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Foreign Direct Investment and Retailing in India: Opportunities and Challenges

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Abstract

India being second most-populous country has immense scope for retail expansion as along with time urbanization and consumerism has also been increasing. Initially India was conservative regarding FDI; it imposed restriction on foreign companies to limit their share in equity capital of their Indian subsidiaries but over the time Government of India gradually liberalized foreign investment in various sectors. Recently in 2011 India permitted 100% FDI in single brand retail and in 2012, 51% FDI permitted in multi brand. Even though organized retail sector in India is at the infant stage, India has today become a budding target for FDI. India today offers the most persuasive investment opportunity for mass merchants and food retailers looking to expand overseas as Indian economy is growing at a rapid pace with consumers having high purchasing power. FDI is a sturdy source for the intensification of retailing and will create enormous opportunities for innovation in retail sector in India but at the same time it is quite likely that a section of the domestic retailing industry will be severely hurt due to the entry of foreign retailers. In this paper researchers have tried to accentuate both the thoughts in detail and concluded the most constructive view on Opportunities and Challenges of FDI in Indian Retailing.

Keywords: Foreign Direct Investment (FDI), retail sector, India, single & multi-brand retail

1. Introduction

Retailing is the largest private industry in India and second largest employer after agriculture. The sector contributes to around 10 percent of GDP and 6-7 percent of employment. With over 15 million retail outlets, India has the highest retail outlet density in the world. This sector witnessed significant development in the past 10 years – from small unorganized family-owned retail formats to organized retailing. Liberalization of the economy, rise in per capita income, and growing consumerism has encouraged larger business houses and manufactures to set up retail formats. Many foreign players have also entered the market through different routes such as wholesale cash-and-carry, local manufacturing, franchising, test marketing, etc.

FDI is a sturdy source for the intensification of retailing and will create enormous opportunities for innovation in retail sector in India but at the same time it is quite likely that a section of the domestic retailing industry will be severely hurt due to the entry of foreign players. Against such a backdrop, FDI stages a number of problems that are worth researching by keen researchers who strive constantly to contribute to useful knowledge. In this proposal the researchers have made a sincere attempt to study on Impact of Foreign Direct Investment on Retail Marketing in Tamil Nadu.

In the Indian retailing industry, food is the most dominating sector and is growing at a rate of 9 percent annually. The branded food industry is trying to enter the India retail industry and convert Indian consumers to branded food. Since at present 60 percent of the Indian grocery basket consists of non- branded items. India retail industry is progressing well and for this to continue retailers as well as the Indian government will have to make a combined effort.

It took 10 years for the first 2500 organized retail stores to emerge in India; the next 2500 could easily get added in the next 5 years' Formats new to the Indian market have emerged rapidly over the past ten years. There is little doubt that retail in India is surging for an exciting phase ahead.

2. Statement of Problem

Now days, too much discussion is going on FDI in retail sector in Indian economy. FDI in retail is also a matter of hot discussion in the parliament of India. Hence it may not be out of place for this proposal to focus on current status of FDI in retails. Pertinent questions such as what may be the benefits of FDI in the Indian single brand and multi brand retail sector? What are the various opportunities and challenges to FDI in retail sector? Arise in our mind and provide ample opportunities for researchers to probe, in search of new knowledge.

3. Need and Importance of the Study

"Keeping in view the large requirement of funds for back-end infrastructure, there is a case for opening up of the retail sector to foreign investment. We must ensure that the FDI does make a real contribution to address the inadequacies of back-end infrastructure. Alongside, we need to address the challenge of integrating the small retailer in the value chain". FDI in retail may be an efficient means of addressing the concerns of farmers and consumers. Opening FDI in retail could also assist in bringing in technical know-how to set efficient supply chains which can act as models of development. It would also help bring about improvements in farmer income and agricultural growth and assist in lowering consumer prices and inflation, it added.

It is apparent from the above discussion that FDI is a predominant and vital factor in influencing the contemporary process of global economic development. This paper will help to know mainly the benefits that can be secured from the FDI in single brand and multi brand retails. Present study tells how the small retailers will be affected by the heat of multinational retail giants. Here, in this researcher, the attempt will be made to focus on the importance of FDI in retail sector in India in the present scenario.

