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A Study on Foreign Direct Investment in Indian Retailing

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Abstract:
Over 90 per cent of consumers said FDI in retail will bring down prices and offer a wider choice of goods. Responses of over 2,000 people (500 each) covering farmers, consumers, kirana store and traders across ten major cities like Delhi, Mumbai, Kolkata, Chennai, Bangalore, Hyderabad, Ahmedabad, Pune, Chandigarh and Lucknow were collected by The Associated Chambers of Commerce and Industry of India (ASSOCHAM) dated 4th December 2011.Lookig at the survey inputs ,the various discussions on FDI in retailing, and the recent inclusion of FDI up to 51% being permitted in Multi Brand Retailing in India with effect from 14th September 2012 has made us to think and examine the same.. The paper makes an attempt to study foreign direct investment in Indian retailing and the various cases for and against FDI in retail markets in India.

Keywords*: Foreign Direct Investment, Retailing, Consumers, Reforms, FEMA*

1. Introduction

Retailing in general sense consists of business activities that are involved in buying and selling of goods and services to ultimate consumer for their own use-ranging from Bread, butter to automobiles to apparels to airline tickets. In India, after agriculture, the retail is the second largest sector that provides enough employment to India workforce. But retailing is at cross roads on the one side, retail sales are making new heights year after year and on the other side, traditional Indian retailers (Kirana stores) face numerous challenges.

Experts believe that retail expansion in coming five to seven years is expected to be stronger than our Indian GDP growth, driven by changing lifestyles and strong income growth, which in turn will be supported by favorable demographic pattern and the extent to which organized retailers succeed in reaching lower down the income scale to reach consumer towards the bottom of the consumer pyramid.

The beginning of retail business in India can be traced back to the emergence of Weekly Bazaars and Rural Fairs (melas). These weekly bazaars, used to be big attraction to both urban and rural people by catering their day to day requirement of grocery utensils, spices, grain, clothing and life stock. Then the traditional age saw the age of emergence of neighborhood 'kirana' store (usually known as convenience or mom and pop stores) to cater the convenience of Indian consumers. The government came forward and supported the rural retail and many local franchises stores. they came to nations main commerce stream with the financial and marketing support of khadi and village industry commission (KVIC).with the opening up of economic in 1980's ,the retailing in India saw huge change in terms of its size and functioning's. S Kumar's Bombay dyeing and Raymond were among few companies to come up with retail change in textile sector.

Indian retail industry is the second largest employer in the country with almost 12 million retailing stores in India .the economic and accounts of Indian retailing is about 14 to 15 percentage of GDP and is fastest growing retail market in the world with 1billion people.

2. Growth

Growth of organized retailing in India reveals the success of retail sector in India over the past five years. The rapidly increasing middle class in India seek more value in terms of improved assortment and quality, one - shop experience, financing option etc.

India witnessed a change in the age and income pattern over the last decade, which is likely to continue in the years to come. Two-third of Indian population is under 35,with the median age of 23 years, as opposed to the world median age of 33, and is home of 20 percent of global population under 25 years of age.

2.1. Growth over 1997-2010

India in 1997 allowed foreign direct investment (FDI) in cash and carry wholesale. Then, it required government approval. The approval requirement was relaxed, and automatic permission was granted in 2006. Between 2000 and 2010, Indian retail attracted about $1.8 billion in foreign direct investment, representing a very small 1.5% of total investment flow into India.

2.2. Growth after 2011

Before 2011, India had prevented innovation and organized competition in its consumer retail industry. Several studies claim that the lack of infrastructure and competitive retail industry is a key cause of India's persistently high inflation. Furthermore, because of unorganized retail, in a nation where malnutrition remains a serious problem, food waste is rife. Well over 30% of food staples and perishable goods produced in India spoil because poor infrastructure and small retail outlets prevent hygienic storage and movement of the goods from the farmer to the consumer.

3. Trends

- New retail formats and combinations are emerging and have opened a new world of opportunities for Indian youth. Bank branches, bill counter, saloons, internet café have open in the mall. 'The cash and carry activities are expected to grip majority of attention.
- Internet age increase computer awareness and shrinking usage charges have made people enabled by things online resulting growth of non store retailing. They are informed about fresh stocks/arrivals through e-mail.
- Sales promotion increasingly becoming professional and targeting differently to different lifestyle groups

4. FDI Policy in India

FDI as defined in Dictionary of Economics (Graham Bannock et.al) is investment in a foreign country through the acquisition of a local company or the establishment there of an operation on a new site. To put in simple words, FDI refers to capital inflows from abroad that is invested in or to enhance the production capacity of the economy.

Foreign Investment in India is governed by the FDI policy announced by the Government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. The Reserve Bank of India ('RBI') in this regard had issued a notification, which contains the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000. This notification has been amended from time to time.

