

The Impact of Economic downturn on brand preference and “Buy Down” Behavior in FMCG sector

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Introduction

The global economic recession continues to be long and deep — and consumers across the globe remain insecure and anxious. They are tightening their budgets

and actively trading down. The impact of the recession has also been evident in India with slower growth, higher interest rates and accelerating inflation. However,

in the midst of all this gloom and doom, one silver lining that has lurked beneath the radar and escaped broader attention has been the strong trading up and consequent rise of the premium segment in India.

Like the previous recessions, during these periods consumers see their purchasing power diminished, and as a consequence private brands gain market weight and brand managers working at top FMCG firms such as Unilever, ITC, Johnson & Johnson, Reckitt Benckiser, Nestlé, and so on, are faced with a complicated but challenging scenario, where the immediate profit is not often aligned with maintaining brand equity.

Although demand in cosmetics and other lifestyle products may decrease a little but no real impact comes in the overall demand of food items (like biscuits and confectionaries); batteries and torches; tea, coffee and other beverages; toiletries (soap, shampoo, detergents) etc, which comprises essential commodities of day to day use. It's the diverse product portfolio which keeps these FMCG companies going even in a slowdown.

Data shows that consumers return to their favorite brands after the recession, partially because they recognize its quality, but it's the recognition the brand has by the time recession comes, as well as the decisions taken during the following days that will decide the extent to which the brand will come out healthy after the storm. This price-sensitivity by consumers leads to the exchange of the usual brands for private brands, and retailers take advantage by dedicating them more shelf-space, since they own those brands they usually offer higher margins.

Literature Review

According to the Nielsen Global Private Label Report (2011) shoppers within developed markets will retain their “value-mindset” even after a recovery of the great economic downturn. These consumers prefer to purchase at stores that offer „everyday low prices” and will tend to be atypically thrifty. According to the In

comparison to developed markets, consumers in developing markets such as India, are less aware of private label brands and assume from the packaging and price that the brand is of inferior quality and specifically aimed for people that cannot afford to purchase better quality manufacturer brands.

A few large corporate houses involved in the Indian retail sector have planned to go ahead with their expansion strategies as per the schedule, despite the world financial turmoil. The Consumer Confidence Index study (2008) further revealed that while Indians's intentions to spend on personal comforts such as new clothes, home improvements/ decorating, technology products are stronger than the global average, their intention to spend on holidays and out of home entertainment is much lower. In a nutshell, this indicates a general tendency among Indians to lead a comfortable day-to-day life by cutting out the frills. For the marketers, investment in brands today is necessary to secure brand loyalty for better times ahead. Ken Favaro, et. al (2009) is of the view that the retailers should use the following five rules for retailing in recession times. But even in these tough times, retailers may win new business and gain customer loyalty by focusing on people who are not their best customers but yet by making sure they offer what those customers really value and demand. The five rules as suggested by Ken Favaro to gain market share and protect margins are as follows:

1. Focus on customers who are loyal neither to the firm nor to their competitors.
2. Close the gap between the customer's needs and the current offering.
3. Reduce the "bad costs", those producing benefits customers won't pay for.
4. Cluster the stores according to local similarities and differences in customers' needs and purchase behavior.
5. Retool the processes – customer research, merchandise planning, performance management, strategic planning to position the company in a much better manner.

By evaluating the pre-recessionary and post-recessionary consumer, the marketer of manufacturer of retailer brands will be able to understand what drives a brand's current and future equity and, the existence of brand loyalty and its contribution to any return on investment, such as market share. Most importantly, both the manufacturer and retailer brands need to be differentiated and positioned in order to increase their return on investment and communicate their added values to the consumer, thus allowing consumers to make a choice between competing brands based on the communication strategy of the particular brand (Govender, Kelisha & Govender, 2013).

Price sensitivity and Strategies in Recession Economies

Financial crisis led to the price of goods and services fluctuated frequently, and with impaction of consumer expectations and rational consumption, the consumer is extremely sensitive to the price of goods and services (Kondawar D. & Jadhav, 2012). Sharma (2011) found that a recession economy can cause severe price destruction and can force retailers to react strategically. Resource abundant firms may use a predatory pricing strategy to maintain their predominant position in a market, but resource-scarce firms must join the price destruction war. However, even for the wealthiest firms, aggressive pricing may not be the solution for

success in a recession economy. Many studies have pointed out that the overuse of price as a promotional tool may damage the prestige of the brand. It is dangerous for firms to rush into price competition without considering the possible side effects (i.e., the consumer perception of the quality of products or services). Firms need to consider both internal and external influences on pricing when forming a sustainable strategy to cope with price destruction.

