International Journal of Management, IT & Engineering
Vol. 8 Issue 1, January 2018,
ISSN: 2249-0558
Impact Factor: 7.119Journal Homepage: http://www.ijmra.us, Email: editorijmie@gmail.com Double-Blind Peer Reviewed Refereed Open Access International Journal - Included in the International Serial Directories Indexed & Listed at: Ulrich's Periodicals Directory ©, U.S.A., Open J-Gate as well as in Cabell's Directories of Publishing Opportunities, U.S.A

The Insight of Foreign Direct Investment in Indian Retail Sector

Dr. Atul P. Naik
Smt. Rajkamal Babaurao Tidke Mahavidyalaya,
Mouda, Dist. Nagpur

Abstract

The retail sector in India is one of the growth oriented sector. According to the Investment Commission of India, the retail sector is expected to grow almost three times its current levels to $800 billion by 2016. Though, in spite of the recent developments in retailing and its immense contribution to the economy, retailing continues to be the least evolved industries and the growth of organized retailing in India has been much slower as compared to rest of the world. Notwithstanding encouraging signs, India's retail market remains largely off-limits to large international retailers like Wal-Mart. Opposition to liberalizing 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 nascent stage. Based on international evidence, we suggest that allowing entry by large international retailers into the Indian market may help tackle inflation especially in food prices. Better linkages between demand and supply have the potential to improve the price signals that farmers receive and also serve to enhance agricultural and other exports. This paper focuses on the various issues involved in FDI including opportunities and challenges of FDI in retail.

Keywords: Foreign Direct Investment, Liberalization, Retail, India

Introduction :

With the globalization, India is fore runner in the world retail sector. 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. Recent signals from the government however suggest that this may be about to change: global supermarket chain stores such as Wal-Mart (United States), Carrefour (France), Marks & Spencer and Tesco (United Kingdom), and Shoprite (South Africa) may finally be allowed to set up shop in India. Foreign direct investment (FDI) in the retail sector in India is restricted. In 2006, the government eased retail policy for the first time, allowing up to 51 per cent FDI through the singlebrand retail route (see Section 2 for a classification of organized retail in India). Since then, there has been a steady increase in FDI in the retail sector, and the cumulative FDI in single-brand retail stood at $195 million by the middle of 2010 (DIPP, 2010).

Foreign investment in the single-brand retail sector in India has been resilient to the global economic crisis of 2007-08. Given India's large population and rapidly expanding middle-class, there is robust and growing demand and a rapidly expanding market. The growth in private consumption expenditures across categories to highlight this trend.

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.

The Current Regulation

The retail sector in India is organized into three categories. According to the Department of Industrial Policy and Promotion (DIPP) of the Government of India, single-brand retail comprises those retailers selling products "of a 'single brand' only, such that products should be sold under the same brand internationally; and single-brand product retailing covers only products which are branded during manufacturing. In this category, FDI is allowed to the extent of 51 per cent. From 2006 to March 2010, around 94 foreign firms applied to invest through the single-brand route of which 57 were approved. Consequently, the percentage increase in FDI flows in the retail sector between 2008 and 2010 was even higher than that in sectors such as the services sector, trading and telecommunications, which have a much higher share in the country's overall FDI (DIPP, 2010).

In contrast, no FDI is allowed in the multi-brand retail category. This includes all firms in organized retail that seek to stock and sell multiple brands, such as large international retailers like Wal-Mart and Carrefour. This is the sector that is most under dispute.

The third segment, called 'cash and carry', refers to wholesale retail. The government defines this segment as the "sale of goods and merchandise to retailers, industrial, commercial, institutional or other professional business users or to other wholesalers and related subordinated service providers".

In India, FDI of 100 per cent is permitted in this segment.