The Ministry of Commerce and Industry, Government of India is the nodal agency for motoring and reviewing the FDI policy on continued basis and changes in sectoral policy/ sectoral equity cap. The FDI policy is notified through Press Notes by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP).

The foreign investors are free to invest in India, except few sectors/activities, where prior approval from the RBI or Foreign Investment Promotion Board ('FIPB') would be required.

5. FDI Policy with Regard to Retailing in India

As a part of the economic liberalization process set in place by the Industrial Policy of 1991, the government of India opened up the retail sector to FDI through a series of steps:

- 1995 – World Trade Organization's (WTO) General Agreement on Trade in Services (GATS) which included both wholesale and retail trade in services came into effect.
- 1997 – FDI in cash and carry (wholesale) allowed up to 100% under the government approval route.
- 2006 - FDI in single brand retail was permitted to the extent of 51%; FDI in cash and carry brought under automatic route.
- 2011 – 100% FDI in single-brand retail permitted with government approval; 51% FDI in multi-brand retail with few conditions.
- 2012 – FDI up to 51% is being permitted in Multi Brand Retailing in India with effect from 14^{th} September 2012.

6. Benefits of FDI

- The implementation of FDI in India it will create employment opportunities in India.
- It will increase the competition in the local markets.
- It helps in increasing the capital of the country.
- It increases the GDP of the country.
- Helps in transfer of new technologies, management skills, and intellectual property.
- Improves forex position of the country;
- Increases competition within the local market and this brings higher efficiencies
- Helps in increasing exports;
- Increases tax revenues

7. Demerits of FDI

- Domestic companies fear that they may lose their ownership to overseas company
- Small enterprises fear that they may not be able to compete with world class large companies and may ultimately is edged out of business;
- Large giants of the world try to monopolies and take over the highly profitable sectors;
- Such foreign companies invest more in machinery and intellectual property than in wages of the local people;
- Government has less control over the functioning of such companies as they usually work as wholly owned subsidiary of an overseas company;
- Work will be done by Indians but profit will go to foreigners.
- Independent stores will close, leading to massive jobs.

8. Reforms in Indian Retailing

Until 2011, Indian central government denied foreign direct investment (FDI) in multi-brand Indian retail, forbidding foreign groups from any ownership in supermarkets, convenience stores or any retail outlets, to sell multiple products from different brands directly to Indian consumers..

The government of Manmohan Singh, prime minister, announced on 24 November 2011 the following: India will allow foreign groups to own up to 51 per cent in "multi-brand retailers", as supermarkets are known in India, in the most radical pro-liberalization reform passed by an Indian cabinet in years.

- Single brand retailers, such as Apple and IKEA, can own 100 percent of their Indian stores, up from the previous cap of 51 percent.
- Both multi-brand and single brand stores in India will have to source nearly a third of their goods from small and medium-sized Indian suppliers.
- All multi-brand and single brand stores in India must confine their operations to 53-odd cities with a population over one million, out of some 7935 towns and cities in India. It is expected that these stores will now have full access to over 200 million urban consumers in India;
- Multi-brand retailers must have a minimum investment of US$100 million with at least half of the amount invested in back end infrastructure, including cold chains, refrigeration, transportation, packing, sorting and processing to considerably reduce the post harvest losses and bring remunerative prices to farmers.
- The opening of retail competition will be within India's federal structure of government. In other words, the policy is an enabling legal framework for India. The states of India have the prerogative to accept it and implement it, or they can decide to not implement it if they so choose. Actual implementation of policy will be within the parameters of state laws and regulations.

9. Indian Retail Reforms on Hold

On 3 December 2011, the Chief Minister of the Indian state of West Bengal, Mamata Banerjee, who is against the policy and whose Trinomial Congress brings 19 votes to the ruling Congress party-led coalition, claimed that India’s government may put the FDI retail reforms on hold until it reaches consensus within the ruling coalition. Reuters reports that this risked a possible dilution of the policy rather than a change of heart.

Several newspapers claimed on 6 December 2011 that India parliament is expected to shelve retail reforms while the ruling Congress party seeks consensus from the opposition and the Congress party's own coalition partners. Suspension of retail reforms on 7 December 2011 would be, the reports claimed, an embarrassing defeat for the Indian government, suggesting it is weak and ineffective in implementing its ideas.

Anand Sharma, India's Commerce and Industry Minister, after a meeting of all political parties on 7 December 2011 said, "The decision to allow foreign direct investment in retail is suspended till consensus is reached with all stakeholders.

On 19 Feb 2013 Tamil Nadu became the first state in the country to stoutly resist MNC 'invasion' into the domestic retail sector. In Chennai, Tamil Nadu CMDA authorities placed a seal on the massive warehouse spreading across 7 acres that had reportedly been built for one of the world’s leading multinational retail giants, WAL-MART.