4. Growth of Indian Retail Industry in the Last Decade

The Indian Retail Industry is the 5th largest retail destination and the second most attractive market for investment in the globe after Vietnam as reported by AT Kearney's seventh annual Globe Retail Development Index (GRDI), in 2008. The growing popularity of Indian Retail sector has resulted in growing awareness of quality products and brands. As a whole Indian retail has made life convenient, easy, quick, and affordable. Indian retail sector, specially organized retail is growing rapidly, with customer spending growing in an unprecedented manner. It is undergoing metamorphosis. Till 1980 retail continued in the form of kiranas that is unorganized retailing. Now big players like Reliance, Tata's, Bharti, ITC, and other reputed companies have entered into organized retail business.

Last decade has indeed witnessed tremendous growth in Indian retail industry and has integrated our Indian economy with the world. Retailing in India is progressively inching its way toward becoming the next boom industry. It has emerged as one of the most dynamic and growing paced industries accounting for over 10 percent of the country's GDP. This growth has become major attraction for foreigners to enter in India.

The challenge to the retail, on the other hand, is the requirement of heavy initial investments which leads to difficulty in achieving break even and this is the reason that many of these players have not tasted success so far. However, the growing trend of the market, changes in the lifestyle of consumer segment, increasing per capita income, and emerging technologies in operations still promise success in the long run with achievement of economies of scale.

5. What is FDI?

FDI refers to capital inflows from abroad that is invested in or to enhance the production capacity of the economy. It can be a subsidiary, joint venture or merger or acquisition and includes Greenfield and Brownfield projects. So, Foreign Direct Investment is an investment made by a foreign company or entity into a company or entity based in another country. Foreign direct investments differ substantially from indirect investments such as portfolio flows, wherein overseas institutions invest in equities listed on a nation's stock exchange. Open economies with skilled workforces and good growth prospects tend to attract larger amounts of foreign direct investment than closed, highly regulated economies.

6. Historical Trends in FDI in India

Starting with the market reforms initiated in 1991, India gradually opened up its economy to FDI in a wide range of sectors. The "licence-raj" system was dismantled in almost all the industries. The infrastructure sector which was in dire need of capital welcomed foreign equity. FDI was especially encouraged in ports, highways, oil and gas industries, power generation and telecommunication. Consumer goods and service sector which was once completely off-limits for foreign equity was also gradually opened up. The reserve bank of India set up an automatic approval system which allowed investments in slabs of 50, 51 or 74% depending on the priority of the industry, as defined by the government. The foreign investment limits were slowly raised and some sectors saw the limits raised to 100%.

6.1 Present Shape of FDI

The retail industry in India is the second largest employer with an estimated 35 million people engaged by the industry. There has been opening of Indian economy to foreign organization for foreign direct investment through organized retail. The union government has sanctioned 51% foreign direct investment in multi-brand like Wal-Mart, Carrefour, and Tesco. This will make foreign goods and items of daily consumption available locally, at a lower price, to Indian consumers. The new policy will allow multi-brand foreign retailers to set up shop only in cities with a population of more than 10 lakhs as per the 2011 census. There are 53 such cities at present. This means that big retailers can move beyond the metropolises to smaller cities. The final decision will however lies with the state governments. Foreign retailers will require a minimum investment US $100 million of which at least 50% of total FDI should be invested in back-end infra-structure which would include capital expenditure on the entire spectrum of related activities including cold chain infrastructure, food processing, refrigerated transportation, logistics. Big retailers will need to source at least 30% of manufactured or processed products from Indian small industries.

7. FDI in Retail Industry

FDI in retail industry means that foreign companies in certain categories can sell products through their own retail shop in the country. At present, foreign direct investment (FDI) in pure retailing is not permitted under Indian law. Government of India has allowed FDI in retail of specific brand of products.

It is a very positive step and it will encourage international brands to set up shop in India. On the other hand, this will also lead to competition among Indian players. The growing dominance of multinational companies in the country's $200 billion retail business, had warned that any move to increase FDI in the retail sector would ruin the business of small and medium traders scattered over the country. Organized retailers in India are opposing the entry of MNCs in retail trading because of their predatory pricing strategy that wipes out competition. When the Government decides to allow foreign players to enter the retail space, it should first restrict them to lifestyle products segment before permitting them to spread their wings into other areas like grocery marketing that has a direct impact on 'kirana stores'.

FDI in retail trade has forced the wholesalers and food processors to improve, besides raising exports and trigging growth by outsourcing supplies domestically. The availability of standardized products has also boosted tourism in these countries. FDI in retail sector has been a key driver of productivity growth in Brazil, Poland, and Thailand. This has resulted in lower prices for the consumer, more consumption, and higher profit for the producer.

