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## DISRUPTING FMCG CONSUMER BEHAVIOUR

Mapping the Impact of COVID-19 on Indian FMCG Market

The Strategy Boutique



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*Honest Consulting*

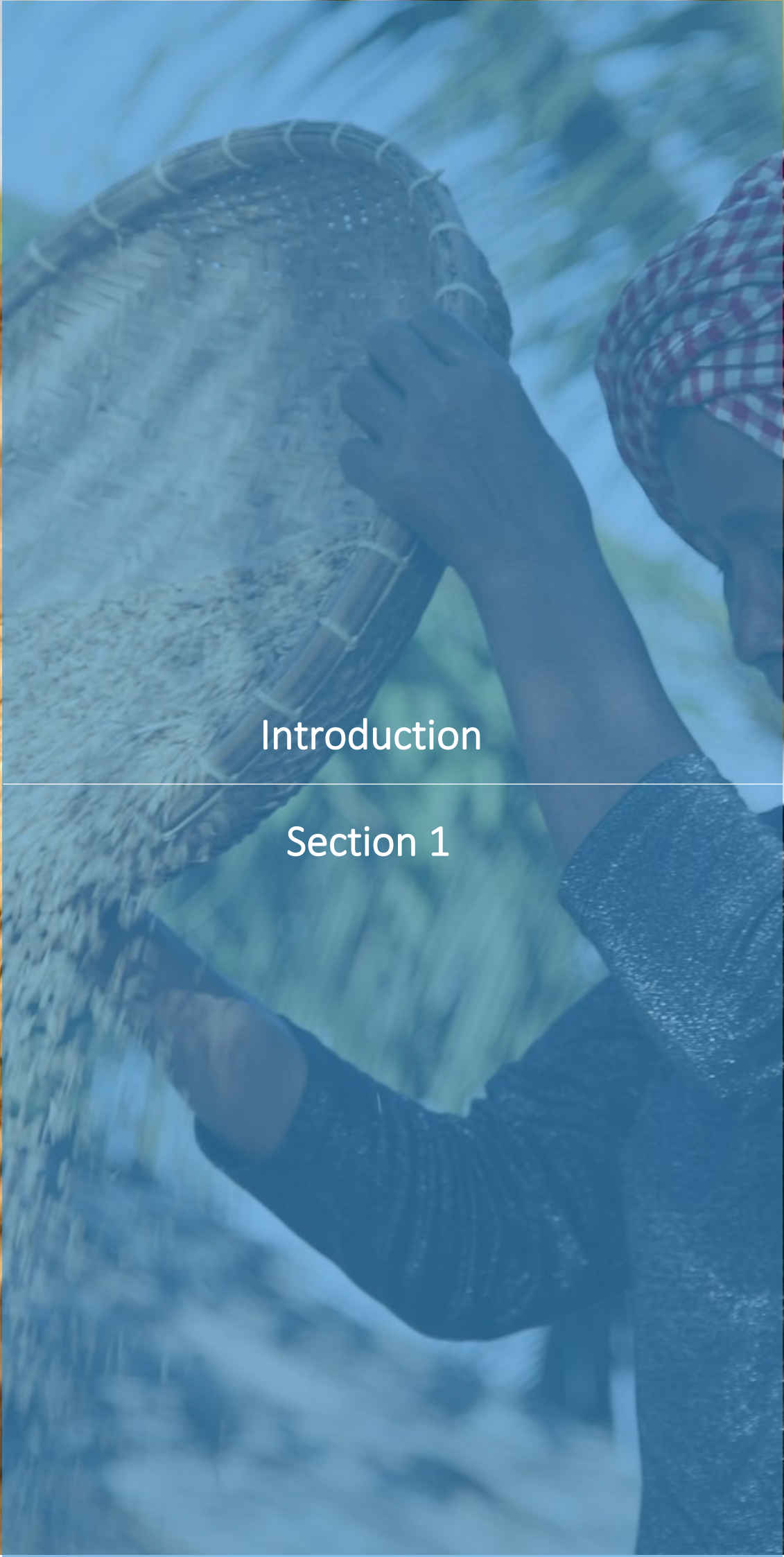


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# Table of Contents

1. Introduction.....	4
2. Indian Overview.....	6
2.1 Market Outlook.....	6
2.2 Market Segments.....	7
3. FMCG Retail Market.....	9
3.1 FMCG Retail.....	9
3.2 Organised and Unorganised Sectors .....	10
3.3 Impact of COVID-19.....	11
3.4 Online Retail.....	13
4. Consumer Behaviour.....	15
4.1 Impact on Consumption Patterns.....	15
4.2 FMCG Consumer Buying Disruptions .....	17
4.3 Way Forward.....	19



Introduction

Section 1

## 1. Introduction

Driven by changing lifestyles, easier access, rising income levels and growing needs the FMCG sector in India is the fourth largest sector in India. While the urban sector accounts for the largest revenue share, the rural sector is rapidly growing and along with semi-urban segments contributes 50% of total rural spending. With the onset of the pandemic the FMCG market rose by 7.1% driven by food items, health, hygiene and rural areas.

