

NESCAFE'

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1. FOREWORD

Giorgio Baruffa, product manager for Nescafé in Italy, was considering the future marketing strategy options for the product.

Nescafé had been in the Italian marketplace for thirty years, yet it had never quite "made it". A recent test to increase market share by cutting the price by 20% had not met the objectives, though it had caused a 25% increase in sales. Moreover, in the area test, the price reduction had weakened consumer perceptions of Nescafé's high quality image which, despite everything, the product had been able to build.

Mr. Bechi, marketing director of Nestlé Italy, had therefore decided, along with Baruffa, to call a meeting to analyze the product's problems and to arrive at a consensus decision regarding the future strategy for Nescafé over the next five years.

The persons involved in the meeting, besides the marketing director, were: Mr. Mazzei, the chief financial officer; Mr. Giuliani, head of strategic planning and Mr. Baruffa with his assistant.

2. THE COMPANY BACKGROUND

Nestlé S.A., headquartered in Switzerland, was one of the most important industrial groups in the world. It had 160,000 employees and 1988 revenues of \$ 20 billion. It was present in five continents, producing, in 362 plants, products which mirrored consumer tastes in each country.

The company had a decentralized organizational structure and the operating companies benefitted from ample autonomy in establishing long term policies, adapting these, of course, to local conditions.

Nestlé' took on the form of a "confederation of companies" which assembles 200 operating firms of diverse importance. Of the 160,000 employees, 43% were in Europe, 23% in North America, 19% in South America and the remaining 12% in Asia, Africa and Australia. Its total revenues, divided by country were as follows: U.S.A. 25%, France 12%, Germany 11%, Japan 6%, UK 4%, Brasil 4%, Spain 4%, Italy 2% and Switzerland 2%, 30% others.

Nestlé' had always been interested in the problems of infant feeding ever since it launched such winning products as "Nestlé' Powdered Milk" and "Condensed Milk." In time, though, the company amplified its product line and undertook a strategy of diversification through growth; both internal, by creating and launching new products, and external, through the merger and acquisition of companies even outside the food sector.

The realization of this strategy had accounted for either the launching or selling of numerous products; among these, chocolate (with such famous brand names as: Gala, Frigor, etc.); instant coffee (with the Nescafé and Taster's Choice brands); other instant beverages (the most famous being Nesquik); bouillon cubes and instant soup (brand name Maggi); preserves and fruit juices. Besides the food sector, Nestlé also operated in the pharmaceutical, cosmetic and hotel industries.

Nestlé was world's most important producer of instant coffee; it was also the major buyer of raw coffee. The idea of producing instant coffee was born in the 1930's when stocks far exceeded demand. Overproduction and excess stocks of raw coffee led to the search for an optimum method by which coffee could be preserved in concentrated and soluble form while maintaining its flavour.

The product's launch in 1938 just before World War Two, resulted in rapid diffusion. Nescafé' was adopted by all the armed forces involved in the conflict; thanks to its easy and convenient use. Consumption of instant coffee was quickly extended throughout the world.

The instant powdered coffee was obtained through the dehydration process and was later packaged in a controlled environment. Granular coffee, instead, was obtained by using the lyophilization method. Even with this process, the final product was later packaged in a controlled environment in order to maintain both its flavour and aroma.

The various package formats as well as the different blends had been developed with one precise goal in mind: to satisfy the specific needs of the consumer. As a result, by 1988, the world drank more than 170 million cups of Nescafé' a day. The advertising budget to promote Nescafé' the world over amounted to 350 million Swiss francs annually, and its market share, of total coffee consumption ranged between 10 and 30% all over the world.

The Nestlé Italy's was a Milan-based company operating in more than ten different industries. Its product portfolio had more than eighty products, generating around 2 billion \$ of revenues.

In the Italian market Nestlé had share leadership in the categories of milk modifiers (Nesquik - 72% market share of cocoa-based modifiers, and Orzoro - 63% market share of orzo-based modifiers) and instant coffee (Nescafé 80% market share of instant coffee).

In Italy, the blends of Nestlé coffee were sold under the brand names: "Nescafé Classic", "Nescafé' Gran Aroma" and "Nescafé' Relax" (a decaffeinated coffee). The Nescafé sales amounted to around 30 million dollars, equal to 1.5% of the total Nestlé Italy's revenues. The volumes of the Nescafé sales were 500 tons in 1982, 580 in 1986 and 650 in 1988 (Exhibit 1).

The main marketing investments on Nescafé were advertising (equal to 5% of the total advertising investment made by Nestlé in Italy), and promotion (equal to 2% of consumer and trade promotion made by Nestlé in Italy). The instant coffee contributed to the 8% of the Nestlé Italy Beverages Division revenues and to the 19% of its net profit.

3. THE ITALIAN CONSUMER MEGATRENDS.

During the 1980s, the percentage of food consumed "away-from-home" in Italy increased. Specifically, within the period 1977-1988 the foods consumed at "home" grew of 445,57%; while those "away-from-home" increased of 695,19%. This tendency could probably be attributed to profound changes in both society and the marketplace.

Among the most important socio-economic changes were: the spread of working hours that include a lunch break, the increased number of women in the workforce, the ever increasing number of one member family units (15% of the total in the 1988).

Other evident sociodemographic changes included: a reduction of members per family, a differently structured population (higher levels of education, lower birth rate - 1.7 children per family, aging of the population), a concentration of shopping in large stores, a strong "personal" involvement in consumption, a greater awareness of the health aspects of a diet and a strong sensitivity to ecological problems.

As a consequence, there was a growing trend in the consumption of fresh, genuine products, especially among young people with average or upper education (fruit and vegetable consumptions increased 11.6% in the 1986-1988 period).

The following is a list of the most significant, sociodemographic changes in terms of impact on consumption patterns.

1. The increased percentage of senior citizens as part of the total population and their disposable income (from an average of 1,250,000 lire per month in 1983 to 1,950,000 in 1988)(1). Furthermore, the demographic forecast seemed to confirm the trend:

POPULATION EVOLUTION (millions)

AGE	1987	1992	1997
0 - 14	18.3	15.9	15.2
15 - 24	16.5	15.4	13.2
25 - 34	14.2	15.8	16.4
35 - 44	13.1	13.6	14.2
45 - 54	12.6	12.5	12.8
55 - 69	15.6	16.9	17.1
70 AND ABOVE	9.7	9.9	12.2

(1) In the 1983 1,250,000 Italian Lire were circa 800 US\$; in the 1988 1,950,000 Italian Lire were circa 1,400 US\$.

2. The increased number of women in the workforce (over 30% of the total female population and circa 50% of the female active population, in 1988) and consequent increase in food consumption outside the home as well as the increase in demand for ready-to-eat and frozen dishes.

3. The increase in international mobility both into and out of the country: resulting in the internationalizing of consumer behaviour, especially in regards to durable consumer goods (in the '80s more than 2 million Italians went abroad each year and in the '88 this figure reached 3 million, equal to 6% of the population).

4. Changes in the ethnic composition of the population as a result of heavy immigration from Northern Africa and Central Asia (from 150,000 to over 500,000 in the last three years).

5. A rising level of education and culture among the population (currently college graduates make up 6% of the population, those with a high school degree 20%, those who finished junior high school 34%, those with only an elementary school education 40%; respectively, in 1980 the percentages were: 3%, 13%, 26% and 56% with a level of illiteracy equal to 1% of the population).

