ICICI Lombard
Nibhaye Vaade

CORPORATE INDIA RISK INDEX

2022

Intelligence partner FROST & SULLIVAN

SECTOR REPORT 2022

FMCG


RISK

Table of Contents

Table of Figures

Preface

Corporate India Risk Index is primarily an academic exercise to understand the level of risk that companies are facing and also assist in developing a successful risk aversion plan, CIRI is a first-of-its-kind risk measurement tool to gauge the level of a company's risk exposure and preparedness.

This Corporate risk comprises of various aspects of the business–spanning customer, competition, regulatory environment, business operations, technology finances, environmental factors etc. The impact of unprecedented events is significantly higher now.

This Index is a comprehensive framework that draws upon global risk management best practices and comprises of 32 risk elements across 6 broad dimensions. The Risk Index is based on the principles of Lean and Six Sigma that qualify business processes by measuring effectiveness and efficiency.

ICICI Lombard's Corporate India Risk Index provides a crucial tool for assessing and addressing risks, fostering resilience and adaptability in the ever-evolving global landscape. In the current climate of increasing macroeconomic uncertainties, it is essential for corporates to prioritize robust risk management. We believe that a proactive approach to risk management not only fortifies individual businesses but also contributes significantly to India's overall economic growth and stability.

Executive Summary

The FMCG sector is one of the fastest-growing sectors in India, with a growing rate of 8.9% in 2022, making it the fourth-largest sector. The rise in the sector can be attributed to rising disposable income, growth in youths, and rising brand awareness.

In the post-covid world, markets have completely opened, and the volume and sale of FMCG are above pre covid levels however, the non-food segment has remained lower than pre-covid levels. There has been a rise in inflation and volatility in commodity prices that has led to lower operational margins. There are several reasons why inflation has been affecting the FMCG sector in India. One of the main reasons is the increase in the cost of raw materials, such as oil, palm oil, and sugar, which are used in the production of many FMCG products. The increase in the cost of transportation due to rising fuel prices has also contributed to inflation.

The government has allowed 100% FDI for food processing and around 51% for multi-brand retail.

There has been consumption growth mainly driven by the food categories; however, consumption has been on a decline for rural markets while urban markets have shown growth. There is also a change in the pricing strategies to develop affordable price points, and there has been more traction towards smaller packs of items.

Introduction

ICICI Lombard Corporate India Risk Index is a one of its kind, unified, credible, standardized corporate Risk Index that spans over the country level, the industry level, and the company level. The index has a comprehensive sector coverage.

Aerospace and Defense, Agriculture and Food Processing, Automotive and Ancillary, BFSI, Biotech & Life sciences, Chemicals and Petrochemicals, Education Skill Development, Energy, FMCG, Healthcare Delivery, Infra and Realty, IT/ITES, Manufacturing, Media and Gaming, Metals and Mining, New Age & Startup, Pharmaceuticals, Telecom and Communication Technology, Tourism and Hospitality, Transportation and Logistics.

The impact is identified across key business risk (internal and external) under the following 'Strategic Risk Areas', The ICICI Lombard Corporate India Risk Index Framework comprises of 32 risk elements across 6 broad dimensions.

Market and Economic Risk

Corporate Risks arising due to market and economy related factors, such as internal or external political uncertainty, global slowdown, taxation-regulatory changes etc. Market and economy related risks are also identified as 'Systematic Risks', we have further classified the risks into below mentioned categories.

- **Inflation:** Inflation is the general increase in prices within the economy. The rising prices for businesses could result in bigger production spending and a fall in profitability. The companies should be attentive, acute, and responsive to changes in inflation to efficiently manage the prices of final products.
- **Taxation:** In a large democracy like India, complexity of multiple taxes (multiple taxes like GST, custom duties, central excise duty, etc.) is a major concern. The changing legislations, increased scrutiny by tax authorities and increasing public attention are together resulting in tax risks for organizations. There is, thus an increasing urgency for firms to manage their tax affairs efficiently to minimize tax risks.
- **Regulatory Risks:** Regulatory risk is the risk of changes in regulations and laws that might affect an industry or businesses. The regulatory changes can pertain to tariffs and trade policies, business laws pertaining to employment, minimum wage laws, financial regulation, Foreign Direct Investment etc.
- **Foreign Exchange Risk:** The exchange rate plays an important role for firms who export goods and import raw materials. The fluctuations in foreign exchange will have great impacts on the prices of traded goods. For

example, if the currency depreciates (devaluation), the exporting firms will benefit. However, the firms importing raw materials will face higher costs on imports. The firms need to hedge their exposure to foreign exchange risks to insulate themselves from the impact from forex changes.

- **Geo-political Tension:** Geopolitical risk means the political and economic risks that are a potential threat to the financial and operational stability of companies.
- **Competitive risk:** Competitive risk is the risk associated with the fact that there are multiple companies competing in the market, each seeking to obtain the highest position and consumer ratings, to gain maximum benefits for themselves. The companies devise different strategies to garner a higher market share and acquire customers from competitors. Any failure in managing the competitive stand could lead to losses in business, thereby making marketing and competition a major risk in market.

Technology Risk

Technology risks are also identified as information technology related risks which may arise due to failure of any installed hardware or software system, spam, viruses or any malicious attack. Also delay/over/under adoption of trending disruptive technologies can lead to technology related risks. We have classified the risks in below mentioned categories.

- **Innovation Risk / Obsolete Technology**: Innovation is the key to success in all the industries. Risk of redundancy and losing out to competition on account of poor R&D is a major concern.
- **Intellectual Property risk:** Dependence on trade secrets and unpatented proprietary know-how.
- **Disruptive Technologies:** These will fundamentally alter the financial prospects of the industry.

Data Compromise: Hardware failure refers to malfunctions within the electronic circuits or electromechanical components (disks, tapes) of a computer system; Software failure refers to an operating system crash. Such failures lead to stoppage of entire computer or operating systems creating substantial losses to business.

Operational and Physical Risk

Risk of losses caused due to faulty or failed processes, systems or human resource related inefficiencies are classified as operational and physical risks. We have classified Operational & Physical risks in below mentioned categories.

- **Critical Infrastructure Failure / Machine Breakdown:** Industries with a heavy dependence on machinery consider any rise in machinery breakdowns a hindrance to their businesses operations. An untimely equipment breakdown can bring businesses to a standstill or be the root cause for fires and explosions. Mostly, human errors and deferred maintenances are the major reasons for such breakdowns. The companies should actively invest in timely maintenance of all machineries.
- **Business Continuity / Sustainability:** Non adoption of Business Continuity/ Sustainability Plans and Lack of Internal Control tools would result in: Failure of businesses, Brand Equity / Loss of reputation, Financial Loss, Business model Failure, Ineffective engagement/communication with stakeholders, Losses in productivity, Lack of opportunity monitoring.
- **Supply chain risk:** Raw Material unavailability and Heavy Dependence on Global Supply Chains / Supplier concentration risk. Unavailability of raw materials owing to disruption in the supply chain or heavy dependency on one source (company/country) which is unable to supply owing to some geo-political tensions, fires, or any other incidents. Transportation is one of the key activities for companies making it an important risk to mitigate. The loss of goods in transit and spillage is one of the major concerns as it accounts for a sizeable loss of revenue to companies.
- **Commodity Price Risk - Volatility in prices of raw materials:** The fluctuations in raw material prices creating a margin pressure / top-line pressure in the scenario of rising input costs.
- **Portfolio Risk:** Loss of key customers, Customer concentration - Key customers accounting for a larger share of revenue, Over-dependence on suppliers, Business Model Risk: Transformative changes in business model, Tail Risks: Ability to overcome or manage extreme worst-case scenarios.
- **Environmental Hazard Risk:** Any environmental hazard having the potential to affect the surrounding environment.
- **Workplace Accident:** Fire and Explosion Hazards, Containment Incidents, Workplace Injuries
- **Human Resource:** Key person risk: This risk occurs when a business or business unit becomes heavily reliant on a key individual. Talent acquisition and retention - The companies require a highly skilled labor force for R&D as well as continuous production. Accessing skilled resources and expertise on an on-going basis is one of the major challenges; moreover, retention of trained staff is imperative. Labor shortages, Union Strikes & Industrial Actions, Employee health, safety, and security (SHE/Sustainability risk).
- **Financial Risk:** Financial Reporting Risk: Material misstatement of Financial Statements, whether due to fraud or error. Interest rates and equity prices: Interest rate risk arising out of working capital borrowings at variable rates. Equity price fluctuations affect the Company's income or the value of its holdings of financial instruments. Liquidity Risk (Credit Risk / Receivables).
- **Breaches of law (local/ international):** Voluntary/ involuntary breaches of law can lead to costly lawsuits.

