

# Three Steps for Developing Consumer Goods Premiumization Strategies

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**In today's inflationary environment, companies are trying to maintain margins and stand out in crowded markets after resorting to price increases to sustain their performance. However, consumers have reached limits and are demanding more in return for higher prices. As Dirk Van de Put, Chairman and CEO of Mondelez International, said at the 2023 Consumer Goods Forum's Global Summit: "I'm worried about where consumers are going to find themselves after another round of price increases and lingering inflation." The reality is organizations cannot continue to increase prices without offering added value.**

One approach to this dilemma that has gained significant attention is premiumization, which is the process of elevating the value of a product or service so you can command a higher price. According to *The New York Times*, premiumization is a hot topic in the business world, with the term being mentioned nearly 60 times in corporate earnings calls and investor meetings earlier this year. By implementing a well-executed premiumization strategy, companies can unlock opportunities to mitigate the effects of inflation.



To maximize the potential benefits of a premiumization initiative, consumer goods companies should consider three fundamental steps. First, companies can benefit from aligning on a standard definition of premiumization. Next, they should adopt a customer-centric, and not a product-centric, approach to their strategy. And, last, they should develop a comprehensive understanding of the unique characteristics of their product portfolio, which will help drive the strategy they adopt. Below we explore these steps with insights from industry examples.

## **Align on a Common Definition of Premiumization**

One of the first pitfalls organizations experience in seeking to make their portfolio more premium is first not aligning on the definition of the strategy. It is not simply a pricing strategy. Nor does it mean that your company must sell its products in the ultra-premium segment of a market. Instead, products fall on a spectrum that goes from recognizable mass premium brands like Heineken and Starbucks to luxury items such as Chanel and Dom Perignon.

Premiumization is the act of capturing a higher price for a product that is justified by an increase in perceived value from the consumer's point of view. The higher price is a consequence of premiumization. This can be accomplished in three ways: by launching or acquiring a new premium product; by repositioning a mass market product up the spectrum; or by improving certain characteristics of an existing product to increase its perceived value (see Exhibit 1).

## Exhibit 1: Methods of Premiumization

### Launch:

In 2015, Danone launched Oikos Triple Zero, a Greek-style yogurt with zero added sugars, artificial sweeteners, and zero fat, to cater to health-conscious consumers seeking premium protein-rich options.

### Reposition:

In 2019, Dunkin' Donuts renamed itself as Dunkin' and simplified and modernized its image with a focus on bright colors and new matte designs in addition to upgrading and emphasizing premium espresso drinks and food.

### Repackage

In 2009, Coca-Cola introduced Coke Mini and it has become a popular size option for consumers looking for 'a small pleasure' that comes in a more portable container.

Consumers are willing to absorb an increase in price up to a certain threshold, after which they will demand more value for what they are paying. To convince consumers that a product or service is indeed premium, companies need to address the following two elements:

- 1. Product Characteristics:** The product and packaging must meet quality standards expected in the targeted premium segment. This will vary based on the product category and where it falls on the premium spectrum. Characteristics are often seen as more premium when the quality of ingredients improves, or the formulation and sourcing is more bespoke. For example, in 2020, Ferrero altered the packaging and improved ingredients for its U.S. candy bar Baby Ruth, which led to a 25% increase in sales.

- 2. Enablers and Drivers:** Premiumization efforts often fall short if the branding and sales channels don't match the product's perceived value. The marketing and branding of products give life to the product characteristics, and the sales channels further strengthen this perception. For instance, Sanpellegrino SpA, the Italian mineral water producer owned by Nestle, targeted the global hotel and food service industry in the early 2000s, developing a presence and building its reputation as a premium water for dining, which simultaneously bolstered retail sales.



By leveraging these essential elements, organizations can differentiate their offerings and establish a compelling value proposition that justifies a premium price point to the consumer, building what we call a house of premiumization (see Exhibit 2). Developing a shared understanding of the strategy across an organization is crucial to its success. It enables teams to set appropriate expectations, focus on improving the right components, and understand where value can be created. Without this common understanding and definition of premiumization, organizations will either overshoot by launching ultra-premium products that overserve market needs or undershoot by launching several subpar premiumization efforts that do not meet the mark.

**Exhibit 2: House of Premiumization**



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**Key Questions to Consider:**

- Have we attempted premiumization in the past? What were some of the lessons?
- Do we have a common understanding of the components of premiumization, such as product characteristics, enablers, and drivers?
- How does a premiumization effort fit into our current strategy?

