A PERSPECTIVE ON FOREIGN DIRECT INVESTMENT (FDI) IN MULTI-BRAND RETAIL SECTOR OF INDIA

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ABSTRACT

The Indian retail industry has experienced high growth over the last decade with a noticeable shift towards organized retailing formats. The industry is moving towards a modern concept of retailing. The size of India’s retail market was estimated at US$ 435 billion in 2010. Of this, US$ 414 billion (95 per cent of the market) was traditional retail and US$ 21 billion (5 per cent of the market) was organized retail. India’s retail market is expected to grow at 7 percent over the next 10 years, reaching a size of US$ 850 billion by
2020. Traditional retail is expected to grow at 5 per cent and reach a size of US$ 650 billion (76 per cent), while organized retail is expected to grow at 25 per cent and reach a size of US$ 200 billion by 2020. Despite encouraging signs, India’s retail market remains largely off-limits to large international retailers like Wal-Mart and Carrefour. Opposition to liberalizing Foreign Direct Investment (FDI) in this sector raises concerns about employment losses, unfair competition resulting in large-scale exit of incumbent domestic retailers and infant industry arguments to protect the organized domestic retail sector that is at a budding stage. Based on international evidence, it is suggested that allowing entry by large international retailers into the Indian market may help tackle inflation especially in food prices. Moreover, technical know-how from foreign firms, such as warehousing technologies and distribution systems can improve supply chain efficiency in India, in particular for agricultural produce. In this paper attempt is made to analyze the direction and impact of FDI on Multi Brand Retailers. The study is based on the secondary data and information.

Keywords: Foreign Direct Investment, Liberalization, Single Brand Retailing, Multi Brand Retailing.

INTRODUCTION

India is now playing a potential role in global multi-brand retail sector. There is something terribly ironic about the current emerging issue over the decision to allow FDI into multi-brand retail. India is a land of retail democracy- hundreds of thousands of weekly haats and bazaars are located across the length and breadth of our country by people’s own self-organizational capacities and interests. Our streets are bazaars - lively, vibrant, safe and source of livelihood for millions. India has the shop density of 11 outlets per 1000 people and number around 15 million, giving India the highest retail outlet density in the world. But only four per cent of them have larger than 500 square feet area. Food constitutes 70 per cent of retail sector, which means it has a direct link with the rural economy.
The US-based global management consulting firm, A T Kearney, in its Global Retail Development Index (GRDI) 2011, has ranked India as the fourth most attractive nation for retail investment, among 30 emerging markets. As India’s retail industry is aggressively expanding itself, great demand for real estate is being created. The cumulative retail demand for real estate across India is expected to reach 43 million square feet by 2013. Around 46 per cent of the total estimated demand between 2009 and 2013 will be come from Tier-1 cities. For instance, Pantaloons Retail added 2.26 million square feet (sq. ft.) of retail space during the fiscal 2011 and booked over 9 million sq. ft of retail space to fructify its expansion plans in future.

Some of the key players in the Indian retail market, with a dominant share are:

1. Pantaloons Retail Ltd, a Future group Venture: Over 12 mn sq.ft. of retail space spread over 1,000 stores, across 71 cities in India.
2. Shoppers Stop Ltd: Over 1.82 mn sq. ft. of retail space spread over 35 stores, in 15 cities.
3. Spencer’s Retail, RPG Enterprises: Retail footage of over 1.1 mn sq. ft. with approx 250 stores, across 66 cities.
4. Lifestyle Retails, Landmark group venture: Has approximately 15 lifestyle stores and 8 Home centres.
5. Other major domestic players in India are Bharati Retail, Tata Trent, Globus, Aditya Birla ‘More’, and Reliance retail. Some of the major foreign players who have entered who have entered the segment in India are
6. Carrefour which opened its first cash and carry store in India in New Delhi.
7. Germany-based Metro Cash and Carry which opened six wholesale centres in the country.
8. Walmart in a JV with Bharat Retail, owner of Easy Day store plans to invest about US $ 2.5 billion over the next five years to add about 10 million sq. ft. of retail space in the country.