Crime & Security Risk

Cybersecurity risks relate to the loss of confidentiality, integrity, or availability of information, data, or information (or control) systems and reflect the potential adverse impacts to organizational operations. These attacks can cause major financial losses, reputational harm, and a loss of client trust. Regarding cybersecurity, the BFSI industry in India has several difficulties, including difficult-to-secure legacy systems, a shortage of qualified cybersecurity personnel, and the requirement for ongoing system and network monitoring. There is a significant investment in cybersecurity tools like network monitoring, endpoint security, access control, and threat intelligence. Many organizations are also implementing cutting-edge technology like artificial intelligence and machine learning to strengthen their security posture. Around 7.4% of the attacks in the Asian region were targeted at India in 2022.

We have classified Crime & Security risks in below mentioned categories.

- **Cyber Crimes:** Data Theft, Spam, scams and phishing, Hacking, Malwares and Viruses, Piracy, Fraud, Corruption, Malicious attacks
- **Counterfeiting:** Counterfeiting of goods/services leads to loss of revenues, profits and ultimately affects the brand equity
- Threat to Women Security
- **Terrorism:** Un-lawful use of violence and intimidation, especially against civilians, in the pursuit of political aims.

Natural Hazard Risk

A natural hazard is the threat of an event that will likely have a negative impact. A natural disaster is the negative impact following an actual occurrence of natural hazard if it significantly harms a community. Due to India's geographical structure, it is one of the most disaster-prone countries in the world. Natural hazards like floods, earthquakes, landslides, and cyclones are common risks faced by India. The situation has worsened due to rise in GHG emissions, loss of biodiversity, deforestation, and degradation of environment. From Surat Gas leak to landslides in the north and cyclones in Bay of Bengal, the year 2022 was no exception. Such natural disasters hamper the day-to-day operations of corporates, and it is important for them to understand that such risks cannot go unheeded. Over the years, Indian corporates have learnt to mitigate such risks by diversifying their supply chains, having multiple logistics partners, diversified geographical presence and multiple vendors.

- **Pandemic and other global epidemic diseases:** Risk to business owing to disruptions caused by COVID-19 pandemic and similar another global epidemic.

Strategic risk

- Strategic risk is the risk that failed business decisions may pose to a company. Strategic risk is often a major factor in determining a company's worth, particularly observable if the company experiences a sharp decline in a short period of time. Several factors, such as unethical or unlawful activities, poor customer service, product recalls, data breaches, or unfavorable media coverage, can lead to strategic risk. An organization's reputation can be severely harmed by a single negative incident, such as a high- profile data breach or fraud scandal, resulting in a loss of clients, income, and market share.

- **Resource scarcity / Misutilization / Overall Utilization:** Difficulties in acquisition of land, water, fuel, or other resources for operations of business.

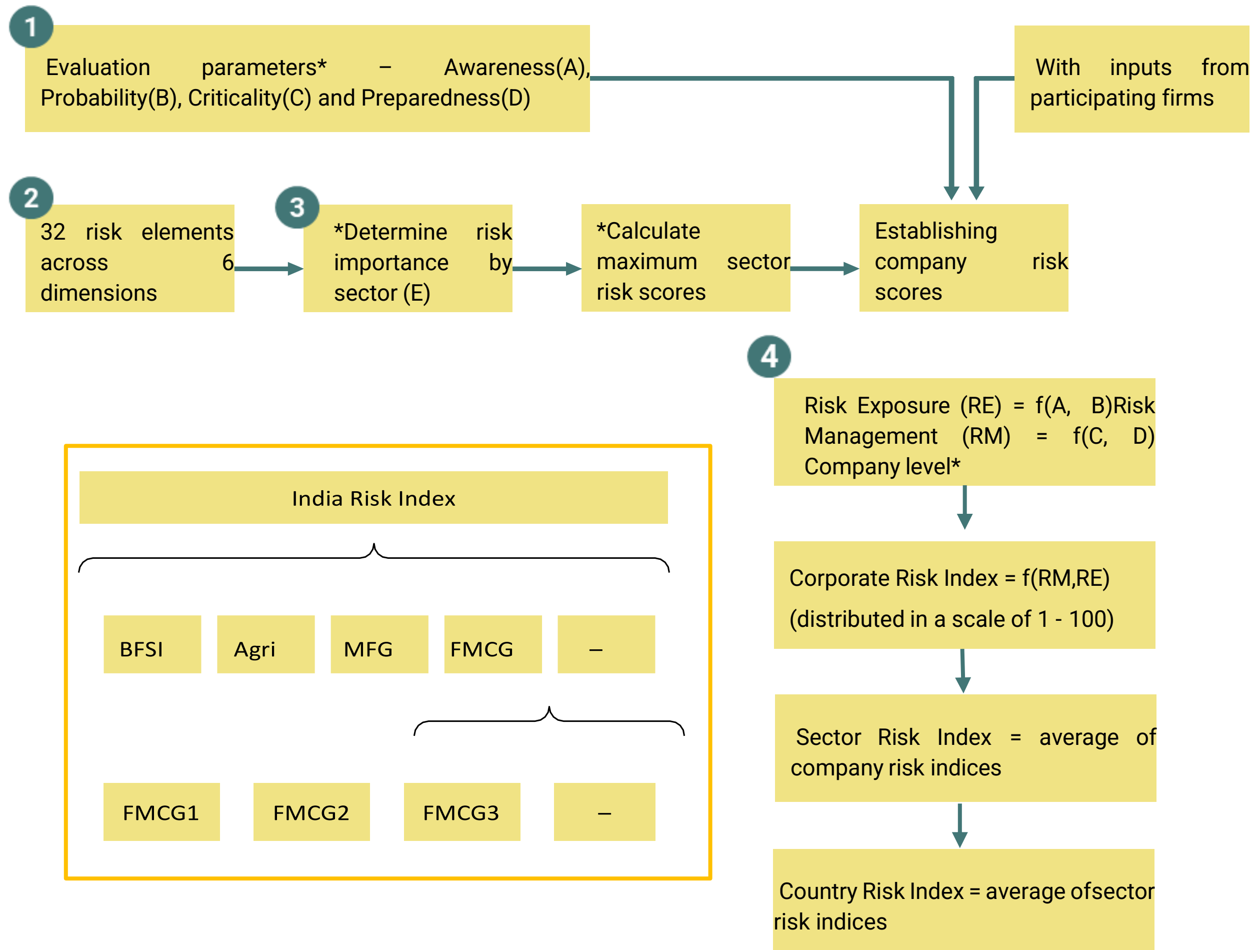
- **Public Sentiment:** Current events playing out in the public scene can change the public sentiment.

- **Delay in execution of projects:** Delays in execution of projects can surge in the capex.

- **Increased number of recalls and quality audits:** Impacts both the brand equity and increased operational expenses.

- **Failed / Hostile Mergers & Acquisitions:** High dependence on inorganic growth.

Bottom-Up Risk Assessment Approach



1. **Evaluation Parameters*:** The index maps the risks faced by any enterprise basis of Awareness, Probability, Criticality and Preparedness against the defined Risk elements. The evaluation Parameters are defined as: Awareness - Level of awareness of potential risk affecting the firm. - Likelihood of risk to affect the business goals of the firm adversely. Criticality - Level of impact of the identified risk on the success of business goals. Preparedness - Risk handling practices/ mechanisms already in place to handle the risk.

2. **Determining Risk Importance*:** Importance/Impact of individual risk element is established against individual sector based on the published corporate risk reports, in depth sector understanding by F&S team and SMEs.

3. **Calculating Maximum Sector Risk Score**: Weighted Sum of all risk elements based on their importance to the respective sector.

