

Retail and Consumer Worlds

July 2008

Contents

P&G and innovation: an interview with Diane Dietz

Vietnam: Open for business

Earning a healthy return on your workforce investment

Increase after-tax return when outsourcing

REACH regulation

Economic crime survey

Olympics quiz

In this issue, you'll gain an inside view into Procter & Gamble. In our cover interview, Diane Dietz, vice president and general manager Oral Care, describes the company's culture of innovation. Dietz describes how the company has "opened up" under the leadership of A. G. Lafley – and offers up interesting examples of how the organisation puts the customer at the centre of everything it does.

For our emerging markets spotlight, we travel to Vietnam, an especially appealing destination for retail and consumer companies, despite some macroeconomic pressures resulting from high inflation. Recently the Vietnam retail market has been ranked as one of the world's most attractive! We've attached a link to our firm's publication "Vietnam – A guide for business and investment" for further reading.

Curious about how savvy companies are addressing the health and wellness concerns of their employees? Inside you'll find out how an integrated people and health strategy can help to build and sustain a vital and engaged workforce.

Retail and consumer goods multinationals are increasingly deciding to outsource business activities to third parties. This trend is growing as the global powerhouse shifts to Asia and new markets. In this issue we examine the tax issues and implications of outsourcing.

Finally, here's a chance to showcase your knowledge of Olympics history! In honour of the upcoming Beijing Olympics, you'll find a quiz inside – with a chance to win a great Olympics-themed prize.

We welcome your comments and suggestions.



A handwritten signature in black ink, appearing to read "Carrie Yu". The signature is stylized and cursive.

Carrie Yu
Global Retail & Consumer Leader



Interview with Diane Dietz

Innovating the road to success at P&G

As a company, Procter & Gamble (P&G) is practically synonymous with innovation and over the years has operated one of corporate America's top research departments. But that hasn't stopped P&G from innovating about innovation. In 2000 when A. G. Lafley became CEO, he brought with him new ideas about the process and culture of innovation, new ways of working with customers and suppliers and a tighter connection between innovation strategy and the business strategy. He and his leadership team coined the phrase "innovation as a team sport" – and pointed the company down a whole new road of collaboration, openness and ideas. Recently, PwC talked with Diane Dietz, VP and general manager, Oral Care, about how P&G "brings the outside in" to continuously improve its ideas and performance.

Diane Dietz

Diane Dietz, vice president and general manager, Oral Care, joined Procter & Gamble in 1989 as a sales representative in the oral care division. Her previous roles included brand manager, Fixodent; brand manager, Crest; marketing director, Crest Toothpaste and Brush; and general manager, Oral Care. Oral Care manages seven different categories, including two of the company's billion dollar brands – Oral B and Crest. Diane was named one of *Ad Age's* Top 50 marketers of the year in 2007. She has been active with Boys & Girls Clubs of America and United Way.

Diane, P&G has established such a great reputation around innovation. Tell us more about this concept of “innovation as a team sport”. How does this actually work at P&G?

First of all, everyone at P&G sees themselves as an owner, and ownership is a very important part of our corporate culture. Everyone on the team has a unique role – and there is a clear end result that each person can focus on. Just as important, we think of innovation in terms of the outside world. Innovation doesn't just happen here at P&G, in isolation, or in a lab. Innovation happens by being in touch with our consumers and their needs. And in a company as global as P&G, consumer needs are very diverse. So really, you have to be in touch with the outside world.

Can you give us some examples of ways you either customise products for a particular market or introduce products only in certain markets based on those diverse needs?

Sure. You know, washing clothes by hand is still very common in certain parts of the world, where there are no washers and dryers. So in our laundry business we noticed, by going out and being in touch with these consumers, that the amount of suds needed for someone who's hand-washing is different from someone who's using a high-performance washing machine. If you look at oral care, which of course is the business that's near and dear to my heart, again needs really vary around the world. In a market like North America, many consumers want not only a healthy smile but a beautiful smile – so whitening teeth and removing stains are important considerations. In other parts of the world, there are major oral health issues. The thought of whitening is not top of mind when you have a lot of health problems and can't even afford to go to a dentist.

So – it starts with the consumer. Sounds like common sense. What's different about that than, say, 10 years ago?

Well, A. G. Lafley has been a big part of this. He came out with the mantra, “consumer is boss.” It's really simple, yet it's very inspiring when you truly look at what consumers want and try to understand through their eyes what they need. Many people would define innovation as superior technology – but there are a lot of things about a consumer's experience that aren't just based on technical performance. Years back, we were very focused on cavity control, but today's oral care consumers have other needs, too. They want fresh breath, a white smile, or even just to enjoy their brushing experience. When we started to think about all of that, it really opened our minds. We'll never stop trying to come out with products that are superior – we're just defining superior in a broader way.

P&G has a huge variety of product offerings. Can you talk a bit about how that works with your retail partners, especially since some of your retail partners are much bigger than others – say, for example, Wal-Mart?

We have teams that work with each of the retailers, so their entire focus is on that retailer. For example, there is an entire team that works directly with Wal-Mart across every one of our businesses, and what we're trying to do is what's right not only for our business but for the shopper at Wal-Mart or the shopper at Target. We work closely with our retailers to understand the unique needs of their shoppers. We have some retailers that are more beauty-focused, some more health-focused, some more kids-focused, and we can use our menu of offerings to work directly with those retailers.

