

LOOKING INTO THE SHADOWS

An Ipsos **BLUEPRINT** guide to:

Measuring and understanding the size, shape, and impact of illicit trade

ESG (Environmental, Social and Governance) challenges are an increasingly critical factor in companies' strategic, financial, and operational decisions. Illicit trade is a major governance issue, but also has far reaching social and environmental implications.

Illicit trade, otherwise known as the shadow economy, isn't new news. The introduction of prohibition in 1920s America, for instance, saw the demand for illicit alcohol filled by Mafia bootleggers and 'speakeasies'.

Fast forward 100 years and the issues with illicit trade are magnifying and multiplying across markets and categories, creating a range of macro and microeconomic problems for governments, manufacturers, and players throughout the supply chain.

Here we outline the nature of the illicit trade problem and how to measure, understand, and manage it, in order to address – if not solve – it for your categories; to inform your channel strategy.

A vast and growing scourge

Definitions of illicit trade, or the shadow economy, may vary by market and jurisdiction. So, it pays – literally – to define yours.

Broadly, the illicit economy (other terms include shadow trade, underground economy, counterfeit, contraband, and informal sector) is defined as where transactions occur illegally. Illicit trade is the production, import, export, purchase, sale, or possession of goods which fail to comply with the domestic legislation of any given country.

Typically, the activities and transactions that occur in the shadow economy are illegal for two reasons:

1. Transactions that would otherwise be licit do not adhere to the prevailing government's reporting requirements, and/or
2. The product or service itself is illegal.

Issues with illicit trade are magnifying and multiplying across markets.



This may include examples such as, but not limited to:

- Price below certain price point, which could indicate taxes not being paid
- Certain brands not being available in the regular economy and only on the 'underground market'
- Product originating from other countries with 'duties not paid'
- Counterfeit product and 'knock offs'.

When looking at illicit trade, it is key to have a clear definition of what would be seen as illicit in your market, because definitions are not the same across the globe, or even across categories.

The scale of illicit trade and the shadow economy is vast and covers a multitude of product categories. The International Chamber of Commerce estimates the global annual loss to the economy from illicit trade to be \$4.2 trillion (2022).¹ Categories affected range from clothing and textiles to food, tobacco and alcohol, second-hand vehicles, flora and fauna (wildlife and protected species), medications, narcotics, jewellery, and even precious metals and metal scrap.

Why it's important to size and understand illicit trade

Illicit trade poses a number of macro and micro level risks to economies, categories, and businesses. These include:

- Lower company profits and unfair competition for legitimate trade
- Illegal imports, meaning lower revenue for government treasuries since not all customs duties and value added taxes due to the government are paid
- Job losses
- Disincentivising innovation by companies
- Erosion of productive capacity in the country
- Circumvention of support put in place by government for local industries
- Undermining government efforts to promote health, security, standards and the wellbeing of its people
- Undermining government efforts to curb corruption
- A major source of funding for organised crime and terrorist organisations.



Ultimately, failure by governments to collect revenue impacts jobs and livelihoods, while threatening communities and society as a whole. It has a negative impact on economic stability, social welfare, public health, public safety, the environment, and on the government itself. The risk of terrorism and exploitation, including human trafficking, can also increase. Illicit trade reduces the customs tax collected by governments, and thus limits their ability to act.

For an individual manufacturer, or, indeed, groups of manufacturers, understanding the size of illicit trade can help with understanding not only statistics such as market or brand share, but also where the biggest problems and opportunities are from both branding and executional (price, promotion and go-to-market) standpoints. Understanding illicit trade can help with determining the scale of the problem, in order to formulate a plan to address at a brand, company, category or even macroeconomic or government level.

How to approach sizing and understanding illicit trade

When sizing illicit trade, the first step is being clear on how you want to use the results. Do you want to use it purely for internal purposes? Do you want to engage government bodies, law enforcement and courts? The media? Local authorities? With whom will the findings be shared? The research method and process are guided by who will be using the data.