In this report, the focus is on FMCG retail market where changing dynamics of organized, unorganized, online and offline markets are considered in the sector. The organized sector composes of supermarkets and retail chains whereas the unorganized sector is largely composed of the neighborhood shops that cater to almost every Indian household.

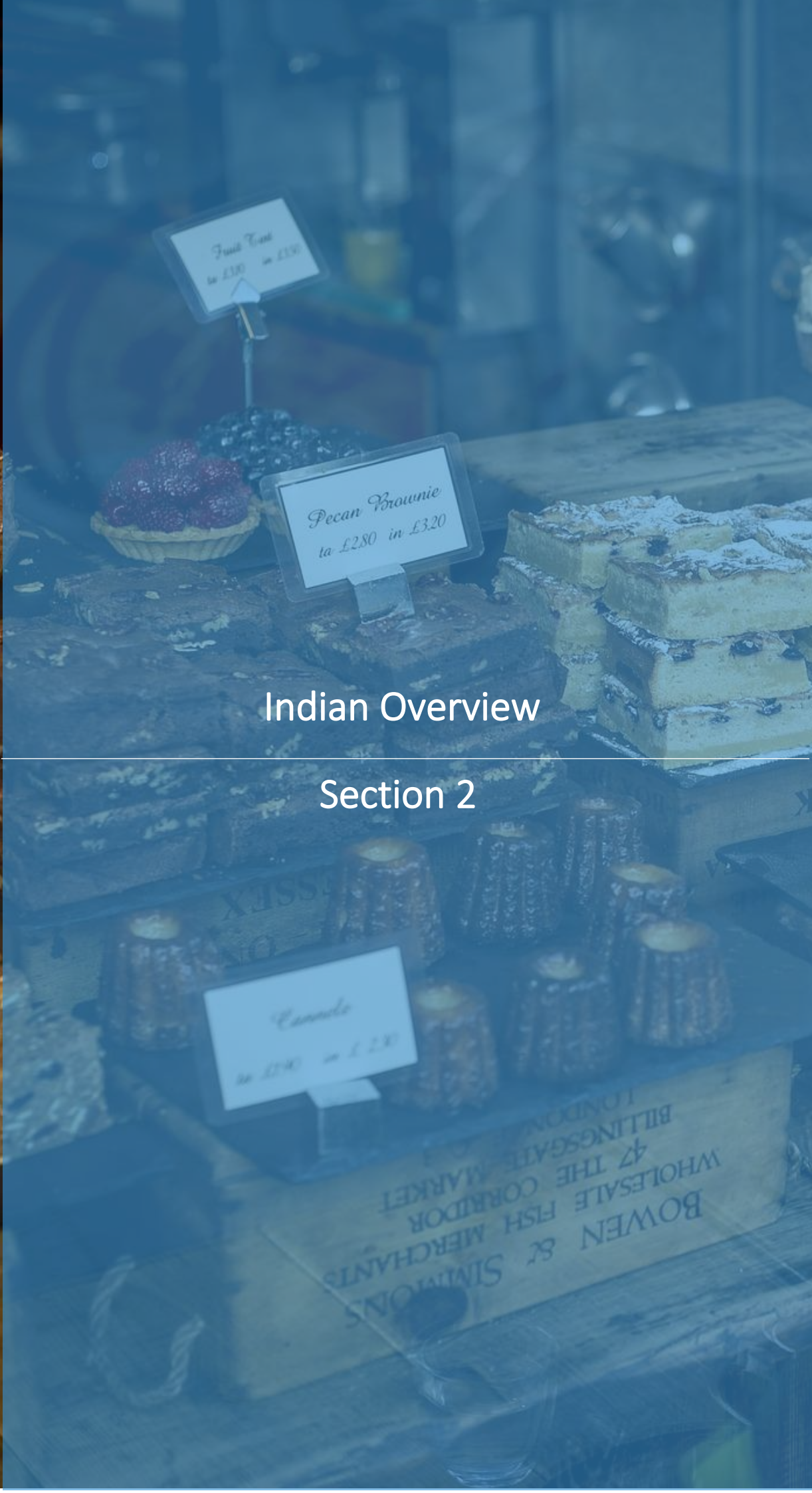
While the online markets are composed of traditional retailers with brick-and-mortar shops, the online retailers compose of the e-commerce platforms offering a wide range of products to its customers on their doorstep.

The pandemic brought about significant changes to the present dynamics of the four segments. Before the pandemic, only a few consumers were experimenting with e-commerce platforms for their FMCG needs that they otherwise fulfilled from their preferable offline shopping stop. With the onset of the pandemic and the frequent lockdowns and rising restrictions on commuting, people changed their shopping modes. While the organized sector through its supermarkets and retail chains had a setback as a result of supply chain disruptions and lockdowns, the unorganized sector formed by the kirana stores flourished. Similarly, e-commerce

platforms seemed to have satisfied a majority of consumers' needs with offline platforms becoming more and more inconvenient to reach unless they were the neighborhood stores. Thus, overall, the unorganized sector and e-commerce have emerged to be the most resilient during the pandemic. The incorporation of unorganized stores by the big e-commerce platforms like Amazon and Jio-Mart has also enabled the sustenance of the friendly neighborhood kirana stores we're all familiar with.