You've been talking about innovation that is consumer-driven and innovation that's driven by collaboration with retailers. I wonder if you can tell us about innovative ways you've been able to involve consumers in the product development process.

What we've found effective is just to be involved with the consumer, often on a one-to-one basis. So my team and I actually go on in-home visits and spend time with our consumers, in their own homes, to understand how they're using our products. We have them demonstrate how they use the products and talk about what they like and don't like. We often shop with them in retail stores and ask what they're thinking about when they make purchases. You can imagine, if you go shopping with a consumer in China it's a very different experience than going along with someone in the U.S.

We've heard the term open innovation and the phrase "connect and develop" used in association with P&G. Is this what we've been talking about – or are these additional concepts?

Sure, this is it. "Connect and develop" is the view that ideas can come from anywhere, not just inside one company. So it really means collaboration – and bringing the outside in. We have situations where an innovation or an idea didn't come from P&G, but we worked with other companies or acquired the idea. Glide dental floss is a good example. Glide was actually developed by Gore-Tex. Years ago we thought about whether we should try to develop something ourselves or look at what was best-in-class and already on the market – and that's when we connected with the Gore-Tex folks and brought Glide into P&G. No one has the monopoly on creativity, so we are very open to looking at where creative ideas may exist outside of P&G.

The current interest in health and wellness certainly fits well with personal care products. What can you tell us about how and when P&G latched onto this trend?

Looking at the oral care business, we have been onto that trend since Crest toothpaste was launched. Back in the 1950s in the U.S., we were the first toothpaste to include fluoride and the first toothpaste to get the American Dental Association seal. The innovation of fluoride is still held up in the U.S. as one of the biggest oral care innovations ever.

The difference I see now, from the standpoint of my product area, is that there are more connections made in the scientific community between oral health and whole body health. The mouth is the gateway to the body and many conditions are first diagnosed in the mouth. That means, for example, that flossing daily helps prevent gingivitis, which is linked to heart health. While we're not advertising that link, we make sure that we are doing our part by emphasising the importance of good oral health. That's where we spend a lot of our time. We also do a lot of clinical research to help advance the field of oral health, and this is shared with the dental community at conventions and so on. So we try to balance the right message for the right constituency.

How about the current economic situation – how do you see it affecting your business and strategy?

The main issue that we have to deal with is obviously rising commodity costs. For some of the ingredients in our products, the prices have skyrocketed, but we have tried to minimise price increases. We have a wide variety of pricing across our products, so hopefully every consumer can find a product they believe is a good value.

Diane, another area in which P&G has gotten accolades is corporate social responsibility. What kinds of programs is the oral care division involved in?

Several years ago, the U.S. Surgeon General issued a report showing that tooth decay is the number-one chronic childhood disease. More than 51 million school hours are lost each year as a result of dental-related illnesses. It's hard to believe that this is the case after so many innovations and so much progress, but it's true. What's been exciting for me personally is that P&G saw this, and we said "OK, this is something we can do something about." Since then we've worked extensively with organisations like the American Dental Association, the American Academy of Pediatrics and Boys and Girls Clubs of America to provide oral health education and access to care in underserved communities. We call the program "Crest and Oral-B Healthy Smiles" and are on track to touch 50 million children by the year 2010.

That's quite a goal.

Yes, it is. If you look at what's possible – and our goal is to give every consumer around the world a healthy, beautiful smile, and a smile that will be healthy and beautiful for their lifetime – it's a really exciting time in oral care. The sky's the limit in terms of what we can do for consumers, shoppers and retailers. ■

Interview conducted by Christopher Michaelson, Advisory Director,
PricewaterhouseCoopers-US

Vietnam: Open for business



Vietnam is a country of 86 million people. The population is young, has more disposable income than ever before and is ready to consume. The country's recent admittance to the World Trade Organization (WTO) presents exciting new opportunities for foreign companies.

Vietnam continues to attract considerable interest from foreign investors. The attractions include a young, well educated and growing population. In fact, with a population of more than 85 million, Vietnam is larger than any member country of the European Union! Real GDP has grown at an average rate of 7.6% since 1991. The country has been moving from a centrally-planned economy to an open, socialist-oriented and multi-sector market economy. In 2007 it was officially admitted to the WTO, registered GDP growth of 8.5% and record high foreign direct investment of US\$ 20.3 billion – almost 70% higher than in 2006.

Strong growth potential

The long-term economic growth potential of Vietnam remains very strong. A macroeconomic study conducted recently by PricewaterhouseCoopers concluded that Vietnam will have the highest GDP growth potential in the world for the next few decades.

Modern organised retail in Vietnam is behind Asian and global averages, and the size of the sector is currently below its potential. The well-documented growth in the economy, increasing consumption, urbanisation and the demographics of the population create many opportunities.

Low penetration of organised, modern retail

According to the General Statistics Office of Vietnam, total retail sales of goods and services in 2007 were 726 trillion VND (US\$ 45 billion), an increase of 23% from 2006. Small street shops owned by individuals, families or small companies are the dominant form of retail. Organised, modern retail is estimated to account for approximately 15% of the market.

