Chapter 3

ABOUT F.M.C.G. INDUSTRY

After reviewing the related studies in the Chapter II, an attempt is made to collect and present the information regarding present trends of FMCG industry in Indian scenario. It is believed that the attempt will deepen the understanding of FMCG Industry in India.

- Introduction
- Accelerating Premiumization
- Growth Prospects of F.M.C.G. in Rural India
- Evolving Categories
- Future Growth
- Future Trends in Modern Trade
- Eco-consciousness
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3.1 Introduction

Products which have a quick turnover, and relatively low cost are known as Fast Moving Consumer Goods (F.M.C.G.). F.M.C.G. products are those that get replaced within a year. Examples of F.M.C.G. generally include a wide range of frequently purchased consumer products such as toiletries, soap, cosmetics, tooth cleaning products, shaving products and detergents, as well as other non-durables such as glassware, bulbs, batteries, paper products, and plastic goods. F.M.C.G. may also include pharmaceuticals, consumer electronics, packaged food products, soft drinks, tissue paper, and chocolate bars. India’s F.M.C.G. sector is the fourth largest sector in the economy and creates employment for more than three million people in downstream activities.

The Indian FMCG industry at INR 1300 billion (in FY2010) accounts for 2.2 per cent of the GDP of the country. Given the inherently essential nature of the products, the sector is more or less immune to recessionary pressures. The last decade has seen the sector grow by 11 per cent annually. Robust GDP growth, opening up of rural markets, increased income in rural areas, growing urbanization along with evolving consumer lifestyles and buying behaviors have all been drivers of this growth.

Over the next decade, all the above drivers are expected to continue to impact the industry favorably. Based on discussions with industry experts as well as Booz & Company analysis, we believe that the FMCG industry will grow at a base rate of at least 12 per cent annually to become an INR 4000 billion industry by 2020. Additionally, if some of the factors play out favorably within an environment of enabling policy and easing of supply constraints, 17 per cent growth may be expected over the next decade, leading to an overall industry size of INR 6200 billion by 2020.
FMCG consumption is becoming more and more broad-based, and has reached an inflexion point where the growth can be expected to take off, following the traditional ‘S-shaped’ curve witnessed across many markets. While on an average, the growth of the industry will be strong, it will not be uniform. Variations are likely across product categories, companies and locations. Based on our research and extensive interviews, we have identified nine mega trends across consumers, markets, and environments which will shape the industry by 2020.

Figure 3.1

Historical Growth of the FMCG Industry

Source: AC Nielsen, news articles, Bost & Company analysis
3.2 Accelerating Premiumization

Continuous income growth coupled with an increased willingness to spend will push consumer up-trading and demand for higher priced, better quality (real or perceived) products.

Evolving Categories: Many consumers with rising economic status will shift from basic ‘need’ to ‘want’ based products. In addition, evolving lifestyle behavior and emphasis on beauty, health, and wellness will see increased requirements for customized and more relevant products.

Goldmine at BOP: A significant majority of the population in the country, especially in the rural markets, will become an important source of consumption by moving beyond the ‘survival’ mode. This bottom-of-the-pyramid (BOP) segment will require tailored products at highly affordable prices with the potential of very large volume supplies.

Rapid Globalization: While many leading foreign multinational companies (MNCs) have operated in the country for years, given liberal policies, the next decade will witness increased competition from Tier 2 and 3 global players. In addition, larger Indian companies will continue to seek opportunities internationally and also gain access to more global brands, products, and operating practices.

Many Indias: Despite the complexities of our language, culture, and distances, the Indian market has largely been seen as a homogenous market. Increased scale and spending power will demand more fragmented and customized business models (across products, branding and operating structures).

Growing Modern Trade: The share of modern trade will increase and may be expected to account for nearly 30 per cent of the total trade by 2020. This channel will compete
with existing traditional trade (approximately 8 million stores which will continue to grow) and offer both a distribution channel through its cash & carry model as well as other avenues to interact with the consumer.