The pandemic has urged customers to take into consideration hygiene protocols, adopt digital solutions and change their buying behavior in response to the changing dynamics. The report analyses the impact of COVID-19 on the consumers in the FMCG market by modeling the decision-making process in the FMCG sector. The framework highlights the opportunity for disruptions in the decision-making process that has enabled the consumers in the market to adopt new modes of shopping and explore new brands. This presents an opportunity for all four segments to understand the changing consumer dynamics and enable growth. Whether the new habits formed as a result of the pandemic would sustain or the consumer behavior would tread back to old habits is yet to be known.

The first section looks at the FMCG market in India, followed by a deep-dive into the dynamics of the four segments, organized, unorganized, offline and online sectors. Finally, the report uncovers the changing dynamics of consumption behavior through decision making framework.



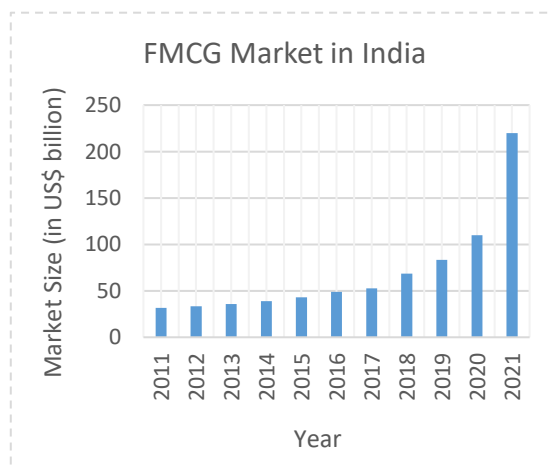
## Indian Overview

### Section 2

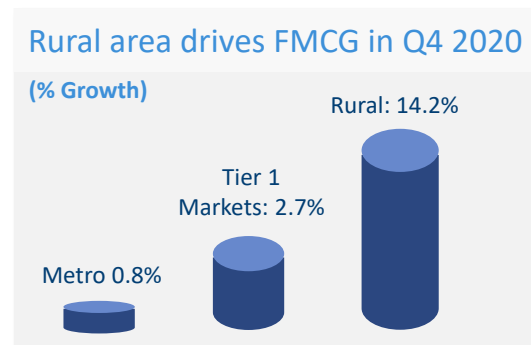
## 2.1 Market Outlook

As the fourth largest sector, the Fast-moving consumer goods (FMCG) industry has been experiencing consistently rising market growth and is expected to grow at a CAGR of 23.15% and record US\$ 103.70 billion in 2021. With a diverse range of products ranging from food and beverages to personal care, household care and other over-the-counter products, different companies dominate the various sub-sectors in the industry. Companies like Dabur, Colgate and Hindustan Unilever are among the top FMCG companies in the market.

Across India, it is composed of urban and rural areas, with urban accounting for 55% revenue share. While the urban area has spearheaded the FMCG sector, the improved distribution channels have allowed FMCG companies for a higher growth in rural areas than urban ones. Leading firms, like Dabur receive about 45% of their domestic revenue from the rural areas, as well as Hindustan Unilever, receiving 35% of their total revenue from rural areas. In response to the rising incomes and aspirations in rural India, consumption has increased owing to the increased demand for branded products.



Source: Nielsen Report



Source: IBEF

The FMCG sector in India plays a consequential role in defining the GDP, policy support measures such as the investment approval of up to 100% foreign equity in single brand retail and 51% in multi-brand retail along with the Union Government's production-linked incentive scheme (PLI) gives companies an opportunity to boost foreign investment and exports. A growing demand for the packaged food market and rising disposable income in rural India allows for an augmenting contribution by India to global consumption, which doubled in 2020 to 5.8%. Homegrown brands such as Patanjali and RP-Sanjiv Goenka Group are venturing into the international markets through set up of a 100% export-oriented manufacturing unit in Milan SEZ and creation of a venture capital fund of \$ 14.74 million to invest in FMCG startups, respectively. Moreover, the transforming Indian consumer sentiments of new age consumers characterized by high awareness, an affinity for health and

nutrition and growing expendable income boosts the FMCG industry further. These attitudinal shifts have contributed to the emergence of the market for organic food staples and gluten free products. The future outlook of the industry is supported by the growth of the pre-existing FMCG segments coupled with emergence of new sub-sectors.