**Take a Customer-Centric Approach**

Companies often try to make their products premium without understanding the market’s unmet needs and the “jobs to be done,” which is the principle that people buy products and services to get jobs done. They often overshoot on quality or packaging and end up failing to fulfill the customer needs.

An example of a company that understood consumer willingness to adopt new premium products is Procter & Gamble. In 2012, the P&G saw that customer desire to have a seamless laundry experience was not being fulfilled. It introduced Tide Pods as a convenient laundry

detergent, with each pod containing the right amount of cleaner in a convenient dissolvable pouch. This innovation, coupled with a targeted marketing campaign, allowed P&G to charge a premium for an enhanced value proposition. Today, Tide Pods are one of the most popular products on the market, underscoring the success of P&G's premiumization strategy.

Another good example of a company taking a customer-centric approach to premiumization is L'Oréal and its Kiehl's apothecary skincare brand acquisition in 2000. From its beginnings, Kiehl's understood the customer job to be done of wanting to feel confident about the safety and quality of the products they put on their skin; Kiehl's was one of the first skincare companies to list ingredients on their products, before it was required. Today, Kiehl's has successfully expanded its premium strategy, highlighting its heritage, unique formulations, and natural ingredients. The minimalist packaging, personalized consultations, and a focus on customer service in upscale retail locations contributed to Kiehl's premium positioning. The brand has experienced significant growth and expanded its presence globally, showcasing the effectiveness of L'Oréal's premiumization strategy.

To have a successful premiumization strategy, companies must gain insights into customer needs and their willingness to pay if these needs are met. This can provide a comprehensive perspective on the customer's most valued product characteristics and enablers that can enhance the perceived value of a product.

#### **Key Questions to Consider:**

- Are today's solutions adequately answering consumer needs?
- What "jobs" do the current offerings of the competition meet?
- Is there an opportunity in the market to premiumize? Have we seen others try premiumization in this space? How fragmented is the market?

## **Understand Your Company's Portfolio to Unlock its Premiumization Potential**

With a clear understanding of the key components that form a portfolio, companies are better equipped to select the optimal path to premiumization. Some may choose to develop products internally by creating a new brand, or market them under existing brand names. Others may opt to acquire new brands to meet the unmet jobs to be done of their target market.

The decision to acquire or build new brands should be driven by the realization that the existing portfolio does not effectively address the market's need. The Italian multinational Ferrero is an example of a company that understands its portfolio's ability to produce paths to premiumization strategies.

Between 2020 and 2023, Ferrero conducted a series of premiumization efforts using its existing brands. For instance, it leveraged the popularity of the chocolate and hazelnut spread Nutella to create new sub-categories, “Nutella B-ready” and “Nutella Biscuits.” It also revitalized two of its North American candy bar brands – Butterfinger and Baby Ruth – which were perceived as stale, upgrading their packaging and enhancing ingredient quality.

When Ferrero sought to venture into ice cream, a new market segment, it made a strategic choice to explore external opportunities instead of building a brand in-house. In 2023, the company acquired Wells Enterprises, manufacturer of Halo Top, a low-calorie alternative ice cream product. This purchase allowed Ferrero to expand its product offerings and cater to a broader consumer base, tapping into the growing demand for healthier product options.

Ferrero’s understanding of its portfolio’s strengths and weaknesses enabled it to maximize its premiumization efforts and demonstrates why having deep understanding of your portfolio is essential for selecting the optimal path to a successful strategy.

### **Key Questions to Consider:**

- **Quality product.** Does the customer value the current quality of the product? Can the perceived level of quality be enhanced?
- **Customer needs.** Is the product perceived as unique by its customers? Does the product fulfill a similar job to be done as a competitor’s offering?
- **Branding.** Does a premiumization strategy align with the brand image? Can the brand be further enhanced?
- **Pricing.** At what pricing segment is the product currently positioned? Is it realistic to aim for the next higher pricing segment for a new product?

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In conclusion, it’s crucial for consumer goods companies to understand that premiumization can be an effective strategy to counter inflationary pressures, one that delivers greater perceived value to customers while driving long-term growth. Companies can ensure this strategy is successful by first agreeing on a common definition of what it means. It is also important that they take a customer-centric, and not product-centric, approach to their strategy, putting the customer needs foremost. Last, they must have a clear understanding of how their portfolio of products works so they can develop a path to premiumization. By addressing these considerations, and fully comprehending the strategies available to them, firms can develop a premiumization strategy that succeeds.

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