**Eco-consciousness:** Global climatic changes, dwindling natural resources, and growing ecological awareness of consumers are increasing emphasis on environmental concerns. The pressure on companies to go green is growing due to the involvement of various stakeholders the government (through policy), the consumers (through brand choice).

**Game-changing Technologies:** Increased relevant functionality coupled with lower costs will enable technology deployment to drive significant benefits and allow companies to deal with complex business environments. This will be seen both in terms of efficiencies in the back-end processes (for example, supply chain and distribution) as well as in the front-end (for example, consumer marketing).

**Enabling Policies:** Many government policies under consideration, if executed, can help create a more suitable operating environment. This will help boost both demand and supply. Demand will go up because of increase in income levels and spread of education and supply will be augmented by removal of process bottlenecks and boost in infrastructure investments.

While some of the above trends can already be observed today, many are yet to break the existing paradigms. In addition, the confluence of many of these change drivers—consumers, technology, government policy, channel partners—will have a multiplier effect and magnify both the magnitude as well as the pace of change. As with any change that is disruptive in nature, there will be winners and losers.

This transition from a stable and homogenous operating model to a dynamic, unpredictable and rapidly changing operating model will have significant implications.
for the industry and its stakeholders. To excel in this new model one will need to enhance current capabilities and build new ones to bridge gaps. In this new setup, FMCG companies will have six imperatives from a business strategy perspective:

1. Disaggregating the operating model
2. Winning the talent wars
3. Bringing sustainability into the strategic agenda
4. Re-inventing marketing for consumers
5. Re-engineering supply chains
6. Partnering with modern trade

Stakeholders including government, retailers, NGOs, and investors will also need to play a key role in supporting the growth of the industry, while continuing to deliver on their core business and social mandates.

3.3 Growth Prospects of F.M.C.G. in Rural India

With the presence of 12.2% of the world population in the villages of India, the Indian rural F.M.C.G. market is something no one can overlook. Increased focus on farm sector will boost rural incomes, hence providing better growth prospects to the F.M.C.G. companies. Better infrastructure facilities will improve their supply chain. F.M.C.G. sector is also likely to benefit from growing demand in the market. Because of the low per capita consumption for almost all the products in the country, F.M.C.G. companies have immense possibilities for growth. And if the companies are able to change the mindset of the consumers, i.e. if they are able to take the consumers to branded products and offer new generation products, they would be able to generate higher growth in the near future. It is expected that the rural income will rise in future, boosting purchasing power in the
countryside. However, the demand in urban areas would be the key growth driver over the long term. Also, increase in the urban population, along with increase in income levels and the availability of new categories, would help the urban areas maintain their position in terms of consumption. At present, urban India accounts for 66% of total F.M.C.G. consumption, with rural India accounting for the remaining 34%. However, rural India accounts for more than 40% consumption in major F.M.C.G. categories such as personal care, fabric care, and hot beverages. In urban areas, home and personal care category, including skin care, household care and feminine hygiene, will keep growing at relatively attractive rates. Within the foods segment, it is estimated that processed foods, bakery, and dairy are long-term growth categories in both rural and urban areas.

Figure 3.2
3.4 Motivation for the Purchase

The motivation for buying premium products varies with consumer income. The rich are willing to buy premium products for their ‘emotional value’ and ‘exclusive feel’, and their behavior is very close to consumers in developed economies. They are well-informed about various product options, and want to buy products which suit their style. The upper middle class wants to emulate the rich and trade up towards higher-priced products which offer greater functional benefits and experience compared to products for mass consumption. Such products are often referred to as ‘masstige’ products.

The rising income of Indian consumers has accelerated this trend towards ‘premiumization’ or consumer up-trading. The improved purchasing power of Indian consumers is supported by greater workforce participation among women and an increasingly younger earning population with higher consumer willingness to spend on lifestyle products. These factors will gradually combine to give considerable push to premiumization in the future, making it more pronounced as compared to the last decade. The premiumization trend can be observed prominently in the top two income groups mentioned already, the rich with an annual income exceeding INR 1 million, and the upper middle class with an annual income ranging between INR 500 thousand and INR 1 million. While these two income groups account for only three per cent of the population currently, it is expected that by 2020 their numbers will double to constitute seven per cent of the total population.

