FDI in Indian Retail: The Road Ahead

Anjali Panda

Abstract--- *The retail sector in India is expanding and modernising rapidly in line with India's economic growth. The overall retail market (both organised and unorganised) is expected to grow at a compounded rate of 15 per cent over the next 5years from Rs. 23 trillion in 2011-12 to Rs. 47 trillion in 2016-17. Organised retail, which constituted a low 7 per cent of total retail in 2011-12, is estimated to grow at a CAGR of 24 per cent and attain a 10.2 per cent share of the total retail by 2016-17. With such rapid growth the consumption rate will witness increased penetration in existing categories and with the launch of new products and categories.*

Liberalization of trade policies for over two decades has made India one lucrative destination for investment. When the process of liberalization started in 1991, Foreign Direct Investment (FDI) was slow and limited to very few sectors like manufacturing and infrastructure etc. India being a signatory to World Trade Organization (WTO)'s General Agreement on Trade in Services (January 1995) which included wholesale and retailing services, the ongoing agenda of India's liberalization policy allowed FDI in 'cash and carry wholesale trade' in 1997. The door was further opened to retailing sector with 51 per cent investment in single brand retail during 2006. The change in FDI policy in September 2012, allowing investment in multi-brand retail stores is expected to bring revolutionary change in the sector. The positive arguments are that FDI in retail can expand markets by reducing transaction and transformation costs of business through adoption of advanced supply chain and benefit consumers and suppliers (farmers). On the other hand, oppositions are raising serious concern regarding employment losses, promotion of unhealthy competition between domestic organized retailers and small retailers which may lead to their exit from the market place and it would distort the urban cultural development. The Union government has downplayed the opposition's concern over allowing FDI in multi-brand retail with justification that when fully implemented, it would touch the lives of only 13.3 per cent of the country's population living in 53 cities; and it has stipulated that retail sales outlets could be set up only in cities with a population of over 1 million. Recently, the Supreme Court has rejected a PIL seeking direction to the Centre to bring out the details at whose instance the policy on FDI in multi-brand retail was introduced by the government. However, issues relating to FDI on multi brand retail sector appear to be challenging particularly on the face of forthcoming general election. It is now on the cross road. Debates across the country are still going on regarding its impact on the economy.

Against this background this paper based on secondary data sources makes a modest attempt to assess the impact of FDI on various participants of retail sector and examines the future challenges.

Keywords--- *FDI, Organised Retail, Liberalization*

I. INTRODUCTION

GOVERNMENT has already passed the bill and claims that the acceptance of foreign direct investment will enhance the creation of better retail infrastructure which helps to support overall sector growth. Despite of this, till date opposition is making much hue and cry. People are yet to understand what is FDI and why FDI in India?

II. GROWTH OF RETAILING IN INDIA- CURRENT SCENARIO

The Indian retail industry is the largest among all the industries in India and a booming one. It is the largest source of employment after agriculture and contributes to 9.4% of the total employment. The retail industry contributes 22% of the country's GDP. (www,assocham.com October,2012). Retailing in India is going through a period of transition from unorganised to organised retail. The reason can be attributed to the shifting attitude of consumers in terms of choice preference, value for money and emergence of organised retail. The current estimated value of Indian retail sector is about 500 billion USD and is supposed to reach 1.3 trillion USD by 2020. (www.pwc.in – The Indian Kaleidoscope: Emerging Trends In Retail- September,2012). As per the research conducted by Mc Kinsey Global Institute (MGI), Indian incomes are likely to grow three fold over the next two decades and India will become the world's fifth largest consumer market worth US$ 1.52 trillion by 2025.(www.iesingapore.gov.sg/wps/portal) In the seventh annual Global Retail

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Development Index (GRDI) conducted by 2008, India is the second most attractive destination for retail investment. (www.atkearney.com/consumer-products-retail/global-retail-development-index-2008)

Presently India constitutes 8% of organised retail and 92% belongs to unorganised retail. The organised retail may grow much faster than traditional retail. It is expected to gain a higher share in the growing retail market in India. Various estimates predict that the share of organised retail will be 20% by 2020. (www.deloitte.com/assets/Dcom-India, 2013)

The traditional retail industry is expected to grow at an average annual rate of 5% over the next year while the organised retail is estimated to grow at a rate of around 25% during this period.