There were also considerable change in the consumption of some categories as beverages, where in the last 5 years non alcoholic beverages consumption increased of around 30% (specifically mineral water (+ 35%), soft drink (+32%) and fruit juices (+40%).

4. COFFEE CONSUMPTION: ITALY VERSUS OTHER COUNTRIES

Ever since the Arabs discovered the roasting process, near the end of the 14th century, inventing the dark brew that has been handed down, coffee has benefitted from both a private and public life. In the first instance, coffee was, and still is, tied to the intimacy of the family and home; while its public life has become enriched by both social and cultural activities connected to it.

Coffee-houses, where coffee was typically served, used to be patronized by the most cultured people in literature and knowledge; sustaining their poetic or political dissertation with the stimulus of the aromatic beverage. Coffee-houses were, in fact, once called "schools of knowledge."

Venetian merchants first introduced coffee to Italy around 1615 and it was no coincidence that the first coffee-house to open was in Venice. In 1720 the "Caffe' alla Veneziana Triofante" was inaugurated; it later became the "Caffe' Florian" and was regularly patronized by such persons as Lord Byron, Jean Jacques Rousseau and Silvio Pellico.

Therefore, even in Italy they became the centers of both cultural and commercial exchanges. The vibrant nature of these locals was underlined by numerous cultural initiatives. In 1764 in Milan, for example, Pietro Verri gave the title "Caffè" to a newspaper which, in theory, should have furnished stimuli and vitality to the narrow culture of that period.

It was interesting to note how the phenomenon of "intellectual attraction" was identical in all the coffee-houses the world over. Coffee houses, so, continued to be a place where journalists, artists, actors and people of culture in general meet, work, passby, debate and argue.

A wide variety of blends, degree of roasting, methods of preparing and habits of consuming coffee could be found in the different consumer countries. Each nation had adapted coffee to its culture and traditions, in particular, to its traditional forms of nutrition.

Therefore, in certain countries coffee was consumed not only for its stimulating properties, but also as a thirst quencher; while in other parts of the world it was consumed with very little water, as if it were an elixir.

The highest per person consumption was found in Northern Europe. Scandinavia registers the highest consumption per person with 12 kg. annually; followed by Denmark with 11 kg., Holland with 9 kg., Belgium and Austria with 8 kg., Germany with 7 kg. and France and Switzerland with 6 kg.. In the United States consumption was at about 4.6 kg. per person annually, although this figure was much higher in the 1970s.

In Italy, where most of people considered themselves to be heavy consumers of coffee, the level of consumption was equal to that of Canada's; about 4.3 kg. per year. Consumption was reduced to circa 2 kg. per person annually in Greece, Yugoslavia, Spain, Great Britain, Australia and Japan. This level was also reached by Hungary while in other Eastern European countries the per-capita consumption rate was less than 1 kg. per year.

There was a close relationship between levels of consumption and methods of preparing coffee: in Northern Europe, where the "filter" method was widespread, consumption was high. This was probably due to the considerable volume of water used in preparing coffee which permitted the beverage to function as a thirst quencher.

In fact, in most Nordic countries it was quite common to sit down to a meal with a large cup of coffee. Although it was unusual to drink filtered coffee by itself; normally it accompanied a hearty breakfast in the morning while in the afternoon it was usually taken with a slice of pie, pastry or biscuits. Those who drank "espresso" or "turkish" coffee, instead, normally coupled it to food only at breakfast (a habit which was not widespread in the Mediterranean area).

Naturally, the "capacity" of the coffee cups used also differs; in Holland, for example, the "capacity" was similar to that of a soft drink can while elsewhere it more resembled a tumbler.

Corresponding to the different "cultures" of coffee were the diverse ways in which it could be prepared. There were two principle methods by which the precious substances of coffee were extracted from ground coffee beans: soaking or percolation.

Utilizing the first method, ground coffee was first put into boiling water and allowed to "soak" for at least 5 minutes before straining the mixture through a filter.

In the case of percolation, a flow of boiling water passes through the ground coffee. Boiling water could be pushed through ground coffee in three possible ways: either by its own weight (gravity), similar to the filter method or the method used in "Neapolitan" coffee pots, or by a light steam pressure, a method employed in "moka" coffee pots, or by high pressure (9-10 atmospheres) furnished either mechanically or hydraulically by an "espresso" coffee machine. As a result, the greater the pressure exerted on the water, the less time it took for the coffee to percolate: therefore, filtered coffee took several minutes, a "moka" coffee pot about a minute and an "espresso" machine about 30 seconds (Exhibit 2).

There were also significant differences in the contents of caffeine per cup: 60-130 mg. per cup when using a "moka" coffee pot or "espresso" machine, 90-125 mg. per cup when utilizing the filter (percolator) method (largely diffused in the U.S.A.), 40-100 mg. for "instant" coffee and 2-5 mg. for decaffeinated coffee.

Instant coffees, that all over the world got a relevant share of the total coffee consumption, had in Italy a very little "niche" of the market: less than 2% of the total coffee market; versus 8% in Netherland, 10% in Germany, 30% in France, 34% in U.S.A., 37% in Spain, 51% in Greece, 78% in Portugal and over 90% in U.K. and Ireland.

The dynamics of the coffee consumption in Italy was affected by the existing differences between North and South, and between every single region of the Country. Particularly, between North and South there were big differences concerning cultural habits (Northern Italy was more cosmopolitan and "european"), affluence (Southern Italy is considered one of the less developed regions of the EEC) and climatic (much more warm and dry in the South).

The different tastes and preferences explained the high number of small and medium size importers and "torrefattori" (coffee roaster) who satisfied demand at the local level in each region: in Italy over 80% of the companies were small firms operating on a local level (Exhibit 3).

The different coffees shipped to Southern Italy were usually stronger and had a higher percentage of Robusta (one of the two main coffee plants type - much more strong and bitter, and less flavoured than Arabica, the other one) while in the North the aroma of the coffee was more important.

In Italy the typical coffee drinker was between 15 and 55 years old. In 1988 the highest level of consumption being in the 45 to 54 age bracket:

age	% who usually drink coffee	annual per capita consumption (kg)	% of total consumption
15 - 24	50	3.04	12.4
25 - 34	70	4.36	20.5
35 - 44	81	4.60	23.0
45 - 54	83	4.90	24.0
55 - 69	67	3.13	15.1
70 and above	60	1.86	5.0

Younger and more health-oriented consumer perceived coffee as a "risky" beverage and tried to reduce their consumption.

Coffee had always been regarded, by Italians, as a digestive or stimulating beverage. Per capita consumption in coffee-houses was the highest in Europe and accounted for about 20% of all the coffee consumed in the entire country.

The consumption of coffee in Italy was characterized by the existence of two large segments of consumers: those who drank coffee at home and those who drank it in coffee-houses or restaurants.

Just how important coffee was, as a staple of the national diet, could be seen by changing the units of measure; going from kilos to value in lire. Assuming an average quantity of coffee per cup of 6 grams, the Italian market amounted to 35 million cups of coffee (around 600 cups of coffee per person). Total coffee sales at retail amounted to 11 billion lire (about 192,450 lire per person). Coffee was one of the items in the food budget on which a large amount of money were spent each year.

5. THE COFFEE INDUSTRY IN ITALY: STRUCTURE AND EVOLUTION

Coffee was the largest commodity market in the world. In this market, two counter-weight interests came into play: on the one hand there was strong competition on price and quantity among producers of raw coffee, on the other there were different commercial and technological needs among the world manufacturers.