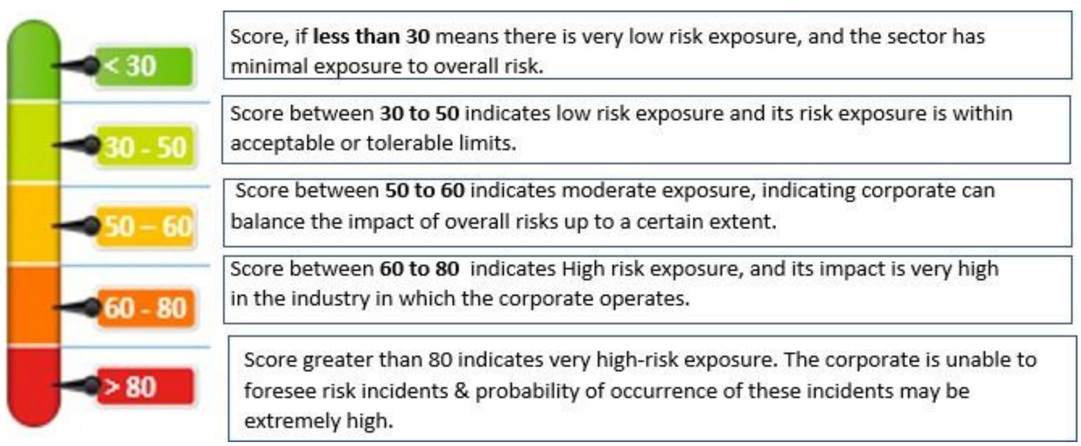
4. **Company Level*:** All the Risk Index scores for companies in a sector are averaged to represent the sector; and sectors average to India. Risk Exposure is defined as the function of corporate's Risk Awareness and Probability of risk occurrence. Risk Management is defined as the function of an enterprise risk preparedness and criticality risk impact assessment.

Defining the Risk Scale

We have selected 20 sectors to understand the current stand of our country today in terms of risk. Risk for various sectors is measured on the risk exposure scale and risk management scale.

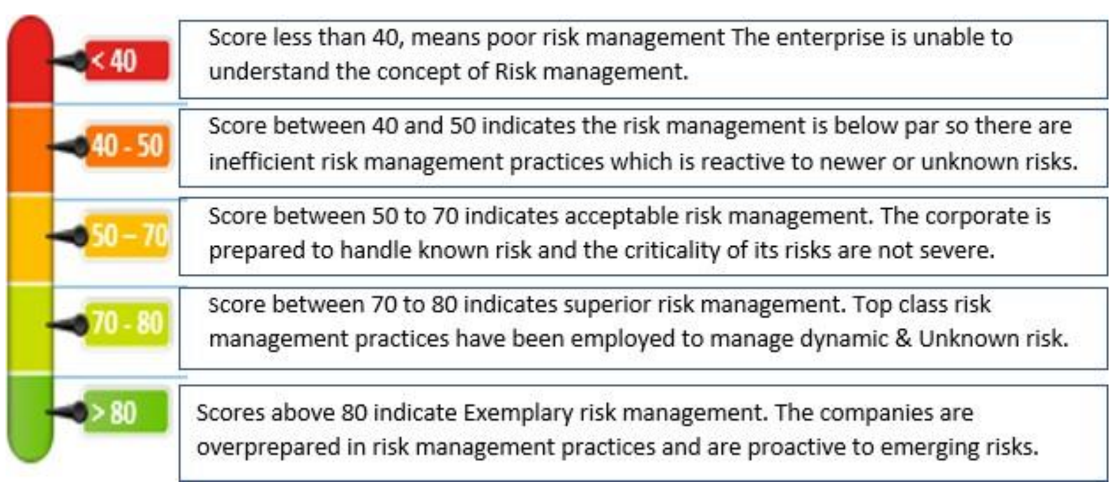
A. ICICI Lombard Corporate Risk Exposure – Scale

Risk Exposure: The impact of any internal, external or strategic occurrence on the financial performance of an organization is defined as the corporate risk exposure. Risk has traditionally been seen as something to be avoided – with the belief that if behavior is risky, it's not something a business should pursue. But the very nature of business is to take risks to attain growth. Risk can be a creator of value and can play a unique role in driving business performance. Let's look at the risk exposure scale.



B. ICICI Lombard Corporate Risk Management – Scale

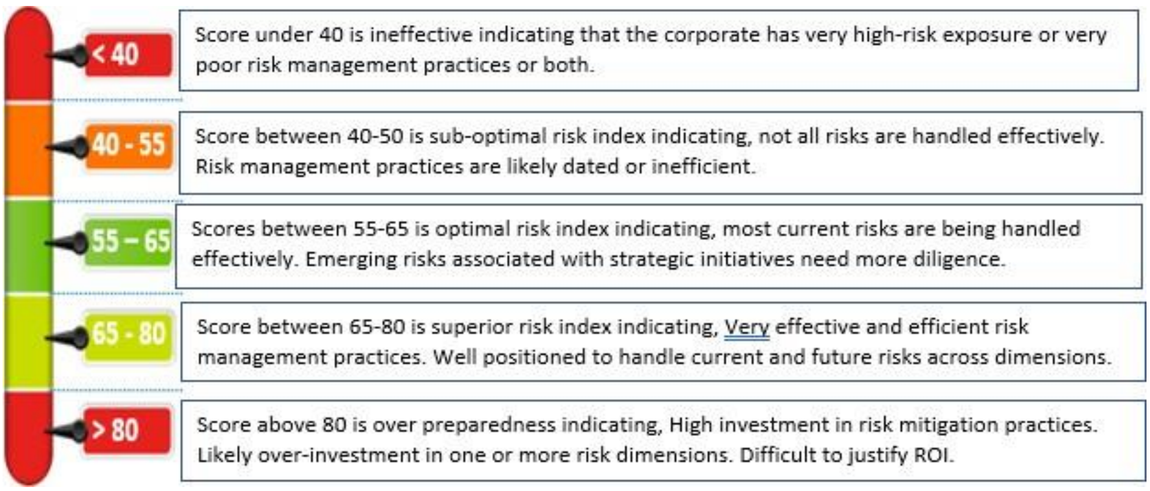
Risk Management: Identification, Evaluation and Prioritization of corporate risks followed by well-coordinated steps to minimize the occurrence of uncertainties in the foreseeable future is defined as the Corporate Risk Management. The risk management scale works in the opposite to that of the risk exposure scale. Let's look at the risk management scale.



C. ICICI Lombard Corporate Risk Index – Scale

Risk Index: Risk Index is a measurement tool to gauge the level of Risk Exposure against Risk Preparedness. The score intends to give companies/Sector/Country access to an extensive and quantifiable metrics of risk management.

Let's look at the risk Index scale.



India - Emerging Superpower with Optimized Corporate Risk Handling

Manufacturing sector contribution to India’s GDP in 2022 stands at 17% and is expected to grow to 25% by 2025, the expected growth is attributed to various favorable schemes initiated by Government of India like ‘Make in India’, ‘Digital India’, Improved Road Infrastructure, implementation of modern technologies of manufacturing resulting in optimized and effective production, Also the pandemic has made business realize that they cannot just rely on a single manufacturing hub; hence notion of “China+1” is making the world realize the significance of India. China is in a trade war with the USA, which is positively shaping the role India will play in the global arena.

The below chart showcases the gradual increase in India’s manufacturing exports.

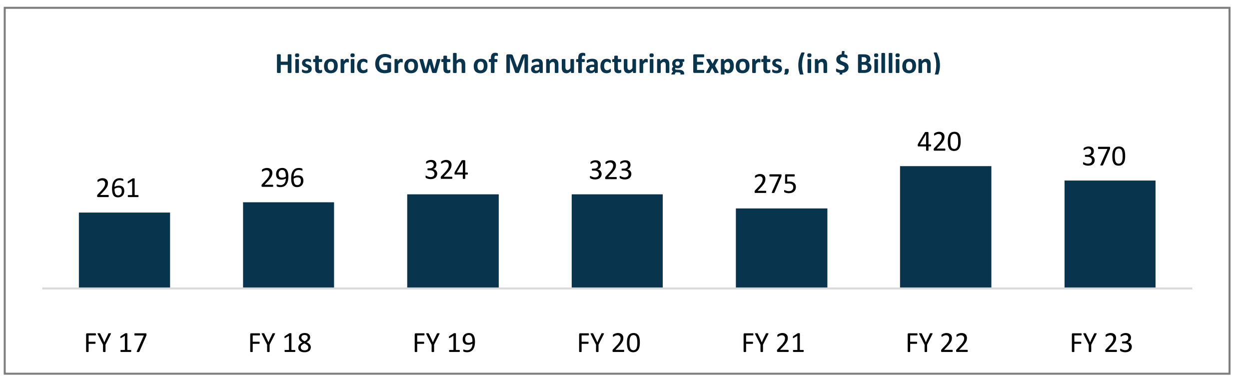


Figure 1: India’s Growth of manufacturing exports. (Source: Redseer)

Indian manufacturing sector is also focusing on electronics manufacturing like mobile phones, industrial electronics consumer electronics, etc. due to government initiatives the production has doubled since 2015.