Internal Influences on Pricing

To deal with the price destruction caused by a falling economy, the most prestigious brands may be able to resist price attacks by competitors and preserve their competitive edge. Nevertheless, most companies need to participate in a price war. The most cost-efficient companies may be able to survive by driving the firms that are short on resources out of the market. It is understandable that resources, whether intangible or tangible, are the key for companies to outperform their competitors during episodes of price destruction. Thus, as stated by the resource-based school of thought, a resource-based view should replace the product-based view in marketing decision making (Sharma, 2011)..

External Influences on Pricing

Although the availability of organizational resources is an important perspective in the consideration of an aggressive or predatory-pricing strategy, the demand-side effects of such a strategy are another concern. Most consumers are sensitive to price. As Mazumdar and Papatla (2000) note, consumers tend to use reference price as a supplementary guide for consumption decisions, in which price information is accumulated either from previous experiences or from comparisons made among available brands. As long as consumers use price as an index for shopping, firms can use price to influence consumer behavior. For example, Miller, Ogden, and Latshaw (2008) show how price can be used to trigger consumer behavior. In their analysis, they manipulate price and product features to influence consumers' preferences for an assortment of products. They find a negative connection between price level and willingness to buy. However, when a product features key values that fit with consumers' needs, firms can raise the price while keeping a preference for the product stable. Chaudhary and Holbrook (2001) provide a similar observation that Brand affect resulting from a wanted hedonic value can increase loyalty to the brand and thus allow for more room for price to rise. Indeed, for a costly purchase, consumers tend to believe that a price is fair when they agree with it. To some extent, price can be subordinate to product worthiness in the consumption decision. In contrast, reference price can also be used to signal product quality

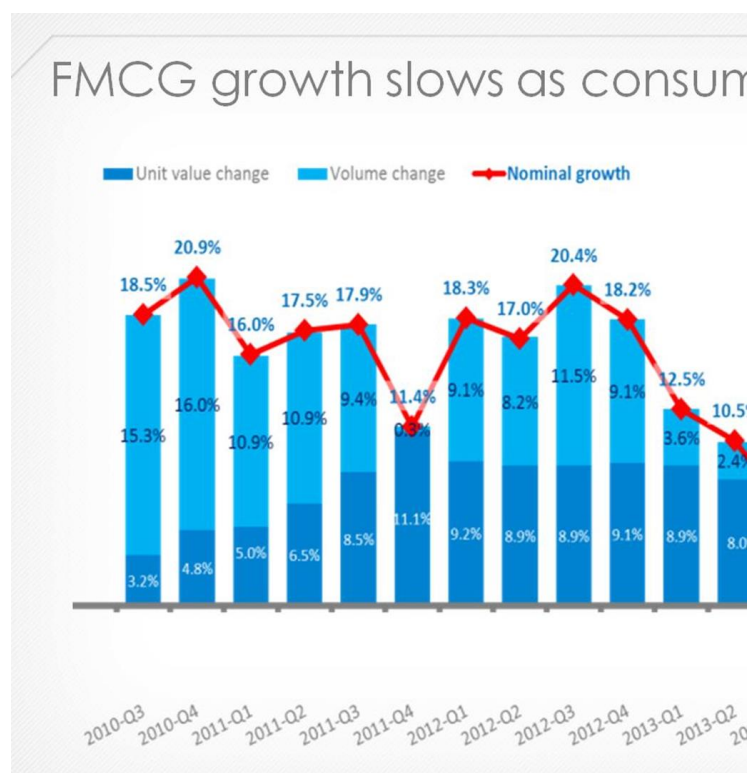
Analysis and Findings

Impact of Recession in Indian FMCG sector

People need to bathe and shampoo and polish their shoes and brush their teeth even in a recession. That would suggest that FMCG firms make money even during a downturn. Turns out that's not true, and India's Fast Moving Consumer Goods' (FMCG) companies, which sell "necessities" like soaps and toothpastes, are currently struggling to cope and players like Procter & Gamble (P&G), Hindustan Unilever Ltd (HUL), ITC

Ltd, Nestle India, Marico and Godrej Consumer Products say they are trapped in a difficult situation amid the increasing price of raw material. The fall of the rupee by as much as 20 per cent against the dollar between May and August 2013 (Sunita Natti, 2013). The overall FMCG sector is seeing a slowdown, going from double-digit growth a few quarters ago to a 2 per cent volume growth now.