The stability of such an important market was constantly threatened by the need for foreign exchange of liquidity on the part of developing countries (producers of raw coffee) which attempted to increase production causing fluctuations in prices.

Coffee processing technology differed among to the type of coffee being made. The different types of coffee were: roasted (normal), decaffeinated and instant (soluble).

The coffee companies sold coffee to the following groups of clients: families, coffee-houses, hotels and restaurants.

In the "family" segment competition was fierce among the companies marketing nationally. Their strategies focused on:

- intensive advertising to enhance the brand image;
- a growing orientation towards modern distribution channels (supermarkets, etc.);
- a strong use of promotion at points of sale;
- a segmentation of the market according to the quality, price and specific use of coffee.

In the coffee-houses, hotels, restuarants ("CHR") segment, competition was among a small number of companies which operate nationally; although there were still many little firms which operated on either a regional or provincial level. Information regarding segments dimension, market shares and the positioning of the major companies in the two different segments are illustrated in exhibitions 4, 5 and 6.

The dominant positions of firms in these two segments differed, but the companies which offer a good product in the "CHR" segment, will probably do the same in the "family" one.

5.1 The industry structure.

The Italian coffee industry was composed by 750 companies, wich employed 7,200 workers; the first four companies market share was approximatly 42% of the total (52% for the first eight) and 1988 sales at factory prices were 1.5 billion dollars (see Exhibit 4 for leading companies market share and Exhibit 5 for retail sales data). Sales volume was expected to expand 2% per year.

The fragmentated structure of the industry was due to low entry barriers. Analyzing the production process only the purchasing of raw coffee could be considered quite profitable to larger companies. They, indeed, were large enough to buy directly in the foreign countries (Exhibit 7 regards specifically the Italian market).

During the last several years, many companies had been pushed out of the market as a result of competitive pressure (coming especially from market leaders) and the price volatility of raw coffee; making it even more important to realize economies of scale in purchases.

5.2 The marketing strategies of the leading companies.

The companies which operated in the coffee market had adopted different marketing strategies in terms of product, price, place and promotion.

Coffee was sold in two forms: either as whole coffee beans or as ground coffee. The former was used in coffee-houses while the latter was used predominantly at home. All of the major firms had a broad range of products with different prices and sizes. Some companies, to offer a complete product line, bought instant or decaffeinated coffee from other firms to later resell under their own brand name.

The innovations in the coffee market had recently involved the packaging and blends offered. In terms of packaging, there were several sizes available: 200/250 gram bags (49% volume share in family segment), 400/500 gr. bags (38%), 500 gr. tins (4%) 1 kg bags (9%).

In the coffee-shop, Hotel and Restaurants (CHR), instead, were mainly used 1 and 3 kg bags.

Instant coffees were available in small glass jars weighing 50 to 125 grams.

The spread of these different size packages depended on the type of consumption, the type of coffee and the type of sales channel.

The most preferred type of package was the pliable bag; in part due to the cost of its raw materials, paper and a plastic film used to cover it, the convenience which it offered (lighter package, less bulky) and, in part, to the variety of different sizes in which it came.

Looking at Exhibit 8, it is possible to understand the presence of major firms in the distribution channels. Among the key success factors in the modern distribution outlets were the brand image and the sizes offered and the product's display. Yet if the brand name was important for selling coffee to the "family" segment, then service was the key for selling it to the "CHR" one. Market shares in traditional outlets, more and more supplied by wholesalers, were continually diminishing.

There were many coffee roasters who made agreements with operators in this latter segment concerning forms of financing and discounts on the use of coffee machines as incentives to maintain customer loyalty.

Given the high quality coffee obtained through the espresso method and the image of "coffee-house" coffee, a brand presence in the "CHR" segment could contribute to its image in the "family" segment. This was due to the widely held belief that coffee made in a coffee-house was better than the coffee made at home; therefore, consumers were often willing to buy the brands found in coffee-houses.

The average national price for a kilo of roasted (normal) coffee, for operators in the "CHR" segment, was about 18,000 lire (VAT included), but there was a wide variance around average. This price became up to seven/eight time bigger for the end consumer, usually paying 800/900 lire for a 6 gr. cup of coffee-shop espresso.

The average national wholesale price for a kilo of roasted coffee was far lower in the "family" segment (around 11,000 lire); while the average price per kilo for decaffeinated or instant coffee was much higher (30,000 the decaf and 50,000 the instant).

By observing the cost structure of firms operating in the market, it became apparent that raw materials (coffee beans) represented circa 70% of total costs; packaging material accounting for 13%; advertising and promotional activities 2%; wages, depreciation and gross operating profits representing 15%. Breaking down the price of a cup of coffee, the values were as such: cost of the blend 15%, cost of sugar 2%, cost of labour 52%, overhead 24% and VAT 6%.

Price was used as a competitive tool when contracting with intermediaries less sensible to quality, service and promotional policies to differentiate the product.

In terms of advertising, it can be demonstrated how this, along with distribution, had an important function within the marketplace. In the "family" segment, market leaders benefited from economies of scale not only in distribution, but also in communications in order to maintain their leadership (Exhibit 9).

Of the total 1988 advertising investments 76.6% regarded Roast & Ground coffees, 20.9% decaffeinated and 2.5% instant.

The awareness of the brand name was promoted using many communication instruments; some of the bigger companies managed to utilize one particular brand name as a "brand umbrella". This was done, for example, by focusing advertising campaigns on one particular product, i.e. "Lavazza Club", and as a result of association, promoting the various other "Lavazza" products.

Sales promotion was another communication tool usually used for the intermediaries of the "family" and "CHR" segments. Among the various forms of promotion were: billboards, brochures, signs both in the store and in store windows and displays which show some originality in presenting the product. Besides these forms of promotion, there were the discounts typical of the consumer goods market: "buy two, get one free" and "two vacuum packed bags of ground coffee sold as one" package were the most common.

5.3 The main competitors.

Among the major competitors, there were some who, because of their importance or size, had acquired an increasing influence on the market.

Lavazza S.p.A. of Turin was family-owned and the tenth largest food company in Italy. It was the coffee market share leader and the only company to offer a complete product line. Lavazza distributed nationally eleven brands and blends at different price, points and with differences in taste and

quality.

Its leadership was heavily supported by advertising for every brand. The company image was strictly connected to a famous Italian actor, testimonial used to claim the "italianity" of the Lavazza coffee. At the same time the TV commercials emphasized the quick stimulating effects of the Italian coffee: "The more you push it down, the more it pulls you up!".

Segafredo-Zanetti S.p.A. of Bologna only produced normal, roasted coffee and was among the first to introduce the combination pack of two vacuum packed bags of coffee for the "family" segment; in which the firm had not operated up until that time.

Segafredo had historically focused on the "CHR" segment, for which it also produced industrial espresso machines sold under the name Segafredo. The company offered an ample variety of roasted blends and it invested heavily in sponsoring both national and international sporting events.

Crippa & Berger S.p.A. (Milano) was the first company to produce decaffeinated coffee in Italy. The firm competed directly with Nestle' through its own brand of instant coffee, Faemino; but its strong point was its decaffeinated coffee Hag (65% market share versus 27% of Lavazza decaf brand). Crippa & Berger's brands were: Gah (a new product featuring low caffeine and low fat), Faemino and Hag. It invested nearly 28% of its revenue in advertising, principally to promote the brand name Hag.