9. British Retailer Tesco Plc (TSCO) in 2008 signed an agreement with Trent Ltd. (TRENT), the retail arm of India’s Tata Group, to set up cash-and-carry stores.

10. Marks and Spencers have a JV with Reliance retail.

Big retail is only a tiny blip in India’s economic radar, nowhere enough to provoke such exaggerated benefits by the government, or such widespread protests by the opposition. But today, it has brought the government to the brink of crisis, which merits an occasion to revisit the claims and counterclaims made by both sides and expose a fresh round of propaganda and the biggest is the concern for the Indian farmers. The government claimed big retailers will help the farmer by buying directly from him or her. In the twenty years since the economic liberalization of 1991, India’s middle class has greatly expanded, and so has its purchasing power. But over the years, unlike other major emerging economies, India has been slow to open its retail sector to foreign investment.

OBJECTIVES OF STUDY

1. To study the need of opening up of FDI in multi-brand retail.

2. To analyze the positive and negative impacts of FDI in multi-brand retail.

3. To review the challenges to be faced by FDI’s while investing in India.

4. To evaluate the change in the customer’s requirements after introduction of FDI in multi-brand retail.
LITURATURE REVIEW

1. The retail experience in Thailand furthers this concern. Sarma (2005) chronicles how traditional shopkeepers continued to suffer even when the Thai economy recovered, after the Asian crisis of the late 1990s. Foreign-owned retailers, he argues, “grabbed a big share of the retail market, often through unethical means.” In response the government instituted safety nets in the form of strengthening the marketing of the products sold by small retailers, the provision of soft loans, and setting up a central logistics system to act on behalf of the small shopkeepers and in particular to moderate the expansion of the foreign retailers. A similar story - of increased regulation of large retailers to prevent market capturing and uncontrolled proliferation - is told by Kalhan and Franz (2009).

2. The UK Competition Commission found in a 2000 study of major retail chains including Marks & Spencer, Sainsbury and Tesco that “the burden of cost increases in the supply chain has fallen disproportionately heavily on small suppliers such as farmers.” Apart from prices, the report states that smaller farmers came under severe pressure from supermarkets due to the latter’s requirement for large volumes of each product, pushing farmers to grow single crops rather than the multiple produce they would usually grow to minimise risk.

3. An article by Koshy Joseph, Partner, Joseph and Joseph Law Offices —FDI IN RETAIL SECTOR Copyright© 2006, describes — The decision of permitting foreign direct investment (FDI) in the retail sector has been a debate in India for a considerable period of time. FDI has been permitted in several sectors by the government of India, however, retail has been as issue deliberated over in view of its expected effect on several sections of the economy, particularly small businesses. However, the said decision of the government permitting FDI in retail has drawn a lot of flak from the leftist and the opposition parties. The gates have opened for multinationals interested and looking forward to set a foot in the booming retail business in India.
4. A Report by Navdanya/ Research Foundation for Science, Technology and Ecology, New Delhi titled —CORPORATE HIJACK OF RETAIL - Retail Dictatorship vs Retail Democracy sets the foot right saying —Giant corporations like Wal-Mart and Reliance have started to try and take over the Indian retail sector. The entry of the giant corporate retail in India’s food market will have direct impact on India’s 650 million farmers and 40 million people employed in tiny retail. More than 6600 mega Stores are planned with Rs. 40,000 crore by 2011.

5. Wal-Mart is the biggest player in retail. In a report —Oligopoly Inc. 2005, the ETC Group has shown that consolidation, cut throat competition and aggressive global expansion are the driving forces in the food retail sector. In 2004, the top 10 global food retailers accounted for combined sales of $840 Billion, 24% of the estimated $3.5 trillion global market. This was up from $ 513.7 billion in 2001. If Wal-Mart and other retail chains get a foothold in India; it will mean displacement of small retailers and farmers.