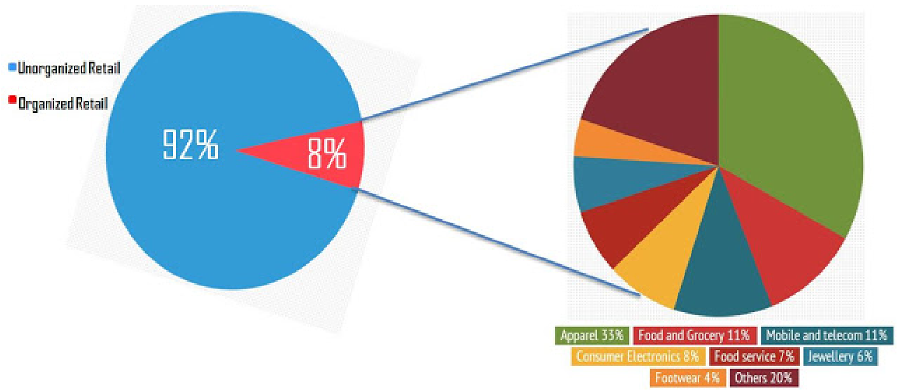

Figure 1: Organised Retail Penetration in India

Source: www.deloitte.com/assets/Dcom-India, 2013

Fig.1 shows that organised retail constitutes 8% of the total retail market and within the organised retail sector, apparel is the largest segment, food and grocery and mobile & telecom are the other major contributors to this segment.

III. Evolution of the FDI Policy in Multi-Brand Retail Trade (MBRT)

The Government of India had been considering opening up of MBRT sector to FDI for some time. India being a signatory to World Trade Organisation's general Agreement on Trade in service (in 1995), which include wholesale and retailing services has to open up the retail trade sector to foreign investment. Liberalization of trade policies for over two decades has made India one lucrative destination for investment. In the beginning when liberalisation started in India in 1991 the pace was very slow and limited to a few sectors. In 1997, FDI in cash and carry (wholesale) with 100% ownership through government approval was allowed. In 2006, FDI up to 51% in single brand product trading under Government approval route was allowed. In May 2010, Department of Industrial Policy and Promotion (DIPP) released a discussion paper soliciting public views on allowing FDI in Retail sector. In November,2011, the Government came out with its proposal for new FDI policy but unable to achieve political consensus on the issue, they had to shelve their plans for the enactment of the policy Finally the government decided to pass the new FDI policy on MBRT in September, 2012.

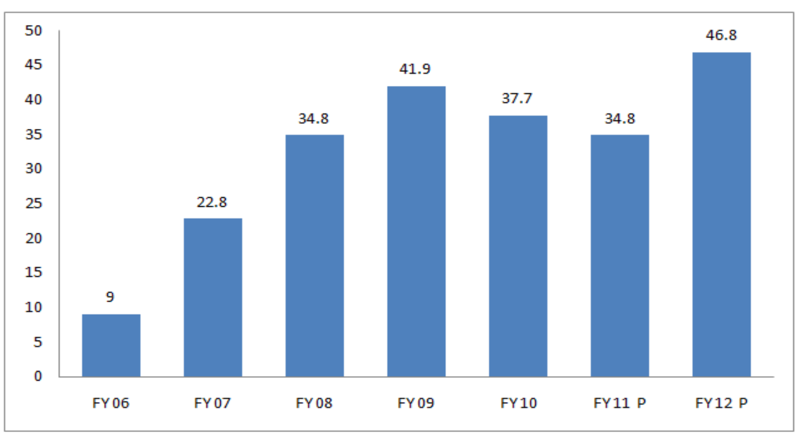

Figure 2: FDI in India (US$ Billion)

Source: RBI Bulletin, 2012

P - Provisional

The present issue is that debate is still going on. All the states are not interested in its implementation. Whether people understand or do not understand they are still apprehensive about future.

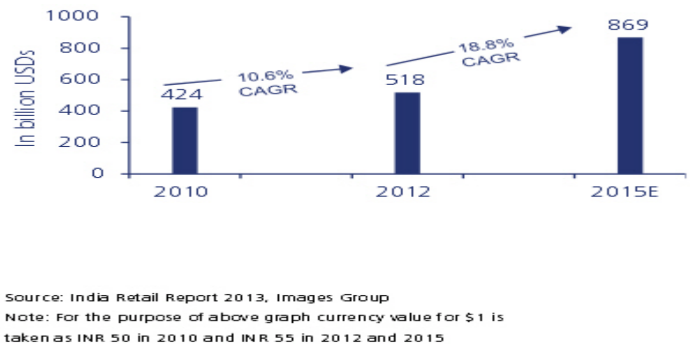

Figure 3: Expected Growth of Retail in India

- *Source: India Retail Report, 2013*

Figure-3 shows that the retail industry has experienced a growth of 10.6% between 2010 and 2012 and is expected to increase at a rate of 18.8% which is USD 750-850 billion by 2015.

