Fast Moving Consumer Goods sector in India – Tending towards oligopoly?

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RESEARCH ARTICLE

Fast Moving Consumer Goods Sector in India – Tending Towards Oligopoly?

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Abstract

We study the performance of the fast-moving consumer goods (FMCG) sector, in India. It is the fourth largest sector in India. Macroeconomic factors, modern production techniques, robust logistics facilities, efficient distribution networks and superior marketing capabilities have given the sector an edge over the other sectors. Firm performance is determined by considering liquidity, solvency and profitability ratios and also by employing common size statements, and comparative statements. We find that the sector appears to be overly dependent on the performance of a few firms. We further find that firm performance is not related to non-commercial factors such as CSR.

Keywords: FMCG, Fast moving consumer goods, India, Firm performance

1. Introduction

Covid19 is expected to lead the Indian economy into a deceleration, if not a recession (Sahoo & Ashwani, 2020). The fast-moving consumer goods (FMCG) sector is a key contributor to the health of the economy, in India. It is the fourth largest sector in the economy and consists of three key segments: household and personal care, health care and food and beverages. The sector is trifurcated into metropolitan, semi-metropolitan and rural segments. Though, currently, the metropolitan segment generates over 50% of the sector’s income, the semi-metropolitan and rural segments are expected to be the growth engines of the future. In light of the significance of FMCG to the economy, it is easy to anticipate that the performance of this sector would have an impact on the overall economic growth of the country (see Table 1).

The impact of the sector, in turn, is influenced by the performance of the players in the sector. However, it is also likely that in a crowded space such as the FMCG sector, a small number of firms may inordinately influence the sector’s performance. Thus, the fortunes of the sector, and consequently the economy, may be at risk from the “all eggs in one basket” syndrome. However, even in instances where the sector’s performance is not contingent upon the fortune of few companies, there is a risk that a segment may impact sectoral performance. An empirical study of the performance of various firms in the sector is warranted in order to comprehend their potential in an economic recovery. This paper, attempts to deconstruct the performance of the firms in FMCG sector and studies the performance of individual firms in order to anticipate their impact on the future of the sector.

We also take cognizance of the possibility that non-economic factors may also influence firm performance. We have chosen to investigate the impact that firm’s CSR may have on its performance. This particular association (CSR-firm performance) has been extensively explored in the literature and so we have chosen not to replicate that research. Rather, we have chosen to employ the CSR expenditure of firms in the sector to proxy for firm level CSR activity. Starting with the premise that successful firms will carry out more CSR, we test whether CSR expenditure is a reasonable indicator of firm performance or vice versa. We explore this...
association in order to understand any influence CSR activity may have on firm performance — it could be that the firm may be rewarded for its social conscience even if its product/service offerings are not the best in the sector.

We employ secondary data using annual reports and the database of the Centre for Monitoring Indian Economy (CMIE). We use this data to analyze the financial performance of the companies in our sample. Our sample consists of FMCG companies listed on the index of the National Stock Exchange (NSE). We describe our methodology and results in greater detail later in the article.

2. Literature review

Fast moving consumer goods (FMCG) sector is a key spoke in the wheel of the Indian economy. It is the fourth largest sector in the economy and consists of three key segments: household and personal care, health care and food and beverages. Household and personal care constitutes 50% of the sector while health care and food and beverages constitute 31% and 19% respectively. According to the India Brand Equity Foundation (IBEF), the sector’s growth can be attributed to certain key macro features such as an affluent urban population, rapid growth in rural markets, changing lifestyles in urban and rural societies, growing brand awareness and a demographic dividend of large base of young consumers (Moneycontrol, 2018). Over the period October 2017 to December 2020 the Indian FMCG sector grew at 7.1% and the rural market is expected to grow to US$ 220 billion by 2025 (2018: US$ 23.63 billion). The sector’s growth forecast, reported by the IBEF, is based on evidence that shows a continuing growth in demand, investment plans of firms, opportunities in exports and e-commerce and favourable government policies.

Ninety percent of the firms in the sample employed in this study have disclosed significant investments in the sector. The merger and acquisition plans of key players in the sector indicate a period of consolidation and rationalization ahead. We study the profitability patterns in the sector by considering a sample of 10 companies that constitute 93% of the market capitalization of firms, listed in the Nifty-FMCG section of the CMIE database. We find that the sectors performance is closely associated to a handful of these companies. This has significant implications for the economy and, consequently, also indicates the need for regulatory interventions that address the dangers of the sector depending so heavily on so few firms.