## 2.2 Market Segments

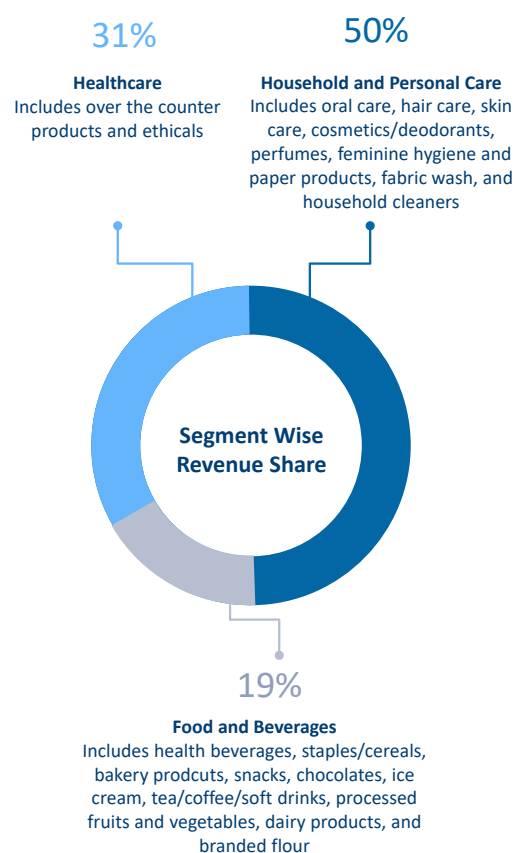
The FMCG market by type can be segmented into Food and Beverages, Household and Personal Care and Healthcare. The growth in the Food and Beverages segment has been fueled by changing preferences of the urban middle-class families. Moreover, India is the second largest producer of food, the food processing industry is among the top five industries in India comprising of production, consumption, export as well as expected growth. The food services sector composed of the QSRs, café outlets, retail outlets, lodging facilities, food services and others boosts through its growth the growth of the organized sector. A rising trend of private labelling has encouraged companies to focus on innovation across various categories across various price points to reach the diverse income groups. Emerging trends in the segment consist of a shift towards vegan and organic food, farm to table menus, emergence of gourmet street food brands, cloud kitchens and growing importance of community driven brands including craft breweries, artisan cafés.

Household care segment is a volume driven market with low margins and stiff competition. Rising household budgets has inspired the innovation of a diverse category of products in the sector. Personal care products include key categories of

bath, shower products, hair care, deodorants and such products. The penetration of the segment has been paced well as a result of the lower priced and smaller quantities of products offered.

In the healthcare segment, a rising awareness of preventative care is driving the growth of categories like nutraceuticals, vitamins and supplements for diet. Moreover, the impact of the pandemic on the segment is monumental with an increased demand for nutritional and preventative supplements as well as use of gloves and protective gears.

COVID-19 impact on each segment is contingent on the changing buying dynamics as a result of growing online retail and shifting consumer attitudes and their impact on each segment.



Source: IBEF



## FMCG Retail Market

### Section 3



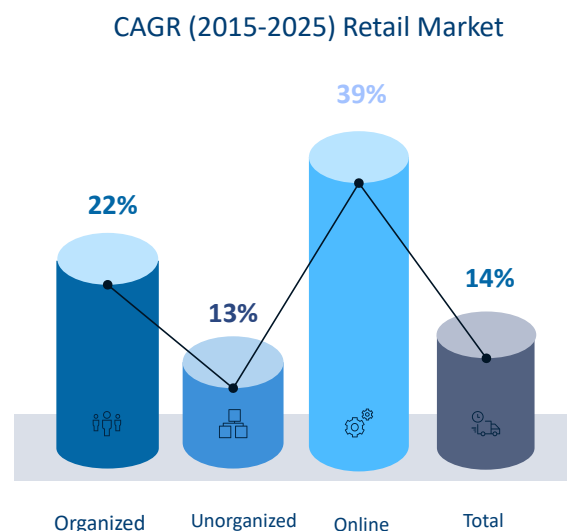
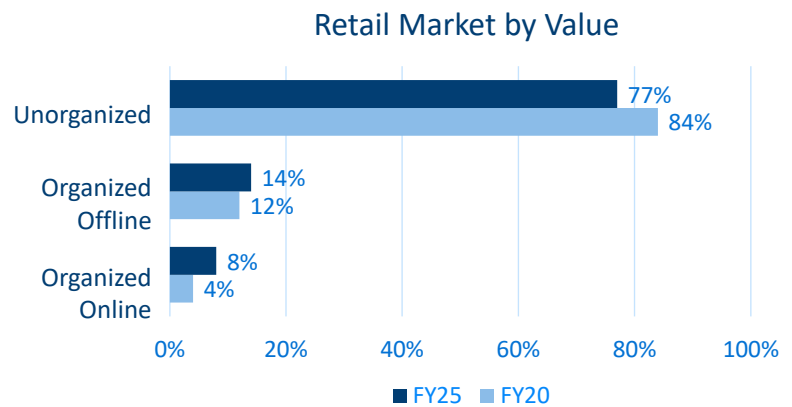
### 3.1 FMCG Retail

Manufacturing, distribution and retail form the key services under the FMCG Industry. A key feature defining the industry is the quickness in which the products vacate the shelf, highlighting the significance of quick restocking to avoid loss of sales opportunities for both manufacturers and retailers. The FMCG sectors can be broadly classified as organized and unorganized sectors.

The conventional FMCG value chain consists producers, distributors, wholesalers, semi-wholesalers, traditional and modern retailers. While modern retailer receives products directly from distributors or the producer and invest in their own warehousing and distribution, traditional retailers follow a lengthy and decentralized process of receiving goods.