6. Singh, Dr. Mandeep, Associate professor of Economics, The Earth Institute of Columbia University in his article —Foreign Direct Investment in Retailing in India - Its Emergence & Prospects published on 3rd August, 2010 says —Since the Indian retail sector is highly fragmented and domestic retailers are in the process of consolidating their position, the opening up of FDI regime should be in phased manner over 5 to 10 years time frame so as to give the domestic retailers enough time to adjust changes. FDI should not be allowed for multi brand stores in near future, as Indian retailers will not be able to face competition with these stores immediately. At present it is also not desirable to increase FDI ceiling to more than 51% even for single premium brand stores. It will help us to ensure check and control on business operations of global retailers and to protect the interests of domestic players.

7. Khatore , Prashant and Parekh , Paresh , partner and senior professional in Ernst & Young’s Retail & Consumer Products Practice in their article —Wholesale FDI in retail in Business Daily from THE HINDU group of publications on Thursday, Jun 04, 2009 said —
There is a need to relook, clarify, and further liberalise the policy on single-brand retailing to promote investments by global chains in India. This in turn would not only boost retail growth in India but would also help realize India’s retail revolution dream.

8. A publication —Top retailers seek 51 percent FDI in multi-brand retail by ICT by IANS Thaindian.com Company Limited on August 12th, 2010 represents the views of big retailers as —Given the state of the supply chain in India, much of the investment in the back-end will be upfront, particularly in the initial years. A fixed percentage of investment on the back-end could therefore lead to a misallocation of resources and take away from where they are most needed to create efficient supply chains, said Bharti Walmart.

9. Of all the myths perpetuated by those for and against retail in FDI, the biggest is the concern for the Indian farmers. The government claimed big retailers will help the farmer by buying directly from him or her. Right now the farmer can only sell to government controlled mandis which are dominated by oppressive middlemen. Commerce Minister Anand Sharma says farmers will get a better price for the produce. He also said retailers will create storage and transportation chains, which will add value to farm produce. The opposition - whether its Mamata Banerjee or Nitish Kumar - says the retailers will hurt the farmer by enslaving them in contract farming. (Source: NDTV News)

10. Recent studies quantify the price impact of entry by low cost entrants. For example, using average city-level prices of various consumer goods, price dynamics in 165 US cities before and after Wal-Mart entry suggest robust reduction in prices for several products while magnitudes vary by product and specification, but generally range from 1.5-3% in the short run to four times as much in the long run (Basker, 2005b) with significant increases in consumer surplus especially for lower income households (Hausman and Ephraim, 2007).

In the past few decades large retailers have experienced substantial growth around the world. Evidence suggests while the impact of entry by large retail chains on employment and incumbent mom-and-pop stores is mixed, there can be substantial benefits to consumers in
the form of lower prices and lowered food price inflation in particular. Similarly, by employing improved distribution and warehousing technologies, large retail chains are in a position to provide better price signals to farmers and to serve as a platform for enhanced exports.

At the same time, public outcry over the impact of these chain stores on other retailers and local communities is reported around the world. Small retailers, farmers, and even large organized competition have concerns about the entry of large global chain stores. On balance, however, in this paper we argue that opening up FDI in India to multi-brand retailers from abroad may be a catalyst to growth and the development of the retail industry, with positive externalities for the rest of the economy.

REGULATORY NORMS

Multiple laws and regulations are in force at the central, state and local levels for governing the retail sector. Absence of specific legislations controlling distribution trade and the existence of a plethora of laws such as the Essential commodities Act, the Cold Storage Order, the Weights and Measures Act, labor laws, the Shops Establishments Act and so on, leads to market distortion.