(Bagchi et al., 2012) studied the influence of working capital management on profitability in Indian FMCG companies. Their findings indicate that the cash conversion cycle, age of debtors, creditors and inventories, debt to assets ratio and debt equity ratio are negatively associated with firm profitability. The findings of the study highlight the significance of sound working capital management in improving a firm’s profitability. In order to consistently perform well in India’s challenging environment, sound working capital management needs to be an integral component of the firm’s strategy.

(Jana, 2018) also analyzed the impact of working capital management on profitability of FMCG companies in India. The study showed a positive relationship between profitability and working capital management. The study was conducted by employing correlation and panel data regressions on a sample of 15 companies. The findings of (Jana, 2018) concur with those of (Bagchi et al., 2012) that efficient management of working capital in FMCG companies is positively associated with profitability.

(Patil, 2016) studied the growth of Indian FMCG Sector. He critically analyzed the sector employing PEST and SWOT analysis. He found that the FMCG sector was relatively recession proof and that growth in the sector was due to increased demand, supply side developments and favourable Government policies. Focused on the significance and evolution of the Indian FMCG sector. The top 10 companies in the sector were ranked according to revenues earned, consumption rate and product offerings. Found that rising incomes and an expanding pool of youth along with brand consciousness were key drivers of growth in the sector and had led to a favourable impact on demand.

(Desai & Oza, 2017) measured the ability of firms in the FMCG sector to generate earnings relative to sales, assets and equity. They analyzed the profitability of these 3 firms by using ratio analysis and ANOVA. They found that Britannia reported better ROCE, ROA and return on net worth than did Dabur Ltd and Marico Ltd. There were significant

<table>
<thead>
<tr>
<th>Company</th>
<th>Increase in profits (In crore)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hindustan Unilever Limited</td>
<td>3904.17</td>
</tr>
<tr>
<td>ITC Limited</td>
<td>8669.89</td>
</tr>
<tr>
<td>Nestle India Limited</td>
<td>1162.17</td>
</tr>
<tr>
<td>Godrej Consumers Products Limited</td>
<td>1449.35</td>
</tr>
<tr>
<td>Dabur India Limited</td>
<td>821.75</td>
</tr>
<tr>
<td>Britannia Industries Limited</td>
<td>1041.09</td>
</tr>
<tr>
<td>Marico Limited</td>
<td>881.68</td>
</tr>
<tr>
<td>Colgate Palmolive</td>
<td>356.04</td>
</tr>
<tr>
<td>Procter &amp; Gamble</td>
<td>240.75</td>
</tr>
<tr>
<td>United Spirits Limited</td>
<td>540.04</td>
</tr>
</tbody>
</table>
differences between the Operating Profit ratio, Net Profit Margin, Gross Profit Margin, and Return on Capital Employed, Return on Net Worth and Return on Assets of the companies. In terms of Return on Capital Employed, Return on Net Worth and Return on Assets is concerned, the performance of Britannia is better as compared to Dabur and Marico. The study also revealed that Britannia Ltd utilized shareholder funds more profitably and efficiently than Dabur Ltd and Marico Ltd.

(Sharma, 2020) analyzed short term solvency of a sample of firms in Indian FMCG sector and found that ITC Ltd relied on maintaining an ideal liquidity ratio while other firms, such as HUL and Colgate relied upon cash from operations to meet short term obligations.

The preceding narrative makes it amply clear that working capital management is critical for the success of firms in the FCMG sector. This has implications for the strategic management of the firms. Inventory, receivables and payables management acquire high importance in these circumstances. We anticipate that our analysis will demonstrate companies with better profitability also report good working capital management ratios. These ratios might vary between companies depending on whether the firms opt to gear up for a strong push towards growth as a response to the expected downturn in consumption or whether they opt to consolidate their operations in order to shore up against consumer caution. If the latter were to happen, then the predicted economic recovery may well be adversely affected but.