Modern trade channels dominate in the developed nations, characterized by efficiently coordinated sales in an organized setting. Developing and underdeveloped nations rely heavily on general trade channels characterized by middlemen in unorganized markets. While the unorganized part forms a large share of the FMCG market, it is greatly influenced by economic fluctuations as characterized by its uniquely chaotic form. Unorganized markets consist of millions of small stores that are a part of relatively longer supply chains and localized middlemen. While the decentralized system seems inefficient, the inefficiencies can be surpassed by leveraging the expertise of the middlemen. In the FMCG category, unorganized sector covers over 90% of the market. There is 1 *kirana (corner shop)* for every 100 consumers and about 80% of these local shops are based in Tier 2 cities.

The organized sector forms a significantly smaller share in the FMCG space where traditional shops dominate. Yet with the transforming consumer attitudes and changing experiences, there is significant growth expected in the organized retail section in the span of 10 years 2015-2025. The organized sector itself is further characterized by online an offline point of sale.



### 3.2 Organized and Unorganized Sectors

India’s retail space is dominated by the unorganized sector consisting of Kirana stores. These act as the convenient neighborly shops that almost every Indian household relies on for some or all their household needs. The growth in the Indian retail market has been witnessed not only in terms of its size but also its sophistication. International retailers have been brought in growth augmenting investment whereas the domestic market is fueling with innovation. A rising retail market is a result of growing urbanization, middle class income groups, higher rate of urbanization and greater availability in rural regions. A driving trend for the organized sector’s growth in the Indian context is premiumization, rise in demand for premium products in apparel, food and durables. This is a result of rising consumer incomes and exposure to global brands. International brands like IKEA, Replay, Ted Baker, American Eagle Outfitters are all in the market now. India ranks among the top two countries in the Kearney’s 2019 Global Retail Development Index,

such that India performs well in terms of market attractiveness, country risk, market saturation as a way of inviting investment and development in the space that’s majorly dominated by the unorganized sector.

The unorganized sector includes stores that sell products ranging from clothes, footwear to groceries and electronics. These store owners have a regular customer base with home delivery and phone orders a common mode of purchase. On the other hand, the organized retail sector, also referred to as the modern retail, is a growing trend in India with Reliance Industries, Future Retail and DMart all competing for customers. The big supermarkets along with the mini-supermarkets that cater urban shoppers buying on a daily basis rather than once-a week purchase form about 12-15% of the total sales of consumer goods.



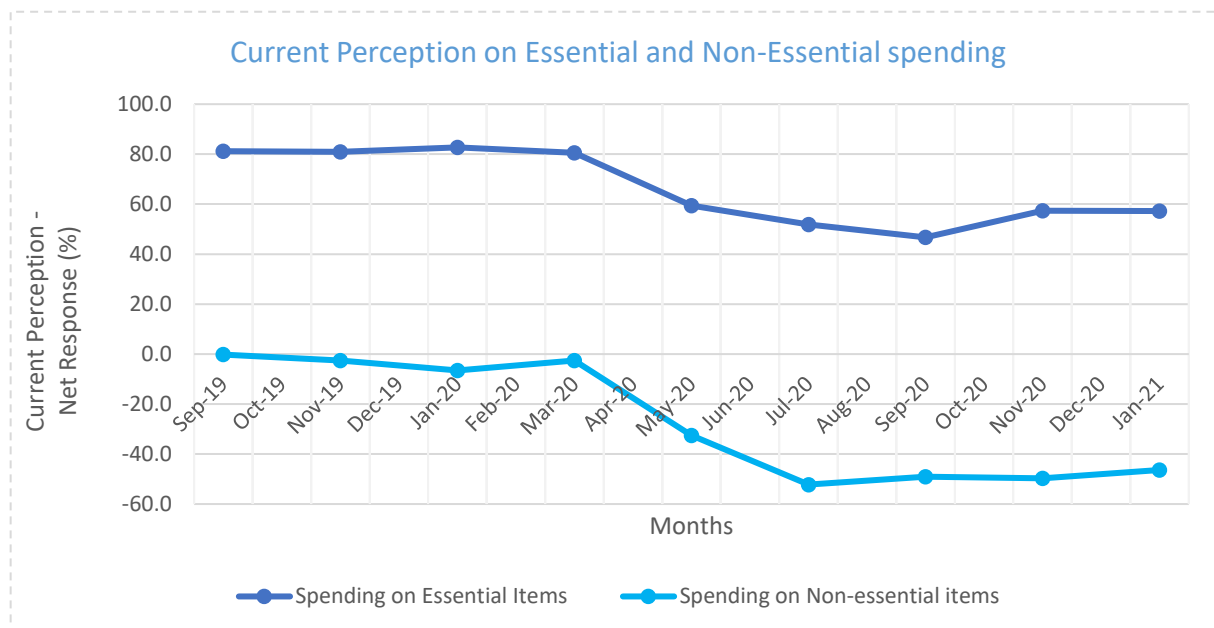
### 3.3 Impact of COVID-19

With the onset of the pandemic, the traditional and modern retail stores have been facing challenges in their business practices. Some retailers have been forced to shut their shops or curb operations to handle the blow of the pandemic. A major change in consumption patterns is the postponement of consumption of non-essential commodities by the consumers as they adapt to the grappling reality of job losses, pay cuts. For the segments in the FMCG space, this means there has been a blow to the personal care products, consumer durables, apparel whereas food and beverage, healthcare have fared better as consumer focus on essential needs. As a result of the local restrictions there have been production delays, store closures, reduced shipping and freight options.