The Crippa & Berger advertising investment mainly aimed to justify the premium price of the Hag brand, both in the "CHR" and in the "Family" segment. They presented, indeed, the several different benefits that the consumer can get using a decaf coffee; in several different contexts. They did not invest on the instant coffee "Faemino" brand.

Procter & Gamble Italia, the Italian subsidiary of the Cincinnati-based multinational, with its "Splendid" brand benefited from strong distribution penetration due to the broad range of the group's "grocery" products. P&G promoted the Splendid series by sponsoring television programs with high viewer ratings (i.e. the most important Italian variety show "Fantastico" in 1988).

The year 1988 was unusual because the advertising budget for Splendid Decaffeinato, close to 15 million dollars, was more than what was budgeted for normal roasted coffee. The positioning was quite different: for Splendid Oro and Classic, presented as the coffee used in the most prestigious restaurants; the other product in the line was targeted, through aggressive promotion, to the large family segment.

Illy Caffè of Trieste produced one blend of normal coffee with seven different degrees of roasting. Illy Caffè was well known for its excellent quality and a series of decaffeinated and low caffeine coffees ("Mite").

All the Illy commercials tried to show that the Illy espresso was better than any other coffee brand: "the best maestro", was the answer of an American patron to the coffee shopkeeper who asked his judgment about the "Illy espresso". The campaigns were briefly put on hold in 1988 because of the intervention of the Italian equivalent to the American F.C.C., which had regulations to contrast comparative advertising, in Italy strictly forbidden. Yet this did not stop the firm from bettering its market position.

Consorzio Sao Caffè gave its brand name in concession to eight different companies who occupied themselves with the production and distribution of the Sao brand. The advertising budget was centrally managed and represented one of the most important moments for the consortium. Its commercials were focused on the Brazilian sound of the name, using the positive association between the country of origin image ("from Brazil: Sao caffè") and the high coffee quality.

Café do Brasil had a strong brand in Café Kimbo, favoured especially in Southern Italy where consumers enjoyed its strong and bitter flavour. Caffè Kimbo had rapidly gained in market share as a result of competitive prices coupled to a strong advertising effort. The TV commercials of Kimbo were based on a very popular testimonial (Pippo Baudo) tasting the strong flavour of the coffee in a roaster plant and emphasizing the consequent freshness and the rich taste of the Kimbo coffee.

The 80% small coffee processors bought raw coffee from importers and sold to different local outlets. Often these companies were able to offer a high quality product adapted to the tastes and traditions of the regions in which they operated.

6. THE NESCAFÉ IN ITALY

Instant coffee was launched in Italy in 1962. The flavour of Nescafé in Italy was particularly "Italian"; due to the degree of roasting, the type of solubilization and the raw materials used (more Robusta and less Arabica). This had always made the formulation of Nescafé in Italy something particular and different from the other European countries.

The Italian market possessed a very specific and deep-rooted coffee "culture." Nestlé's main objective when it launched Nescafé was to have the product, although soluble, perceived as "real" coffee.

Marketing decisions were aimed at fighting the inevitable suspicions of a coffee that was simultaneously "good, convenient and easy to use", a convention often voiced in Nestlé Italy's marketing office.

As a result, every effort was made to affirm the goodness and quality of the product; comparing it directly to other Italian coffees.

The advertising message, essentially aimed at an emotional response, underscored the goodness of the coffee with claims such as: "Hmm, what is it...what's happening....I smell coffee...., Nescafe', the best of them all". Nonetheless, consumers perceived the product to be a coffee which was "missing something" and which could not substitute for "real" coffee. Nescafe came to be viewed as a "backup" product which was only to be used in case of an emergency and was best suited to singles or older people.

The decision to compare Nescafe' directly to Italian espresso, evident in the advertisement, didn't convince consumers in terms of product quality or goodness.

A 1978 study confirmed a rigidity in the product's image meanwhile sales had remained constant at about 400 tons since 1972.

From 1979 to 1983, marketing aimed at obtaining a more "personal" involvement on the part of consumers. As a result, advertising campaigns no longer were centered on the product, but rather presented "testimonials" by real people who demonstrated a strong commitment to their everyday work.

The marketing department had, in fact, opted for a "multisubject" campaign which showed "typical" people in the workforce: a forest ranger, a dockworker, a train conductor, etc.. The campaign aimed to show that Nescafe was coffee suited to and made for anyone who "wants something more out of life" and "gives something more to it". The claim was: "You deserve a better coffee, Nescafe'". The advertising message was reinforced with sampling and displayings at the point-of-sale.

However the 1981 tracking study did not show any image improvement. Nescafe was still an unattractive product to those who wanted "gratification and a 'recharge'" from their coffee. Sales increased very slowly (still around 500 tons in 1982).

Between 1984 and 1986, an advertising campaign entitled "The train" was imported from France after its huge success in that country. It achieved high recognition in Italy as well. The ad described an exotic train journey aimed at stimulating an emotional involvement; while the rational aspect was represented by the emphasis on suggestive images of locations where coffee is grown.

The ad fundamentally underscored the value of a good coffee, boasting about Nescafe's origins without comparing it directly to typical Italian coffee.

The 1985 tracking study, showed some change in the image of Nescafe; the product had gained in perceived prestige and reliability. There was a corresponding increase in sales volume that in the 1986 jumped to 580 tons, and by then reached 640 tons.

The recent study, handed out by Baruffa at the meeting, demonstrates how in recent years, Nescafé had become used disproportionately by older people who were more sensitive to the effects of caffeine. Nescafé was preferred because of its less "aggressive" image and for its ease of preparation during moments of relaxation.

Those aged 55 and above, represented about 80% of Nescafé consumers though their per capita consumption did not exceed one cup a day. In the broader family market Nescafé was considered "emergency provisions" by many Italian families especially when on holiday.

Considering that instant coffee was generally retailed to the public at 60,000 lire per kilogram, against 13,000 lire average for normal coffee, it can be said that the product was prospering in a "splendid niche".

The price to wholesalers was 85% of the retail price and the variable manufacturing costs amounted to 37.5% of the retail price; therefore, there was a gross operating profit equal to 47.5%. Sales and distribution costs represented 15.3% and all of this insured a high operating profit equal to 32.3% (Exhibit 10).

Nestlé Italia's management showed signs of dissatisfaction with the results so far obtained, and considering the widest presence in the distribution channels, the executives believed that more could be done.

A new, "strategic" plan had to be defined to increase sales. Manufacturing could readily increase the quantity of coffee available to support increased plan.

At the meeting, Baruffa wanted to present some important information on the results of certain qualitative inquiries (psychological and motivational studies) and data regarding the present consumption of Nescafé.

Among this data (Exhibit 11), the most interesting findings were those measuring the "cultural resistance" of Italians to Nescafé in terms of notoriety and use of the product.

Nescafé brand awareness was high at 83% of the sample population (more than 3,000). However Nescafé had been tried by only 39%. Its market share for all types of coffee was 1.4% while its market penetration (presence of at least a Nescafé package at home) equals 14%. Sales were concentrated in some big cities and in the North of Italy (Exhibit 12).

6.1 Marketing strategy options for Nescafé.

Baruffa expected to discuss four strategic options that he presented as follow:

1. Focusing on the older segment, already heavy consumers of the product.
2. Broadening the use of Nescafé as milk modifier, particu-

larly in the morning.