A deceleration in certain discretionary segments at the top-end personal care products and packaged foods is posing a medium-term glitch for the otherwise recession-proof fast-moving consumer goods (FMCG) sector. As consumers tighten their purse strings, volumes have got impacted. Previous quarter performance of some of the major FMCG companies is an indicator to this trend. The current growth rates in comparison to the last few quarters on an overall basis are relatively lower. As per industry estimates, the volume growth of the FMCG industry during the quarter hovered around 9%, which means it has lost some ground from the low double-digit growth levels it achieved a couple of years ago.



The FMCG sector is the fourth-largest sector in the economy with a market size of over \$13.1 billion. It is estimated to touch \$33.4 billion in 2015, but this seems quite an ambitious target in current market conditions.

Hit by a weak rupee and high financing cost, the Indian unit of the world’s largest consumer goods firm P&G posted a record loss before tax of `371.17 crore last fiscal. This was P&G Home Products’ biggest loss since the \$82.6-billion Cincinnati-based multinational entered India more than two decades ago. “In the period, especially in the second half of the year, we saw unprecedented devaluation. We still have import reliance on our products and due to high devaluation, we saw a sudden increase in cost of goods sold,” explains Tapan Buch, CFO, P&G India, which sells Tide detergent, Pantene shampoo and Olay skincare range.

P&G is not alone. Even sales of the country's largest FMCG player HUL, which owns the Surf, Fair and Lovely, Clinic Plus and Lipton brands, among others, slowed for the sixth straight quarter (July-September) owing to weak consumer demand. The company said the worst was not yet over and sluggish demand would drag until next year. "The slowdown in business environment has continued in this (September) quarter both in terms of volume and value growth... In particular, premium segments and discretionary categories are under pressure.

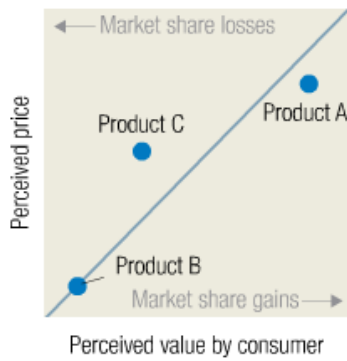
Volume growths of Hindustan Unilever, Marico and Godrej Consumer Products (GCPL) have moderated in the December quarter of the current fiscal. Colgate-Palmolive (India)'s toothpaste volume growth in the third quarter was the lowest in 20 quarters at 8%. The blame has been put on discretionary spends in the FMCG sector which came under pressure, raising the question whether the sector was completely insulated? "It is true that the FMCG sector to some extent is insulated and doesn't really get impacted by economic slowdown. The same is true even during periods of boom. However, it has been a while since there is a lack of feel good factor in the economy. GDP growth estimates continue to come down and when such factors extend over a longer period, some impact even on a defensive sector such as FMCG cannot be ruled out completely (Singh, 2013).

Changes in Consumer Behavior

Traditional consumers were usually not involved in production, defined as conformists and most often uninformed. Their behaviour was largely motivated by a need for comfort. According to the survey of McKinsey in August 2009 found that, in any given category, an average of 18 percent of consumer-packaged-goods consumers bought lower-priced brands in the past two years. Of the consumers who switched to cheaper products, 46 percent said they performed better than expected, and the large majority of these consumers said the performance of such products was much better than expected. As a result, 34 percent of the switchers said they no longer preferred higher-priced products, and an additional 41 percent said that while they preferred the premium brand, it "was not worth the money."

For FMCG firms attempting to address the change in consumer behaviour, understanding the economic theory can help to inform decision making. Changes in the relationship between how much consumers are willing to pay, on the one hand, and their perception of the value they are receiving, on the other, supports behavioral changes.