1. **Falling business volumes** with lockdown restrictions. Businesses in the sector, especially in the Personal Care segment have been known to doing March/ year end sale. These seasonal sales have taken a hit with the pandemic.

2. Consumers are stressing more on spending on essential commodities with the fear of job loss, income losses and the adverse health effects of COVID-19. This has resulted in a consistent **fall in the consumer confidence** index. The figure below depicts the sudden drop in the perception of spending on both essential and non-essential commodities post the first nationwide lockdown in Mar 2020. It is evident that the decline in the perception about the spending on non-essential commodities is much more pronounced than the essential commodities.

3. A shift in favor to the unorganized sector through the **increase in demand from the neighborhood stores** has been witnessed. Consumers especially those in the middle-class groups have shown diminishing brand loyalty to their usual shopping areas where both their essential and non-essential needs were being met.



The commutation restrictions during lockdown encouraged consumers to make purchase from the nearby retailers.

4. Moreover, both unorganized and organized retailers have witnessed **operational difficulties** and have been influenced to change their way of doing business. Organized retailers are facing supply chain disruptions, restrictions in footfall as a result of social distancing, hygiene improvements in terms of sanitation protocols, adherence to social distancing protocols and temperature checks. This has been accompanied by a withdrawal from promotional campaigns to avoid over crowding in stores. Unorganized retailers are also facing challenges in terms of hygiene practices, home delivery and switch to e-payments.

### 3.4 Online Retail

The move towards online purchasing that had commenced before the pandemic with a rise in online payments, e-commerce platforms and growing digitalization, found an impetus with the frequent lockdowns and restrictions on commuting. Online retail penetration had increased from 3% at the end of 2019 to 6-10% in the last months of 2020. Indian shoppers are turning to e-commerce to make purchases of various product categories. The market has received a boost along with online discounts and development of rapid delivery services in India. The market e-commerce is dominated by players like Amazon, Walmart and Flipkart in India couple with smaller startups with app-based services for daily delivery of essentials like milk, bread, eggs and more. E-commerce currently accounts for 5-6% of the Indian retail market but growth estimates for the market suggest a promising future.

With the pandemic, supply chain disruptions by key e-commerce brands influenced the ability of these brands to meet orders and demands of their customers. The inability of delivery stakeholders to travel long distances with the imposed restrictions further made it difficult for e-commerce. During these times, the neighborhood shops stood resilient as they were the most convenient option for people after several of their apps failed them. Kirana store owners with their personal rapport with their customers, often times themselves picked up orders from distributors to meet the demands of their loyal customer base. There is a growing trend wherein the there

is some organization of the unorganized sector being seen, platforms like Amazon, Jio-Mart are trying to leverage India's kirana ecosystem to grow their business, without having to spend on entirely new infrastructure.

With Amazon's local shops initiative announced in August 2020, 50,000 kirana stores have been roped in. E-commerce venture Jio-Mart has undertaken similar efforts, Walmart-owned Flipkart onboarded 70,000 small stores in 2020. Overall, the efforts are promoting small and medium businesses from tier 1 and tier 2 cities. The movement towards incorporation of these neighborhood shops was driven by the high penetration, effective management of facilities, inventories, sourcing and other supply chain factors. The favorableness of the kirana stores is further augmented by their relationship with customers.

These traditional stores have transformed with the changing payment dynamics. The neighborhood shops have been accepting online payments through wallets, orders on WhatsApp and employing tech-enabled partners for fulfilling deliveries.

Mapping the changing dynamics of the kirana stores' business model starts with pre-2013 with procurement from traditional distributors using cash payments, with the association with e-commerce between 2013-2017, 2018-2019 saw the digitization push by retailers, in 2020 with the onset of the pandemic kiranas started online business as resellers on marketplaces.



# Consumer Behavior

## Section 4

## 4.1 Impact on Consumption Patterns

Before the onset of the pandemic factors that were driving consumption included rising households' income, increasing share of affluent households, greater access to shopping complexes, multiplexes for a premium experience during shopping, positive outlook towards future prospects and greater propensity to increase spending. This was coupled with the increasing discretionary expenses and a tendency to shop anywhere, anytime.

With the pandemic these factors came under pressure wherein there was falling consumption spending with job losses, shutdown of businesses and commercial establishments that impacted supply chains, emergence of negative outlook towards the economy and losing consumer confidence and income crunch. Safety concerns about going out and the growing focus on savings further reduced discretionary expenses. The pandemic caused the retail sector to shrink the first time in 2020 by 3% wherein it was growing 12-13% growth rate in the previous decade from 2010 to 2019. Different formats of retail were impacted in different magnitude with the pandemic, while traditional stores were resilient, modern stores faced a downturn and e-commerce received a boost in their sales. The cause for the changing dynamics of the retail sector underly in transforming consumer behavior.