In February 2014 Vasundhara raje led newly elected Rajasthan Government reversed the earlier Government's decision of allowing FDI in retail in the state. It reasoned that the sources of domestic retail are primarily local whereas international retail affects domestic manufacturing activity and hence reduces employment opportunities

10. Single-Brand Retail Reforms Approved

On 11 January 2012, India approved increased competition and innovation in single-brand retailing.

The reform seeks to attract investments in operations and marketing, improve the availability of goods for the consumer, encourage increased sourcing of goods from India, and enhance competitiveness of Indian enterprises through access to global designs, technologies and management practices. In this announcement, India requires single-brand retailer, with greater than 51% foreign ownership, to source at least 30% of the value of products from Indian small industries, village and cottage industries, artisans and craftsmen.

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11. Case For and Against FDI

11.1. Cases for FDI

- Organized retail will need workers. Wal-Mart employs 1.4 million people in United States alone. With United States population of about 300 million, and India's population of about 1200 million, if Wal-Mart-like retail companies were to expand in India as much as their presence in the United States, and the staffing level in Indian stores kept at the same level as in the United States stores, Wal-Mart alone would employ 5.6 million Indian citizens. Wal-Mart has a 6.5% market share of the total United States retail
- India needs trillions of dollars to build its infrastructure, hospitals, housing and schools for its growing population. The Indian economy is small, with limited surplus capital. The government is already operating on budget deficits. It is simply not possible for Indian investors or the government to fund this expansion, job creation and growth at the rate India needs. Global investment capital through FDI is necessary. Beyond capital, the Indian retail industry needs knowledge and global integration. Global retail leaders, some of which are partly owned by people of India.
- With 51% FDI limit in multi-brand retailers, nearly half of any profits will remain in India. Any profits will be subject to taxes, and such taxes will reduce Indian government budget deficit. Many years ago, China adopted the retail reform policy India has announced; allowing FDI in its retail sector. FDI-financed retailers in China took between 5 to 10 years to post profits, in large part because of huge investments initially made. Like China, it is unlikely foreign retailers will earn any profits in India for the first 5 to 10 years.
- States have a right to say no to retail FDI within their jurisdiction. States have the right to add restrictions to the retail policy announced before they implement them. Thus, they can place limits on number, market share, style, diversity, homogeneity and other factors to suit their cultural preferences.
- Finally, in future states can always introduce regulations and India can change the law to ensure the benefits of retail reforms reach the poorest and weakest segments of Indian society, free and fair retail competition does indeed lead to sharply lower inflation than current levels, small farmers get better prices, jobs created by organized retail pay well, and healthier food becomes available to more households.
- Indian small shops employ workers without proper contracts, making them work long hours. Many unorganized small shops depend on child labour. A well-regulated retail sector will help curtail some of these abuses.
- Organized retail has enabled a wide range of companies to start and flourish in other countries. For example, in the United States, retailer Whole Foods has rapidly grown to annual revenues of $9 billion by working closely with farmers, delighting customers and caring about the communities it has stores in.

11.2 Cases against FDI

Critics of deregulating retail in India are making one or more of the following claims:

- Independent stores will close, leading to massive job losses. Wal-Mart employs very few people in the United States. If allowed to expand in India as much as Wal-Mart has expanded in the United States, few thousand jobs may be created but millions will be lost.
- Wal-Mart's efficiency at supply chain management leads to direct procurement of goods from the supplier. In addition to eliminating the "middle-man", due to its status as the leading retailer, suppliers of goods are pressured to drop prices in order to assure consistent cash flow.
- The small retailer and the middle man present in the retail industry play a large part in supporting the local economy, since they typically procure goods and services from the area they have their retail shops in. This leads to increased economic activity, and wealth redistribution. With large, efficient retailers, goods are acquired in other regions, hence reducing the local economy.
- Wal-Mart will lower prices to dump goods, get competition out of the way, become a monopoly, and then raise prices. It is argued this was the case of the soft drinks industry, where Pepsi and Coca-Cola came in and wiped out all the domestic brands.
- India doesn't need foreign retailers, since homegrown companies and traditional markets have been able to do the job. Work will be done by Indians, profits will go to foreigners. Like the East India Company, Wal-mart could enter India as a trader and then take over politically. There will be sterile homogeneity and Indian cities will look like cities anywhere else.

12. Conclusion

The Indian Government, however, 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. So it is very difficult to predict the future of Indian retail sector.

But the government of India must be cautious about the apprehensions raised by the critics and adequate safeguards must be taken so that the positive effects may outweigh the negative ones and the traditional retailers coexist even after big foreign retailers enter the market.

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