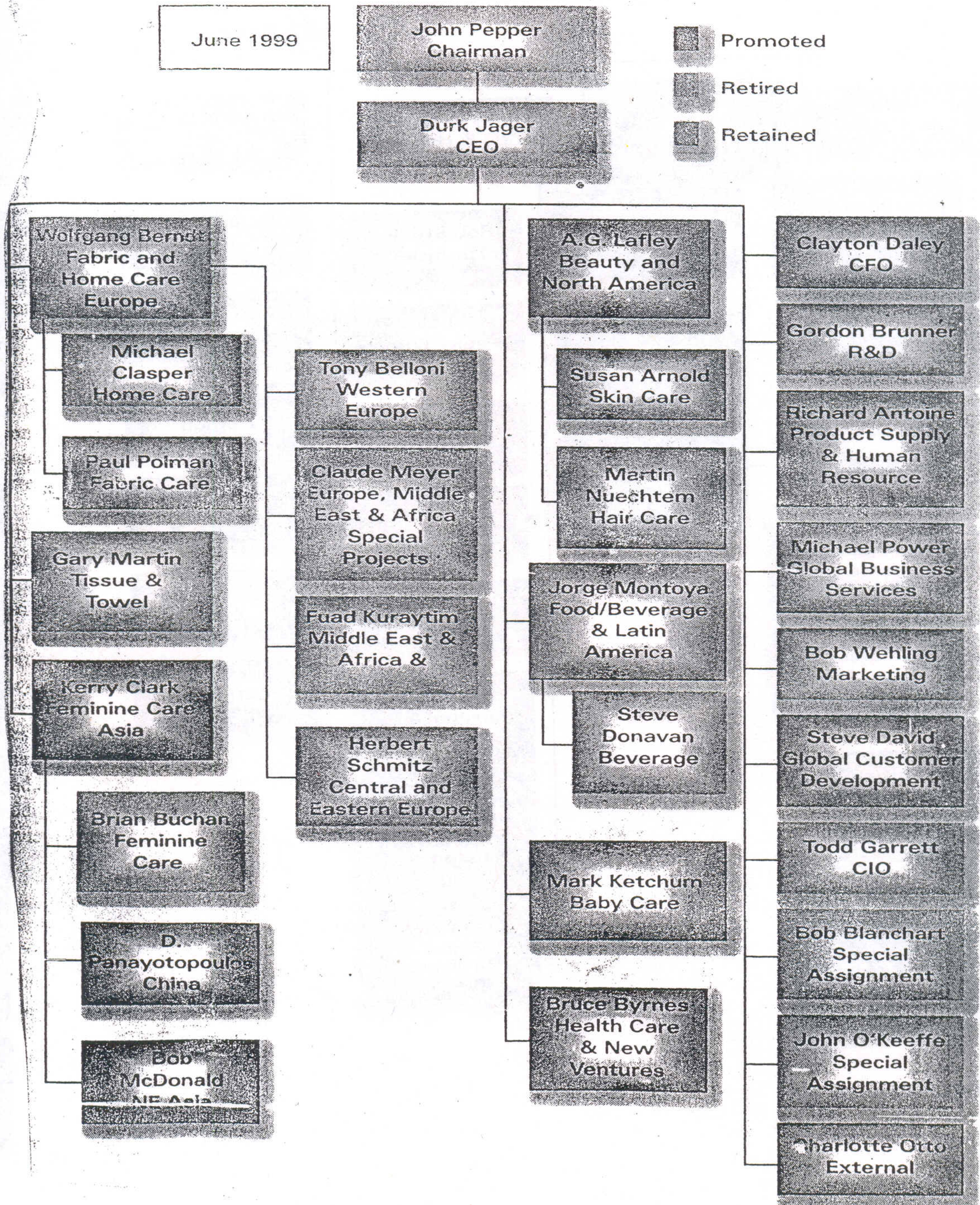