3. Trying to market Nescafé for younger and more "cosmopolitan" professionals, changing the product positioning and marketing Nescafé as "the international coffee beverage".

4. Trying to penetrate the CHR segment of the market.

Baruffa began the discussion on the first option, considering it the less attractive. He affirmed, indeed, that the limited coffee consumption by the older people would not allow a significant increase of the Nescafé sales; though the demographic trends showed that segment as the more attractive.

The Marketing Director, Mr. Bechi, instead shifted the focus on the second option presented by Baruffa. He believed that, as the recent research showed, "the youngster" should be the Nescafé main target for the next five years. At the same time, Bechi was concerned about the positioning of Nescafé as milk-modifier, because of the leadership of Nestlé Italy in that category with Nesquik and Orzoro (market share data here). He warned the group about the high probability of a cannibalization effect and the eventual internal conflict with the milk-modifiers product management.

At this regard Baruffa pointed out that younger people appreciation for Nescafé was an opportunity to catch emphasizing the product both as a milk-modifier and as a "new less caffeine alternative coffee".

Mr. Mazzei, the CFO, instead asked to put away the entry option on the CHR segment. He argued that the trade promotion investment in that segment seemed to be so relevant that very hardly Nescafé sales in CHR would pay back the initial investment needed to entry and distribute the product. He also thought that a switching from espresso to Nescafé in a Coffee-shop was very hard to figure out.

The meeting at that point focused on the proposal made by Mr. Giuliani to radically modify the Nescafé positioning, marketing the coffee as an international coffee (not as an Italian coffee) to the cosmopolitan segment that prevalently lives in the big Northern cities. Mr. Giuliani point of view was founded on his personal feeling that the Nestlé traditional food products should become standardized by the 1990, at least in European market.

To support his idea Mr. Giuliani explained that big organizational benefits could come from this policy and that, looking at the marketplace, there was a growing "transnational consumers" segment that, traveling and living all over the world, was achieving "universal" consumption habits.

At this point the discussion was going towards more specific evaluation of each option, aiming to define a new marketing strategy and a new marketing plan for Nescafé.

Exhibit 1 Nescafé volumes ex factory

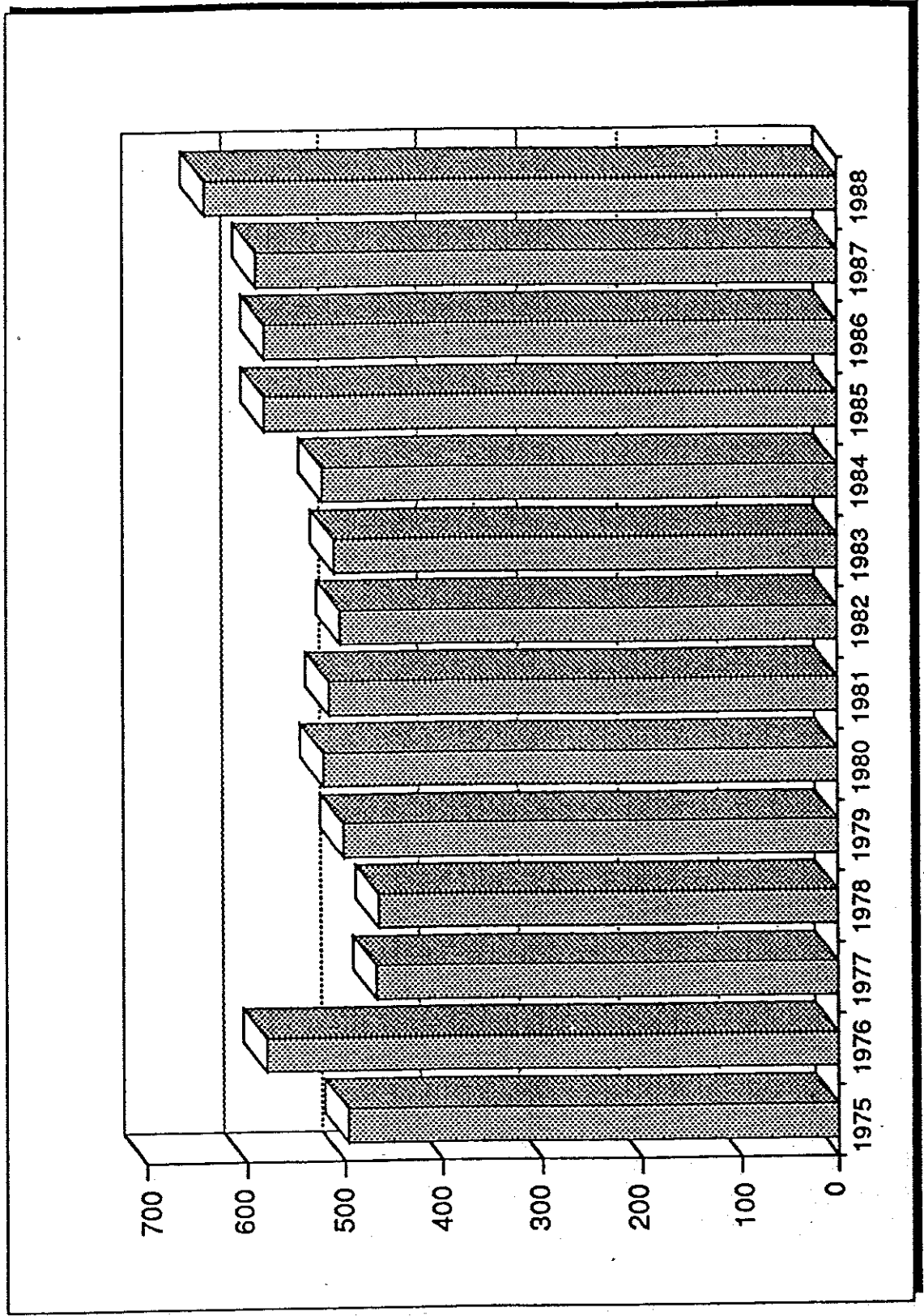


Exhibit 2



Turkish Process

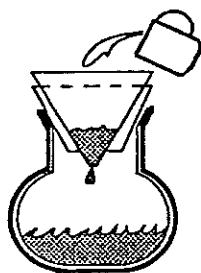
Water is brought to a boil in a copper pot, to this is added finely ground coffee sometimes already sweetened. The coffee can then be consumed in two distinct ways:

- by either pouring the coffee immediately into a cup and allowing it to settle
- by letting it settle in the pot itself and then gently pour into a cup



Mellor Process

The coffee pot can range in serving size from 1 to more people. Water is boiled in the pot and ground coffee is later added to it. A metallic filter, of equal diameter to the coffee pot, is then fitted on. With the aid of a handle, the filter is gradually pushed down into the pot: coffee, therefore, passes through the filter while the grounds settle at the bottom.



Percolator

Ground coffee is placed into a fabric or paper filter which is later put on top of a glass pot. Boiling water is poured into the filter and passes through it became coffee.

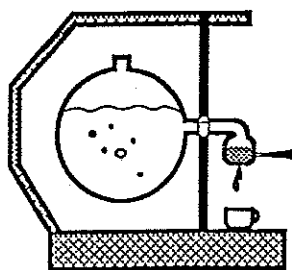


Moka

Water is brought to a boil in the lower part of the pot and under the pressure of steam flows into the top part of the pot through the filter where the coffee is located. The filter must be filled to the right level, it must not exceed the brim and the coffee must not be pressed down. This is essential to making a good pot of coffee.

