Action Items: Keys to Success and Competitive Challenges for Fragrance Manufacturers of All Sizes

Part 3 of 3: Benchmarking the fragrance industry—conclusions and recommendations[a]

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In 2011, students at the Samuel Curtis Johnson Graduate School of Management at Cornell University, in conjunction with Marcum LLP, a public accounting and advisory services firm, conducted a survey of the fragrance industry in the United States. The following is the third and final part in a series of articles published in *Perfumer & Flavorist* magazine in which data, analyses and conclusions are shared. The Cornell student authors conducted this survey independently; subsequent analysis is the product of their collaboration with Kevin McGann, a partner at Marcum LLP and its fragrance industry practice leader.

The three-part series resulting from this research has examined collected data by size of company (based on revenue) and respondents' rates of growth over five years, and will now offer the authors' conclusions based on answers to three industry-specific questions:

- What drives growth?
- What are the key competitive challenges?
- Where are the growth opportunities?

Survey Methodology

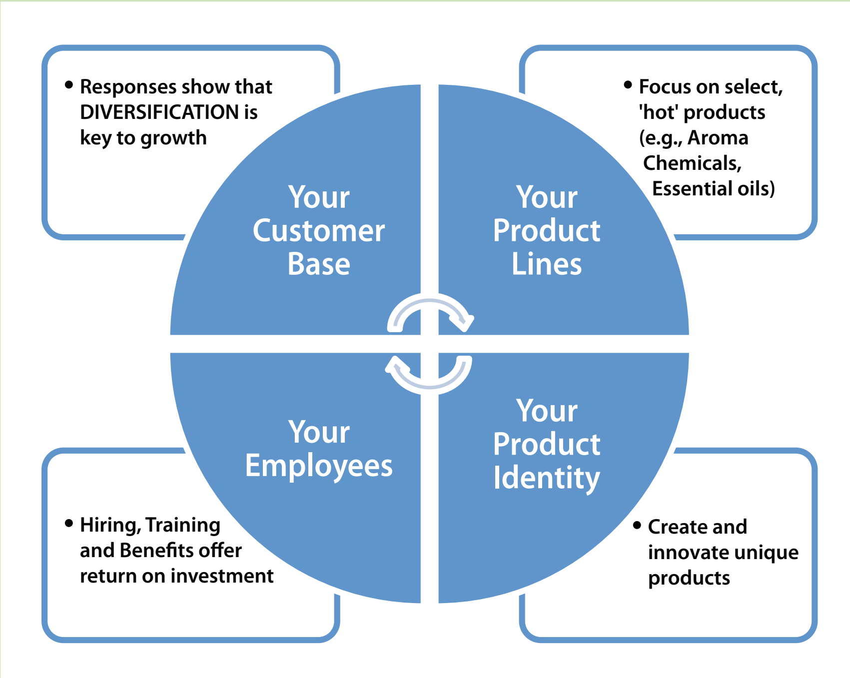
The survey construction was shaped via qualitative research with industry experts. Those that took the survey were offered modest incentives. The data discussed in the article comprises feedback from 70 companies. This total was achieved after the elimination of bad data (e.g., participants that took fewer than 15 minutes to fill in the survey or skipped vital information such as revenue or number of employees).

The four key elements for growth in the current fragrance industry environment: customer base, product lines, employees and product identity.

Size and Growth Rate

Based on the responses in the 2011 survey and the analysis provided in the first two parts of this series, the time has arrived to answer the three key questions posed from

The keys to growth in today's fragrance industry are customer base, product lines, employees and product identity **F-1**



[a] Part 1 in this series, "One Size Doesn't Fit All: Varying Factors of Success in Small-, Medium- and Large-sized Fragrance Manufacturers," appeared on page 50 of the August 2011 issue of *Perfumer & Flavorist* magazine; part 2 in this series, "Overachievers and Underachievers: What it Takes to Beat the Industry Average," appeared on page 58 of the October 2011 issue of *Perfumer & Flavorist* magazine; *www.perfumerflavorist.com/magazine/pastissues/*.

the start. The series has examined which companies are growing and how they are making it happen. From this the author has distilled four key elements for growth in the current fragrance industry environment, illustrated in **F-1**: customer base, product lines, employees and product identity.