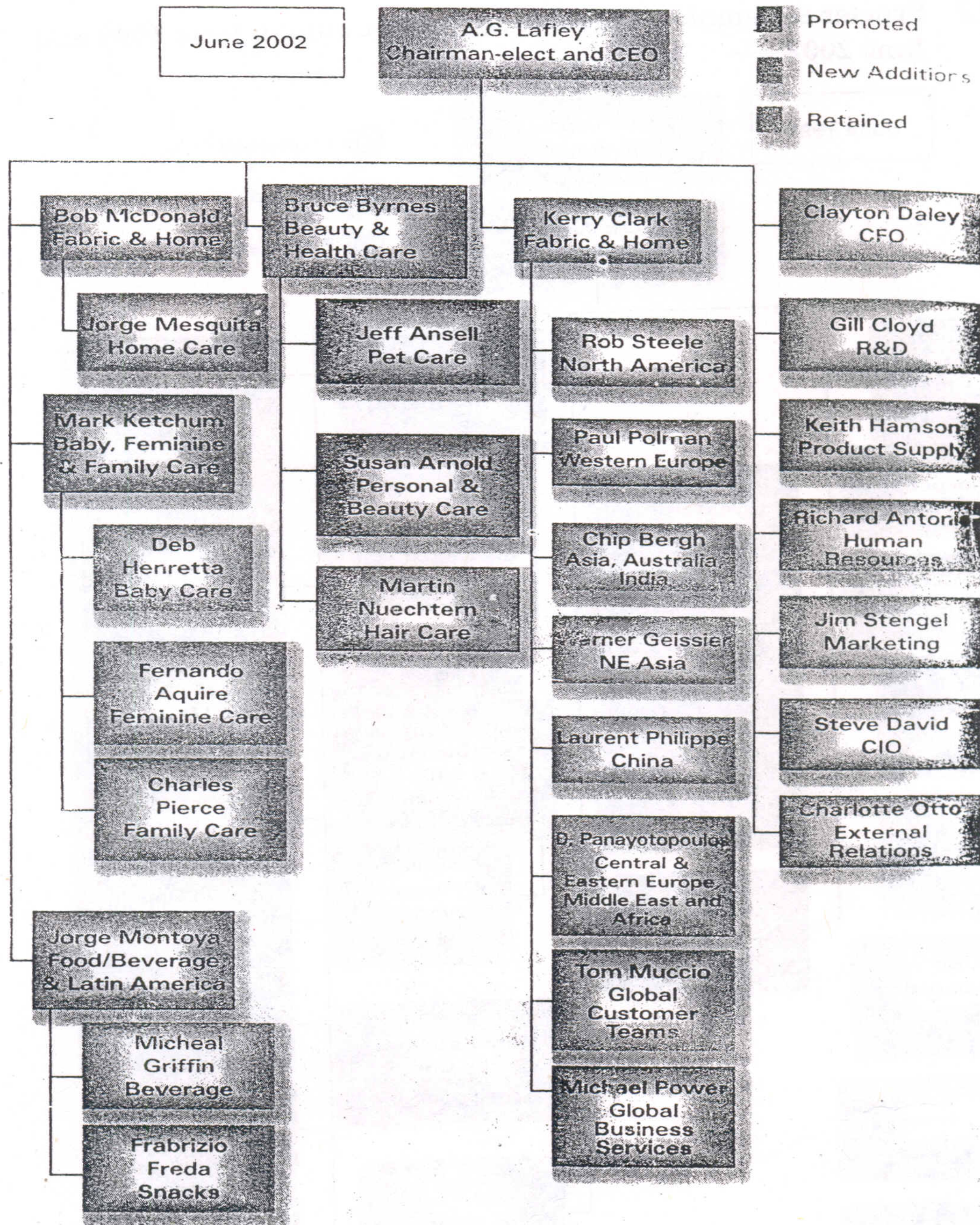