A pandemic creates a situation of unsettlement wherein consumers ultimately have to adapt to the changing dynamics of their buying environment and also internal concerns of hygiene and insecurity about the future. Immediate effect of the lockdowns imposed as a result

of rising COVID-19 cases in the country have led to the following changes in consumption patterns and consumer behavior.

### 1. Hoarding

To manage the uncertainty about the future supply of essential products, people reacted through stockpiling products that fulfilled basic needs such as bread, disinfecting and cleaning products. Hoarding of essential medicines also led to the emergence of gray market where middlemen stocked on these essential commodities to increase the prices and profit off the sudden emergence in demand.

### 2. Improvisation

With the innumerable constraints on commuting and the fear of the disease, people have improvised where they shop. While earlier, for the relatively affluent income groups, shopping was done in supermarkets and modern stores with the realization of premium products, with the closure of these shops during lockdowns, the consumer has started to purchase essentials from their neighborhood shops that dominate the unorganized sector and have also moved towards online platforms to fulfill their needs for non-essential commodities.

### 3. Delaying Consumption

With the crunch in income and focus on savings demand for discretionary products and services such as movies, automobiles, homes and other high ticket value products shifts to the future. Such that with the easing of restrictions, consumers start acting on this pent-up demand.

#### **4. Move towards digital**

The already growing digital adoption received impetus with the pandemic as consumers started reaching out to the various e-commerce platforms to satisfy their demand for essential and non-essential commodities. The pandemic also witnesses boomers adopting digital solutions to the growing restrictions outside. The demographic pool of online retail has further expanded with consumer behavior amongst the group that is known for slow or no adoption of digital tools has relied on online retail for their basic needs.

The speedier and universal adoption of new technologies to address the need to work from home, stay connected with family and bring all the 'normal' activities done outdoor and transform them into an indoor experience will lead to sociological and cultural changes that will dramatically change the consumer behavior, accelerated by the pandemic. How consumer shop and the touchpoints will see a change that will need to be addressed by companies in the sector. Each segment has received a digital transformation impetus, that is to modernize the way we shopped.

#### **5. Home-delivery**

With a growing demand for bringing the store to the home in response to the lockdowns, the effect on the planned and un-planned purchasing needs to be mapped. As shopping for FMCG products shifts online, consumers may face greater impulsive buying behavior. In response to special offers, unplanned purchases are made by shoppers. Impulsive buying accounts for about 30-40% of online purchases and is likely to increase in these times with shopping shifting online.

The result of this immediate impact of the pandemic on consumer buying patterns is expected to modify some old habits and bring on some new habits among consumers. The future holds the course of whether the old habits will stay and the sudden change in consumption patterns are here to stay or will the new normal only last momentarily and we would go back to the old habits in due course as the vaccination drive completes. Will e-commerce keep growing or experience stagnation as restrictions ease and people go back to the in-store shopping experience? Consumption patterns might permanently change for some demographics as they embrace the convenience and home-delivery experience. While how the offline-online dynamics of FMCG Retail change is reliant on the consumers' responses, the adapting power of the retailers themselves will also define the post-COVID era.



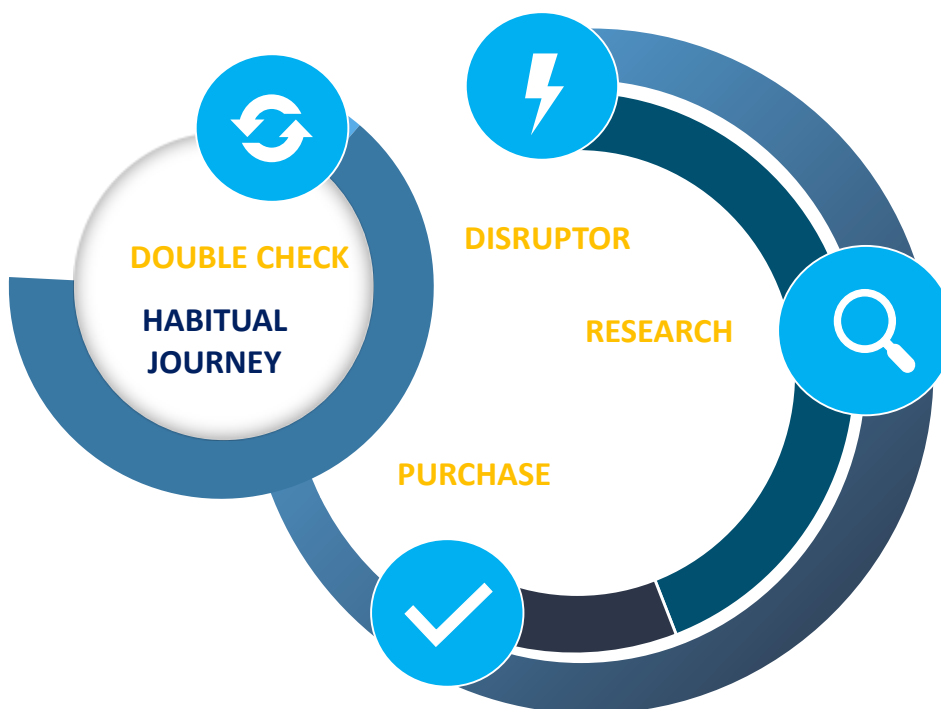
## 4.2 FMCG Consumer Buying Disruptions

To understand the shift in consumer preferences with respect to the mode of purchase, the consumers decision journey is studied in the FMCG industry. The consumers on the basis of their mode of purchase have been segmented into two categories; **Offline reliant consumers** and **Online-reliant consumers** in the pre-COVID period. The distinction is made on the basis of the final point of purchase, to be sensitive to the consumer’s decision journey being influenced by both offline and online touchpoints in making the final purchase.