IV. OBJECTIVE OF THE STUDY

Against this backdrop the present paper makes a modest attempt to assess the impact of FDI in multi-brand retail on the economy and examine the future challenges based on secondary literature.

- *Why FDI in Multi-Brand Retail?*

Foreign Direct Investment (FDI) implements and supplements the domestic investment. The domestic companies are benefitted through FDI, by having enhanced access to supplementary capital and enhanced technologies, exposure to global managerial practices and get integrated to global markets.

Government had undertaken a study through the Indian Council for Research on International Economic Relations (ICRIER) on the subject "Impact of Organised Retailing on the Unorganised Sector" submitted its report in 2008. The study by ICRIER indicated towards significant benefits for various stakeholders like consumers, farmers, manufacturer etc- arising from the growth of organised retail.

From the experiences of other countries the Government is hopeful that implementing the policy of permitting 51% of FDI in multi-brand retailing is likely to facilitate better inflow of FDI in to front and backend infrastructure, technologies to unlock the potential of the agricultural value chain, employment generation and global best practices. All these expected to benefit consumers and farmers in the long run both in terms of quality and price.

The government provision for 30% mandatory sourcing condition is expected to encourage local value addition and manufacturing. The increased level of activity both in the front end as well as in back end resulting from greater FDI inflows is expected to create employment opportunities both rural and urban youth. It is also expected to encourage the existing traders and upgrade themselves which will resulted into better consumer service and better remuneration to producers.

- *Highlights of the FDI policy with respect to Multi-Brand Retailing*

  - FDI up to 51% permitted under Government approval route.
  - Fresh agricultural produce including fruits, vegetables, flowers, grains and meat even unbranded may also be traded.
  - Minimum investment of USD 100million to be infused by foreign investor.
  - At least 50% of the foreign investment to be invested in the backend infrastructure within 3years of induction of FDI to include investment made towards- processing, manufacturing, distribution, design improvement, quality control, packaging, storage, warehousing, agriculture market produce infrastructure and logistics.
  - Minimum sourcing 30% of manufactured and processed products from small scale industries.
  - Government of India to have the first right to procurement of agricultural products.
  - Self certification by the company on compliance of the above conditions and these may be verified by the government.

- These outlets may be set up in cities with population of more than 1 million as per 2011 census.
- For states and Union Territories not meeting the above criteria the outlets may be set up in cities as decided by the respective state governments.
- Retail trading in any form by means of e-commerce would not be permissible for companies with FDI engaged in the activity of multi brand retailing.

- *Implications of FDI Policy on different Participants*

a. Farmers

Increased penetration of organised retail will reduce the role of middlemen to enable the famers to get better price of their produce. Farmers will be able to have better access to large markets through organised retail chains. Development of back end infrastructure will be helpful in reducing the wastage and increasing the gain of the farmers, which in turn will encourage best practices in crop management and improve product safety and hygiene.

b. SME Segment

The policy condition of 30% sourcing should be from the SME segment will provide opportunities to work with large retailers and lead to increasing access over a large part of the country and also world market.

c. Traditional Retail

The apprehensions regarding the displacement of kirana stores, small traders and commission agents, push cart vendors due to the growth of organised retail is a bit exaggerated. It has been observed that in India both the organised and unorganised is growing simultaneously. The rising cost of real estate in prime locations in cities have resulted in the growth of traditional retail as a convenience store next door and the organised retail is growing in the outskirts and suburbs of large cities. There is enough scope for the co-existence of organised and unorganised retailers in India as they offer different value propositions to customers. Organised retailers provide both ambience and discounts where as traditional retailers provide convenience. The experience of China and Indonesia shows that traditional and modern retail can coexist and grow although at different rates.

d. Consumers

A significant proportion of the expenditure of Indian consumers are spent on food and grocery followed by apparel. The consumer is more brand conscious while purchasing electronics, footwear and electronics but for food and grocery the expenditure is mainly on non branded products. With the entry of FDI in multi-brand retail the consumer will have a wider choice and a better shopping experience. There might be a gradual shift in consumption pattern like consumption of branded products in grocery items.

e. Food Supply Chain

The policy condition that at least 50% of the total FDI brought in should be invested in backend infrastructure, storage and warehousing, cold chains and processing etc- would likely to benefit the farmers and consumers in general.