8. Retail Formats in India

In India, at present, retailing activities are being carried through wide varieties of formats ranging from 'pheriwala' in streets to Modernised Malls in Metro cities. However, from study point of view these formats can easily be classified into the following three Groups:

The following Figure 1 shows clearly that the retail formats in India:

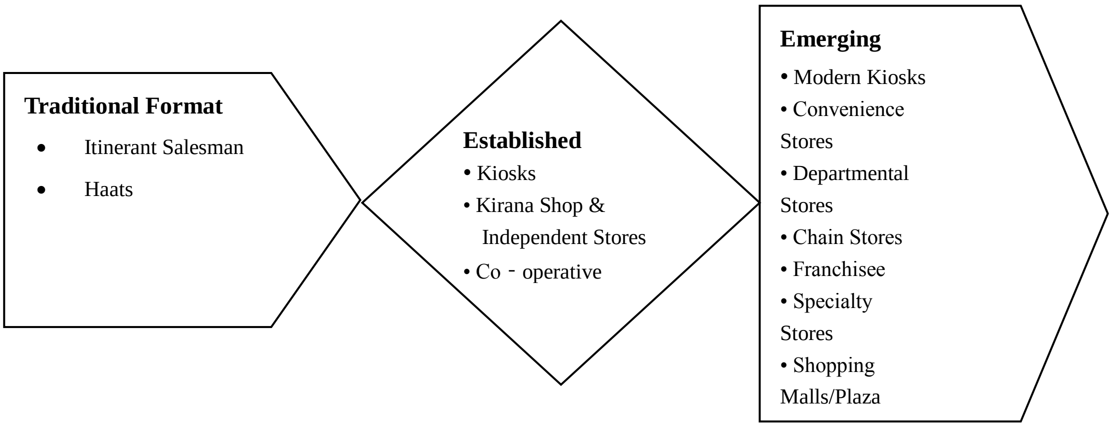

Figure 1. Formats of retailing

Emerging Modernized formats of retailing working in India will be examined in detail under the head “Modern Retail formats in India” wherein only traditional and established formats will be dealt with in detail.

9. Major Indian Retailers

Indian apparel retailers for instance, are increasing their brand presence overseas, particularly in developed markets. While most have identified a gap in countries in West Asia and Africa, some majors are also looking at the US and Europe. Arvind Brands, Madura Garments, Spykar Lifestyle and Royal Classic Polo are busy chalking out foreign expansion plans through the distribution route and standalone stores as well. It plans to open three stores in London by 2008-end.

The low-intensity entry of the diversified Mahindra Group into retail is unique because it plans to focus on lifestyle products. The Mahindra Group is the fourth largest Indian business group to enter the business of retail after Reliance Industries Ltd, the Aditya Birla Group, and Bharti Enterprises Ltd. The other three groups are focusing either on perishables and groceries, or a range of products, or both.

- REI AGRO LTD Retail: 6TEN and 6TEN kirana stores;
- Future Groups-Formats: Big Bazaar, Food Bazaar, Pantaloons, Central, Fashion Station, Brand Factory, Depot, aLL, E-Zone etc.
- Raymond Ltd.: Textiles, The Raymond Shop, Park Avenue, Park Avenue Woman, Parx, Colourplus, Neck Ties & More, Shirts & More etc.
- Fabindia: Textiles, Home furnishings, handloom apparel, jewellery;
- RP-SanjivGoenka Group Retail-Formats: Spencer’s Hyper, Spencer’s Daily, Music World, Au Bon Pain (Internaional bakery cafeteria), Beverly Hills Polo Club;
- Reliance Retail-Formats: Reliance MART, Reliance SUPER, Reliance FRESH, Reliance Footprint, Reliance Living, Reliance Digital, Reliance Jewellery, Reliance Trends, Reliance Autozone, iStore;
- Reliance ADAG Retail-Format: Reliance World;
- Nilgiri’s-Formats: Nilgiris’ supermarket chain;
- Marks & Spencer: Clothing, lifestyle products, etc.
- Pyramid Retail-Formats: Pyramid Megastore, TruMart;
- Next retail India Ltd (Consumer Electronics);
- Vivek Limited Retail Formats: Viveks, Jainsons, Viveks Service Centre, Viveks Safe Deposit Lockers PGC Retail -T-Mart India, Switcher, Respect India, Grand India Bazaar,etc.
- German Metro Cash & Carry;
- Shoprite Holdings-Formats: Shoprite Hyper;
- Paritala stores bazar: honey shine stores;
- Aditya Birla Group - “More” Outlets.