When the first drops of coffee appear, the flame under the pot should be lowered. A high flame at this stage could give the coffee a "burnt" flavour; it is therefore best not to abandon the pot once it has been put on the burner and it is always better to use a low flame.

After its use, the coffee pot should be cleaned thoroughly, especially the filter and trimmings. Detergents should only be used to clean the exterior.



Espresso

It should always be remembered that coffee is an unstable liquid; after a short time altering its characteristics. This is one of the reasons that led to the introduction of the espresso machine which permits a higher level of extraction and the instant production of individual cups of coffee. The espresso process, working under greater pressure, allows for more of the coffee's natural oils and minerals to seep into the cup; these oils and minerals are responsible for the coffee's richness, flavour, aroma and consistency.

EXHIBIT 3

DATA SUMMARY - 1988

NUMBER OF COMPANIES	750
NUMBER OF WORKERS	7.200
VALUE OF PRODUCTION (factory prices - billion lire)	1.981
PRODUCTION SHARE - FIRST 4 COMPANIES (value)	41,9 %
PRODUCTION SHARE - FIRST 8 COMPANIES (values)	52,0 %
FORECASTS FOR THE EXPANSION OF PRODUCTION	
- 1989/1988	2 - 3 %
- medium term trends	1 - 2 %

EXHIBIT 4

ITALIAN COFFEE MARKET (Retail Sales) 1988

(IN THOUSANDS OF TONS AND BILLION LIRE)

	FAMILY SEGMENT			CHR SEGMENT			TOTAL		
	volume ('000 tons)	percent	value (billion lire)	volume ('000 tons)	percent	value (billion lire)	volume ('000 tons)	percent	value (billion lire)
NORMAL	144.9	69.0%	2,105	65.1	31.0%	8,267	210.0	96.7%	10,372
DECAF	2.9	58.0%	48	2.2	44.0%	410	5.0	2.3%	457
INSTANT	0.7	87.5%	69	0.1	42.9%	72	2.1	1.0%	141
TOTAL	148.5	68.6%	2,222	67.4	31.4%	8,749	215.8	100%	10,970

100% 20.3% 79.7% 100% 100% 100%

EXHIBIT 5 NORMAL ROASTED COFFEE: ITALIAN MARKET SHARES OF MAIN PRODUCERS
1988 "FAMILY" AND "CHR" SEGMENT

	FAMILY		CHR	
	QUANTITY ('000 tons)	VALUE (billion lire)	QUANTITY ('000 tons)	VALUE (billion lire)
LAVAZZA	42.0	30.7%	3.0	6.5%
PROCTER & GAMBLE	12.3	9.0%	-----	-----
CAFE' DO BRASIL	10.2	7.4%	0.5	1.1%
SEGAFREDO	4.4	3.2%	4.3	9.4%
SAO CAFE'	7.0	5.1%	-----	-----
ILLY CAFFE'	0.4	0.3%	1.5	3.2%
TOTAL MKT	137.0	1,170	45.7	520

INSTANT COFFEE: ITALIAN MARKET SHARES OF MAIN PRODUCERS- 1988

	QUANTITY (TONS)	PERCENT	VALUE (BILLION LIRE)	PERCENT
NESTLE'	650	77.7%	35	80%
CRIPPA & BERGER	110	13.1%	7	15.9%
OTHERS	76	9.2%	2	4.1%
TOTAL	836	100%	44	100%

EXHIBIT 6
 ITALIAN
 COFFEE MARKET
 STRATEGIC
 GROUPS

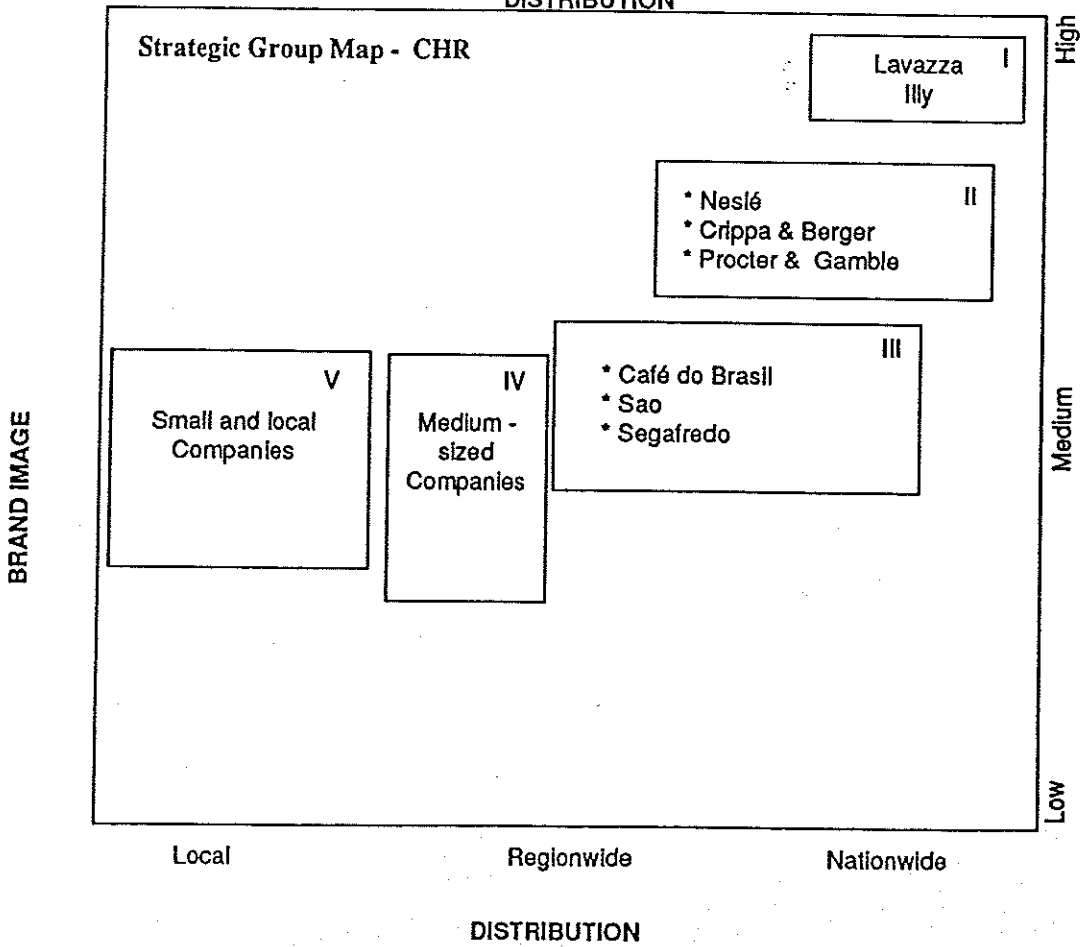
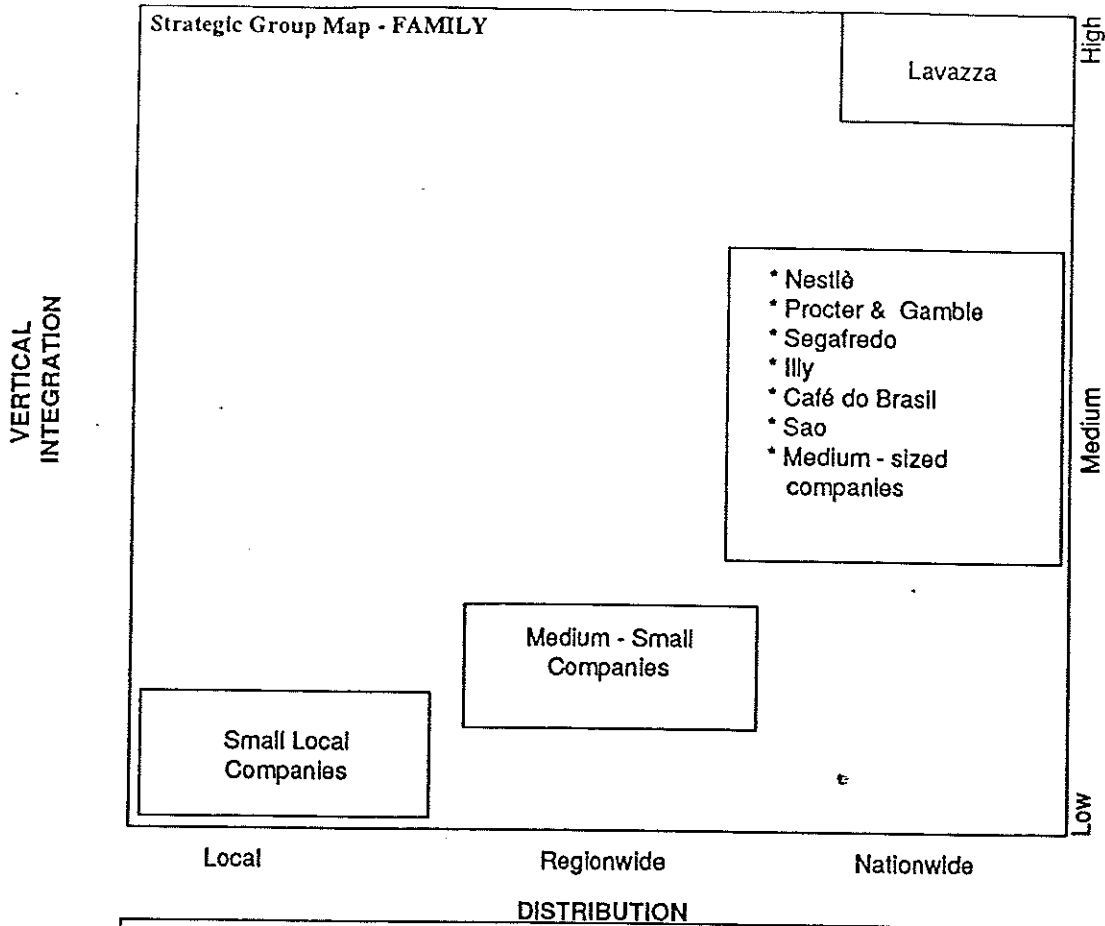