Driving Growth

Customer base: As established in the research and enumerated in the second article in this series, the Marcum/Cornell survey shows that high-growth companies rely on a larger customer base than slow-growth companies (high-growth have, on average, 20 revenue-generating customers; low-growth companies have 10). If high-growth companies are twice as diversified as low-growth companies, it stands to reason that the diversification of the customer base must be a top priority for a successful company. The Marcum/Cornell study found a direct correlation between companies exhibiting above-average growth (greater than 6%) and greater customer-based diversification. According to the survey, the winning principle here is "think big," or at least "think bigger" when it comes to customer base.

Product lines: Staying on the cutting edge is a key factor to a company's success in any industry. According to the Marcum/Cornell survey, tapping into market trends and embracing contemporary product lines is key to driving revenue stream. In particular, divining which scents and/or flavors will be the next "it" item in a particular market segment is a knack worth developing and investing in (R&D and human capital come to mind).

Based on survey results, a focus on aroma chemicals and essential oils proved to be a differentiator among companies with high growth; this is an area to watch in the 12 months to come. Specifically, both high- and low-growth respondents indicated that these two product segments represented a major percentage of their sales. In fact, that percentage of sales was, on average, twice as high for the high-growth group companies (high-growth respondents indicated that 20% of their revenue came from this product line while low-growth respondents indicated a 10% revenue share from the same product).

Product identity: In any sector of the business world, management struggles with the balance of value, innovation and profitable margin. The Marcum/Cornell survey endeavored to discover where its participants place their company along that spectrum. While conversations in the marketplace and in mainstream advertising tend to be value-driven, the survey found that the companies which most closely identified with the term "value" had a majority presence in the low-growth category. Seventy-nine percent of respondents who found themselves in the high-growth category described their product as "innovative;" 71% would use the word "unique."

When identifying and branding one's product, internally or externally, the survey results clearly show that

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high growth is linked with at least the perception of innovation. This will have further ramifications when looking at dollars and cents subjects such as percentage of budget devoted to R&D and investments in human capital.

Human capital: As cited in the previous two articles of this series, addressing the human capital needs of a company, in the general sense, is another key differentiator between successful companies and those that struggle. For example, the largest of the respondents dedicate a larger portion of their overall budget toward the acquisition of key talent in key roles. Likewise, those companies defined by their high rate of growth offer better incentives and benefits (they are two and a half times more likely to offer 401(k)s and twice as likely to offer defined benefit plans).

This final element of growth and success boils down to where a company spends its money. The most successful companies participating in this survey, as defined as large and fast-growing, prioritize the happiness of their employees equal to any other expenditure in their budgets.

Overcoming Competitive Challenges

Although the keys to success are shared here, one doesn't wish to paint too rosy a picture. The path to success is challenging in different ways to companies of different sizes. Without exhibiting caution to the following discoveries, based on the Marcum/Cornell survey data, both large and small companies will find they have a tough row to sow.

As defined in the survey, smaller and larger companies must approach revenue success in different ways. Smaller companies must resist the urge to seek immediate returns on all of their dollars and dedicate a higher percentage of their resources to R&D. The temptation to move product is great among those who seek success but, as noted earlier, innovation and unique market offerings are the real secret when it comes to driving revenue growth.

Larger companies have a different battle to fight—one of scale. Their size offers certain advantages over those smaller companies, to be sure. They have more resources to build larger, better compensated sales organizations, which have been defined as a key element of success. They also have added significant automation to their manufacturing process, enabling them to produce product at lower cost and thus be more price competitive. However, because they reduced profit margins along with market costs, large companies are affected by an increase in commodity prices to a much greater extent compared to their smaller competitors. Additionally, the large company group identified in the Marcum/Cornell survey typically deals with unionized labor (e.g., unionized labor constitutes 10–12% for large, 0% for smaller), which tends to be a more costly staffing scenario.

When the survey respondents are looked at as a whole and their challenges are compared better or worse, the larger companies come out ahead of the smaller companies based on their ability and track record of acquiring those smaller companies when they become a challenge. The upward mobility of a small company could be hampered by the appetite for mergers and acquisitions that currently exists in the largest of these respondents.

Next Steps

The author and researchers of these articles, Marcum LLP and the Samuel Curtis Johnson Graduate School of Management at Cornell University want to thank all of the participants in this inaugural survey as well as the publishers of *Perfumist & Flavorist* magazine. The author and researchers are pleased to announce that these organizations will be continuing this survey as an annual benchmark tool and a predictive weather vane for trends and products to come.

To participate in next year's survey, please contact Kevin McGann at kevin.mcgann@marcumllp.com. The author and researchers will be actively looking for your contributions to content and questions of the 2012 Marcum LLP/ the Samuel Curtis Johnson Graduate School of Management at Cornell University survey.

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