Urbanisation a key factor

Vietnam is yet to experience the urban population explosion taking place in other fast-growing countries in Asia. Approximately 23 million people live in urban areas. The 27% urbanisation ratio is one of the lowest in Asia. Organised retail is centered in the capital Hanoi and Ho Chi Minh City in the south. Both cities are home to modern retail outlets including cash and carry superstores, Western style department stores, speciality stores and luxury boutiques controlled by brand owners.

Doing business

Vietnam remains an emerging market with unique characteristics, opportunities and challenges. First, *the tax and legal environment differs from other countries*. Legislation changes faster and is subject to more frequent reform and

amendments. One unusual factor is a stipulation in the corporate income tax law that allows only limited tax deductions for advertising and promotion expenses – a major concern for fast moving consumer goods (FMCG) companies.

Second, *the lack of infrastructure, especially outside big cities, can be limiting* and hinder investment. Despite continuous improvement, standards of corporate governance and transparency are behind international norms. A developing legal framework means that there are gaps and inconsistencies in execution.

Third, while the cost of blue collar labour remains low even by Asian standards, *the shortage of skilled human resources* has led to wage inflation in major cities and in certain professions including marketers, controllers, supply chain managers and general managers. On the other hand, Vietnam is able to draw on the talents of overseas Vietnamese returning to the country of their origin. The Highlands Coffee chain and the Pho 24 restaurant chain are two examples of businesses that have achieved strong brand recognition in the major cities and which were founded by overseas Vietnamese.

Rapid growth in FMCG sector

Sales of FMCG are growing rapidly in urban Vietnam, and the competition between multinationals and domestic players is intense in many product categories. Affluent young Vietnamese consumers expect to be courted by brand owners in a similar fashion as they are treated by motorbike and mobile phone handset manufacturers. A recent well-publicised manifestation of this is the fact that Vinamilk, a major state owned enterprise, has entered into a US\$ 2 million promotional agreement with UK Premier League Football Club Arsenal in an effort to promote their products. Private Vietnamese companies can also be formidable competitors. 2007 market data indicates that the fastest growing FMCG product in Vietnam was “Khong Do” a carbonated tea drink produced by THP, a company also known for popular beer and energy drink brands.

Another indication of the momentum in FMCG is Amway Vietnam’s recent establishment of manufacturing operations in the country and the company’s plan to begin local distribution of more than a dozen products. It is worth noting that Avon and Oriflame have already established operations.

Privatisation and mergers and acquisitions (M&A) create market entry opportunities

The Vietnamese government is committed to privatising state-owned enterprises, and this creates interesting market entry opportunities. In addition, M&A activities are increasing rapidly, creating new avenues to entry. During recent months, beer companies have been especially active in M&A. In April Carlsberg announced the completion of its long-anticipated US\$117 million acquisition of an equity stake in the Hanoi Beer, Alcohol and Beverages Company, after the privatisation and IPO of the former state-owned company earlier this year. Among the competitors of Carlsberg, Heineken and Tiger are already well established and are brewed locally.

In another important deal demonstrating interest in the market, last summer Sojitz Corporation of Japan acquired a 20% stake in Interflour, the second largest milling company in Vietnam. Due to rising incomes and growing consumption of meat, demand in Vietnam is on the upswing for cereal grains that can be processed into animal feed.

Foreigners interested in buying stakes in Vietnamese companies not only face tough price negotiations but also high expectations for technology and know-how transfer.

Infrastructure and land usage rights are challenges

Infrastructure development in Vietnam has not been able to keep abreast with the rate of economic growth. Companies doing business in the country have to adjust their practices to take into account limits in port capacity and weak air and road networks. Development of commercial real estate projects has been slow, and there are limited immediate options for locating retail outlets. Progress is being made, with a large number of building projects in the pipeline, but in the short term shortages of retail space still exist.

Retailers, shopping mall developers and others that aim to build need to be aware of regulations concerning land. In Vietnam, land is considered the property of the people and is subject to exclusive administration by the State. Foreign land users are entitled to lease land from the State or from Vietnamese or foreign-invested enterprises, with certain restrictions. For foreign land users the maximum lease period is generally 50 years, although in special cases it may be extended to 70 years. Foreign-invested enterprises may only use land for the permitted purpose.

Compliance with WTO commitments opens the door in January 2009

Vietnamese enterprises are free to carry out retail and distribution activities in Vietnam, but this is a sector which is still being gradually opened up to foreign investment. Currently, in the absence of local manufacturing, 100% foreign owned enterprises in Vietnam are restricted from selling imported finished products directly onto the Vietnamese market and must onward sell the goods to locally appointed domestic distributors. Vietnam has however committed to allow 100% foreign ownership of retail and distribution entities from 2009. The business community in Vietnam expects a large number of entrants once the new rules are in place; however, there are some uncertainties about the speed at which authorities will be able to clear applications for new

businesses. While there is a general commitment to allow 100% foreign ownership of retail business from 2009, the Vietnamese government has legislated an Economic Needs Test (ENT) which will be used to evaluate how many retail outlets a foreign investor will be allowed to operate. This restriction was unexpected and is of concern to foreign retailers that have visions of multiple outlets. How the government intends to implement the ENT and assess foreign retailers in practice remains to be seen, but it can be anticipated that delays will arise in getting permission to open multiple outlets.