Timely and effective implementation of GST will help bring about market integration. Stream lining the barriers for interstate movements and removal of all octroi and sales tax check points is possible if the implementation of GST is done with a national, on-line tax payment system. There should be quick implementation of all the provisions of the APMC Act, in letter and spirit, namely the institutionalization of market intermediaries, contract farming and so on.
CHALLENGES FACED BY THE RETAIL SECTOR

Some of the key challenges faced by the sector are:

Shortage Of Skilled Manpower

Front-end/retail assistant profiles in stores form a major proportion of the employment in the retail sector while store operations account for 75-80 per cent of the total manpower employed in the organized retail sector. Unfortunately, there are very few courses specific to the retail sector and graduates/ post graduates from other streams are recruited. Further, retail training opportunities such as niche courses for areas like merchandising, supply chain and so on are limited. The condition is more alarming in the unorganized sector where the manpower is not equipped with even the basic level of retail specific and customer service skills, which adds to their incompetence vis-à-vis the organized sector. A cohesive effort to develop skills within the sector can have a significant potential impact on productivity and competitiveness, both within the sector and on the wider economy.

Lack of Industry Status

Due to the absence of ‘industry status’, organized retail in India faces difficulties in procurement of organized financing and fiscal incentives. The Government should grant the much needed ‘industry status’ to the sector so that the sops that come with it help promote both big and small retailers.
Policy Induced Barriers

Organized retail in India is managed by both the Ministries of Commerce and Consumer Affairs. While the Ministry of Commerce takes care of the retail policy, the Ministry of Consumer Affairs regulates retailing in terms of licenses and legislations. There is need to govern retail operations through a single apex body. A single agency can take care of retail operations more effectively, especially with regard to addressing the grievances of retailers. The development of the retail sector can take place at a faster pace if a comprehensive legislation in enacted.

Real Estate

Lack of sophisticated retail planning is another major challenge the sector faces. Available space is easily interchangeable between commercial and retail use. In most cities, it is difficult to find suitable properties in central locations for retail, primarily due to fragmented private holdings, infrequent auctioning of large government owned vacant lands and litigation disputes between owners.

BENEFITS OF FDI AND COMPETITION IN ORGANIZED RETAIL

The changing structure and scale of retail can critically impact several industries in the short term- the retail industry itself, manufacturing, and real-estate, to name a few. And in the long term, spill-over effects can be felt in other industries. The growth of retailing has the potential
to impact the performance of interlinked sectors such as manufacturing of consumer goods and agriculture-based industries.

We begin by discussing the potential benefits of allowing entry by large foreign discount retail chains on lowering inflation, improving distribution and warehousing technologies. We do so by comparing findings from US studies that examine the effects of Wal-Mart and other large chains entering the US retail sector and the upheaval in the retail landscape brought about in the US beginning in the early 1990s. The section concludes by describing a couple of policy recommendations made in the Indian Government’s recent discussion paper on opening up the retail sector with a view to protecting domestic firms and increasing employment in the retail sector.

1. Lowering Inflation and Food Prices

Evidence from the United States suggests that FDI in organized retail could help tackle inflation, particularly with wholesale prices. Inflation is a politically sensitive subject, particularly for incumbent governments in a democratic country such as India, in particular because rising food prices tend to be regressive in their impact. This is underscored by the fact that the weight of food in rural and agricultural household consumption baskets is approximately 65-70%.

Taking into account demographics, store characteristics, and market conditions, corroborating evidence suggests that Wal-Mart decreases prices by 6%-7% for national brand goods and by 3%-8% for private label goods. Price decreases are most significant in the dry grocery and dairy departments. Moreover, Wal-Mart sets grocery prices significantly lower than its competitors (Volpe and Lavoie, 2008).
Hausman and Leibtag (2004) also argue that a more appropriate approach to estimating CPI figures which would lead to a continuously updated expenditure weighted average price calculation in comparison to the official Bureau of Labor Statistics (BLS) approach. Estimates using their new approach would lower food at home inflation by about 0.32 to 0.42 percentage points, in turn lowering the estimated inflation rate by about 15% per year (Hausman and Leibtag, 2004). In India, food accounts for nearly 50% of the consumption basket and the impact on inflation reduction could therefore be significant.