Exhibit 7

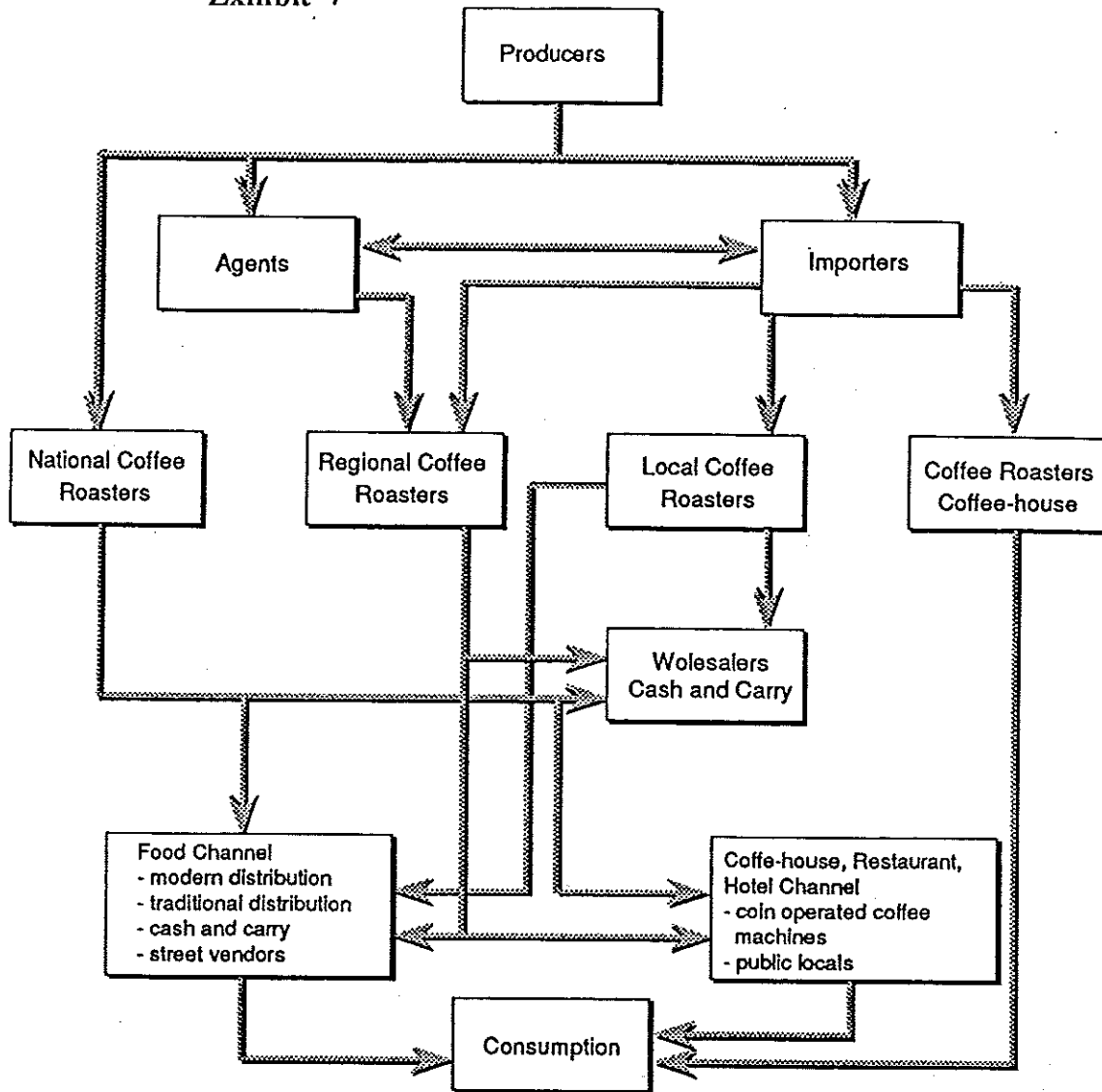


EXHIBIT 8

THE DISTRIBUTION OF MAJOR COMPANIES: OCTOBER 1988 (% AND AVERAGE NUMBER OF REFERENCES)

	HYPERMARKETS		SUPERMARKETS		CONVENIENCE STORE	
	%	Average	%	Average	%	Average
NESTLE'	100.0%	5.7	100.0%	7.2	100.0%	6.1
LAVAZZA	100.0%	12.2	100.0%	11.1	95.5%	10.9
CRIPPA & BERGER	100.0%	5.5	100.0%	5.4	95.5%	3.6
SEGAFREDO	69.6%	3.9	60.7%	3.9	9.1%	2.0
PROCTER & GAMBLE	100.0%	5.9	94.6%	5.9	95.5%	4.7
CAFE' DO BRASIL	30.4%	2.2	8.9%	3.0	25.5%	1.5
SAO CAFE'	69.6%	4.5	70.5%	4.5	40.5%	3.0
ILLY CAFFE'	10.5%	2.0	15.7%	2.0	5.5%	1.0