In summary, the time is right for foreign retailers and consumer goods companies to consider their Vietnam market entry or expansion strategy. The market opportunities are considerable and regulatory constraints are disappearing.



For more about the market in Vietnam, download “Vietnam – A guide for business and investment” at <http://www.pwc.com/vn>



Richard Irwin
Tax Partner, Mekong Practice,
PricewaterhouseCoopers-Vietnam

Earning a healthy return on your workforce investment: From wellness to well-being



Leading companies are looking beyond wellness to well-being. Well-being can encompass a broader people agenda of rewards, learning and development, work/life, and diversity, as well as physical and emotional well-being. Employee performance is maximised when these broader drivers of performance are considered collectively.

In a world with constantly changing technology, an increasing awareness of our environment, strict cost control pressures, and a global war for talent, can focusing on the health and vitality of employees and their families really make a difference? Organisations around the globe are betting on it.

Organisation leaders are interested in a renewed focus on the health of their people, both domestically and globally:

- In the U.S. alone, over 75% of the nation's medical spending is for people with chronic diseases, which are widely prevalent and largely preventable.
- Productivity costs associated with health can range to as much as 35% of labour costs, including the costs of unplanned absences and disabilities, reduced workplace safety, and reduced effectiveness while at work.
- Employees feel more valued, engaged and loyal when their employer demonstrates a concern and support for their overall health and well-being.
- Corporate responsibility, reputation and sustainability are enhanced when good health is integrated into the overall green agenda of an organisation and its communities.

In fact, leading organisations are integrating health and well-being into their overall people agenda – tailoring their approach to both the mission of the organisation and the critical health needs of their employees and communities. These strategies focus on three types of interventions:

- **Personal support** – increasing awareness, readiness to change, and reducing specific risk factors that contribute to poor health (e.g. smoking, nutrition, lack of exercise, stress). These strategies range from broad-based education and awareness programs such as employer or community health fairs to providing individualised information about personal health risks and what one can do about them. For people with the highest health risks, intensive one-on-one behaviour modification interventions can be offered.
- **Environmental support** – modifying the environment to encourage and support healthy choices in the workplace. This can include evaluating the choices available in vending machines, cafeterias and business meetings as well as encouraging the use of stairways and walking paths by making them more personally inviting and safe. Some organisations have gone a step further by implementing on-site clinics, fitness centres or meditation rooms and integrating these facilities with overall health promotion efforts.

- **Cultural support** - integrating health and well-being as part of the cultural fabric of the organisation and the community. Through visible leadership, integrated systems of accountability and cross organisational and community collaboration and support, measurable improvements in health status can be achieved. Visibility can be enhanced with team-based competitions and incentives to drive excitement and participation. Accountability can be integrated into management programs much like quality and safety initiatives.

Companies will do well to consider the following when examining health within the context of the workplace:

- **Embed health and vitality into corporate values**
Health and well-being initiatives will be most effective when they are viewed as a natural extension of the values of the organisation and leadership “walks the talk” and takes an active role to energise and champion the efforts.
- **Educate and motivate to reduce behaviour risks**
An organisation’s efforts can make a real difference in peoples’ lives and in business results. This is particularly true when combined with appropriately targeted education at all levels of the organisation. Beyond basic education, messages need to recognise diverse individual and organisational motivations to improve health and well-being.
- **Re-evaluate whether it is easy to do the right thing**
Results are more easily achieved when the healthy choice is the easy choice. Consider the food in the cafeteria, bicycle racks, on-site programs and support with access at work and at home, and extended outreach to the family and community.
- **Measure both individually and organisationally**
Individualised reports can help people to “know-their-numbers” and guide them as to how to improve their health profile. Aggregate reports can focus broader organisational efforts to impact the overall people and health agenda and serve as a common framework for measuring baseline and progress over time.
- **Make it personal, profitable and private**
People can be motivated by personal stories, personalised information and targeted incentives to participate and succeed. At the same time, this needs to be balanced with organisational commitment to protect the privacy and equity among employees.

An effectively-integrated people and health strategy can make a difference in people’s lives and help build and sustain a vital and engaged workforce. As with most change management efforts, the best results are achieved with committed and visible leadership and an artful and disciplined approach to execution. In the end, the health and well-being of our organisations and communities can be optimised by improving our focus on the health and well-being of our people.

Heather Lessely, Manager, Healthcare Practice,
PricewaterhouseCoopers-US

Kathryn Stein, Managing Director, Healthcare Practice,
PricewaterhouseCoopers-US

Michael Thompson, Principal, Healthcare Practice,
PricewaterhouseCoopers-US

Increase after-tax return when outsourcing



Combining savvy tax planning with an operational decision to outsource will give retail and consumer goods companies the best financial result.

Retail and consumer goods multinationals have increasingly looked to outsourcing to third parties or related entities to reduce their cost, increase efficiency and promote customer satisfaction. This trend is growing as the global powerhouse shifts to Asia and new markets open up.

Managing this activity centrally enables a single point of contact to be responsible on a global or regional basis. The major responsibility lies in managing the critical risks, functions and overall strategic direction of the outsourcing activity.