exhibit 12 (concluded)



Source: The Cincinnati Enquirer.

developing new products in Poland. The new CEO gave top priority to P&G's best-selling brands, which generated over $1 billion in sales. He announced they would get the bulk of P&G's resources, manpower, and financial backing.

Lafley also announced plans to improve the company's competitiveness and revitalize long-term growth through initiatives that seemed to be an expansion and acceleration of Organization 2005. This would be achieved by streamlining P&G's cost structure by further reducing overhead and manufacturing costs. The company expected savings on this count to be approximately $600–$700 million annually by fiscal year 2003–04. These savings would be in addition to those projected in the original Organization 2005 program. During 2000, Lafley reduced staffing by about 9,600 jobs worldwide, or 9 percent of P&G's workforce. About 40 percent of these cuts were in the United States, and about 60 percent were overseas. Two-thirds of the reductions came from nonmanufacturing functions across all levels of the company. In manufacturing functions, reductions came as a result of both plant closures and rationalization.

P&G also completed the remaining 7,800 separations that were part of the Organization 2005 restructuring announced in 1999. The combination of separations from the new program and remaining separations from the Organization 2005 program totaled 17,400. The company anticipated that part of the workforce reduction would have to be made through involuntary separations, but it intended to minimize that number. The company also continued to review its businesses and new investments with the goal of achieving sharper focus on its core businesses. While no decisions had been reached, the company believed it could incur additional restructuring costs as a result of this strategic review. Lafley said:

> The cost benefits of strengthened competitiveness and improved productivity are significant, but this is not just a cost-cutting program. No one ever cost-saves their way to sustainable growth. We will invest these savings in getting our consumer value and pricing right, continuing to invest in innovation on core businesses and the most promising new businesses, and continuing to provide strong marketing and sales support for our brands. All of these actions are necessary to deliver P&G's long-term financial goals.[4]

To boost growth, Lafley introduced several new products. Big brands like Tampax (tampons) rolled out new extensions in 2002. P&G started shipping its new Ohm by Olay line of body care products, which was the company's first skin care foray and which used natural products like ginger and jasmine, and also included new technologies such as body mist. Research-oriented units like P&G Pharmaceuticals continued to invest in new products. Sales of the unit's flagship brand, the Actonel osteoporosis drug, approached $400 million in 2002. In baby care, Pampers rolled out its Baby Stages line in Europe and North America. In laundry, Tide and Downy were offered in different fragrances.

Lafley singled out progress in oral care, baby care, and dish care businesses as one of the best outcomes of the restructuring initiatives. All these businesses had struggled and lost market share in the 1990s but posted sales and market share gains in 2002. P&G's fabric and home care business posted 9 percent sales growth in 2002 on unexpectedly strong gains in cases of brands such as Cheer, which recently had been offered in reduced pack size and price to combat a similar move by rival Unilever's Wisk. Sales in P&G's baby and family care businesses grew by 5 percent despite increasing competition from players like Kimberly-Clark. In 2002 the company dropped numerous brands—including Jif, Crisco, and Clearasil—that did not fit with its global strategy. By early 2003 P&G had finished reviewing its portfolio of brands. The sales growth of 6 percent in 2003 had been the biggest gain since 1996. Another accomplishment for Lafley was enabling Crest to return as the number one oral care brand in the United States, a position it had lost to Colgate in 1998.

Lafley believed that a key enabler for Organization 2005 was information technology (IT). The company's IT spending reached $1 billion in 2002 and continued to increase. Organization 2005 incorporated several IT initiatives, including collaborative technology to facilitate planning and marketing, business-to-consumer e-commerce, Web-enabling P&G's supply chain, and a data standards and data warehouse project that delivered timely data to desktops worldwide. The company decentralized its 3,600-person IT department so that 97 percent of those employees now worked in P&G's individual product, market, and business teams or were part of global business services, which supported shared services

[4] "Procter & Gamble Announces Next Step in Overall Plan to Restore Competitiveness and Growth," P&G press release, March 22, 2001.

such as infrastructure to P&G units. The remaining 3 percent worked in corporate IT. Lafley said, "I have made a lot of symbolic, very physical changes so people understand we are in the business of leading change."[5]

THE FUTURE

P&G expected to conclude its Organization 2005 initiative by June 2003. After the ouster of Jager, Lafley had shifted the focus from new initiatives to advancing the market share of big brands in developed markets. Lafley believed that, overall, Organization 2005 had brought much-needed discipline to P&G's global marketing efforts. But he felt a lot of work remained in convincing people that the program had a broad application. Lafley believed that P&G could innovate and cut costs while growing profits by double-digit margins every year. But Lafley realized the same basic question that had prompted Jager to start Organization 2005 still remained: With already-dominant market positions in mature markets, how much more growth could P&G really generate? With company's stock price trading in the $80–$95 range throughout most of 2002, what more could be done to boost the company's performance prospects?

[5]A. G. Lafley, "The Best and the Worst Managers," *Business Week*, Special Report, January 11, 2003.

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