f. Employment

FDI in retail will generate employment since new entrants will need to hire employees. The employees of unorganised retail sector do not get any health care or other benefits. Once individuals become absorbed in retailer operations, they can access more equitable wages and benefits. The effects of modern trade will be more apparent at the bottom of the population pyramid, because it will create more opportunities like non-agricultural employment for rural youth and better standard of living for agricultural society.

g. India as a Sourcing Hub

Global retailers have been sourcing from India for years and their retail presence in the Indian market will boost exports from India, as they develop and leverage relationship with local suppliers. The extent of sourcing from India will increase when global retailers are allowed to operate in the Indian market.

h. Existing Multi-Brand Retailers

FDI is likely to accelerate the pace of investment in supply chain in order to meet the demands of increasing scale which in turn will benefit the existing local players. Indian players have no restriction on e-commerce, location of retail stores- investments in backend infrastructure would hold a competitive advantage over any retail chain with FDI.

- *Challenges of FDI execution*

The announcement of FDI policy of September 2012 opened the way for modernization of Indian retail sector, but the journey ahead is full of challenges. The multinational retailers have to be alert and be cautious towards the Indian political, social and competitive landscape if they want to succeed in the Indian retail sector.

a. *Rising cost of Retail Space*

Establishment of hypermarkets require more than 60,000sq ft and departmental stores require more than 20,000sq ft of retail space. Availability of such retail space in prime location is scarce, so they have to shift to the outskirts and suburbs of large cities. In many emerging markets organised retailers came in at a different time in their economic cycle much earlier relatively to India. Since the organised retailer came at a later point to India, it is seriously affected by the cost structures- especially real estates and human resources. The cost structures are difficult to change.

b. *Policy Clarification*

The FDI policy do not provide any clear clarifications regarding the investment in backend infrastructure, whether it should be a fresh investment or the foreign companies can buy stakes in already established backend infrastructure.

c. *Political risk*

The opposition parties in India are opposing FDI in retail sector and the leaders are of the view that they will scrap the policy if their party comes to power. Any political change in the state and central government will pose a political risk on investment in retail.

d. *Getting approval from the government*

To enter into the retail sector a multi brand MNC retailer has to go through different stages of approvals from different governments before getting the final permission to go ahead.

e. *Skilled Manpower*

The most crucial challenge faced by the existing retail players is the scarcity of skilled human resource which will not be different for the new foreign retailer who are planning to enter Indian market.

f. *Challenges related to Infrastructure*

The infrastructure facilities like roads, ports, electricity etc- will ultimately increase the cost of the retail chain.

g. *Selection of a Right Partner*

The choice of a right partner plays an important role in the success of the business. The foreign player can use its expertise in supply chain and logistics along with an existing partner who will help in reaching the customers and together they can enhance operational efficiency.

- *Road Ahead*

The journey of FDI in multi brand retail in India will not be a smooth one. There are many challenges lying ahead. The future of multi brand retail in India is not very clear. The main opposition party of India and its allies are opposing the FDI in Indian multi brand retail. Many of the ruling party allies like DMK, UDI (Kerala) are also against the policy. Elections are due in near future in many states like Karnataka, Madhya Pradesh and Chhattishgarh and these states may change their stance on FDI in multi brand retailing depending on who comes to power. The opposition party supported FDI in multi brand retail when it was in power at the centre in 2002. Many of the current allies who oppose the policy are still supporting the UPA government.

Recently the Supreme Court has rejected a PIL seeking direction to the centre to bring out the details at whose instance the policy on multi brand retail was introduced by the government. However, the issues relating to FDI on multi brand retail appears to be a challenging particularly on the face of the forthcoming elections.

Policies evolve with changes in the business environment and the political landscapes of a country. The FDI policy in single brand retail has also evolved when the Indian market became more matured and the political scenario became more stable. Similarly it is hoped that multi brand retail and its implications may evolve with time.

- *ODISHA and FDI in Multi-Brand Retail*

The Odisha government is strongly opposing Foreign Direct Investment in multi brand retail. The Odisha Chief Minister Mr. Naveen Patnaik said that as the centre has left the decision to the state governments, the Odisha government will have a thorough examination of the situation and the issues related to it and do whatever is best for the state. It is argued by the state government that no city of Odisha is eligible for such projects and by the census of 2011

Bhubaneswar has a population of 8.37 lakh people. The Chief Minister of Odisha is of the opinion that instead of allowing FDI in retail the Union government should have strengthened the marketing opportunities for farmer and small scale manufacturers of the country by having investment in rural infrastructure and research and development for augmenting farm productivity. So the road ahead for FDI in Multi Brand Retail in Odisha is not going to be a rosy one and the future is still not predictable.

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