3. Methodology

This study uses secondary data sourced from annual reports, company websites and various print media. Our sample consists of the top 10 firms (by market capitalization) from the Nifty FMCG Index of the PROWESSIQ database maintained by the Centre for Monitoring Indian Economy (CMIE). These 10 companies represent almost 93% of the market capitalization in the index. We confirm that the sample is representative of the sector by cross-referring to the CMIE BSE Top 100 index. We exclude financial companies from the BSE Top 100 index and are left with 79 firms. Our sample represents a fifth of the market capitalization of non-financial firms listed on the BSE Top 100 index in PROWESSIQ. The firms in our sample are, Hindustan Unilever Ltd, Nestle Ltd, ITC Ltd, Godrej Consumer Group, Dabur India Ltd., Britannia Industries Ltd, Marico Ltd, Colgate Palmolive (India) Ltd., Procter and Gamble Ltd and United Spirits Ltd. The period of the study is from 2010 to 2020.

We use an assortment of techniques employed in analyzing financial statements such as, Common Size Statements, Comparative Statements and Ratio Analysis. Common Size Statement helps to identify each item as a percentage of a common base figure. Common size statements are normally prepared in one of two formats, vertical or horizontal. Common size statement analysis mitigates the limitations of comparative statement analysis. For example, comparative statements not helping the comparison of financial statements of two or more business, because there is no common base.

Comparative Financial Statement is a method which compares the current year’s figures are compared with the previous years to determine the percentage changes during period under review. It enables us to measure operational efficiency and financial soundness of the firms. Ratio Analysis is commonly used as an analytical tool in order to establish the association between financial measures disclosed in audited annual reports. Such analysis facilitates comprehension of prior performance, identification of significant trends and estimations for the future.

As mentioned in the previous section, profitability ratios, at a very prosaic level, ought to be complemented by liquidity ratios. Therefore, we examine the following sets of ratios:

3.1. Profitability ratios

They help determine the ability of a business to generate earnings relative to its revenue.

3.2. Liquidity ratios

These ratios determine a company’s ability to pay its short-term debt obligations.

3.3. Leverage/solvency

They ratios are used to determine the ability of a firm to repay debts Inter alia we examine, Net profit Margins, Gross Profit Margins, Operating Profit Margins, Current ratios, Quick ratios, Return on Equity, Return on Investment and Return on Assets.

4. Results

From comparative statement analysis we determine the average increase in profits of the 10 companies over a 10 year period (see Graph 1).
For example, the net profit margins of Procter and Gamble Ltd, Nestle India Ltd, Marico Ltd and HUL display a similar pattern. Following a decline in 2017, all four companies record increases in 2018. Nestle India Ltd reported that it launched 15 products between 2016 and 2017 with a focus on innovation and renovation in its Maggi and KitKat portfolios. It also introduced ready to drink Milo in the market. In the case of Marico Ltd, Saffola Oats franchise consolidated its lead in its category and achieved a 70% market share (by volume). Further, the company lowered retail prices of various products over the period July–December 2017, thus allowing them to pass on the benefits of lower GST rates to consumers. Euromonitor reports that the branded food market grew from INR 4.3 trillion to INR 5.1 trillion over 2017-18. According to the research agency this growth is attributable to consumers switching away from non-branded food products. Colgate Palmolive Ltd and Dabur Ltd show a steady growth. Britannia Industries Ltd also shows a steady growth, probably due to lack of innovation in products. Except for a dip in 2014, United Spirits Ltd displays a steady growth too (see Graphs 2–9).

Gross profit shows how well sales cover the direct costs related to the production of goods. ITC Ltd, HUL, P&G Ltd, Marico Ltd and Nestle India Ltd report good profit and from 2011. It indicates that the companies are producing their product more efficiently and they can cover their costs. Colgate Palmolive Ltd, Dabur Ltd, United Spirits Ltd and Britannia Industries Ltd has lower gross profits in comparison to the rest of the sample. The reason may be higher cost of production, decline in sales price or a change in sales mix.