Some questions you may want to ask when sizing illicit channels include:

- What is your market's definition of illicit?
- How big is illicit trade in category X in your market? Is it growing over time? How is it impacting your brand's growth?
- Where does illicit trade occur? Store types and geography?
- Who are the illicit players and how many of them are there? What are they ranging? How are they pricing their illicit products – are they priced cheaper than your/branded products?
- How is illicit trade changing over time?
- Which channels does illicit trade move through?
- Do the store owners and consumers consider trading in illicit products as illegal?
- What are the compliance levels by channel and region?



IMPACT STORY

\$510M

ILLEGAL CIGARETTE TRADE COST SOUTH AFRICA \$510M IN JUST ONE YEAR

Channel Sizing research undertaken by Ipsos' Channel Performance experts, on behalf of the Tobacco Institute of Southern Africa (TISA) and leading local and international tobacco brands, revealed that the illegal cigarette trade cost South Africa \$510M in 2018.

Between 2018 and 2022, illicit cigarette trade in South Africa grew exponentially. In 2018, one in every three cigarettes sold via the 'informal trade' channel was found to be selling below the legal price, indicating that tax was not being paid, with obvious implications for the government and society as a whole. An illicit brand had become the number one tobacco brand, with another illicit brand the fastest growing in the country, posing significant risks for manufacturers, including putting 12,000 jobs in jeopardy. In 2022, this has grown to two in every three cigarettes (66% of the total market) being illicit.

Since TISA put out the tender to various research agencies to become involved in measuring the growing illicit tobacco trade, and the tender was awarded to Ipsos due to their very professional approach to this matter, our experience with Ipsos has been nothing but exemplary!

The Ipsos team consists of the ultimate professionals, each team member an absolute expert in his/her particular field of the specific research project. I always found it very impressive how the different team members work together seamlessly to give the client a perfect end result.

On top of it all, the Ipsos professionals are also extremely pleasant to work with as human beings. I can recommend them based on many years of experience without a hint of hesitation.

FRANCOIS VAN DER MERWE

Chairman and CEO of TISA

FOR FURTHER INFORMATION, VISIT:

- [Illicit tobacco: 7 shocking figures on illegal smokes](#) | Business (news24.com)
- [Illicit Trade Surges in South Africa](#) | Tobacco Reporter

How to go about it

Throughout the process it is important to engage frequently with your stakeholders and to get their buy-in and alignment with the definition of illicit, as well as what is in and out of scope for the study.

To ensure a 'proper' sizing of illicit trade channels, it is key to cover all relevant store types and non-store distribution channels, including online and street markets. You also need to ensure that your methodology can capture low distribution products, as illicit often starts small and fragmented. If you miss low distribution products, the true size of illicit may be understated. To keep a regular eye on illicit trade and the impact on your brands and the rest of the legal industry, ideally you would track the illicit trade at least biannually, if not quarterly. And, unless there is a very good reason to do so, ensure you do not change the methodology you started with, over time. Changing anything within the methodology could result in data trends that do not reflect the market reality.

When collecting data, be careful of the language used. If the store owners and/or consumers see illicit as illegal, it might be more difficult to collect data.



TAKING TO THE STREETS WITH EMPTY PACK SURVEYS

Empty pack surveys are a commonly used methodology and have been carried out in multiple countries in the EU.

They can be used for any discarded packaged product likely to be found in street gutters and rubbish bins, such as alcohol.

Thousands of empty packs are collected from gutters and rubbish bins and their labels checked. From this it is possible to see whether it is a foreign product or one on which duty has not been paid, and so to estimate the percentage of illicit product.

Whilst there are some limitations with this methodology – as it doesn't capture product usage and only a percentage of products may be thrown into street gutters or public bins – it does provide an indication of the scale of penetration of illicit product in a category.

