International Journal of Economics & Finance Research & Applications
Vol. 1, Issue 1 - 2017

RETAIL SECTOR - A HAVEN FOR FOREIGN DIRECT INVESTMENT IN INDIA

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ABSTRACT

Amidst the global meltdown, and financial crisis, India has managed to display resilience and attract good investments with her sound and astonishing macroeconomic variables and a GDP projection of 7.2%, and has earmarked its striking capital flow in the recent period with the private (debt and equity) flows as a lion's share of the total capital flows. Also it envisages indirectly that the copious flow of FDI can be recalibrated at the State level. These increases in flows are towards the real estate and construction, computer related, metallurgical, petroleum industries and so on. However, recent inklings by the central government evince the consideration of foreign direct investment in retail trade and has put in debate whether it is good or not towards the advisability and consequence of this policy. This article throws light on the different sectoral roles of FDI and discusses its effect in the Indian retail scenario.

INTRODUCTION

Foreign Direct Investment (FDI) can be defined as a type of investment made in order to gain unwavering and long-lasting interest in enterprises that are being carried out outside of the economy of the investor.

Retailing is the largest private sector industry in the world economy with the global industry size exceeding $6.6 trillion and a recent survey has projected India as the top destination for retail investors and it contributes around 10 % to the total GDP, which is next to agriculture; and a further upsurge is anticipated in the retail sector as the Government opened up 51% FDI in single brand retail outlets. The retail industry in India is of late often being hailed as one of the sunrise sectors in the economy. AT Kearney, the well-known international management consultancy, recently identified India as the 'second most attractive retail destination' globally among thirty emergent markets. It has made India the cause of a good deal of excitement and the cynosure of many foreign eyes.

SCENARIO OF RETAIL SEGMENT IN INDIA

Indian retail trade is of enormous size ($180 billion), nearly 10 per cent of GDP, employing 21 million persons, which is about 7 per cent of the labor force. It is six times bigger than Thailand and five times larger than South Korea and Taiwan.

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China's retail trade is 8 per cent of GDP and 6 per cent of employment. Even more importantly, it believes that the retail trade's organized sector, which currently accounts for only 2% of total retail sales in India and is an estimated INR 250bn (US$5.75bn), has the potential to grow extremely fast (Merrill Lynch). The growth and development of organized retailing in India is driven primarily by two factors viz., i) Lower prices and benefits that the consumers can't resist. ii) Economics of scaling down the cost of supply chain, the benefits of which can be passed on to the consumers by retailers.

The retail industry is compartmentalized into organized and unorganized sectors. Organized retailing – simply it means, the trading activities undertaken by licensed retailers, that is, those who may be registered for sales tax, income tax, etc. These include the hypermarkets, supermarkets, multibrand outlets, departmental stores and retail chains, and also the privately owned large retail businesses. Unorganized retailing refers to the traditional formats of low-cost retailing, for example, the local *kirana* shops, owner manned general stores, *paan/ beedi* shops, convenience stores, hand cart and pavement vendors, etc. According to the AT Kearney's 2005 Global Retail Development Index, India would be the most compelling opportunity for retailers, which can be substantiated by the reason that as the country is becoming richer, close to a quarter of the population is in the 20-34 years age group in demand by marketers, and risk expenditure is anticipated to pick up in a major way.

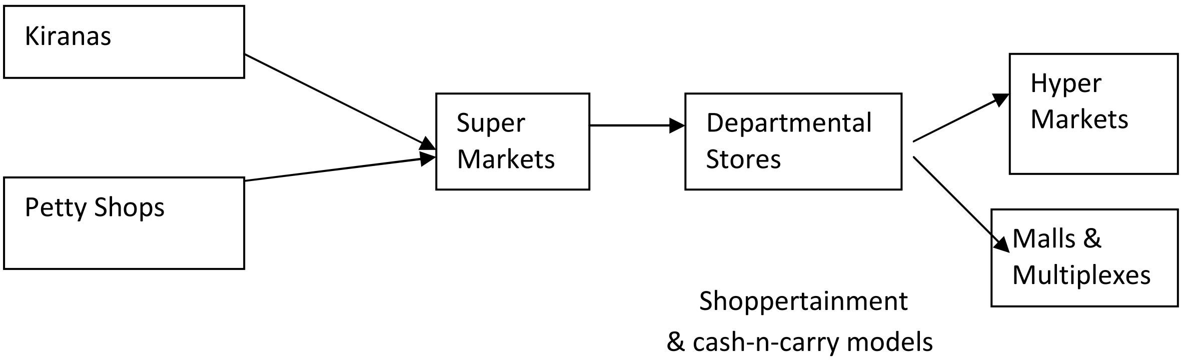

Figure 1.Metamorphosis of Retail Marts

It is inevitable that owing to the factors influenced by the global environment and from the change in the customers' mindset, the very concept of a normal brick-and-mortar retail shop has been metamorphosed to a hyper mall or a multiplex.