Operating profit margin is one of the key ratios that is used for the evaluation of a company and is a good indicator of how efficiently a company manages its operating expenses. As seen in the graph P&G Ltd, Nestle India Ltd, Marico Ltd and HUL registered growth in 2017. But P&G outperformed the other companies. This was probably because P&G strengthened their product portfolio in 2017 by launching new products like Whisper ultra-soft with superior value proposition for customers. P&G’s health care sector, with products like Whisper and Vicks Vaporub had high market penetration and gained share in 2017. Similarly, HUL introduced new variants in the food and personal care sector which helped the company’s market penetration. These initiatives were probably aided by growth in income and increased urbanization. In the case of Nestle India Ltd, a 11.8% increase in sales was attributed to increase in sales of Maggi noodles and coffee products like Nescafe. Exports also witnessed growth in 2017. Parachute, a product from Marico Ltd, recorded a volume growth of 4% in 2017. Colgate Palmolive Ltd, Dabur Ltd, and United Spirits Ltd report lower profit as compared to the companies discussed earlier in this paragraph. This could be due to sub-optimal use of resources and

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*This segment includes categories such as edible oils, diary, pasta and noodles, savoury snacks and biscuits.*
effective marketing. Britannia Industries Ltd shows a steady growth, despite exchange rate variances Africa and the Middle East. An economic downturn in critical export markets and significant price rise in key commodities also probably affected the company’s performance (see Graphs 10-18).

ROE is an important measure of the return earned by shareholders and informs investors about the returns earned from money that was being ploughed back into the. The graph shows that the decline in ROE started from 2011 to 2017. The trade disruption in 2017 was followed by a recovery in 2018, by which time the companies had adjusted to demonetization and so profits improved from 2018. Procter & Gamble, Marico Ltd, Nestle India Ltd and Hindustan Unilever Limited show similar growth patterns, implying that these companies have successfully deployed equity funds towards business growth. ITC, though at the bottom of the graph shows a steady trend through the years. This could be due to the diversified product portfolio spanning various segments that ITC has. This diversification
may have averaged out the highs and lows of different segments, leading to a steady trend. The role of accounting policies followed by the company cannot be discounted but it is outside the scope of this paper. Colgate Palmolive, Dabur India Ltd, ITC Ltd, Godrej Consumer Products Ltd, Britannia Industries Ltd and United Spirits Ltd show a declining trend and investors may be well advised to investigate the reasons for this.

ROI is useful to both determine attractiveness of an investment opportunity and also compare potential returns from various investment opportunities. The ROI of the sampled companies is very similar to the ROE of these companies. A general decline till 2017 is reversed from 2018 onwards largely due to reasons explicated in the discussion on ROE.

ROA measures management's efficiency in generating earnings from the firm's assets. Procter & Gamble, Nestle India Ltd, Marico Ltd and Hindustan Unilever Limited have a good ROA implying that their asset utilization is efficient and generates
good returns. Godrej Consumer Products Ltd and ITC Ltd display ROA that are very similar to each other. This is interesting since their product portfolios are dissimilar. Since the companies performing very well have the food and beverage in common among them, it can be posited that ITC’s non-food segment may be diluting the superior performance of their food segment. Colgate Palmolive, Dabur India Ltd, United Spirits Ltd and Britannia Industries Ltd, have a low ratio as compared to the other companies indicating that perhaps their asset investment policies may need to be reviewed.

We find that after 2015, the current ratio of most companies in the sample displays a sharp increase after 2015. Prior to this point the ratio of each company follows a steady incremental upward trend. Post the spike in 2015, the following years display a return to the steady incremental growth of the pre-2015 years. Compared to other companies, Procter &
Gamble has the highest current ratio. Though Britannia Industries Ltd, has a low ROA they have a satisfactory current ratio. An investigation of their financials shows that the company's sundry debtors increase year on year. It is not good for a company to have high sundry debtors because it affects liquidity negatively. Nestle India Ltd, Marico Ltd, United Spirits Ltd, Marico Ltd and ITC Ltd can be grouped together on the basis of the movement in their current ratio. When we studied their financials, we found that from that these companies showed an increase in cash and cash equivalents and inventories. The favourable trend in cash and cash equivalents notwithstanding, the growth in inventories may be a cause for concern due to the risk of locking working capital in inventories.

The quick ratio of the companies in the sample follows a somewhat similar pattern as their current ratio. The striking difference between the two (quick ratio and current ratio) is that subsequent to the
spike in 2016, the quick ratio declines (while the current ratio steadies from 2016 onwards). P&G has the high quick ratio among the sampled companies implying that their current assets are dominated by liquid assets. The reason behind this could be faster conversion of inventory to sales and high recovery from debtors. The quick ratios of Godrej Consumer Products Ltd, Marico Ltd, Hindustan Unilever Limited move together across the years. Brittania Industries Ltd has the lowest quick ratio in the sample and investors may want to investigate whether long term investments offset this short-term liquidity concern.