By 2020 these groups will constitute large enough numbers to merit a dedicated business strategy that FMCG companies will do well to adopt and follow. As per estimates, the ‘Rich’ will grow to approximately 30 million people in 2020, which is more than the
current total population of Sweden, Norway and Finland put together! Similarly, the ‘Upper Middles’ will be a population of about 70 million in 2020, which is more than the current population of the UK.

The Indian population is also quite young compared to those in developed economies. People in the age group of 15-44 comprise approximately 60 per cent of the population. There are multiple ways in which the burgeoning younger population is supporting premiumization. First, the profile of the young population reveals more actively employed people. This means, increased incomes available in households to spend on expendables. Second, young people tend to spend more compared to their parents and grandparents, and are easily attracted towards ‘high-end’ products. Third, they are more exposed to the media and its influences, specifically new platforms such as the internet, mobile phones etc. Their awareness levels are higher, and they are better informed about developments around them. Continued favorable age distribution is a driver for premiumization in the future as well. There are several examples of consumers up-trading to more premium products, as well as FMCG companies launching various products to capture the premium market:
3.5 Evolving Categories

There are three ways in which a category can evolve. First, as consumers’ needs change, they start purchasing more evolved and sophisticated products within a category, hence, the product offering must also transform to keep pace with demand trends. For instance, consumers have moved from toothpowders to toothpastes and are now also demanding mouth-wash within the same product category.

**Increased Product Variety**

Consumers are increasingly demanding customized products which are suited to their individual needs. Micro-segmentation for product development and mass-customization for identifying different product variants is already underway. For instance, a decade ago, only a limited variety of products such as shampoos was available within a particular brand. Now most large players have launched many variants in accordance with hair types (oily / dry / normal), the seasons in which these can be used (winters / summers) as well as consumer categories, targeted separately at men, women, and
children. P&G’s Head brand which started with two variants in 1997 now boasts 11 variants to choose from. Mass-customization in India will intensify in the future with FMCG players profiling the potential buyer by age, region, personal attributes, skin type, ethnic background, and professional choices. Micro-segmentation will amplify the need for highly customized market research so as to capture the specific needs of the consumer segment targeted, before the actual product design phase gets underway.

3.6 Growing Modern Trade

No strategic exercise is complete without a business strategy for the retail sector, as the FMCG industry depends on retail for consumer sales. While India’s retail sector has been growing at over 7 per cent annually, a large proportion of it is unorganized retail in the form of scattered Also, volume per retail store is very low. However, modern trade or organized retail has created a concentrated (high volume)channel for distribution by FMCG players. Second, the share of some consumer product categories such as processed food and beverages is also expected to grow rapidly within organized retail, which makes the latter a very crucial contributor to the industry.

Modern trade is still at a nascent stage in India; the share of modern trade in retail last year was only about five per cent. However, it has been growing very rapidly displaying approximately 25 per cent annual growth.

Several formats exist within modern trade and organized retail, such as, hyper marts, supermarkets, and cash-and-carry (which is essentially organized wholesaling). While super-markets have the highest share in terms of the number of stores (approximately 85 per cent of total modern trade stores in 2009), hyper marts account for the highest area (approximately 70 per cent of the total area under modern trade). Cash-and-carry is still
nascent with only about eight stores in 2009. In a large and growing market such as India, we expect existing formats to evolve and new formats to come up in the future, driving the growth of various FMCG categories.

Local Indian players have been experimenting with different business models with mixed success. The Future Group is one of the prominent players in this space and operates more than 1000 stores with different formats such as Big Bazaar (hypermarket), Food Bazaar (supermarket), Central (urban mall), futurebazaar.com (online shopping portal), hometown (home furnishings), and Aadhar (rural retailing).

The economic slowdown dented the growth of organized retail during 2008 and 2009. Lower footfalls resulted in lower sales growth and margins contracted as retail expansion had been financed through debt and the interest rates were now rising. There were also increasing funding constraints. However, growth has picked up again and expansion plans are now being announced.