In making a commercial decision to outsource, rarely is tax included in the metrics; however, given that moving to a centralised business model will require the transfer of functions, assets and risks across borders, there will always be tax consequences. Consequently, there are significant opportunities to substantially improve the bottom line by combining tax planning with the commercial decision.

Tax can add value to the operational benefits and increase after tax-return by:

- Helping justify and improve project returns by adding tax savings to the operational savings;
- Ensuring operational change does not create tax exposure, risk or incremental cost;
- Reducing and managing product costs by integrating indirect tax planning in the supply chain design;
- Managing where profits and cash sit in the supply chain, including providing additional funds for reinvestment; and
- Minimising the administration of tax and associated costs.

Creating tax savings

Tax benefits can be achieved by locating the point of contact in a low tax jurisdiction, thus reducing tax on profits migrated there from existing operating activities and also capturing the savings and future growth from initiatives undertaken by the principal. The extent of the tax benefits will depend upon the territory chosen and which “value added” activities are transferred to the principal.

However, it should be noted that forcing your business to centralise the management of outsourced activities in a location not suited to your business needs will fail. It is crucial that the business is able to live comfortably within the tax model, rather than within artificial straight jackets.

Direct tax issues, exposures and risks

Every transaction gives rise to different issues, exposures and risks; however, the common issues that require consideration are:

Exit charges – outsourcing can often result in the transfer of valuable information to the offshore territory. When the transfer includes intangible assets, such as brands, trade secrets, know-how, licenses, patents, etc, this can crystallise a tax liability.

Transfer pricing – a primary requirement for tax purposes when transacting with related parties cross border is to price the resulting transactions on an arms-length basis. In assessing pricing policy it is necessary to consider what functions, assets and risks belong to each entity, as these drive economic value and arms-length return.

CFC's – Most territories have controlled foreign company (CFC) regimes which are designed to stop companies shifting profit to low tax jurisdictions via intra group transactions. Therefore, care needs to be taken so as to structure the transaction flow either outside the CFC rules or within an exemption.

Permanent establishments – as retail and consumer goods businesses are increasingly managed by product lines, customer profiles or regions, the risk of creating a taxable presence in an overseas country via a permanent establishment (PE) increases. In overview, if employees of one group company provide management, consulting, or similar services in another country, then this can give rise to a PE. Similarly, if employees of a group company habitually exercise an authority to conclude contracts for an overseas group company this also gives rise to a PE.

Profit extraction – Consideration needs to be given as to how to repatriate profits and cash from the principal to the ultimate parent. There are a number of means of achieving this via royalties, dividends, interest payments, upstream loans, and so on. Planning is required to minimise any tax leakage which can arise due to withholding tax, dividend tax or differentials in tax rates.

Indirect taxes

Outsourcing has the propensity to introduce new indirect tax charges into the supply chain as services and goods move cross border. In addition to the traditional indirect taxes, being sales taxes and customs duties, governments are creating ever-more inventive ways of increasing levies: business tax, energy tax, environmental tax, general services tax, excises, the list goes on. Consequently, if indirect tax burdens are not managed, profit margins will decrease and cash-flow requirements and risks will increase.

In managing indirect taxes local country variations must be identified and dealt with as well as potential cash flow disadvantages on transition; for example, on any transfer of stock. Systems will need to be updated and appropriate registrations obtained to ensure goods flow freely and are not stuck at borders.

Conclusion

Tax planning and managing of tax compliance should be a key consideration at the design stage of any global outsourcing project. With good advice, careful planning and precise implementation you may be able to obtain significant tax savings and cash-flow benefits.

Retail and consumer goods companies whose planning complements the supply chain reorganisation will be the winners, with bottom line improvements and a tax model which will grow as the business continues to flourish and expand.



Matthew A. Ryan
Director, International
Tax Restructuring,
PricewaterhouseCoopers-UK

EU Regulation on Registration, Evaluation and Authorisation of Chemicals (REACH)



REACH regulation to impact retail and consumer sector

While the REACH regulation came into force in June 2007, a key compliance period began on 1 June 2008. Preregistration of chemicals is needed before 1 December 2008 to take advantage of the phase-in timetable for registration of existing substances.

REACH can have a number of compliance and commercial risk implications for businesses in the retail and consumer sector; however, there are three key potential impact areas:

- Registration of a chemical substance will be needed by any business manufacturing or importing the substance into the EU. This could include household cleaning and other home products, inks and coatings. In some cases, registration of a substance contained in articles may be required.
- Notification may be required where an article is manufactured or imported into the EU and contains more than 0.1% of a particularly hazardous substance; for example, a substance that is carcinogenic, mutagenic, toxic to reproduction or very persistent and bio-accumulative.
- There are a range of supply chain commercial risks. For example, will your suppliers comply? Will REACH cause a supplier to stop selling a key raw material or product, or will price or quality significantly change?

A PricewaterhouseCoopers REACH survey, “Waking up to REACH”, published earlier this year, showed that retail and consumer businesses had less awareness of REACH than businesses in the chemicals, pharmaceuticals, industrial manufacturing and forest, paper and packaging sectors. The survey also showed that businesses were more aware of REACH in Europe, with less awareness in North America and the Asia Pacific region. Overall, awareness was lowest in North America.