10. FDI Policy with Regard to Retailing in India

- It will be prudent to look into Press Note 4 of 2006 issued by DIPP and consolidated FDI Policy issued in October 2010 which provide the sector specific guidelines for FDI with regard to the conduct of trading activities:
- a) FDI up to 100% for cash and carry wholesale trading and export trading allowed under the automatic route.
- b) FDI up to 51 % with prior Government approval (i.e. FIPB) for retail trade of Single Brand ‘products, subject to Press Note 3 (2006 Series).
- c) FDI is not permitted in Multi Brand Retailing in India.

10.1 Revised FDI Policy in Single Brand Retail

10.1.1 Single Brand Product Retail Trading 100% Government Route

- (1) Foreign Investment in Single Brand product retail trading is aimed at attracting investments in production and marketing, improving the availability of such goods for the consumer, encouraging increased sourcing of goods from India, and enhancing competitiveness of Indian enterprises through access to global designs, technologies, and management practices.

- (2) FDI in Single Brand product retail trading is subject to the following conditions:
- (a) Products to be sold should be of a 'Single Brand' only.
- (b) Products should be sold under the same brand internationally i.e. products should be sold under the same brand in one or more countries other than India.
- (c) 'Single Brand' product-retail trading would cover only products which are branded during manufacturing.
- (d) The foreign investor should be the owner of the brand.
- (e) In respect of proposals involving FDI beyond 51%, mandatory sourcing of at least 30% of the value of products sold would have to be done from Indian 'small industries/ village and cottage industries, artisans and craftsmen'.
- (3) Application seeking permission of the Government for FDI in retail trade of 'Single Brand' products would be made to the Secretariat for Industrial Assistance (SIA) in the Department of Industrial Policy & Promotion. The application would specifically indicate the product, Product categories which are proposed to be sold under a 'Single Brand'.
- (4) Applications would be processed in the Department of Industrial Policy & Promotion, to determine whether the products proposed to be sold satisfy the notified guidelines, before being considered by the FIPB for Government approval. Revised Position w.e.f.20.9.2012.

10.1.2 FDI in Multi Brand Retail

- The government has also not defined the term Multi Brand. 51% FDI in Multi Brand retail implies that a retail store with a foreign investment can sell multiple brands under one roof with the following conditions:
- 1. FDI in multi brand retail trading, in all products, will be permitted, subject to the following conditions: Fresh agricultural produce, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products, may be unbranded.
- 2. Minimum amount to be brought in, as FDI, by the foreign investor, would be US $ 100 million.
- 3. At least 50% of total FDI brought in shall be invested in 'backend infrastructure' within three years of the first tranche of FDI, where back-end infrastructure' will include capital expenditure on all activities, excluding that on front-end units; for instance, back end infrastructure will include investment made towards processing, manufacturing, distribution, design improvement, quality control, packaging, logistics, storage, ware-house, agriculture market produce.
- 4. Infrastructure etc. Expenditure on land cost and rentals, if any, will not be counted for purposes of back end infrastructure.
- 5. At least 30% of the value of procurement of manufactured, Processed products purchased shall be sourced from Indian 'small industries, which have a total investment in plant & machinery not exceeding US $ .1.00 million.
- 6. This valuation refers to the value at the time of installation, without providing for depreciation. Further, if at any point in time, this valuation is exceeded, the industry shall not qualify as a 'small industry' for this purpose. This procurement requirement would have to be met, in the first instance, as an average of five years' total value of the manufactured.
- 7. Thereafter, it would have to be met on an annual basis.

11. States in Favour of FDI in Multi Brand Retail

The following are the States in favour of FDI in Multi Brand Retail:

Maharashtra, Haryana, Andhra Pradesh, Rajasthan, Jammu and Kashmir, Utrakhand, Manipur, Assam and Delhi Uttrakhand, Manipur and Assam have no cities with population of one milllion but capital cities of these states can be considered for opening multibrand retail stores. These states cover 19 cities like Delhi, Mumbai, Pune, Nagpur, Jaipur, Hyderabad, Vijayawada and Srinagar.

12. States Opposing FDI in Multi Brand Retail

The following are the States opposing of FDI in Multi Brand Retail:

Gujarat, Uttarpradesh, West Bengal, Bihar, Tamilnadu, Kerala, Chatisgarh, and Odisha. Through FDI Policy in Multi Brand Retail has been approved by the Cabinet, yet the final authority for granting the trade licence rests with the states under the irrespective Shops and Establishment Acts. Also, foreign retailers will only be allowed to set up shop in cities with a population of more than one million.