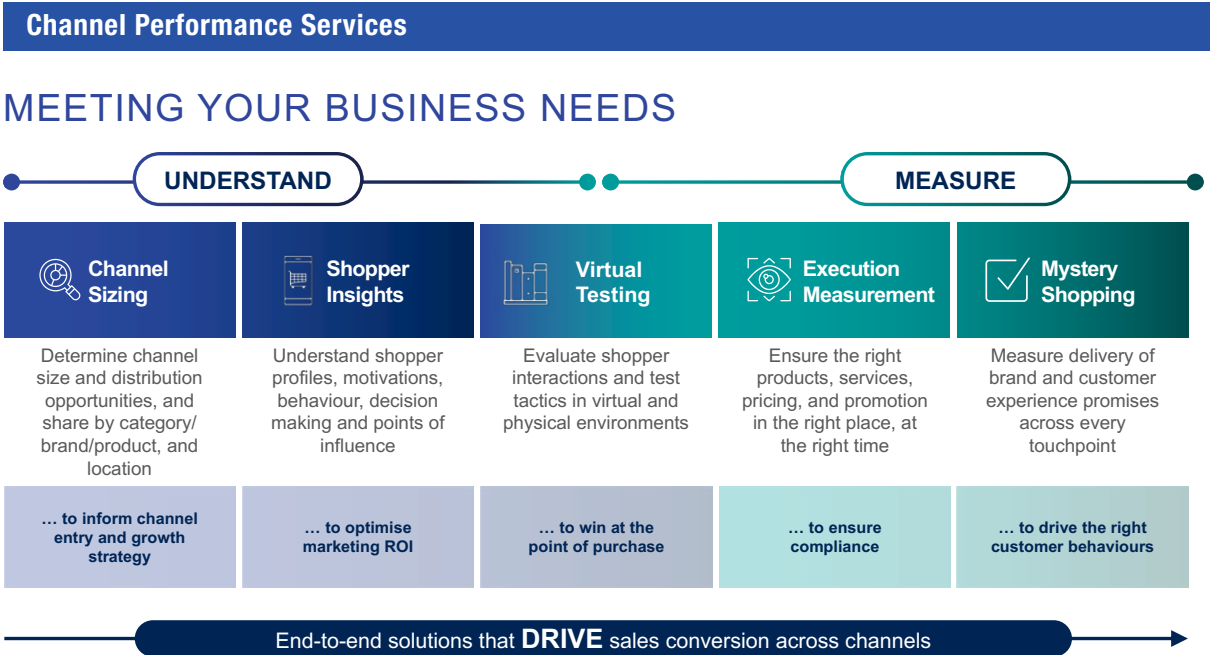
When collecting data, be careful of the language used. If the store owners and/or consumers see illicit as illegal, it might be more difficult to collect data, and alternative data collection methods might need to be considered. So, carefully consider how you ask questions: “do you stock cheap brands and products?” may be more appropriate than “do you stock illegal products?”.

The data collection methodology will be guided by the nature of the individual market and where illicit products can be bought. Ipsos can advise on the most appropriate approach, as it can on all other aspects of sizing and assessing illicit trade. Methodologies may be hybrid and include consumer research and online surveys, mystery shopping, depth interviews, intercept interviews in the street, empty pack surveys, and retail audits, for instance.

How Ipsos can help

At Ipsos we have significant experience in measuring and assessing illicit trade in multiple markets, including emerging economies across various categories. We can assist in designing and implementing a methodology fit for your unique market characteristics. We can support you in putting the findings to work to shape your channel strategy, and work with relevant stakeholders (including governments, trade associations) and communications teams.

Channel Sizing - of both licit and illicit trade - forms part of Ipsos’ Channel Performance offer concerned with: understanding channel context and opportunities, shopping behaviours and attitudes; and measuring purchase and service experience, activation and touchpoint execution, in order to drive sales conversion across all channels.



REFERENCES

1. <https://www.theparliamentmagazine.eu/news/article/shedding-light-on-the-shadow-of-illicit-trade-24070>

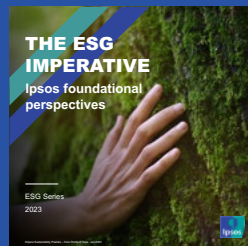
FURTHER READING

1. Channel Performance Management: Three key areas for driving growth
<https://www.ipsos.com/en/channel-performance-management>
2. Informing better decision making in relation to all aspects of ESG
<https://www.ipsos.com/en/ipsos-and-esg>
3. A New World Disorder? Navigating a polycrisis
<https://www.ipsos.com/en/global-trends>

FURTHER LISTENING

- 1 Customer Perspective podcast,
[Series 5, Episode 7](#)

Hear from Distell about the alcoholic drinks industry coming together in a sustainability initiative to drive a better future; advancing licensing and reducing alcohol abuse.



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