As can be seen from the graph, the companies in the sample can be grouped into three distinct groups based on their debt-to-equity ratios (DER). The first group report a high DER in 2015 and then decline steadily till 2017 before dropping sharply in 2018. The second group shows a gradual decrease in DER from 2015 to 2018. The third group shows a steady increase in DER from 2015 to 2018.

Graph 10. Consolidated graph of return on investment.

Graph 11. Return on assets.
2018. Subsequently, the DER of this group plateaus till 2020. The next group consists of ITC which, like the first group spikes in 2015, but unlike the first group falls steadily till 2019 and then maintains that level in 2020. The third group of companies have almost zero DER from 2014 onwards till 2019. In general, this would imply that the firms in the first two groups are less leveraged and can be considered good investments. The last group might require investigation as to the underlying reasons behind the growth in DER since 2019. If debt was incurred to finance future expansion, then the growth in DER may not be a bad move. However, if it is to finance current operations then this trend needs further scrutiny. The current ratios and quick ratios of these companies may need to be studied alongside the DER to arrive at the risk (opportunity) they face.

In unreported results we investigate this to see if their social reputation has an influence on the

Graph 12. Consolidated graph of return on assets.

Graph 13. Current ratio.
performance measures we employed. We used the firms’ CSR expenditure as a proxy for their social reputation and ran OLS regressions with CSR as the dependent variable and the performance measures as independent variables. We controlled for industry effects. After addressing multi-collinearity variables, we found no significant associations between CSR expenditure and the performance measures used in our study. This leads us to surmise that the performance we have reported are due to firm specific factors and no related to exogenous macro-factors. Further, this would reiterate our earlier suggestion that legislation and structure of the high-performance firms be investigated in order to reduce their skew on the performance of the sector.

A scrutiny of the results show that there is a possibility that an oligopoly could develop in the

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**Graph 14. Consolidated graph of current ratio.**

**Graph 15. Quick ratio.**
Another development that warrants closer scrutiny is that the firms in the sector can be clustered in groups that display similar trends. We propose that an oligopoly would be detrimental to the overall development of the sector. The fact that the same set of firms, invariably, dominate the performance measures we have investigated could also imply that they have certain structural advantages over the other firms. This further increases the risk of a sectoral collapse in case a structural crisis occurs. Moreover, the clustering of firms ought to be examined more to determine if the lower performing firms are those that have greater operations in semi-metropolitan or rural segments. If this were the case then these firms have good prospects and may rank alongside the higher performing firms in the coming years. However, this does not detract from our concerns about an oligopoly in the sector.

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**Graph 16. Consolidated graph of quick ratio.**

**Graph 17. Debt to equity.**
In that context, we would recommend regulatory attention in this sector and perhaps legislation curtailing such a development is urgently required.

5. Conclusion

This paper attempted to determine the performance of the FMCG sector in India. Employing a sample of top ten companies (by market capitalization) listed in the NIFTY FMCG Firms section of the PROWESSIQ database maintained by CMIE, the study spanned the period 2010–2020. Various financial measures used to analyze performance indicate that the sector is overly dependent on a few firms. The performance of these firms does not seem to be influenced by non-operational factors such as CSR. This dependence of the sector on a few firms could be risky in the event of an exogenous shock such as firm specific scandals or unfavorable legislation. Therefore, our study indicates regulatory intervention may be required to redress structural “advantages” enjoyed by these companies.

This study is subject to a few limitations. First, the study is based on a relatively small sample of firms (although they constitute a significant portion — by market capitalization - of the FMCG sector). Second, the investigation relies entirely upon financial information. Consequently, the study is subject to all the limits characterize analysis relying on financial reports only. Third, the measures used for the study have their own limitations which will also reflect in this study. For example, common size statement analysis, does not help to take decisions since there are no standard ratio or percentages to serve as benchmarks. Similarly, in the case of ratio analysis, it does not takes into account external factors such as a worldwide recession.

The study also possibly exposes a lacuna in policy making and regulation that has led to a potential oligopoly in a critical sector of the economy. This may require scrutiny and amendment post haste.

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Conflicts of interest

There is no conflict of interest.

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