The survey adds to the calls from regulators and industry bodies for businesses to react to REACH as soon as possible. Companies need to understand and mitigate commercial risks, particularly in relation to supply chain, in the retail and consumer sector. Here, where registration is required, failure to comply can result in inability to legally market a product in the EU. As REACH states: “No data, no market”.

For more information on the implications of REACH, contact Simon Taylor at simon.z.taylor@uk.pwc.com.

Economic crime hits hard at industry



The retail and consumer industry is one of the sectors hit hardest by economic crime, with more respondents reporting many more incidents than in other industries, according to PricewaterhouseCoopers (PwC)'s 4th biennial Global Economic Crime Survey – Retail and consumer industry supplement.

In the retail sector, companies face a two-fold threat, from “shrinkage” on the one hand, to crimes such as accounting fraud, corruption and bribery, and IP infringement on the other. The huge cost of shrinkage is no secret within the industry – one source estimated global shrinkage for 2007 at nearly US\$100 billion¹.

Counterfeiting in the retail and consumer industry is also a growing, and expensive, problem. One source estimates that international trade in illegitimate goods may have reached US\$200 billion annually in 2005 – and if domestically produced goods were included, the number would likely be substantially higher².

And while the direct financial costs of both shrinkage and other types of economic crime are substantial, the potential indirect or collateral damage to one of retail and consumer companies' most valued assets – reputation and brand value – may potentially have even more far-reaching negative consequences. In this article we summarise major findings from the report.

Prevalence and types of frauds

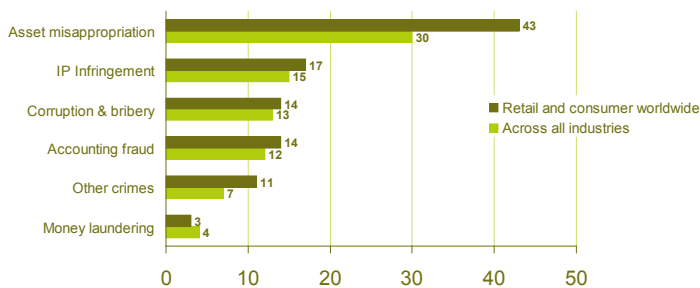
Nearly three-fifths (57%) of respondents reported that their company had been the victim of economic crime. The level of economic crime in North America was even higher. All in all, the situation for retail and consumer companies is extremely serious.

Asset misappropriation stands out as the most pressing problem for retail and consumer companies. In the retail sector, asset misappropriation includes shrinkage – theft of product in transit or at the point of sale. Many retailers are employing a number of well-established strategies for reducing this type of economic crime, including the use of CCTV, tagging, RFID, and EPOS data mining. Strategic merchandising strategies are another means used, by making goods with high shrink rates less easily accessible to thieves. Many companies are also beginning to look further back in their supply chain to help gain a fuller picture of shrinkage, including reviewing stock files and identifying areas with frequent write-downs.

¹ Bamfield, J. (2007) *Global Retail Theft Barometer*, Nottingham: Centre for Retail Research

² (2007) *The economic impact of counterfeiting and piracy: Part IV, Executive Summary*. Organisation for Economic Co-operation and Development (OECD)

Figure 1: Percentage of companies surveyed reporting different types of economic crime



Source: PricewaterhouseCoopers, *Economic crime: people, culture & controls: The 4th biennial Global Economic Crime Survey*

The internet is becoming an increasingly important channel for retailers – and an increasingly lucrative avenue for enterprising fraudsters. The potential for economic crime in the e-tailing space includes dramatically increased rates of credit card fraud, as well as the risk of the theft and inappropriate use of customer information. The former type of fraud may cost significantly less per incident, but numerous small thefts can add up to large numbers. It is currently being combated by techniques such as real-time verification of addresses from other public sources. The latter type of fraud has far greater potential negative repercussions, both in terms of direct liability and damage to the brand. Initiatives such as the Payment Card Industry (PCI) Data Security Standard represent established protocols to mitigate these types of risks as much as possible.

Fourteen per cent of respondents also reported incidents of accounting fraud over the past two years. In the retail and consumer sector, revenue recognition schemes such as trade loading/channel stuffing practices to boost sales at or close to the end of the period, and bill-and-hold transactions, where legitimate sales orders are received, processed, and readied for shipping, even though the customer is not ready, willing or able to accept delivery of the product at that time, are common.

Retail and consumer companies are well aware of the collateral damage that economic crime can cause. More than half of companies in the retail and consumer industry worldwide who detailed serious incidents of economic crime reported having suffered collateral damage from the same (57%), and 9% described these types of intangible damage as severe.

The emerging markets

Global retail and consumer companies are continuously looking to emerging markets, both as a source of lower-cost goods and as a key marketplace. Companies in the retail and consumer industry suffered above-average victimisation through fraudulent offenses in the E7 (Brazil, China, India, Indonesia, Mexico, Russia, Turkey) markets. Nearly three-fifths of retail and consumer companies report victimisation in this region.

IP infringement stands out as a particular problem, with more than a quarter of respondents (26%) reporting incidents in the E7. Many consumer goods

manufacturers have shifted large portions of their production activities to areas with low labour costs such as China. These types of moves, while they may be necessary to maintain competitiveness, also increase the risk of counterfeiting at remote production facilities.