Aerospace and defense sector in India have evolved significantly, Govt. of India have identified A&D as area of focus due to the belligerent neighborhood, steps like Make in India(Atmanirbhar Bharat) is helping the overall defense sector, however India still remains the largest importer of arms and ammunition, favorable policies and ease in regulations is helping the drone industry in India and many new start-ups and big players are entering in this space.

Urbanization is another phenomenon evolving in India and it is estimated that by 2030 more than 400 million people will be living in cities, due to this megatrend huge push towards realty and infra sector is observed which is also the growth of ancillary industries like metals, cement, water availability, sanitation, mobility etc., the government along with the private sector is working on multiple initiatives to manage the huge inflow.

India has observed a steady adoption towards EVs in recent years, though India adoption still remains very low in comparison to Europe, Canada, China, however all big auto players are coming with new lines of EVs, and significant strategic investment have been made. The adoption is primarily due to lower running costs, lower maintenance, zero tailpipe emissions, tax and financial benefits by the government, convenience of charging.

BFSI sector in India is showcasing a significant robustness in the time of global crisis, there is a growing demand for financial services as there is a gradual rise in income across income brackets, with a rapid increase in mobile penetration and internet availability more than 2100 fintech companies have emerged in India, the traditional banks are also adopting the digital technologies at a required pace, investment on making the systems secured from cyber threats is utmost priority. Policy support by the government in the union budget 2021-22 is taking up shape and is helping the BFSI sector in 2022 and coming years, like government approval of 100% FDI for insurance intermediaries have increased the FDI limit to 74% from 49%.

Healthcare sector is also continuously growing healthcare has become the one of the India's largest employers, employing around 4.7 million people, though in 2021-22 India only spends 2.1% of its GDP in healthcare, in the union budget 2022-23, US$ 11.28 billion was allocated to the Ministry of Health and Family Welfare (MoHFW). there is still huge room for improvement in the overall healthcare system in India. Efforts towards having well trained medical professionals in India is top priority. There were exemplary development in the vaccine manufacturing by India, Bharat Biotech Covaxin and Oxford AstraZeneca's Covishield manufactured by SII, helped India get a protection shield against Covid. There is a plan by the government of India to infuse US $ 6 billion to boost the healthcare infrastructure in India.

The IT/ITes sector is a key engine for fueling India's economic growth and contributing to 7.5% of India's GDP in 2021-22, the Big four IT firms in India have recruited over 1 million employees, As the world is moving towards era of digital economy Indian IT-sector will be contributing significantly towards this journey, the rollout of 5G communication technologies and adoption of new age technologies across industries; like AI, Robotics, Internet of Things will further increase the size of Indian IT sector.

Indian enterprises are also concerned about the risks emerging out of the growing economy and the globalization India is heading towards, its observed that Indian enterprises are taking significant steps towards risk management and keeping budget allocated to implement best in class risk mitigation practices.

India Showcasing an Optimized Risk Handling

Figure 2: Corporate India Risk Index 2022

Corporate Risk Index Score of 63 implies that Indian enterprises are handling the risk in an optimal way but still there is scope of improvement to get into superior risk handling territory, Indian enterprises have a well-defined risk management practice in place for inherent risks, however risk management can be improved further as a potential buffer against potential risk events arising from market & economy, operational and technology related Risk events, openness towards adoption of technology and having a well-defined risk management team was observed across enterprises in India.

Sectorial categorization across above stated five categories, it was found that risk management is getting a paramount importance in the growth strategy of every organization and all the organization fell either into ‘Superior Risk Management’ or ‘Optimal Risk Management’ category.

From a risk exposure front the intensity of impact due to market and economy related risks increased due to the heightened inflation, global recession, and geopolitical tensions though from a regulation point the sector specific policies by the government helped the industries. Some of the inherent risks exposure due to the operational aspect did not see a significant change as compared to previous year, however companies are adopting diversification, technologically enabling the supply chain, and creating better hedging against financial related risks, whose results will be seen in coming years.

Below is a broader categorization of sectors in terms of risk index:

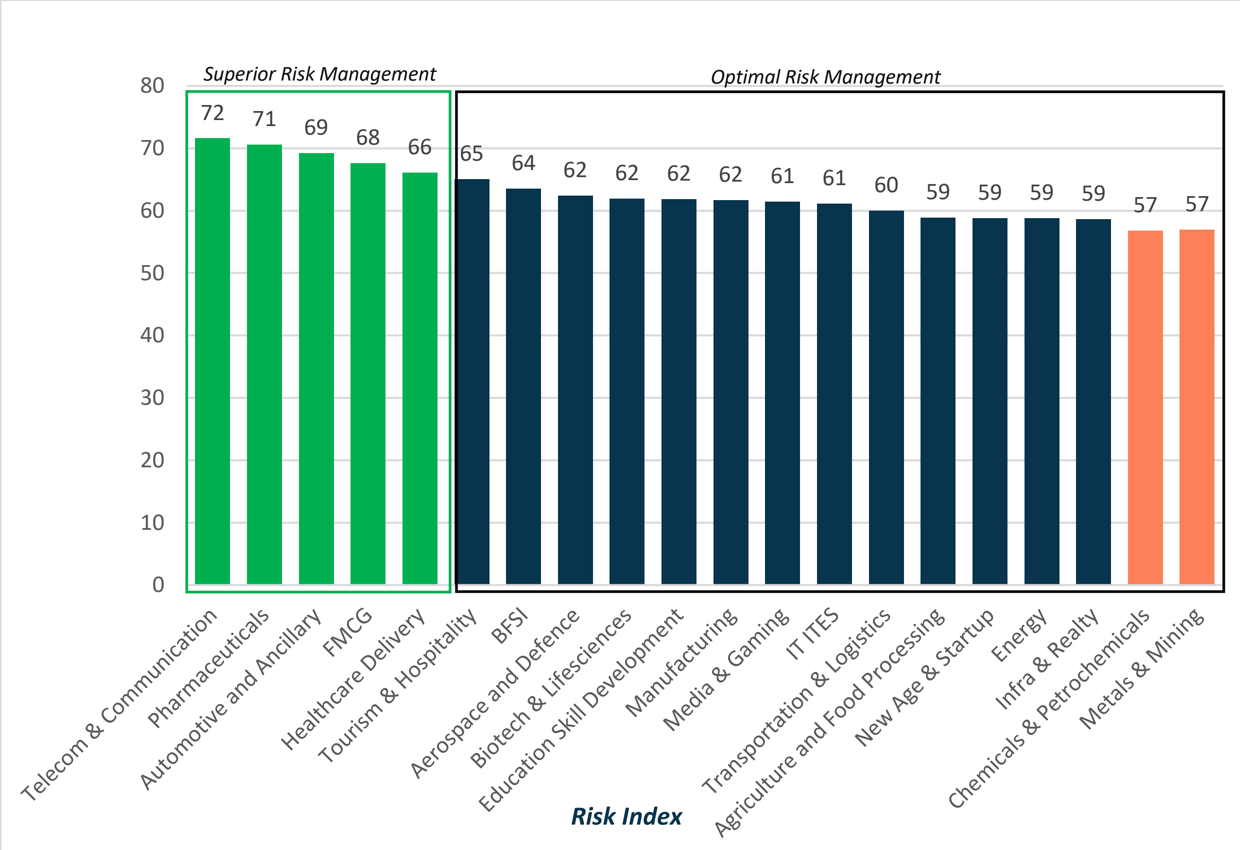


Figure 3: Corporate India Risk Index 2022 Sector Score

Superior Risk Index

Superior risk handling was found in five industrial sectors: Telecom & Communication, Pharmaceuticals, Automotive & Ancillary, FMCG, Healthcare Delivery.

Optimal Risk Index

Optimal risk handling was found in 15 industrial sectors: Tourism & Hospitality, BFSI, Aerospace & Defence, Biotech & Lifesciences, Education Skill Development, Manufacturing, Media and Gaming, IT & ITES, Transportation & Logistics, Agriculture and Food Processing, New Age & Startup, Energy, Infrastructure & Realty, Chemicals & Petrochemicals, Metals & Mining.