As per the 'cash and carry' structure commonly employed in India, the wholesale and retail entities are maintained as separate entities without any cross-shareholdings. The retail entity is owned and controlled by the Indian partner while the wholesale entity can be owned by the foreign partner up to 100 per cent. Wal-Mart, for example, has already established a successful presence in this category of wholesale operations by entering into a joint venture with Bharti Enterprises Ltd. of India. The new entity, Bharti-Wal-Mart, is in operation with stores opening around the country. The yardstick used to determine whether an operation is wholesale or not is the type of customers to whom the sale is made and not the size and volume of sales.

Forecasts for Retail Sector Growth in India

The data from private consulting company reports suggest that growth in the retail market has been rapid despite major restrictions on FDI. In the third-quarter report of 2010, the BMI India Retail Report forecasts that the total retail sales will grow from US$ 353 billion in 2010 to US$ 543.2 billion by 2014.

An important consideration, the report suggests, is the fast-growing middle and upper class consumer base. The analysis also suggests that in the next few years there will be major opportunities in India's smaller cities.

Even if growth is more conservative than estimated, the spill-over effects of this rapid expansion could be felt by many other sectors of the economy. A report published by Knight Frank India in May 2010 looks at the question of land and available retail space. It estimates that, during 2010-12, around 55 million square feet of retail space will be ready in the major cities like Mumbai the national capital region (NCR), Bengaluru, Kolkata, Chennai, Hyderabad and Pune. Furthermore, between 2010 and 2012, the organized retail real estate stock is expected to grow from the existing 41 million square feet to 95 million square feet.

Concerns about Opening up Indian Retail to FDI

A number of concerns have been raised about opening up the retail sector for FDI in India.

The first concern is the potential impact of large foreign firms on employment. Following agriculture, in 2007-2008, the retail sector is the second largest employer in India Retail trade employed 7.2% of the total workforce which translates to 33.1 million jobs (DIPP Report, 2010).

Moreover, the share of retail employment has risen significantly when compared to its share in 1993-1994. The pattern holds for both males and females, in rural, and in urban areas.

In the Indian policy debate, a contrasting view is that growth in organized retail is expected to benefit producers, without (significantly) hurting smaller traders and that they may preserve their smaller domains without being swallowed up by large retailers. However, the experience of organized retail in other parts of the world does not always bear this out.

Benefits of FDI and Competition in Organized Retail in India

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.

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% .

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.

Improving Distribution and Warehousing Technologies

It is expected that technical knowhow 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.

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-andmedium 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.

Challenges for Foreign Firms in Organized Retail

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.

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.

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.

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.

Conclusion

India's retail sector remains prohibited 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 apprehension 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 partial competition and ultimately result in large-scale exit of incumbent domestic retailers, especially the small family-owned business. A third concern raised by domestic obligatory firms in the organized retail sector is that this sector is under-developed and in a nascent stage. The potential benefits from permitting 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. Arguably, it is now the turn of retail.

References :

- Anand Dikshit (August 12 2011). "The Uneasy Compromise – Indian Retail". The Wall Street Journal
- Farmer Organisations back retail FDI. The Financial Express, 2 December 2011.
- Fdi Policy In Multi Brand Retail. Ministry of Commerce v/s Government of India. 28 November 2011.
- Global Powers of Retailing 2011". Deloitte. 2011.
- India government puts foreign supermarkets on pause. Reuters. 4 December 2011
- Indian Retail Industry: A Report". CARE Research. March 2011.
- Indian retail: The supermarket‘s last frontier". The Economist. 3 December 2011.
- India's retail reform: No massive rush". The Economist. 2 December 2011.
- Majumder, Sanjoy (25 November 2011). "Changing the way Indians shop". BBC News.
- Retailing in India Unshackling the chain stores". The Economist. 29 May 2008.
- The Bird of Gold - The Rise of India's Consumer Market". McKinsey and Company. May 2007.
- Tripathi, Salil (29 December 2011). "India needs Supermarkets". London: The Guardian.
- www.wikipedia.org
- www.researchgate.net/

***