Companies need to be sensitive to possible ethical issues at suppliers. In this area, the emerging markets are the site of the majority of foreign offenders. Retail and consumer companies reported a large proportion of cases including offenders external to the company, with 72% of the companies reporting at least one case. One quarter of these external offenders came from abroad. They were most commonly involved in money laundering (54%), IP infringement (34%), and corruption and bribery (31%) offenses. When foreign offenders were involved, they notably came most frequently from China, Central and Eastern Europe (24%) and Russia (23%).

Combating the fraud triangle

Interestingly, respondents in the retail and consumer industry tended to be overly optimistic regarding future economic crime. Although 57% of respondents reported that their company had been the victim of economic crime in the last two years, only 14% expect that their company will be subjected to economic crime in the next two years.

In the report *A Deeper Dive: Protecting retail and consumer companies against fraud and misconduct at the business process level*, PwC looked at the fraud

triangle, the three conditions fraud experts say are always present whenever fraud occurs:

- Opportunity,
- Incentives or pressures, and
- Justifications to commit fraud or rationalisation.

Addressing any one of these areas can have significant benefits. Opportunity for fraud can be combated particularly well at the business process level. Preventive systems such as ethical guidelines and anti-corruption programs can help combat the rationalisations perpetrators may use to commit fraud. Attacking opportunity and offender justification is an excellent start; however, retail and consumer companies also need to be aware of how increased pressures and incentives to commit fraud contribute to the overall picture around economic crime, a factor which may contribute significantly to the future outlook for the industry.

Summary

Retail and consumer companies are facing a number of serious challenges. The industry is currently in the midst of a period intense change. Companies are looking across the globe in order to focus on growth markets, placing an ever-growing emphasis on electronic retail channels, and realigning and relocating production locations. Companies need to strategise how they cope with the industry's challenges and the increased risk of economic crime they pose. Retailers and consumer goods manufacturers need to look beyond a narrow focus on shrinkage to enhance monitoring, detection, and investigating activities across their organisations.

Economic crime: people, culture & controls: The 4th biennial Global Economic Crime Survey is available for download at pwc.com/crimesurvey.

Olympics trivia quiz

In honor of the Beijing 2008 Olympics – and PwC's role as Accounting Services Supplier of the Games – answer the following trivia questions correctly, and you'll be entered into a drawing for one of five souvenir PwC Olympics commemorative A4 Leather Portfolios. The Leather Portfolio is a limited edition item – each features PwC and Beijing Olympics logo in silver and includes a 100-page A4 writing pad.



All decisions are at the discretion of the judges. Winners' prizes will be forwarded to them on or about **30 September**.

Email your responses to esther.kl.mak@hk.pwc.com with an email subject "Olympic trivia quiz". Answers must be received on or before **22 August**.

1. Who was the first Ethiopian man to win the Olympics marathon – and what was unusual about his victory?
2. Who was the final torch bearer at the 1984 Los Angeles Olympics?
3. Who was the final torch bearer at the first modern games in 1936?
4. In what three scheduled years did the Olympics not hold competitions?
5. Which country has hosted the most Olympics Games (including both summer and winter)?
6. What woman was the only U.S. athlete to win a gold medal at the 1968 Winter Olympics?
7. Who won more gold medals in a single Olympics than any other athlete in Olympics history – and how many?

An International Network

PricewaterhouseCoopers (www.pwc.com) provides industry-focused assurance, tax and advisory services to build public trust and enhance value for its clients and their stakeholders. More than 146,000 people in 150 countries across our network share their thinking, experience and solutions to develop fresh perspectives and practical advice.

Our Global Industry Program demonstrates our industry strengths and drives value for our clients. The program's foundation is a deep understanding of business and industry issues, connected with meaningful solutions. Companies leverage our extensive industry resources and knowledge to compete more effectively in specific marketplaces. Our global retail and consumer industry group has designated professionals and territory sector leaders in more than 50 countries around the world, serving all types and sizes of retail and consumer goods companies. A network of retail and consumer-focused subject matter experts assists with transactions, global sourcing, international accounting regulations, transfer pricing, customs, tax and other issues.

Editorial team

Carrie Yu
Global R&C Leader
carrie.yu@hk.pwc.com

Susan Eggleton
Global R&C Marketing Senior Manager
susan.d.eggleton@hk.pwc.com

Denis Smith
Global R&C Senior Knowledge Manager
denis.s.smith@hk.pwc.com

Esther Mak
Global R&C Marketing Coordinator
esther.kl.mak@hk.pwc.com

RETAIL & CONSUMER INTERNATIONAL NETWORK

Global & A7 Retail & Consumer Leader (Hong Kong)
Carrie Yu + 852 2289 1386
carrie.yu@hk.pwc.com

Argentina
Gabriel Martini + 54 11 4850 4762
gabriel.martini@ar.pwc.com

Australia
Stuart Harker + 61 3 8603 3380
stuart.harker@au.pwc.com

Austria
Ian Murdoch + 43 1 501 88 1420
ian.murdoch@at.pwc.com

Belgium
Filip Lozie + 32 32 593 348
filip.lozie@be.pwc.com

Bolivia
Cesar Lora Moretto + 591 3336 4050
cesar.lora@bo.pwc.com

Brazil
Ricardo Neves + 55 11 3674 3250
ricardo.neves@br.pwc.com

Bulgaria
Jean-Pierre Vigroux + 359 2 9355 238
jean-pierre.g.vigroux@bg.pwc.com

Canada
Christopher Kong + 1 416 869 8739
christopher.p.kong@ca.pwc.com

Central & Eastern Europe
George Johnstone + 48 22 523 42 43
george.johnstone@pl.pwc.com