FMCG Sector Insights 2022

The FMCG sector has undergone a drastic transformation over the decades and is estimated to be the fourth largest sector in India. It is expected that the sector will grow at a CAGR of 14.9% and reach $220 Billion by 2025. The industry experienced a value growth of 8.4% in 2022, but there was a decrease of 1.5% in the volume. Given the fact that India has one of the greatest middle classes in the world, no FMCG company can afford to neglect this market. As more people begin to climb the economic ladder and the general public has access to the advantages of economic advancement, the FMCG market in India is expanding. More critically, with a median age of just 27, India's population is becoming more consumerist due to rising ambitions. This has also benefited the government. In the post covid era, the industry has displayed strong resilience and has successfully bounced back from the supply chain disruption with revenue growth of 10-12%, double the last fiscal year. The change can be attributed to price hikes across various product categories to offset the increase in raw Despite an increase in advertising expenses and raw material prices, the operating margin for this fiscal year is expected to return to its normal level of 19-20%, albeit with a slight moderation of 80-100 basis points. It is noteworthy that in the previous fiscal year, the operating margin had improved by around 100 basis points despite lower revenue growth due to the reduction in advertising and promotional expenses. The primary growth factors for the industry have been greater awareness, better access, and shifting lifestyles. The largest contributor to the entire revenue produced by the FMCG sector in India (which accounts for a revenue share of about 55%) is the urban segment. Yet, compared to urban India, the FMCG market has risen more quickly in rural India during the past few years. The semi-urban and rural populations are expanding quickly, and 50% of all rural expenditure is on FMCG products. In addition, the quarter between July and September saw a substantial increase in the amount of television advertising, totaling 461 million seconds—the most since 2021. With a 29% increase in ad volumes during the same period in 2019, FMCG maintained its top spot. Even the e-commerce industry displayed a respectable 26% increase from 2020. As an initiative, govt has also allowed 100% FDI in India's FMCG sector, as a result, India recorded FDI of up to $ 21 billion during the year 2020-22

According to CRISIL ratings, the FMCG players have displayed high stability attributed to huge cash flow generation, moderate need for capital spending along with capitalized balance sheets, and high liquid surplus. As consumer behavior and channel preferences change, Indian consumer packaged goods companies are adapting their strategies to remain competitive in the market. The number of internet users and smartphone owners is predicted to grow with the introduction of 5G telecom services by the end of 2023. As a result, online search results, ratings, reviews, and influencers will have a greater impact on customers. The sector is facing several challenges with persistent inflation and shrinking demand, leading to a shift in customers' behavior.

The pressure of reduced consumer spending has been exceptionally high for customers in 11% of India, and the rural markets have witnessed continuous negative consumption growth. There have been persistent efforts made by major players to gain the rural market share by introducing smaller packs of most of the products to overcome the demand-supply gap. There has also been a tremendous increase in D2C FMCG brands in India, and the number is expected to grow to 200,000 by 2025. The FMCG industry has benefited from significant investments and government support in recent years. Between April 2000 and March 2022, the sector attracted healthy FDI inflows of US$20.11 billion. The Department of Consumer Affairs has been allocated Rs. 1,725 crores (US$222.19 million), while the Department of Food and Public Distribution has been allocated Rs. 215,960 crore (US$27.82 billion) in the Union Budget 2022-23. To help Indian food product brands expand in international markets, the government approved the Production Linked Incentive Scheme for Food Processing Industry (PLISFPI) with an outlay of Rs. 10,900 crore (US$1.4 billion) in FY 2021-22.

A combination of rising income and stronger aspirations has led to an increase in rural consumption. In rural India, there is a rising desire for branded goods. On the other hand, with the unorganized market's share in the FMCG sector declining, the growth of the organized sector is anticipated to increase with higher levels of brand consciousness, strengthened by the expansion of contemporary retail. The expanding youth population, particularly in metropolitan areas, is a significant element driving India's demand for culinary services. India has a sizable population of young customers, who make up most of the labor force and who, due to time restrictions, only sometimes have time to cook. Internet portals are anticipated to be crucial for businesses looking to expand into the hinterlands. The internet has significantly helped by making it easier and more affordable for businesses to expand their reach. By 2025, India's internet user population is anticipated to reach 1 billion. By 2020, 40% of all FMCG purchases in India are anticipated to be made online. By 2030, there will be a projected 11% growth in the share of e-commerce in all FMCG sales. According to estimates, India will gain US$ 15 billion annually from the implementation of GST. GST and demonetization are anticipated to stimulate demand in both urban and rural areas, long-term structured economic growth, and enhanced performance.

The robustness of the supply chain has been enhanced by government incentives and FDI funds, capturing higher visibility for FMCG brands. The government PLI schemes have also given a boost to manufacturing capacity along with exports.

FMCG Sector Risk Index 2022 Vs 2021

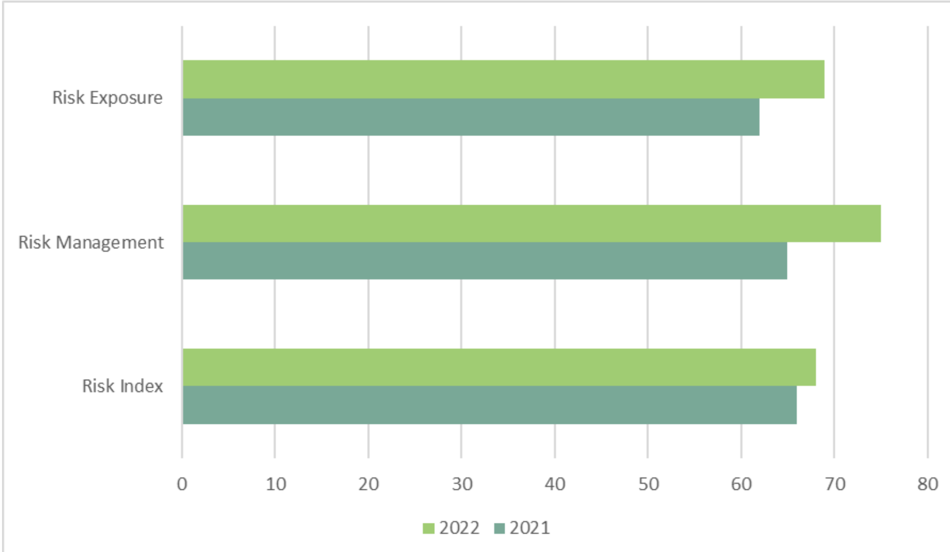


Figure 4: Detailed Comparative Analysis 2021 Vs. 2022

FMCG Sector Risk Index 2022 Vs 2021

The overall Risk Index for the sector slightly improved to 68 from 66 in 2022 that can be attributed to easing out of supply chain and more coverage through infrastructure development and signs of stability in prices of a few commodities. There has been more innovation in terms of product variety and varied packaging to increase availability of products to larger masses.

FMCG sector Risk Management 2022 Vs 2021

The sector risk management has significantly improved from 65 to 72 which is due to improved innovation in technology and improved operational efficiency. The risks pertaining to inflation are also being properly managed leading to increased sales volume and there is potential for improved operating margins.

FMCG Sector Risk Exposure 2022 Vs 2021

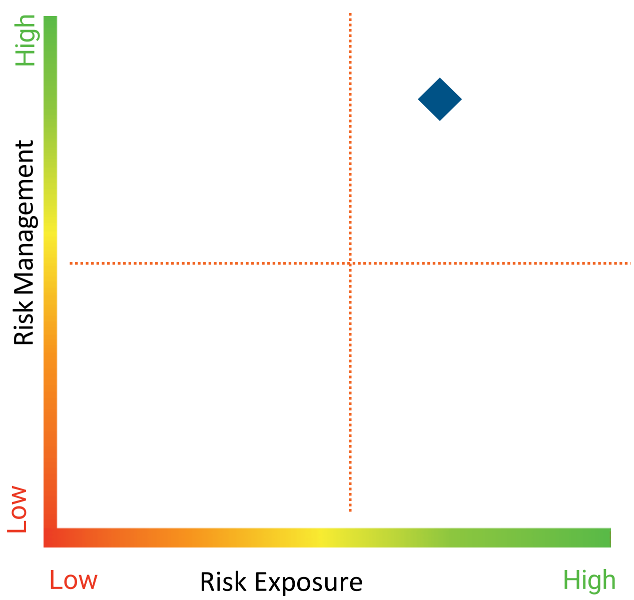
The risk exposure for the sector has substantially increased from 62 to 69 in 2022 which is due to the challenges arising in the demand environment with inflation impacting consumption. The increased commodity prices and volatility in input prices have led to reduced margins and advancement of market in rural areas is on the decline.

