

## Cashing in on the booming market for dietary supplements



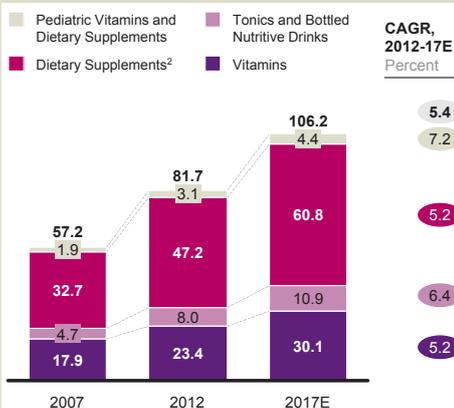
By Warren Teichner and Megan Lesko

George Bernard Shaw once said: “Give a man health and a course to steer, and he’ll never stop to trouble about whether he’s happy or not.” Around the world, more and more people are realizing the value of good health, fueling rising interest in all the things that promote it. As populations in the U.S., Europe and Japan age, more and more people are looking for remedies to cure what ails them and elixirs to help them stay healthy well into their twilight years. Health is not just a goal. It is both a lifestyle choice and a thriving consumer market.

Over the last decade, sales of vitamins, minerals, and nutritional and herbal supplements (VMHS) have surged and many new companies have entered the space. Globally, the market is now valued at \$82 billion, with roughly 28 percent of that in the U.S., where sales increased by approximately \$6 billion between 2007 and 2012. Growth is expected to remain strong through 2017 – between 5 and 6 percent a year both globally and in the U.S.

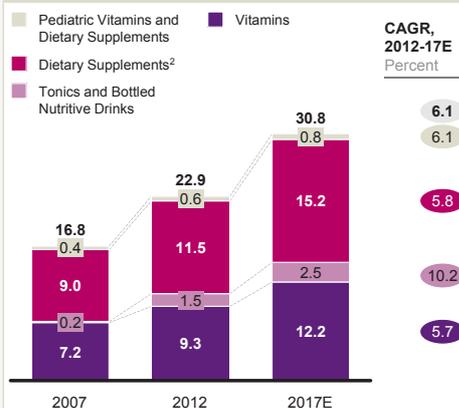
Exhibit 1:  
VMS segment overview

### Global Vitamin, Mineral and Supplement market<sup>1</sup>



Source: Euromonitor  
1. Market size based on retailer sales  
2. Includes herbal and combination dietary supplements

### US Vitamin, Mineral and Supplement market<sup>1</sup>



Source: Euromonitor  
1. Market size based on retailer sales  
2. Includes herbal and combination dietary supplements

Source: Euromonitor, team analysis

## *What's behind this growth?*

There are five important factors driving an increased interest in healthy living and the various products associated with it. Although the phenomenon is global, this article focuses primarily on the characteristics of the U.S. market.

### **1. An aging population**

Much has been made of the way that the aging of baby boomers will transform the U.S. economy. Their sheer numbers will shift spending in healthcare and realign markets, creating considerable new opportunities. The phenomenon is already visible in the vitamin and dietary supplement business, where purchases have grown by 6 percent annually from 2007-2012, much of this coming from eye, bone and joint supplements. As of 2012, consumers 65 and older accounted for 36 percent of U.S. VMHS sales<sup>1</sup>, a trend that is expected to continue for the foreseeable future.

### **2. Increased consumer awareness for preventative healthcare**

A quick look at magazine stands, TV lineups and news articles reveals that many Americans have an almost insatiable appetite for information pertaining to preventative healthcare. Celebrity doctors like Dr. Oz and Dr. Sanjay Gupta, online forums like [bodybuilding.com](http://bodybuilding.com) and [Livestrong.com](http://Livestrong.com), and magazines like Shape, Fit, and Men's Health all regularly dispense both diet and lifestyle advice and offer details about new products. This barrage of information has been a key driver for consumer purchasing.

Also driving heightened consumer awareness has been the efforts of VMHS manufacturers, which have increased their marketing efforts aimed directly at consumers. Such marketing focuses on new product innovation and the enhanced effectiveness and safety of products, and it has successfully influenced a wide range of consumers at multiple touch points and given increased credibility to the role VMHS can play in contributing to preventative healthcare.

### **3. The rise of the self-directed consumer**

Gone are the days when primary care doctors gave patients all the answers. Consumers are increasingly relying on alternative channels to self-diagnose and to identify targeted health needs. This is partly driven by the fact that insurers are increasing co-pays and thus incentivizing their customers to take preventative care measures. Today, 96 percent of internet-using adults have used online health information to help them make decisions throughout all parts of the health journey (pre-diagnosis, diagnosis and treatment).<sup>2</sup> A majority of people consult the internet both before and after their visits to doctors, to both inform their conversations with their physicians and validate medical advice after consultations.