DISTRIBUTION ANALYSIS: NUMERICAL AND WEIGHTED

	NUMERICAL	WEIGHTED VOLUME INDEX (NESTLE'=100)
LAVAZZA	73	90
PROCTER & GAMBLE	65	77
CRIPPA % BERGER	23	70
NESTLE'	70	100
SAO CAFE'	28	60
CAFE' DO BRASIL	18	30

EXHIBIT 9

COFFEE ADVERTISING INVESTMENT FOR THE MAIN PRODUCERS (BILLION LIRE)

	ADVERTISING INVESTMENT		% OF SALES	
	1987	1988	1987	1988
LAVAZZA	34.0	62.0	6.8%	11.8%
PROCTER & GAMBLE	22.6	40.4	18.3%	36.2%
NESTLE'	7.4	4.3	9.1%	5.6%
CAFE' DO BRASIL	9.4	18.0	10.1%	20.3%
SAO CAFE'	3.5	1.3	5.2%	2.3%
SEGAFREDO	4.3	9.5	4.6%	9.4%
CRIPPA & BERGER	7.6	13.2	15.2%	28.3%
ILLY CAFFE	6.0	7.4	15.9%	16.8%

DIVISION OF AD INVESTMENT FOR THE MAJOR COMPANIES (1988)

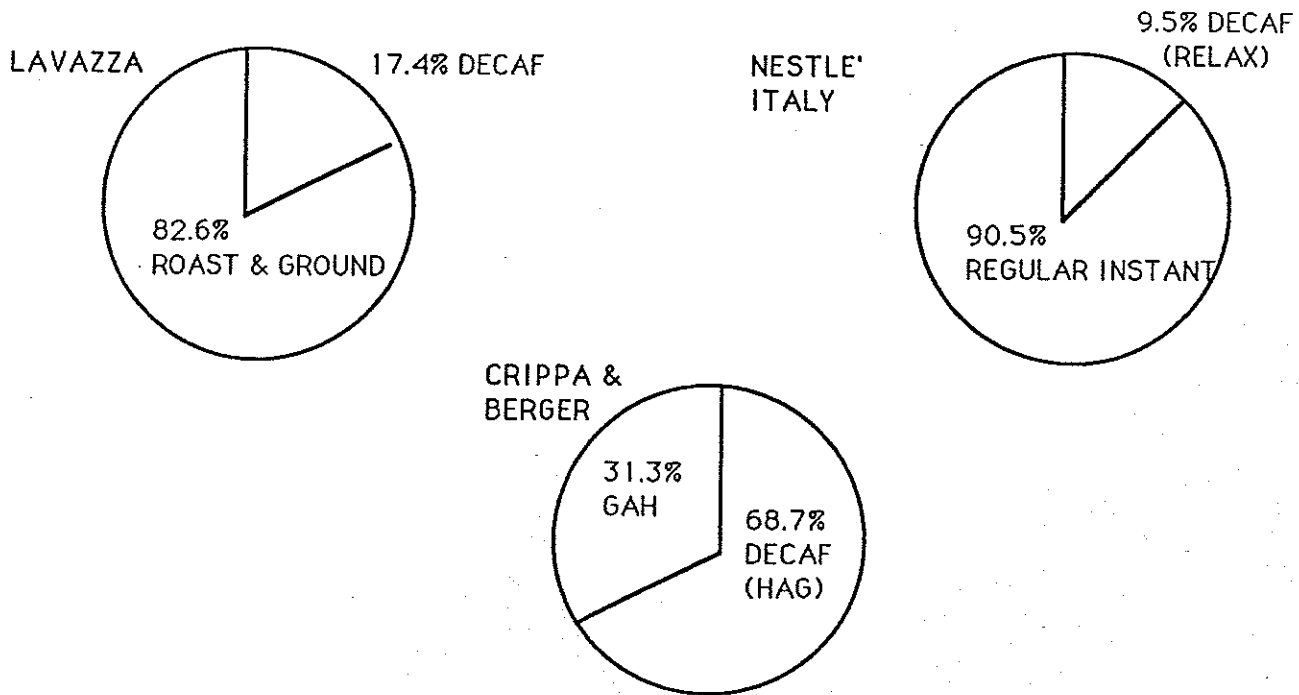


EXHIBIT 10

COSTS AND CONTRIBUTIONS: NESCAFE' VS. ROAST & GROUND (AVERAGE 1988 - LIRE)

	250 GR (R&G)	125 GR (NESCAFE')	6 GR (ESPRESSO)
SUGGESTED RETAILER SELLING PRICE	3,250	7,500	800
PRODUCER SELLING PRICE	2,600	6,375	111
COST OF GOODS SOLD	2.157	3,160	79.7
- MANUFACTURING	1,490	2,812	55.8
- DISTRIBUTION	660	550	25.9
CONTRIBUTION MARGIN	442	3,013	29.3
SALES PROMOTION	45	374	0.25
- TRADE	10	250	0.25
- CONSUMER	35	124	-----
ADVERTISING	30	426	0.5
CONTRIBUTION AFTER MARKETING EXPENSES	367	2,213	19.3

Exhibit 11 Results of the motivational study

(The following affirmations were reported with significant frequency during the course of extended interviews on the relationship between the interviewee and coffee; in particular Nescafé.)

- | | |
|-----|---|
| 1. | "Espresso is true coffee." |
| 2. | "Nescafé isn't as strong as normal coffee." |
| 3. | "Espresso coffee is strong, flavourful and aromatic." |
| 4. | "Nescafé isn't a real coffee." |
| 5. | "Nescafé is easier to handle." |
| 6. | "Nescafé is used only in <i>emergencies</i> ". |
| 7. | "Nescafé is for older people" |
| 8. | "Preparing a pot of coffee is not a waste of time indeed."
(predominant response by coffee drinkers who don't drink Nescafé) |
| 9. | "Coffee is a risky product and its consumption should be reduced"* |
| 10. | "Coffee, tobacco and alcohol.**" |
| 11. | "Coffee is a risky product and its consumption should be reduced." |

Certain specific results on Nescafé

- 2/3 of Nescafé drinkers prefer it during meals or in the afternoon;
- the remaining 1/3 use it as a "milk modifier" in the morning;
- the different brands of Nescafé are easily distinguished;
- 43% of consumer consider it "lighter" than an espresso or "moka" coffee, 20% "as much as", 37% "do not know";
- 40% of those who "know" the product, judge it to be "lighter" than an "espresso" or "moka" coffee, 10% "as much as", 50% "do not know".

* Frequently heard affirmations and associations of children and young adults

EXHIBIT 12

DISTRIBUTION OF NESCAFE' VS. ROAST & GROUND COFFEE CONSUMPTION FOR MAJOR ITALIAN MARKET

	POPULATION (%)	ROAST & GROUND (%)	NESCAFE' % OF TOTAL SALES
ROME	7%	9.1%	4.2%
MILAN	4%	5.7%	29.5%
TURIN	2.5%	3.1%	5.1%
NAPLES	3.2%	4.2%	0.9%
BOLOGNA	2.2%	2.7%	2.4%
FLORENCE	1.8%	1.9%	2.7%
PALERMO	1.6%	1.8%	0.7%