Key Highlights

Risk Dimension Analysis: Market and Economy

Risk Exposure Score: 76

Risk Management Score: 73



Inflation

- The industry has faced a decline in gross margin due to unprecedented inflation and volatility in input costs across commodity baskets.
- Raw material inflation has been unprecedented across raw material baskets of agricultural commodities, commodities linked to crude, and palm oil.
- While some commodities have recently experienced a correction, others had already begun to do so earlier this year, which is anticipated to lead to an increase in operating profit for FMCG companies.

Taxation

- KV Hariharan, who is in charge of data analytics and strategic planning at Amway India, stated that an increase in the tax exemption limit would boost disposable income, leading to increased spending and growth across various industries, including the FMCG direct selling sector. He emphasized the need for tax rationalization to reduce the burden on traders, lower logistics expenses, and deter smuggling activities across states and the country. Currently, the FMCG business is subject to a duty rate of around 22-24%, but the implementation of GST at a normal rate of 18-20% could address this issue.

Geo-political Tension

- In its quarterly update released on Wednesday, Godrej Consumer, a leading FMCG company, reaffirmed that the Indian FMCG industry has remained weak in the quarter, with inflation levels worsening due to geopolitical tensions.

Competitive risk

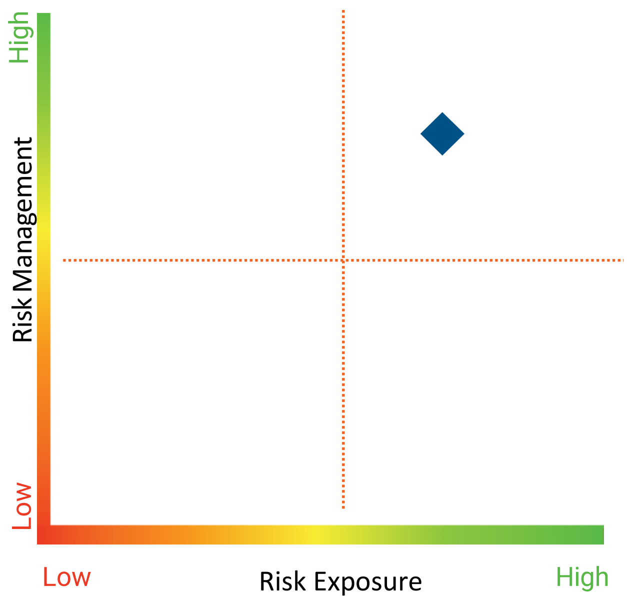
- The FMCG industry is facing various challenges, including the growing need for differentiating itself through sustainable and eco-friendly products and packaging, which are part of a circular supply chain.

- Large FMCG companies are being disrupted by smaller, local brands that can offer personalized experiences to their customers, gaining a cult following and loyal brand advocates.

Risk Dimension Analysis: Technology

Risk Exposure Score: 67

Risk Management Score: 73



Innovation Risk / Obsolete Technology:

- According to a report released by Nielsen, only 0.14% of the 16,914 FMCG launches between 2012 and 2016 were deemed to be breakthrough innovations suggesting that the FMCG sector in India faces significant risks when it comes to developing new products.

Intellectual Property risk

- The Indian Trademark Office has reported a 12% increase in trademark applications filed in India in 2020, indicating a rise in trademark disputes and the possibility of infringement risks for FMCG companies. In addition, patent filing also increased by 5.5% in 2021 in India.

- In 2020, there was a significant surge in patent applications filed in India, with a record number of 53,000 applications submitted suggesting an increasing emphasis on intellectual property protection within the country.

Data Compromise

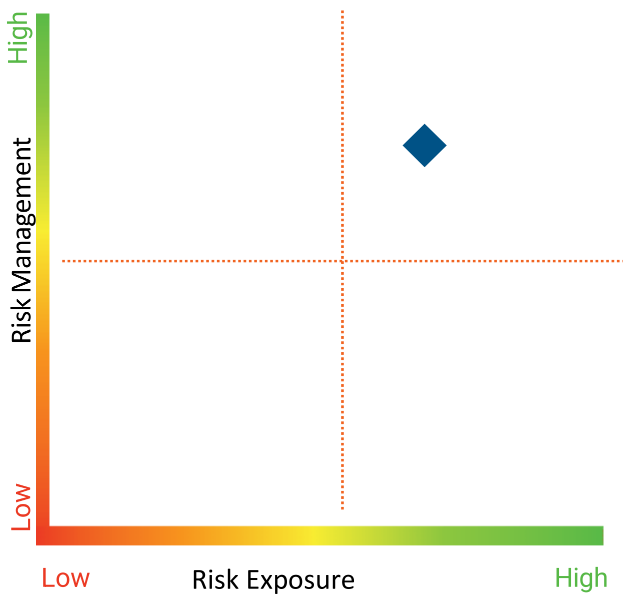
- The FMCG industry in India is under a considerable risk of data breaches. IBM's report suggests that the average cost of a data breach in India is INR 16.5 crore (approximately $2.2 million), highlighting the severity of the issue.

- To address this, in 2020, the Indian parliament introduced the Personal Data Protection Bill, which aims to create a regulatory body to oversee data protection and establish a framework for safeguarding personal data.

Risk Dimension Analysis: Operational and Physical

Risk Exposure Score: 69

Risk Management Score: 74



Critical Infrastructure Failure / Machine Breakdown

- Insufficient infrastructure can lead to excessive logistics costs, which can significantly affect delivery and operational efficiency.
- The FMCG industry faces significant challenges due to poor road conditions, an imbalanced transportation system, and a lack of technical support.

Business Continuity / Sustainability

- KPMG's report highlights that FMCG companies in India faces business continuity and sustainability risks as one of their primary risks in 2022. The report indicates that these risks arise due to factors such as climate change, natural disasters, and supply chain disruptions, which could affect the sustainability and continuity of FMCG operations in India.

Supply chain risk

- The FMCG sector in India has faced supply chain risks due to multiple factors, including infrastructure, government policies, logistics, and transportation as per a Deloitte report. The COVID-19 pandemic has further exacerbated the challenges faced by the sector.
- The FMCG industry in India is heavily reliant on seasonal agricultural output, which can significantly impact its overall performance. Crop failures, droughts, and natural disasters can disrupt the supply chain, resulting in shortages of raw materials and finished goods.

Commodity Price Risk - Volatility in prices of raw materials

- Consumer stocks drew attention as crude oil prices surged to multi-year highs, driven by escalating tensions between Russia and Ukraine and the US ban on Russian oil.
- FMCG companies are directly impacted by the rising oil prices as they rely on palm oil for their soap business, which accounts for approximately 20% of their consolidated sales. Any shortage in the supply of raw materials or increase in transportation costs due to the spike in oil prices will adversely affect the FMCG sector.

Environmental Hazard Risk

- Expected growth on ESG issues accounts for 50% of the enterprise value for top consumer-packaged-goods companies as per a McKinsey report.
- ESG risks, including environmental pollution, social instability, and supplier fraud, can build up and spread throughout the value chain, potentially leading to negative impacts on the operational efficiency, brand reputation, and financial performance of a company.