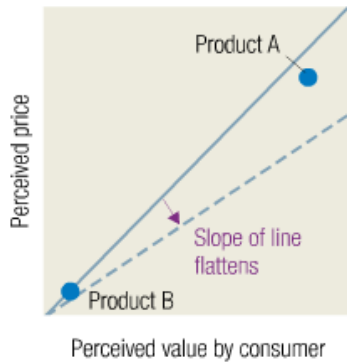
Before the downturn



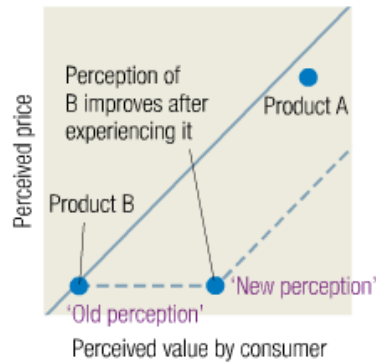
- Consumers are indifferent at any point on the diagonal 'demand line,' where perceived value and price are equal
- Product A is preferred because it is seen as a better value for the price
- Product C is at a disadvantage because its perceived value is too low given its perceived price

After the downturn

Change in willingness to pay



Change in perceptions



(Source: Bohlen (2009), McKinsey Quarterly)

As it may be seen in the figure; if consumers perceive enough value in a premium-brand product (Product A) they will favour it over the product of a more basic brand (Product B), despite the premium product's higher price. In a recession, though, consumers become less willing to pay more and the preferences of some consumers begin to shift from Product A to Product B.

For companies attempting to recognize the changes in consumer behaviour, understanding the economic theory can help to inform decision making. It can be declared by the recent report by Retail Systems Research [6] listed the biggest changes in purchasing behaviour retailers are facing nowadays. They can be summarized as following: keeping up with evolving consumers shopping patterns, getting consumers to engage online, maintaining growth rates, managing the online assortment, uncertain consumer demand being difficult to anticipate and plan for, providing more ways for consumers to connect to their brand, stemming cart abandonment and balancing online growth against poor store sales.

The 2011 data reveal the percent buying the brand they —want mostl has dropped 11 points since 2008 across the twelve categories examined. In 2011, just 43 percent of shoppers typically purchase their most-desired brands, indicating that more consumers continue to be motivated by economic factors compared to prior years.

Optimistically, the year-to-year decline does show signs of decelerating. The extent of the buy down behavior and the severity of the decline vary by both market segment and product category. Figure below

shows the percent of respondents who purchase their most desired brand for each category.

Market Segment	Product Category	2008	2009	2010	2011	Net Shift 2008 to 2011
Topline Average Across Categories Examined		54%	50%	45%	43%	-11%
Health & Beauty Aids	Toothpaste	67%	64%	57%	55%	-13%
	Mouth Rinse	61%	59%	44%	47%	
	Shampoo	65%	64%	52%	53%	
OTC	Cough/Cold/Allergy	58%	59%	43%	41%	-17%
Apparel	Jeans	54%	49%	39%	42%	-12%
Food	Soup	56%	51%	52%	44%	-11%
	Pasta Sauce	53%	48%	45%	43%	
	Fruit Juice	51%	44%	40%	39%	
Household Products	Laundry Detergent	57%	50%	47%	48%	-6%
	Facial Tissue	43%	40%	39%	35%	
	Paper Towels	36%	34%	35%	35%	
Housewares	Small Appliances	45%	38%	34%	37%	-8%

Source: <http://www.wafiles.org/>

It is interesting to note that many categories witnessed the most severe drop in percent of respondents between 2008 and 2010, with a smaller decline between 2010 and 2011, with one notable exception -- Soup. The Soup category saw a significant decrease in consumers buying the brand they want most between 2010 and 2011, while witnessing a comparatively small decrease in prior years. Noticeably, the 2010 percentage for Soup was higher than any other category outside of Health and Beauty Aids.

Among the other product categories studied, Health and Beauty Aids have seen a substantial increase in buy down behavior. However, it is important to note that at the beginning of the recession, this category saw comparatively low levels of buy down behavior, and despite the large overall increase in buy down, in the most recent survey it remained the leader versus the other market segments in terms of shoppers buying what they want most. This may be because consumers are generally more reluctant to purchase lower cost alternatives in categories that are more personal in nature.

Overall, it is OTC Cough, Cold and Allergy products that show the largest decline since 2008 in the number of consumers buying the brand they want most. It is likely that the relatively high price of these categories is the key reason why the decline has been so severe. Although the decline was much less severe compared to 2010, it continued on a slight downward trend in the most recent survey.

Changing Strategies in FMCG Sector

The overall impact on the FMCG sales will be marginal. Heavy dependence on the agri-sector and FMCG not being very capital-intensive are among the factors that have insulated the sector from the downturn. But rising input prices, inflation and increased commoditization of products are forcing FMCG companies to adopt new strategies, to have a viable business proposition. Let me enlist few of the strategies which companies have adopted and the outcome of the same.

