

## US Future Consumer Index 9: How inflationary pressures have brought consumers' pricing worries to a head



In the ninth edition of the index, we dig deeper into the consumer impact of one of today's most significant market dynamics: inflation.

Inflation is at its highest level in the US in 40 years. The push and pull of pent-up demand and constrained supply and labor have fueled a combustion of price. Consumer goods and retail companies were already feeling the squeeze from increased input costs for everything from energy and transportation to raw materials and commodities. As these input costs increase, so does price inflation, only to be further exacerbated by the volatile geopolitical landscape.

Now, as input costs rise faster than pricing increases, where do consumers fit in this picture? How are they responding to the inflationary pressures, and what does it mean for retailers and brands?

### Will price dynamics settle consumer demand?

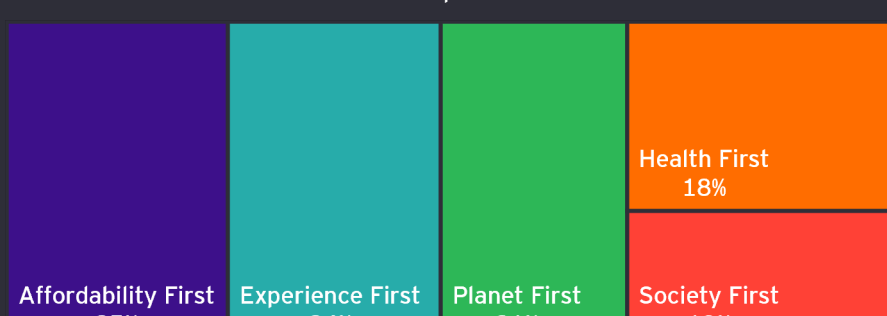
We've seen it on the grocery shelf, on our restaurant bill and at the pump as of late – a rise in the total cost of our purchases. And, while early incremental price increases may have gone unnoticed, the larger, and likely permanent, spikes in the cost of everyday essentials will likely temper the COVID-19-fueled, pent-up demand from consumers. Why?



50% of US consumers say rising costs of goods and services are making it hard to afford things.

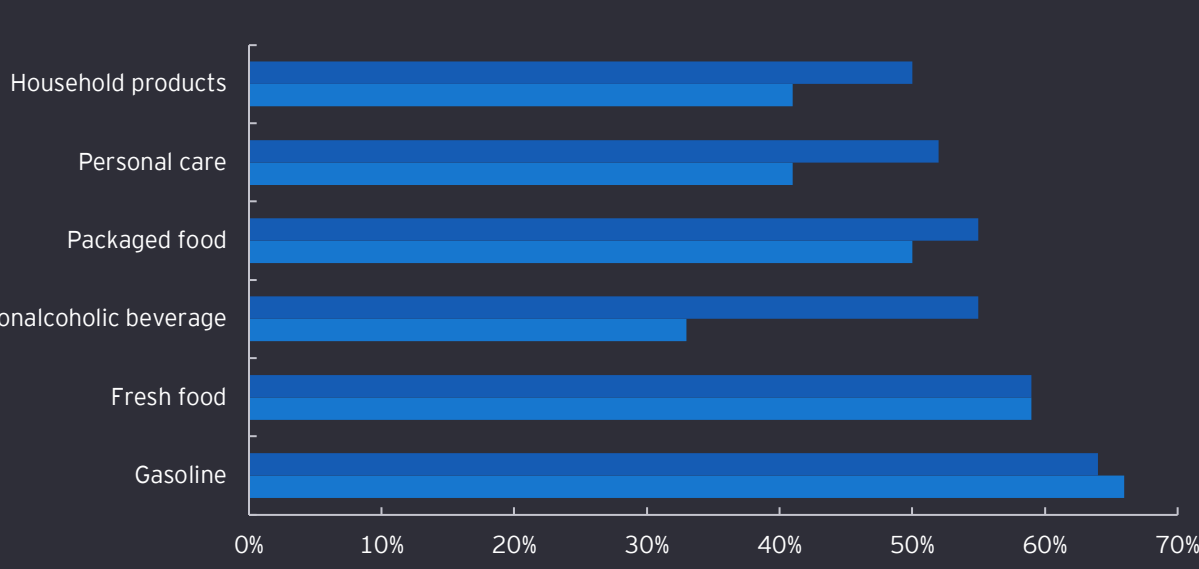
Increased price sensitivity may push demand even lower as consumers seek out value to justify cost. Of the five future segments, Affordability First remains the largest segment for another quarter. Further, 58% of US consumers say that price is the most important purchase criterion now, second only to product availability (60%). As consumers look ahead, price bubbles to the top, with 64% citing it as the most important purchase criteria in three years' time.