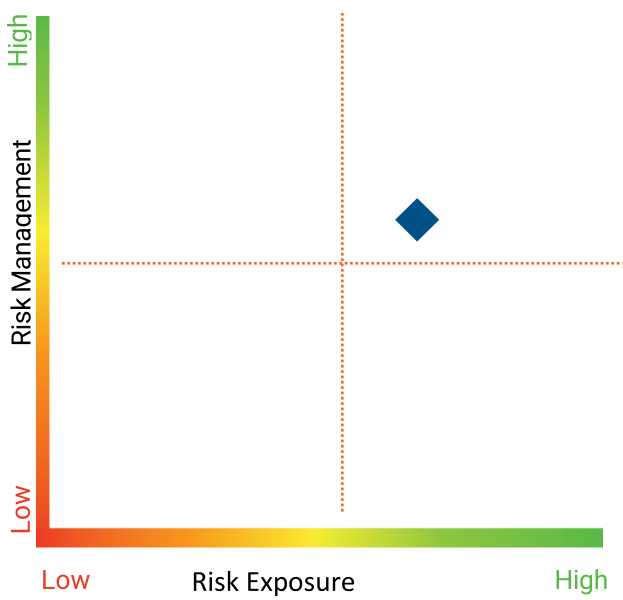
Financial Risk

- Insufficient cash flow to meet financial obligations like debt repayments or supplier payments could expose FMCG companies to liquidity risk, while defaulting customers or suppliers can result in credit risk leading to bad debts and financial losses. Additionally, fluctuations in exchange rates could impact FMCG companies' profitability, balance sheets, and cash flows.

Risk Dimension Analysis: Crime and Security

Risk Exposure Score: 68

Risk Management Score: 72



Cyber Crimes

- It is expected that cyber criminals will become even more advanced in 2023 when it comes to penetrating supply chains for the purpose of stealing from or harming businesses.
- Cyber criminals could also exploit vulnerabilities in simple warehouse equipment like barcode readers or Internet of Things (IoT) devices utilized in manufacturing and operational sites.

Counterfeiting

- The FMCG sector contributes to 75% of the total counterfeit value of goods. This results in a significant loss of legitimate employment, with an estimated 1.596 million jobs lost, with the FMCG industry being responsible for approximately 68% of the job losses.

- Illicit goods are estimated to cause a tax loss of ₹58,521 crore to the government, with the heavily regulated and taxed tobacco and alcoholic beverage industries accounting for 49% of the total tax loss. According to recent study conducted, counterfeits accounted for loss of sale worth more than Rs 300 billion for the FMCG sector every year.

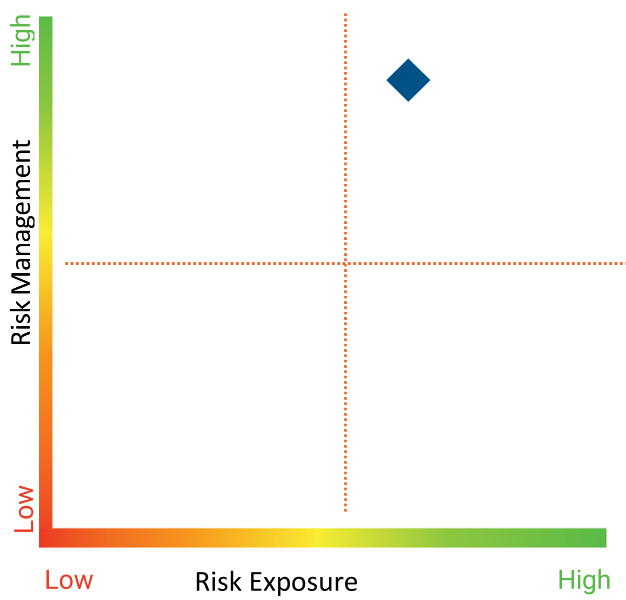
Terrorism

- The Indian FMCG sector has reportedly suffered losses amounting to INR 2,000 crore (USD 275 million) over the last five years due to disruptions caused by terrorism, as per a report by FICCI-CASCADE. And as per the Global Terrorism Index 2022 India is ranked 13th most affected country in the world.

Risk Dimension Analysis: Natural Hazard and Event

Risk Exposure Score: 66

Risk Management Score: 68



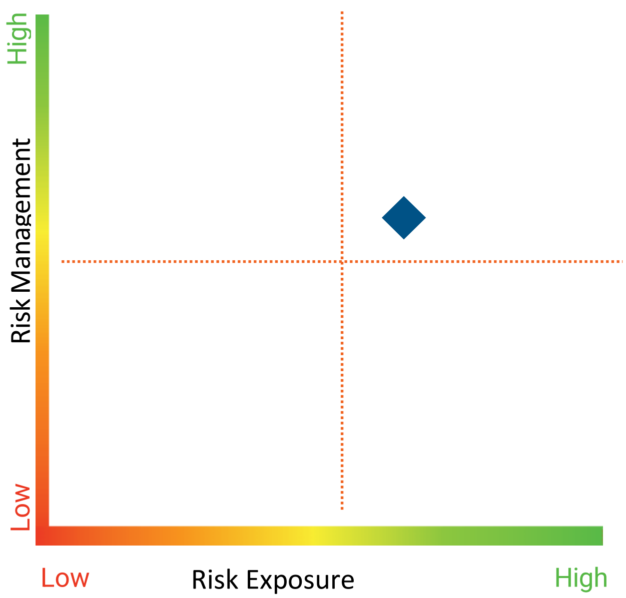
Natural Hazards:

- The flooding that occurred in Assam and Bihar in 2021 caused the shutdown of multiple factories and warehouses belonging to major FMCG companies like Coca-Cola, PepsiCo, and Britannia Industries. As per the National Disaster Management Authority's (NDMA) report, natural disasters have led to a loss of around INR 16,000 crore (USD 2.2 billion) to the Indian economy over the last two decades. To measure the risk due to natural hazard Global Disaster Risk Index is followed, where India is ranked 2nd most risky country out of 193 for risk of natural disasters in India.

Risk Dimension Analysis: Strategic Risk

Risk Exposure Score: 67

Risk Management Score: 75



Increased number of recalls and quality audits

- FMCG companies in India are facing increased scrutiny from the Food Safety and Standards Authority of India (FSSAI), which is prioritizing the safety and quality of FMCG products. As a result, there has been a rise in the number of quality audits and inspections. However, despite these efforts, in 2019, over 15,000 FMCG products were recalled by companies due to quality issues such as contamination, mislabeling, and packaging defects. This represents a significant 40% increase from the previous year. Quality issues and product recalls can have severe consequences for brands, including damage to their reputation, loss of customer trust, and declining market share.

Resource scarcity / Misutilization / Overall Utilization

- A report by the National Institution for Transforming India, a government body, suggests that by 2050, water scarcity in India could result in a 6% reduction in the country's GDP. This could affect the accessibility and cost of water for FMCG firms, causing production disruptions and higher expenses. Additionally, energy prices in India are among the world's highest, with an average industrial tariff of about 9 cents per kWh. As significant energy consumers, FMCG companies in India may experience greater costs due to rising energy prices and energy efficiency regulations.

Delay in execution of projects

- In India's FMCG industry, launching new products within a short timeframe is a significant challenge for 70% of executives, as revealed by a McKinsey & Company survey. Project delays may result in missed market opportunities and a loss of competitive advantage.
- According to a report by KPMG, project delays lead to cost overruns for 75% of FMCG companies in India. Such delays can increase material, labor, and equipment costs and financing expenses.
- Reputation risks are a significant challenge for 49% of FMCG executives in India, as per a survey by PwC. Delays in project execution can harm a company's reputation, as it might be perceived as an indication of poor management or lack of commitment.

- A report by EY indicates that 54% of FMCG companies in India are at risk of non-compliance with regulatory requirements due to project delays. Such delays can result in fines, penalties, and legal liabilities.

Public Sentiment

- FMCG companies rely heavily on their brand reputation to drive sales. Negative public sentiments can damage a company's brand reputation and lead to a loss of market share. According to a survey by Edelman, 59% of Indian consumers have boycotted a brand in the past year due to its actions on social or environmental issues.
- Social media has become a powerful tool for consumers to voice their opinions and hold companies accountable. Negative social media posts or online campaigns against FMCG companies can damage their brand reputation and lead to a loss of sales.
- Public sentiments can also lead to legal and regulatory risks, as companies may face fines or legal action for actions that are seen as harmful or unethical.

Strategic Risk

- A company's growth prospects in the FMCG sector can be adversely affected by strategic risks such as insufficient market research, ineffective strategic planning, and failure to innovate, as stated in a report by Deloitte. The report also highlights that strategic risks are one of the primary risks confronting the FMCG sector in India in 2022.

Failed / Hostile Mergers & Acquisitions

- The FMCG industry in India experienced a substantial drop in M&A operations in 2020 because of the COVID-19 pandemic, as stated in a report by EY India. Nevertheless, the industry is projected to observe a rebound in M&A activity in 2022, mainly driven by the necessity to consolidate and attain economies of scale, diversify to mitigate risks, and enhance product portfolios.