1. Increase in price: Due to increase in raw material prices, many companies were forced to increase their prices and pass on the cost to the consumers.

a) HUL: Hiked the price of its detergent bar Surf Excel (120 g) earlier known as Rin Supreme from Rs 13 to 15. They have also increased some of their toilet soap brands

b) Tea Companies: Tata Tea and Duncan's Tea have also hiked prices for select brands in their stables. Even regional players like Royal Girnar and Society Tea have increased prices of their brands to compete with national players

c) Britannia: Hiked the price of its popular brand „Britannia NutriChoice Digestive“ from Rs 14 to 15.

Some companies have been able to maintain the prices. Parle Agro has not changed the price of Frooti in spite of upward pressure on prices.

It may be easy to increase the prices of premium products but in case of popular products, the preferred choice is between reducing grammage and maintaining the same price points or introducing another price point to suit consumer pockets.

2. Introduction of lower SKUs: To prevent down trading, the companies have introduced packs with lower SKUs so that per unit purchase does not pinch the consumer's wallet. With that companies are sharpening their focus on the existing smaller packs and increase their availability.

a) Henkel: Introduced a new 400 gm pack of Henko washing powder at Rs 40 and withdrawn the 500 gm pack that used to sell for Rs 46. As quoted by Henkel, “A family of four requires only 400-425 gm. of washing powder in a month. We withdrew the 500 gm packs as they were making consumers spend more and consume more”. They have reintroduced Pril liquid for Rs 50 (425 gm bottle), down from Rs 55 (500 gm). They recently brought out its popular Fa deodorant in 75 ml and Margo soap in 40 grams.

b) Procter & Gamble: P&G has reduced the pack size of its flagship detergent brand „Tide“ from 1 kilo to 850 gm while maintaining the price point at Rs 62. They have also also reduced the size of its 500 gm to 480 gm at the same price.

c) Gujarat Cooperative Milk Marketing Federation: Amul introduced 25 gm packs of butter few months back, which is now registering higher sales than the traditional 100 gm and 500 gm packs. Same has happened to their milk powder. They used to sell more of traditional packs of 200 gm, 500 gm and 1 kg, with the 500 gm packs selling the most. In the recent scenario, 25 gm and 50 gm packs are selling in higher numbers. As an outcome, companies are registering faster off take in the mid-sized packs.

3. Cost Cutting Strategies: While companies resorted to price hike, many companies are exploring ways to cut down cost.

a) Companies are busy in strengthening their distribution and logistics, by bringing in more efficiency and innovation in the supply chain. Companies are closely monitoring their stock levels and loading patterns

b) Soap companies have shifted to cheaper options of raw materials to source their products at a competitive price.

c) Some companies have cut down their spends on advertisement

Conclusion

As economic recovery gathers pace, consumption and spending will increase but consumer after recession is likely to consume very differently. The post-recession consumer thinks twice and sometimes three times about making purchases, big or small. The recession affected all social classes and has fundamentally changed how consumers consume. And also on the basis of the secondary research and other studies being taken into consideration in this paper, the research question can be answered. It is clear that during the economic recession many changes have made their presence, resulted in the new consumer shopping behaviour. And many of these changes will retain also in the post-recession time, as consumer got accustomed to behave purposefully and responsibly. The behaviour associated with wasteful, impulsive spending was replaced by thoughtful, responsible spending which is and also will be more socially acceptable.

FMCG companies face the same dilemma in the recession world – how to convince consumers to switch back to their ‘old’ brands or try new brands when they have experienced and been satisfied with the quality of a lower-priced option they’ve switched to during the recession. Success in the period of recession is based on achieving the right combination of value, product innovation and competitive differentiation. In addition to product innovation, manufacturers now have to consider the impact of brand values and corporate responsibility on sales. Brand values used to be the domain of the marketer but these days, it has become a purchasing factor.

Recommendations

The FMCG companies should focus on expanding and growing the consumer base rather than expanding margins in the short term. They should taken a portfolio approach and if needed are ready to sacrifice on short-term margins in order to accelerate the growth rate of new customer acquisitions. In fact through their pricing strategy by making price adjustments in select packs they have offered more value to the consumer as it is easier for the consumer to upgrade to their products.

Companies should be able to identify and drive categories\brands during various situations. Judicious investment on brands during this time is a must rather than cutting down their entire spends which is what companies often resort to. During the time of down-turns it is essential for the brands to engage the consumers and not turn the other way.

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