The first category of consumers before the COVID-19 pre-dominantly relied on offline retail outlets in the form of traditional stores and modern supermarkets and retail shops. The second category of consumers pre-COVID predominantly relied on online retail outlets through e-commerce platforms and mobile applications for their purchase.

Consumer’s decision journey in the FMCG industry can be described through the framework given below. Their decision-making process is characterized by the habitual journey, wherein the consumers’ level of involvement is low. The repeated purchase of basic household necessities has inculcated preferences for certain brands in their decision process. Their orders form a part of a routine. Consumers as a part of their habitual journey can be influenced during the short purchase decision, known as the ‘double-check moment’. The habitual journey is disrupted when the cost of switching is low. With disruption, consumers go out to their routine to engage in research.

There are two modes of disruptions here, one is the exchange between offline and online retail platforms and the other is in the consumers’ brand choices.



## **Disruption of Channels**

With the pandemic and the multiple lockdowns, restrictions and concern for safety, the offline-reliant consumers have been forced to reduce their reliance on offline modes and adapt to more online channels. These categories of consumers are changing their product purchasing patterns as a result of lower frequency of visits to stores. Although these customers still visit their local supermarkets and traditional stores for basic needs, these consumers have started ordering regular products from online channels. Products for regular needs such as milk, eggs, bread, medications have attracted online sales as well as sales from neighborhood stores.

While before the pandemic the cost of switching to online channels required the customers to sift out of their old habitual behavior and abandon in-store experience, the growing concern for safety and restriction on mobility have reduced the cost of switching to online platforms for these customers.

The consumers reliant on online channels have experienced a reverse shock as the e-commerce platforms they heavily relied on failed to make the products available and deliver with the supply chain disruptions and movement restrictions. At times like these, people shifted to their local neighborhood stores for meeting the demand for essential commodities.

## **Disruption of Brand Loyalty**

As consumers shifted from offline to online modes, with exposure to greater peer reviews, different special offers and convenience, people have experienced disruption in their habitual selection of commodities to experimenting with new

brands. A switch from online to offline modes has had a similar effect as consumers are unable to find their preferred brands easily available in general nearby stores.

Whether the consumers shifting their modes of purchase with rising necessity is a permanent change is yet to be seen with the completion of the vaccination drive and a step into the new normal.

The consumer decision framework gives an important implication for the retailer. For online retailers it provides an opportunity to gather the switching offline consumers as their loyalists by providing attractive offers and greater interaction with products. For offline retailers, the overall scenario seems favorable to unorganized sector as consumer rely on this shop directly as well as indirectly through e-commerce giants like Amazon and Jio-Mart. For the modern retail outlets, survival is dependent on the imposed restrictions, facilitation of a safe shopping experience and adoption of tools to attract the pre-COVID footfall.

### 4.3 Way Forward

The unfolding of the consumer behavior in the upcoming period with vaccination drive for the COVID-19 pandemic underway and the changing consumption patterns will be interesting to see. With the resilience of the unorganized FMCG retail segment and incorporation in the organized retail through e-commerce platforms has allowed for the growth of the two segments over, offline modern retail segment.

As discussed, the consumer decision making in the FMCG space is a result of habitual and less involved processes. The pandemic has resulted in disruptions in this habitual behavior driven by dynamic shift between online and offline channels along with shifting brand loyalty. As consumers move from offline stores like supermarkets to online e-commerce platforms, they are exposed to new brands and special offers, driving their consumption patterns. As those consumers that were unable to meet their demand from e-commerce platforms as a result of supply chain disruptions start buying from neighborhood stores, there is a rising consumer base for unorganized sector.

For retailers in both the online and offline segments this means an opportunity to explore the new habits formed by consumers and to overcome loss as old habits faded out. While the unorganized sector with its neighborhood shops has the opportunity to increase the adoption of e-payments and use of wallets to attract and provide convenience to those customers seeking refuge for essential items at their store, the online retail channel needs to

allow customers in-store experience wherein the consumers are not burdened with choice overload and innumerable offers. Moreover, strengthening of the supply chains will be an essential step to retain consumer confidence. As the pandemic led to disruptions to the e-commerce supply chains and several items displayed unavailability, the consumers switched to their local supermarkets to maintain their unmet demand. Hence, a resilient supply chain is necessary to adapt to the uncertain circumstances.

The ultimate change in the consumer behavior as a result of the pandemic is yet to be seen. Whether the adoption of new habits will continue even after the pandemic or if old habits will reemerge after the vaccination drive is complete will define the future of the FMCG market. The resilience of the unorganized sector and the coping of the organized sector will depend on the status of disruptions in FMCG consumer decision framework.



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