

SUSTAINABILITY AT NESPRESSO¹

"Today, our ambition is to provide the highest quality and most sustainable portioned coffee in the world."

Jean-Marc Duvoisin, CEO Nespresso

Nespresso's sustainability strategy was based on Nestlé's Creating Shared Value (CSV) approach. This meant that the company's activities aimed further than mere compliance with the law, and went ahead to ensure the conservation of the environment for future generations and the creation of value for its clients, providers, employees, stakeholders and society in general. Creating a Shared Value was Nestlé's platform to reach further into sustainability, creating long-term value for society. For this reason, sustainability had long been an integral part of Nespresso's strategy since 26 years ago. An important step in this regard was taken with the creation in 2003 of the "Nespresso AAA Sustainable Quality™ Program" jointly with the NGO Rainforest Alliance (devoted to ensuring a sustainable future for coffee farming communities).

Thanks to this program, over 70,000 coffee farmers in 12 participating countries (Costa Rica, Guatemala, Colombia, Mexico, Nicaragua, Brazil, India, Indonesia, Kenya, Ethiopia, Peru and South Sudan) sourced more than 80 percent of the coffee that the company used in 2016, while they also benefitted from the advice that experts at Nespresso gave them.

To Jean-Marc Duvoisin, Head at the company since 2013, it was clear:

"You cannot have a business strategy and then a separate sustainability strategy. Sustainability has to be embedded in your business model. Our sustainability strategy cannot change when a new CEO is appointed. It is something that should go beyond management. And to achieve that, it has to be part of the business model."

¹ The Research Division of San Telmo Business School, Spain, has published this case. Written by Professor Antonio García de Castro and research assistant Ms. Rocío Reina Paniagua. This case has been developed as a basis for class discussion only and is not intended to illustrate any judgment on the effective or ineffective management of a specific situation.

This has long been the case at Nespresso. We have done our share of work, we know the total impact of the farm, of the cup and the recycling, and we know what we have to do to achieve our goals."

In Jean-Marc's words:

"The Nespresso story began with a simple idea: we wanted to make it possible for anyone to create the perfect cup of espresso coffee – just like a skilled barista would. From its beginning in 1986, Nespresso has defined and revolutionized the way millions of people enjoy their coffee. That is what we should keep on doing."

NESPRESSO

Portioned Coffee

In 2017 Nespresso was a pioneer firm and global leader in the portioned coffee market. Beginnings are never easy, and it took several years to see any profit. Exhibit 1 shows a timeline of Nespresso's history.

Jean-Marc explained:

"Some 30 years ago, Nespresso was a pioneer in the portioned coffee market. Nowadays, the company is still a trendsetter for innovation and quality, and it still creates demand within the segment. Our brand is still a reference and preference for coffee connoisseurs around the world."

For most of its history, sales at Nespresso grew at an annual average of 30 percent, with an estimated income of CHF 5,000 million in 2016, just over 5 percent of the total revenue of the company. Nestlé, as published in *Expansión*, in February 2016². This was still far from the CHF 14,500 million Nestlé sold with Nescafé, but some experts considered it would be the Nescafé of the 21st century. The business had higher margins than instant coffee and was growing at a faster pace, although, according to some investment bank, like the Jefferies, it did not reach the 20 percent growth it had had a few years ago³. Also, Nestlé had launched Nescafé Dolce Gusto, which resembled the Nespresso concept.

The coffee pod market was around EUR 13,450 million, it was the most dynamic and fastest growing segment in the global coffee market, and the trend seemed to remain positive. In Exhibit 2 you can see some graphs in this regard. Some estimates by Reuters predicted that, within a decade, capsule coffee would be the main segment of the global coffee market. In Jean-Marc's words, Nespresso had the best model to remain in its leading position:

² Nespresso fights its rivals in the market and justice

³ Nespresso did not publish economic figures, beyond the consolidation in Nestlé's annual accounts.

“Our passion for quality and for exceeding our customers’ changing expectations has been the driving force behind our sustained growth. In 2017, we once again proved the strength of our business model by offering a solid growth worldwide.”

According to the general opinion in the industry and the experts, Nespresso was one of Nestlé’s most profitable and fastest growing business units, and one of the multimillionaire brands with which Nestlé made 70 percent of its sales, as you can observe in Exhibit 3. Moreover, as it was known by experts and the sector, its EBIT margin was way higher than the company’s average of 15 percent. This high profitability appealed to many competitors, and new ones appeared, apparently not discouraged by almost 2,000 patents in 2017. That year there was talk not only of pods that were compatible with Nespresso but also of devices by other brands that were compatible with Nespresso capsules. According to some analysts and pundits, Nespresso and its senior management needed to pay closer attention to those short-term issues.

Nespresso sold millions of capsules each year. The EBIT of the same, (with approximately 5 grams of ground coffee and an average sale price of between 0.5 and 0.57 Swiss francs per unit⁴, depending on the type), was estimated to be nearly 40 percent more than that doubled the average of the Nestlé Group, according to an article in the Financial Times⁵. The price of the Nespresso capsules was totally linked to the quality of the coffee. Nespresso selected the best beans from the finest coffee producing regions. It was coffee of the highest quality, according to experts, thus fulfilling the requirements of flavor and aroma. They also offered personalized services that adapted to the way of life of the moment and the preferences of their consumers. The evolution of Nespresso capsule varieties is shown in Exhibit 4. In 2017 the Nespresso assortment was 23 varieties of "grand cru"⁶ for home consumption, 11 for HORECA channel and 16 for the new Vertuoline range.

Innovation for Nespresso was key. Patrice Bula, vice president of Nestlé in charge of Nespresso, said: *"We want to be one step ahead [of the rest]. We do not want to be fighting in the trenches."*

Competitors

The first competitors Nespresso had to face in the portioned coffee market had patented their own systems. Among the first were Senseo – developed by Philips for Sara Lee’s European division (in 2015, JDE, specialized in coffee, a joint venture of Mondelez and Master Blenders), – and Keurig’s Green Mountain system in the United States.

⁴ These prices are those of capsules marketed in Switzerland. The prices varied according to the countries.

⁵ “US Coffee trend bodes ill for growers”. Financial Times, 21st July, 2015

⁶ Grand crus is a concept born in the world of wine to refer to high quality wine: "great soup". In the case of Nespresso it is used to refer to the great Nespresso coffees.