This trend has benefited VMHS manufacturers because many supplement purchases are the result of consumers taking their health into their own hands, not the direct advice of a doctor. VMHS manufacturers have encouraged this self-directed behavior by improving their education and marketing efforts, and targeting consumers both on and off-line. Additionally, as consumers become more educated, they are increasingly interested in personalized VMHS solutions and are leveraging online tools provided by retailers and manufacturers to create a personalized regimen.

### **4. Channel proliferation**

VMHS manufacturers are highly fragmented and are accessing new sales channels to reach a diverse and broad set of customers. The leading manufacturer Living Essentials, for instance, maintains only 7 percent market share, and the top five branded manufacturers together hold less than a 25 percent market share. Private label accounts for 10 percent of sales<sup>3</sup>. Such fragmentation is the result of a general lack of brand awareness and an absence of consumer loyalty within the category.

The highest concentration of VMHS sales are in super/hyper markets, with online stores and specialty retailers such as GNC following closely behind. As they've grown in popularity due to their perceived higher product quality and private label options, specialty retailers have contributed significantly to channel proliferation. Internet sales have experienced significant growth over the past five years

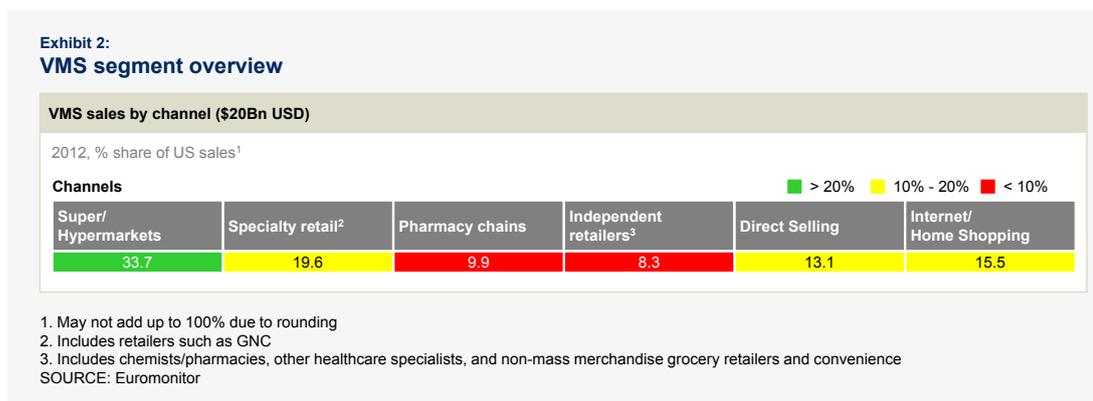
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1 Euromonitor, 2012

2 Harris poll, 2010

3 Euromonitor, 2012

(17 percent CAGR 2007-2012), a trend that is expected to continue as consumers become more familiar with the category and leverage the convenience of online shopping for repeat purchases.



## 5. A shift from ingredient focused messaging to broader brand positioning

Historically, VMHS marketing has been focused on promoting a specific ingredient that addresses a consumer health need – e.g. omega 3 for heart health or lutein for eye support. This emphasis created a market in which products were commoditized and consumers had difficulty differentiating between brands. To combat this, marketers have recently begun to tailor their consumer messaging to include a focus on a holistic benefit platform, in the hopes of encouraging usage of a broader array of products.

One manufacturer’s family of preventative eye health solutions and General Mills’ heart healthy cereals are prime examples of this growing trend. Through targeted marketing efforts, these companies have successfully created a need and sold a benefit oriented solution to consumers. VMHS manufacturers are also using the benefit platform as a way of achieving a differentiated, premium positioning in the marketplace, appealing, for instance, to expectant mothers, heart health, 60+ men, or other specific consumer segments. The resulting expanded suite of product offerings has been a primary driver of growth within the category.

### *Trends that will shape the VMHS market in the future*

We anticipate that, over the next five years, there will be five phenomena influencing the VMHS category that manufacturers will need to understand in order to thrive in this dynamic market:

#### **1. Private label as an attractive alternative to national, branded VMHS products**

As branded product recalls continue to occur and more purchase decisions are based on specific needs (e.g. joint health), consumers’ comfort with private label substitutes gains in strength. Retailers like Walmart and Costco are also fueling the trend by continuing to enhance their own private label offerings through new branding and formulations, improved packaging, and in-store consumer education. Many retailers are also now positioning their store brands as “lifestyle brands,” in an attempt to set them apart and build loyalty with customers. Safeway, for instance, has publicly stated that in ten years it will no longer be a grocery store selling wellness products. Rather it will be a wellness store selling food, with the Safeway brand leading the change. Given the attractive margins and consumer loyalty that private label VMHS brands can garner, retailers are likely to continue investing in these products, further fueling their growth.