Chile
Luis Enrique Alamos + 56 2940 0007
lealamos@cl.pwc.com

China
Sonny Doo + 86 20 3819 2248
sonny.doo@cn.pwc.com

Czech Republic
Thomas Linder + 420 2 51 15 20 14
thomas.linder@cz.pwc.com

Denmark
Henrik Trangeled Kristensen + 45 8932 5662
henrik.trangeled.kristensen@dk.pwc.com

Ecuador
Sandra Vargas + 59 34 228 8120
sandra.vargas@ec.pwc.com

Finland
Mikko Nieminen + 358 9 22 80 12 57
mikko.nieminen@fi.pwc.com

France
Sabine Durand-Hayes + 33 1 56 57 85 29
sabine.durand@fr.pwc.com

Germany
Gerd Bovensiepen + 49 21 19 81 29 39
gerd.bovensiepen@de.pwc.com

Greece
Vassilios Goutis + 30 210 6874 620
vassilios.goutis@gr.pwc.com

Hong Kong
Michael Cheng + 852 2289 1033
michael.wy.cheng@hk.pwc.com

Hungary
Andrew Simonds + 36 1 461 95 51
andrew.m.simonds@hu.pwc.com

India
N. V. Sivakumar + 91 80 2558 5663
n.v.sivakumar@in.pwc.com

Indonesia
Eddy Rintis + 62 21 521 2901
eddy.rintis@id.pwc.com

Ireland
Kevin Egan + 353 1 662 6069
kevin.egan@ie.pwc.com

Italy and Eurofirms
Roberto Adami + 390 422 69 69 11
roberto.adami@it.pwc.com

Japan
Jack E Bird + 81 3 5251 2577
jack.bird@jp.pwc.com

Korea (South)
Sanghoon Kwak + 82 2 709 0301
sanghoon.kwak@kr.pwc.com

Lithuania
Christopher C Butler + 370 5239 2303
chris.butler@lt.pwc.com

Malaysia
Phoon Soon Keong + 60 3 2382 0913
soon.keong.phoon@my.pwc.com

Mexico
Miguel Olvera + 52 55 5263 5856
miguel.a.olvera@mx.pwc.com

Netherlands
Sytso Boonstra + 31 10 407 5326
sytsboonstra@nl.pwc.com

New Zealand
Robert Harris + 64 3 374 3139
harris.r@nz.pwc.com

Norway
Petter Vold + 47 9526 0000
petter.vold@no.pwc.com

Philippines
Che Javier + 63 2 459 3010
che.javier@ph.pwc.com

Poland
Katarzyna Witaszewska + 48 22 523 41 82
katarzyna.witaszewska@pl.pwc.com

Portugal
Jorge Costa + 351 213 599 414
jorge.costa@pt.pwc.com

Romania
David Fuller + 40 21 202 8805
david.fuller@ro.pwc.com

Russia
Chris Skirrow + 7 495 967 6390
chris.w.skirrow@ru.pwc.com

Singapore
Ooi Chee Kar + 65 236 3228
chee.kar.ooi@sg.pwc.com

Slovak Republic
Maria Frühwaldova + 421 259 350 111
maria.fruhwaldova@sk.pwc.com

Slovenia
Francois D Mattelaer + 386 1 4750 145
francois.d.mattelaer@si.pwc.com

South Africa
Diederik Fouche + 27 11 797 4291
diederik.fouche@za.pwc.com

South America
Henrique Luz + 55 11 3674 3601
henrique.luz@br.pwc.com

Spain
Josep Sole Farre + 34 915 684 836
josep.sole.farre@es.pwc.com

Sweden
Anna-Carin Bjelkeby + 46 8 555 333 07
anna-carin.bjelkeby@se.pwc.com

Switzerland
William Wright + 41 58 792 8243
william.wright@ch.pwc.com

Taiwan
Douglas Chang + 886 2 2729 6621
douglas.chang@tw.pwc.com

Thailand
Paul Stitt + 66 2 344 1119
paul.stitt@th.pwc.com

Turkey
Adnan Akan + 90 212 326 6060
adnan.akan@tr.pwc.com

United Kingdom
Mark Hudson + 44 20 7804 5141
mark.hudson@uk.pwc.com

United States of America
John Maxwell + 1 973 236 4780
john.g.maxwell@us.pwc.com

Uruguay
Richard Moreira + 59 82 916 0820
richard.moreira@uy.pwc.com

Venezuela
José Enrique Sánchez + 58 212 700 6243
jose.sanchez@ve.pwc.com

Vietnam
Richard J Irwin + 84 8 8230 796
r.j.irwin@vn.pwc.com

Retail & Consumer Tax Services
Clare Bolton + 44 161 247 4032
clare.bolton@uk.pwc.com

pwc.com/r&c

© 2008 PricewaterhouseCoopers. All rights reserved. "PricewaterhouseCoopers" refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.