2. Improving Distribution and Warehousing Technologies

It is expected that technical know how from foreign firms, such as warehousing technologies and distribution systems, for example, will lend itself to improving the supply chain in India, especially for agricultural produce. Here there are multiple inefficiencies in the supply chain that leads from farm to the dinner table. While the Indian government is the largest purchaser of food crops for many farmers, the consequence of a poor distribution system is that much of the stockpile fails to reach consumers, and ends up rotting or as waste. India is the world’s second largest producer of fruits and vegetables in the world after China, producing around 180 million tonnes per year. Official estimates are that about 25-30 per cent of this produce goes waste between harvest and consumption.

Encouraging wholesale trading can create demand throughout the supply chain. In this spirit, the recent discussion paper talks of earmarking 50 per cent of FDI inflows for building up of back-end infrastructure, logistics and agro processing (DIPP Report, 2010). In theory, if fresh produce is collected efficiently at the farm-gate, and end-to-end cold-chain is maintained in storage and transportation until it reaches supermarket shelves as in developed countries,
this wastage can be eliminated, translating into better prices for farmers and lower prices for consumers besides greater availability of the produce for processing, export and other value-addition.

Creating better linkages between demand and supply also has the potential to improve the price signals that farmers receive. This could allow them to better respond to market demand, and thus reduce uncertainty. The Indian Prime Minister, Dr Manmohan Singh, called for a debate on the opening up of the sector on similar lines, pointing to the vast difference between farm gate and consumer prices. In this context, the DIPP’s discussion paper points out that the farmers get just a third of the total price paid by the final consumer, as against two-thirds realized by farmers in nations with a higher share of organized retail. FDI in retail, therefore, could be an efficient way of addressing concerns of farmers and consumers (DIPP Report, 2010). Evidence from the United States also however suggests by connecting suppliers worldwide with downstream buyers, the retail sector as a whole, has become more efficient at providing consumers with the goods they want at better prices and with increased convenience (Basker, 2007).

An added benefit of improved distribution and warehousing channels may also come from enhanced exports. A recent study notes that each of the world's largest retailers---Wal-Mart, Carrefour, Tesco, and Metro---entered China after 1995 and that their subsequent expansion in China may have influenced Chinese exports through two channels (Head, Jing and Swenson, 2010). First, the authors argue that large retailers may have enhanced bilateral exports between the retailers' Chinese operations and destination countries also served by stores in the retailers' networks. Second, Chinese city-level exports to all destinations may have grown if multinational retailer presence enhanced the general export capabilities of local suppliers.
Evidence from Chinese city-level retail goods exports supports the capability hypothesis as the expansion of Chinese city exports follows the geographic expansion of the retailers' Chinese stores and global procurement centers (Head, Jing and Swenson, 2010). Wal-Mart has therefore contributed to the trend of increased outsourcing which could bode well for agricultural exports from India.

3. Employment Effects and Small Domestic Firms

The Indian Government recommends that retail firms source a percentage of manufactured products from the small and medium domestic enterprises (DIPP Report, 2010). With a restriction of this sort, the opening up of the retail sector to FDI could therefore provide a boost to small-and- medium enterprises.

Moreover, expansion in the retail sector could also generate significant employment potential, especially among rural and semi-urban youth. The discussion paper considers the possibility of reserving 50 per cent jobs in FDI-funded retail outlets for rural youth. Other issues up for debate include identifying possible locations for such outlets. The current thinking is that these stores could initially be allowed to come up in cities with populations of over one million, particularly on the outskirts.

4. Challenges for Foreign Firms in Organized Retail

1. The first challenge is competition from the unorganized sector. Traditional retailing has been established in India for many centuries, and is characterized by small, family-owned operations. Because of this, such businesses are usually very low-margin, are owner-operated, and have mostly negligible real estate and labor costs. Moreover,
they also pay little by way of taxes. Consumer familiarity that runs from generation to generation is one big advantage for the traditional retailing sector. It is often said that the mom-and-pop store in India is more like a father-and-son enterprise.

2. Such small shops develop strong networks with local neighbourhoods. The informal system of credit adds to their attractiveness, with many houses ‘running up a tab’ with their neighbourhood kirana store, paying it off every fortnight or month. Moreover, low labor costs also allow shops to employ delivery boys, such that consumers may order their grocery list directly on the phone. These advantages are significant, though hard to quantify. In contrast, players in the organized sector have to cover big fixed costs, and yet have to keep prices low enough to be able to compete with the traditional sector.