ICICI LOMBARD: Key Solution Offerings

Property

a. Businesses are always prone to risks and fire eruption and fire insurance provides a comprehensive protection against damages caused due to fire explosion and other risks. Besides fire related perils, it also protect damages caused due to any natural calamity, bursting of water tanks, theft etc. The built in covers include alterations or extensions, stocks on floater basis, tempoprary removal of stock, cover for specific contents, start-up expenses, professional fees, costs for removal of debris etc

b. Solutions

i. Property Loss Prevention exercise - We have developed the methodology of Property Value Added Services for corporate customers which focuses on technical engagement with detail risk visit, followed by benchmarking of the risk (Industry Risk Profiling).

ii. Fire Hydrant IoT - Fire hydrant online monitoring devices use IoT to monitor fire hydrants and assure their availability in emergencies. We've helped multiple corporate customers maintain and monitor this important fire safety component in real time.

Marine

a. We offer specially curated plans for covering the risk of theft, malicious damage, shortage, and non-delivery of goods, damages during loading and unloading, and mishandling of goods/cargo

b. Marine Cargo insurance primarily covers loss during transit caused due to fire, explosion, hijacks, accidents, collisions, and overturning

c. Solutions

i. GPS Device Tracking: With the help of our advance GPS devices we can have bird eye view on the consignment and vehicle from anywhere in the world. OurSAAS allows us to track and get the visibility of the vehicle on the basis of our requirements which is fully customizable

Liability

a. Comprehensive general liability:

i. This policy is important for every small and medium sized businesses to protect the insured entity against claims arising out of legal liability where they are heldresponsible for third party bodily injury or property damage due to insured's business, premises or products. It should be taken by every new business as it covers all risk a business may face.

b. Cyber - With cyber risk steadily increasing, security/ data breaches affect millions of records a year. Cyber Risk insurance coverage is designed to help an organization mitigate its risk exposure by offsetting costs involved with recovery after a cyber-related security breach or similar event.

c. Solutions

i. **Simulated phishing tests** - Simulated real looking phishing tests andrecord employee behavior to phishing attacks along with training collateral in form of co-brandable posters, infographics and videos

ii. **Cyber maturity assessments** - Assess the security posture of your organization and identify the potential risks with our assessment based on ISO 27001 Control measures for Information security

iii. **D&O** - The need of Directors & Officers Insurance is more than ever before. Any breachor non-performance in the duties can result in claims against directors, officers and employees by reason of wrongful act and need to incur various expenses like defense costs, damages or compensation and other incidental costs. This can affect company's growth and performance.

Group Health

a. Employees are the backbone of an organization and the most valued asset. OurGroup health insurance product is designed to offer health coverage to suit employees of all business types ranging from small & medium enterprises to large organizations.

b. Solutions:

i. **IL Take Care -** AI enabled mobile app for employees

ii. **Health assistance services -** Health Assistance is a dedicated medical care service that assists you in all your health related queries for identifying specialist/hospital/fixing an appointment with doctors/nutritionist /facilitating2nd opinion

iii. **Tele Consultation** – Hello Doctor

iv. The insured is eligible to avail unlimited General Physician consultations for routine health issues over the phone by aqualified doctor

v. **Diagnostics & pharmacy services** – Book a lab test or home delivery of medicines

Bibliography

https://www.thehindubusinessline.com/opinion/curb-counterfeit-trade/article66023296.ece

https://www.5paisa.com/blog/how-inflation-and-volatility-is-affecting-fmcg-companies

https://amlegals.com/key-legal-disputes-arising-in-the-fmcg-sector/

https://www.business-standard.com/article/companies/fmcg-firms-likely-to-face-supply-disruptions-in-assam-bihar-due-to-floods-121072201045_1.html
(https://economictimes.indiatimes.com/markets/stocks/news/fmcg-stocks-may-suffer-as-lockdown-impacts-demand-supply-chains/articleshow/74829356.cms

https://www.nielsen.com/in/en/insights/report/2019/the-power-of-her-a-womenomics-report/
https://economictimes.indiatimes.com/industry/services/retail/india-inc-wakes-up-to-womens-safety-concerns/articleshow/70284568.cms
https://economictimes.indiatimes.com/why-99-9-of-fmcg-innovations-fail/articleshow/46918237.cms

https://www.ficci.in/ficci-in-news-page.asp?nid=14268

https://getswipe.in/blog/post/impact-of-gst-on-fmcg-sector

https://sabpaisa.in/blog/fmcg-supply-chain/

https://www.business-standard.com/article/companies/fmcg-firms-expects-less-price-hikes-low-inflation-robust-growth-in-2023-123010400822_1.html

https://www.thesterlingchoice.com/fmcg-industrythe-future-of-jobs-and-skills/#:~:text=These%20challenges%20include%20the%20increasing,'better'%20for%20the%20user.

https://ipindia.gov.in/writereaddata/Portal/Images/pdf/IP_India_English_29.08.21_Final_.pdf
https://www.wionews.com/opinions/india-is-emerging-as-an-important-producer-of-counterfeit-goods-212263

https://www.expresscomputer.in/news/indian-companies-says-tech-adoption-digital-disruption-to-affect-businesses-in-2021-2030-says-protiviti-top-risks-survey/79922/

https://www.ibm.com/security/data-breach

https://www.businesstoday.in/current/economy-politics/data-protection-bill-may-tighten-compliance-for-firms/story/416227.html

https://www.linkedin.com/pulse/problem-selling-fmcg-online-ashish-kovuri/

https://fmtmagazine.in/food-recalls/
https://www.indiaretailing.com/2019/02/05/product-recall-the-big-challenge-for-food-businesses/

https://www.thehindu.com/sci-tech/energy-and-environment/india-faces-worst-water-crisis-niti-aayog/article24165708.ece

https://m.rbi.org.in/Scripts/BS_ViewBulletin.aspx?Id=20568

https://www.mckinsey.com/~/media/mckinsey/industries/retail/our%20insights/perspectives%20on%20retail%20and%20consumer%20goods%20number%208/perspectives-on-retail-and-consumer-goods_issue-8.pdf

https://www.edelman.co.in/trust-in-india

Disclaimer:

Notes:

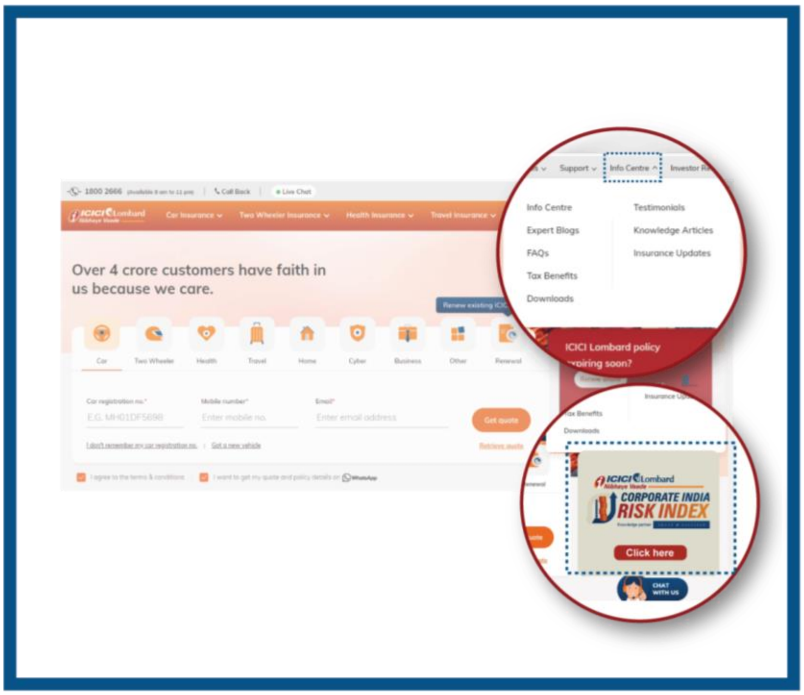
ICICI Lombard
Nibhaye Vaade

CORPORATE INDIA RISK INDEX

Intelligence partner FROST & SULLIVAN

Now accessible at

www.icicilombard.com/corporate-india-risk-index



Please send a mail to ciri@icicilombard.com to get your customized ICICI Lombard Corporate India Risk Index Report

ICICI Lombard
Nibhaye Vaade

CORPORATE INDIA
RISK INDEX

Intelligence partner FROST & SULLIVAN