Figure 3.4
3.7 Future Growth

Modern trade is expected to grow very rapidly in the future with its share in total retail projected to reach 11 per cent by 2014 and 30 per cent by 2020. This growth will be supported by:

**High economic growth**: GDP is expected to grow at 8-10 per cent in the future, boosting growth in all sectors.

**Increasing incomes**: Incomes are expected to continue to rise which should further drive convenience shopping.

**Increasing urbanization**: Organized retail will continue to increase presence in Tier 1 and Tier 2 cities, which are growing faster than metros.

**Improving infrastructure**: The government is increasing its thrust on improving infrastructure. A recent example is the construction of the Golden Quadrilateral, a dedicated freight corridor which will result in improved supply chain efficiencies.

3.8 Future Trends in Modern Trade

Organized retailers are going to be increasingly interested in reducing time-to-market. To achieve this, it will be important to invest in inventory management and related technology for capturing sales data, forecasting demand and generating automatic replenishment. Decreasing inventory levels will also require strong backward integration with distributors or manufacturers. Retailers will also need to optimize logistics further in terms of warehousing and transportation etc. For this it will be imperative to increase supplier collaborations.
Emergence of Private Labels: Private labels or products manufactured and marketed by retailers have been growing in India as they are very attractive to retailers for three reasons:

1) They help retailers to improve profitability as the margins for private labels are higher (30-35 per cent on average) compared to the manufacturer’s brands.

2) They help retailers to create differentiation between competitors as they are unique to their stores.

3) The emergence of retailing as a specialist function and the growth of multiple retailing have helped retailers push manufacturers towards greater margins.

Experience has shown that the retailers who most consistently exceed expectations are rewarded with higher average sales, more repeat business, and invaluable goodwill. All these are critical stepping stones on the journey to sustainable loyalty. Further, penetration by private labels in India is quite low compared to other developed countries. Due to all these factors, it is expected that private labels will become a major threat to FMCG players in the future.
3.9 Eco-Consciousness

What makes sustainable business practices essential? Increased eco-sustainability of business will be extremely important for FMCG companies in the future. Global climatic changes and the growing scarcity of natural resources have already led to increased concerns about the environment. The pressure on companies from key stakeholders to be environmentally responsible is gradually on the rise. Various stakeholder responses to eco-concerns are showcased below.

**Consumers:** Concern for the environment has changed the purchasing behavior of consumers. An Edelman survey of 6000 global consumers conducted between August and October, 2008 found that 87 per cent believed it was their ‘duty’ to contribute to a better environment. Becoming increasingly vocal in their protests against companies which have been polluting the environment or not engaging in judicious use of resources. Some NGOs routinely monitor and track the CSR efforts of FMCG companies in India, driving awareness and importance of such initiatives

**Competitors:** Some FMCG companies have started pioneering ‘sustainability’ efforts. For example ITC has been publishing an annual report on sustainability and has also conducted sustainability audit of businesses and subsidiaries. HUL has been focusing on ensuring sustainable practices in business. Nestle has initiated pollution-free waste disposal at manufacturing plants, while Dabur has been focusing on reducing energy consumption, increasing renewable energy and plans to become carbon positive in the next few years. Such measures are forcing other players to also involve themselves considerably in driving green practices.
Channels: Some of the global modern trade players have mandated sustainability requirements from their suppliers. Wal-Mart has been at the forefront of such initiatives. Such practices will soon be implemented in emerging markets like India.

Investors: Foreign investors have also been driving the sustainability agenda in the companies they invest in by benchmarking with global practices. Some of the top sustainability issues worldwide have also been identified for the FMCG industry in India. The most important of these are packaging, water-use, harmful emissions and the impact of products on health. These have been detailed below:

Packaging: Primary and secondary packaging costs typically constitute approximately 8-10 per cent of the total cost base for most FMCG players. A significant proportion of packaging is polymer-based and non-biodegradable. It has been observed that for essential commodities such as milk, the packaging issue is not given much importance by the consumers or regulators; while for products such as snacks, packaging sustainability has attracted more attention. Hence, FMCG players should take a closer look at their packaging cost-base and try to eliminate or reduce the quantity of packaging material used and upgrade to bio-degradable packaging materials.