3. Getting customers to switch their purchasing away from small neighbourhood shops and towards large-scale retailers may be a major challenge. The experience of large Indian retailers such as Big Bazaar shows that it is indeed possible. Anecdotal evidence of consumers who return from such shops suggests that the wholesale model provides for major bargains - something Indian consumers are always on the lookout for.

4. The other major challenge for retailers in India, as opposed to the US, is the storage setup of households. For the large-scale retail model to work, consumers visit such large stores and return with supplies likely to last them for a few weeks. Having such easy access to neighbourhood stores with whom, as discussed above, it is possible to have a line of credit and easy delivery service, congested urban living conditions imply that few Indian households might be equipped with adequate storage facilities. In urban settings, real estate rents are also very high. Thus the opportunities in this sector are limited to those retailers with deep pockets, and puts pressure on their margins. Conversely, for retailers looking to set up large stores at a distance from residential neighbourhoods may struggle to attract consumers away from their traditional sources of groceries and other products.
THE FUTURE ROAD MAP

Organized retail is a new phenomenon in India and despite the downturns, the market is growing exponentially, as economic growth brings more of India’s people into the consuming classes and organized retail lures more and more existing shoppers into its open doors. By 2015, more than 300 million shoppers are likely to patronize organized retail chains.

The growing middle class is an important factor contributing to the growth of retail in India. By 2030, it is estimated that 91 million households will be ‘middle class’, up from 21 million today. Also by 2030, 570 million people are expected to live in cities, nearly twice the population of the United States today.

Consumer markets in emerging market economies like India are growing rapidly owing to robust economic growth. India’s modern consumption level is set to double within five years to US$ 1.5 trillion from the present level of US$750 billion. Thus, with tremendous potential and huge population, India is set for high growth in consumer expenditure. With India’s large ‘young’ population and high domestic consumption, the macro trends for the sector look favorable.

Online retail business is another format which has high potential for growth in the near future. The online retail segment in India is growing at an annual rate of 35 per cent, which would take its value from Rs 2,000 crore (US$ 429.5 million) in 2011 to Rs 7,000 crore (US$ 1.5 million) by 2015. For instance the Tata Group firm Infiniti Retail operates its consumer durables and electronics chain of stores under the ‘Croma’ brand, is in the process of tapping net savvy consumers. Similarly, the Future Group, that operates a dedicated portal.
‘Futurebazaar.com’ for online sales, has revealed that it is targeting at least 10 per cent of the company’s total retail sales through the digital medium.

CONCLUSION

India’s retail sector remains off-limits to large international chains especially in multi-brand retailing. A number of concerns have been raised about opening up the retail sector to FDI in India. The first concern is the potential impact of large foreign firms on employment in the retail sector. A second related concern raised in the DIPP’s report is that opening up FDI would lead to unfair competition and ultimately result in large-scale exit of incumbent domestic retailers, especially the small family-owned business. A third concern raised by domestic incumbent firms in the organized retail sector is that this sector is under-developed and in a nascent stage.

In this paper we argue that the potential benefits from allowing large retailers to enter the Indian retail market may outweigh the costs. Evidence from the United States suggests that FDI in organized retail could help tackle inflation, particularly with wholesale prices. It is also expected that technical know-how from foreign firms, such as warehousing technologies and distribution systems, for example, will lend itself to improving the supply chain in India, especially for agricultural produce. Creating better linkages between demand and supply also has the potential to improve the price signals that farmers receive and by eliminating both waste and middlemen also increase the fraction of the final sales prices that is paid to farmers. An added benefit of improved distribution and warehousing channels may also come from enhanced exports. India’s experience between 1990-2010, particularly in the telecommunications and IT industries, showcases the various benefits of opening the door to large-scale investments in these sectors and is the effective turn of retail.
REFERENCES