#### What will the consumer prioritize in the future?



### Digging deeper into price sensitivity

Certain categories fare better in high inflationary environments than others. Necessities such as gas and food, while still subject to price sensitivity, are less susceptible than the nice-to-have categories, such as apparel. Across many of the necessity categories, consumers say that they have not changed purchases despite price increases, and that they are bracing for, but have accepted, the fact that those prices will likely continue to rise.



### Mitigating the impact of inflation

Though inflation will not likely peak until later this spring as higher commodities prices push it even higher in the near term, we do expect a settling of things to come. With that in mind, how reactive, and permanent, should consumer-facing companies' response be?

The best course of action is to take near- to medium-term actions to mitigate the impact of inflation.

#### Exercise pricing power

One of the primary mitigation tactics that most consumer goods companies are employing is exercising their pricing power. Chief financial officers (CFOs) across consumer packaged goods (CPG) companies have pointed to raising prices as a key way to protect their margins.

It's a delicate balance, though, as we've seen with the price sensitivity sentiments exhibited by consumers. There is a threshold where consumers will no longer take on price, and companies would do well not to exceed it by using scenario model managing pricing based on real-time demand and supply dynamics.

#### Protect margins

In response to the impacts of COVID-19, we discussed five things consumer goods companies should consider. The efforts arounds margin protection still ring true in a high inflationary environment:

- ▶ Hedging and future commodity price management: Increased transparency on hedging methods and alignment with finance and supply chain leaders can drive tangible benefits quickly.
- ▶ Procurement contract review: Supplier contract adherence to penalties and incentives for pricing continuity and material availability can preserve margin gains.
- ▶ Converting earnings to cash flow: Companies can also take a page from the [Kellogg Company CFO's handbook](#). Kellogg has focused on refreshing and enhancing data-driven capabilities in revenue growth management.
- ▶ Automate forecasting: Artificial intelligence (AI) can support forecasting and decision-making that directly impact margin enhancement and cash conversion.

CFOs are also taking cost-cutting measures in other parts of the business, such as advertising spend, reducing operating expenses and rationalizing product SKUs.

#### Invest in productivity gains

While some consumer goods companies and retailers may rely on using the levers of revenue growth management to drive efficiency, some are investing in technology to drive efficiency, speed and agility:

- ▶ Accelerate the use of automation: Use AI for demand forecasting, leveraging automation and robotics in manufacturing facilities and DCs to drive efficiencies.
- ▶ Modernize systems: Upgrade legacy systems to drive more speed and agility.

Today's high inflationary environment will not soon pass; however, there are strategies that consumer goods companies and retailers can take to navigate through it. What remains is how the consumer will respond to those strategies. The costs of goods and services has, and will continue to have, a marked impact on not only consumer demand, but also long-term sentiments around price sentiment. Companies must walk the tightrope of meeting consumers' needs around pricing and managing the cost pressures in their wake.



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#### About the survey

The ninth edition of the EY Future Consumer Index is based on a February 2022 survey of respondents in the US, Canada, Brazil, the UK, France, Germany, Denmark, Sweden, Finland, Norway, Italy, Spain, India, UAE, Saudi Arabia, China, Indonesia, Japan, Australia and New Zealand. Of those, the article above focuses on the 1,000 US respondents.

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