Harmful Emissions: This is a problem area for FMCGs given these are logistics-intensive businesses that also release greenhouse gases during their manufacturing processes. Since fuel scarcity in the future is likely and transportation is a major GHG culprit, companies should strive to make transportation more efficient and encourage usage of renewable energy through use of hybrid vehicles for transportation.

Water Utilization: With depleting groundwater and scarcity of fresh water, FMCG companies should resort to water-efficient technologies during manufacturing, and recycle used water.
Health impact of products: This is a big concern for both consumers and the government. It has been observed that increasingly, consumers are reading through the nutritional information on products, and becoming more conscious of the harmful impact of categories such as snacks and fast foods. The FMCG industry needs to lead by example in this case and shift towards healthier products.

Others: FMCG players should partner with suppliers which provide green (organic) raw materials, drive the usage of renewable energy sources and more energy efficient technologies such as CFL for lighting up offices and factories.

3.10 FMCG Roadmap to 2020

FMCG industry may grow at a base rate of at least 12 per cent annually to become INR 4000 billion industries in 2020. Additionally, if some of the positive factors play out favorably, it could even record a 17 per cent growth over the next decade, leading to an overall industry size of INR 6200 billion by 2020. These growth rates, however, depend on varying economic scenarios. Base Case models an ‘As-Is’ scenario where the key assumptions are that GDP growth will continue at the same pace (of about 7 per cent) in the next decade and there will be no major change in regulations.

Optimistic Case models a 'Transformation' scenario where key assumptions are that GDP growth will touch 9 per cent in the next decade, and favorable changes in regulations (such as FDI in multi-brand retailing or rolling-out of the GST) will unlock industry potential.

While the overall growth rates may be anticipated to lie in the 12-17 per cent range, many product categories are likely to grow much faster as consumer incomes increase, behaviors evolve and requirements change. In some areas one would expect Indian FMCGs to
follow well-established growth-evolution paths. However, in many product categories growth may be accelerated by the explosive economic rise, young consumer base and the influence of the ubiquitous media. Some of that impact is already evident in a category like liquid hand-wash which has shown very strong growth driven by increased consumer awareness around personal hygiene specifically for children.

Given the nascent stage of development across many categories even supply-led actions can help trigger rapid growth. For example, many packaged food categories (such as soups, breakfast cereals, and fruit juices) have seen rapid growth rates driven by increased presence of modern trade.

Evolutions in other markets and discussions with industry experts and practitioners helped identify nine key forces that will change the face of the industry over the next ten years. These trends may be categorized into three broad groups, based on their origins or sources. However, their impact will be freely felt across multiple stages of the industry value chain.

![Figure 3.6](image)

Figure 3.6

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3.10.1 Consumer-related Trends

Changing demographic profiles and evolving behavior significantly impact the way consumers consume and interact with products and services. Numerous and diverse consumers in India throw up an equally mind boggling diversity of consumption trends and patterns. At the same time, three prominent trends merit some discussion. The first one is increasing ‘premiumization’ which will see consumers trading up the price ladder in search of additional functionality or brand promise. Second, at the middle of the pyramid, the evolution of consumption behavior will be seen to lead to significant changes within and across product categories. And finally, many companies will find increasing value at the Bottom of the Pyramid (BOP) by serving products customized to specifically meet the requirements of this large market. It may be said that there will be significant scaling up at each step of the consumer income–pyramid to be able to justify independent commercialization of the business potential.

3.10.2 Market-related Trends: The separation to evolving geographical markets or channels for the FMCG players. The key trends within this segment will be the viability of sub-markets in India, growing organized retail and the increasing globalization of FMCG players. These players need to be conscious of such trends and adapt their products as well as go-to-market strategies as per their target markets.

3.10.3 Environment-related Trends: These are influenced by socio-political, legal, environmental and technological reprioritizing that is inevitable in a dynamic environment. Changing government policies, growing importance of sustainability, evolving media platforms and technology will compel FMCG players to adopt business strategies which keep the interests of communities and the environment in mind for inclusive development.