#### **2. E-commerce growth**

Despite VMHS being a relatively difficult category for consumers to shop for online without prior product knowledge, online sales have experienced a dramatic increase over the last five years. The primary driver of this has been retailers’ focused efforts on improving the online shopping experience through better online education and targeted marketing. This has increased the comfort level consumers have for buying this category online. Amazon, for instance, recently launched a site dedicated to products appropriate for the 50+ demographic, one that’s easy to shop for by need state. Competing with Amazon are a variety of start-ups and established players (e.g., vitacost.com) who are creating a meaningful online presence as a specialty VMHS destination. Many sites now have live chat

options to help instantly address the sorts of specific consumer questions that were previously a barrier to online purchases.

Another key growth driver of online sales is the increased interest in Eastern health and wellness products. As the alternative medicine trend continues to grow it is likely that demand for Eastern medicine products will accelerate, especially among younger consumers. Easy and convenient online access to these products will help companies leverage this growth opportunity.

The final growth driver is the increasing number of personalized online VMHS systems available to consumers free of charge. Both manufacturers and retailers are beginning to offer free access to “wellness tools” that create a customized VMHS list based on a consumer’s specific conditions and needs (e.g. GNC’s online interactive vitamin guide that designs a customized supplement plan).

### **3. Volatility will remain as health fads come in and out of vogue**

Health-conscious media celebrities such as Dr. Oz, Deepak Chopra and Jillian Michaels have always had a major impact on VMHS sales because consumers trust their advice. They are responsible for driving specific product fads and there is no reason to expect that their influence will wane going forward. While aggregate industry revenues will remain stable, thanks to the diversity of products in the VMHS category, individual manufacturers will need to anticipate the ebbs and flows of easily-influenced consumers. Additionally, as personalities continue to drive trends, manufacturers will need to compete with the celebrity factor by finding new, creative ways to get consumers’ attention.

### **4. Increase in M&A activity and enhanced category sophistication**

The high level of fragmentation within the VMHS category makes it a prime candidate for mergers and acquisitions. Within the last three years, we have seen pure play companies, such as New Chapter, NBTY and Alacer, get acquired by large firms who are eager to deepen or broaden their category presence. Both pharmaceutical companies and consumer packaged goods (CPG) makers have publically committed to expand their consumer health division, suggesting that the acquisition trend in the space will continue. Non-traditional players are also beginning to explore the category as a possible source of incremental growth.

CPG expansion into the VMHS space will likely enhance overall category sophistication as these companies are more likely than traditional VMHS players to find new ways to innovate in both delivery and packaging. Large CPG companies will bring marketing expertise, category management best practices and deep consumer insights that will successfully align products with consumer trends and needs. This will further accelerate the awareness of the VMHS category among a wide range of consumers, contributing to additional sales.

### **5. Regulatory pressures will continue to increase**

Continued growth of the VMHS category will be coupled with increased oversight and a tightening of regulations around manufacturing, product safety and efficacy claims. Over the past year, there has been a noted increase in FDA enforcement actions pertaining to food and dietary supplement labeling violations. Manufacturers will need to be more careful with the language they chose to put on labels to avoid making either implied nutrient content claims or efficacy/health benefit claims. Tighter regulations will also be applied to manufacturing processes and practices in order to help ensure quality and safety in light of recent recalls. Between 2004 and 2012, more than half of all Class 1 recalls by the FDA were dietary supplements. Sexual enhancement, bodybuilding and weight loss products were the top three problem categories.

There has also been an increased focus in the last few years on potential FDA bans of certain vitamins and supplements that may be harmful, such as a form of vitamin B6 and certain energy supplements. An increasing number of clinical research trials are being done to test the efficacy and long term health benefits of taking vitamins, some of which have suggested that large doses of certain vitamins may actually increase the risk of cardiac events in elderly people or those with heart disease. While tighter regulations will add a new measure of complexity for manufacturers, it will also provide an opportunity for the good actors to shape the market. Major players should proactively work with regulatory bodies to help set a more stringent bar for supplements. Such regulatory changes and industry-government cooperation will ultimately engender greater consumer confidence in the safety and efficacy of VMHS products, thus benefiting the overall market.

### *In summary*

Strong category growth is expected to continue amid both increased consumer interest in health and retailers' efforts to position themselves as one-stop health and wellness destinations. Manufacturers will need to closely watch regulatory shifts and adjust accordingly in order to avoid consumer backlash or supply disruption due to product quality concerns. Yet taking on these challenges is well worth it. The expansion of the VMHS space throughout the next decade offers a unique opportunity for retailers and manufacturers to capitalize on a robust growth sector.

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