13. Major Players Expected to Enter Indian Retail Sector

The following are the major players expected to enter Indian Retail Sector:

• Wal-Mart Stores inc

• Carrefoursa

• Tesco plc

• Metro ag

• Ikea

14. Challenges and Opportunities

Retailing has seen such a transformation over the past decade that its very definition has undergone a sea change. No longer can a manufacturer rely on sales to take place by ensuring mere availability of his product. Today, retailing is about so much more than mere merchandising. As the Indian consumers have agained more insight, they expect more and more at each and every time when they step into a store. For manufacturers and service providers the emerging opportunities in urban markets seem to lie in capturing and delivering better value to the customers through retail. However, manufacturers and service providers will also increasingly face a host of specialist retailers, who are characterized by the use of modern management techniques, backed with seemingly unlimited financial resources. Organized retail appears inevitable. Retailing in India is currently estimated to be a US$ 200 billion industry, of which organized retailing makes up a paltry 3 percent or US$ 6.4 billion.

The following Figure 2 depicts clearly that the Challenges and opportunities in Retail Marketing in India:

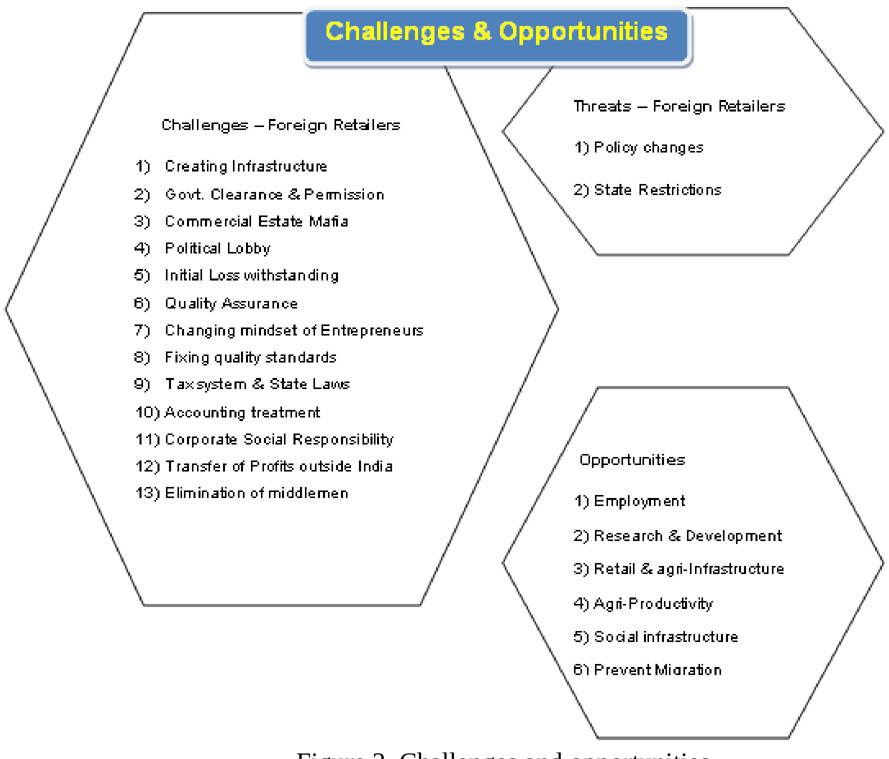

Figure 2. Challenges and opportunities

15. Summary & Conclusion

India being one of the major economies in the world has been enjoying huge and regular FDI from investor of all around the world. Majority of this FDI in India has been made in the sectors of telecommunication, construction, computer software and hardware etc. FDI in retail sector was permitted to enter in 2006 and gradually it was liberalized and recently in 2011, 100% FDI in single brand retail was permitted and in 2012, 51% FDI in multi brand retail was permitted. This has led to debate regarding implication of this policy. FDI has positive impact on some sectors while negative on others. In our study we hope to see that FDI will bring investment for modernizing farm as well as retail sector and will also improve supply chain. As a result of these factors food inflation will come down and it will benefit consumers as well. In fine, FDI in retail sector may boost the socio economic development of the entire country if implemented wisely and carefully and taking extra care while signing the agreements with the Foreign Investors.

So this is the time to shift gears and accelerate the pace of retail development in India. Finally, of late, there has been a lot of debate about the merits and demerits in liberalizing FDI in retail, insurance, pension, and aviation sectors in India. With the issue of FDI still being hot, it is important for the government to take due care in formulating its FDI policies so as to reduce the regional disparity rather than aggravating it.

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