FDI – INDIA'S STANCE

Table 1.Comparative Figures of Organized Retail with Other Countries

Countries	Organized Retail (%)
India	4
US	85
Malaysia	55
Russia	33
China	20
Thailand	40

Source: www.indiafdiwatch.org

Table 2.Composition of India's Total Retail Market [6]

Category	Percentage
Food and Grocery	77
Clothing	7
Durables	4
Jewelry	4
Home Furnishings	2
Health & Beauty	2
Medical Services	2
Footwear	1
Books and Music	1

FDI IN RETAIL – INDIA'S STANCE

During 2006, the then UPA Government promulgated its step to promote organized retail in India by opening up 'single-brand retailing' to foreign direct investment (FDI). According to this proposal, FDI up to 51 per cent is currently permitted in Indian companies engaged in retail trade of single-brand products with prior government approval and is also subjected to prescribed conditions. FDI in retail trade of "single brand" can be subjected to the following conditions:

i) Products to be sold should be of a "single brand" only.
ii) Products should be sold under the same brand internationally.
iii) "Single brand" product-retailing would cover only products which are branded during manufacturing.

(Source: Foreign Direct Investment Policy of India)

Additionally, the question on whether co-branded goods (specifically branded as such at the time of manufacturing) would qualify as single brand retail trading, remains unanswered.

Further, the requirement of goods being sold under same brand internationally, limits the potential for FDI infusion in the case of single-brand goods developed by Indian entrepreneurs and sold locally. A policy on these fronts is required to provide much needed clarity to foreign retailers who are looking at entering single-brand retailing in India.

SIZE & GROWTH OF RETAIL MARKET

($ billion)	Total size	Organised retail	% of total market
2005	244	8	3
2006	276	11	4
2007	316	15	5
2008	362	19	5
2009	368	22	6
2010	425	28	7
2011	471	35	7
2012*	528	44	8
2013*	590	55	9

* forecasts Source: Boston Consulting Group

Source: Boston Consulting Group from Financial Express

Figure 2.Size and Growth of Retail Market

Further, an obvious question that pops-up is with regard to the rationale behind allowing only 51 per cent FDI as against 100 per cent in single-brand retailing.

This question becomes imperative considering the benefits offered by investments in the single-brand retail segment. These benefits are plentiful in the form of better job opportunities, superior human resource skills, enhanced consumer satisfaction, and support to ancillary industries.

Single-brand retailers typically deal in high-end luxury brands and thus an upmarket location is a prime factor for setting up a retail store. This factor can provide the much-needed boost to the mall development process in India in an otherwise difficult economic situation at present.

REASONS FOR AGGREGATION OF GLOBAL RETAILERS

GENERAL DEMOGRAPHIC FACTORS

i) India has high population next to China.
ii) India comprises a heterogeneous group of people with multi-lingual, multi-cultural people, so a chance of varied market segmentation is possible.
iii) India ranks 5th on global retail development index.
iv) It assumes the top position among the top 10 FDI destinations of the world.
v) It is assumed to be the fastest growing tourism market as it holds many tourism spots and pilgrimages.
vi) It has a conducive business environment with high magnitude of professionalism and business ethics.

CONSUMERS' PERSPECTIVE

i) Very limited (around 5%) proportion of organized retailing among the total retailing when compared to the other countries.
ii) Manifold increase in the disposable income of an average employee.
iii) Increase and variations in the customer aspiration because of the influences created by different media and the celebrities.
iv) Increase in expenditure of luxury items because of increase in income level and also because of change in the generation levels.
v) A geometric progression of increase in the purchasing power of people witnessed by the increase in the employment opportunities especially with increase in IT fields.

FACTORS FAVORING FDI IN RETAIL SECTOR

i) FDI towards the retail industry may trigger any sluggish economy, thereby enhancing the desired GDP growth.
ii) Entry of global competitors may nurture a healthy competition among the players.
iii) Because of the diversified marketing channels, retailing and its associated parameters as supply chain management, and logistics is no longer a cumbersome process.
iv) May lead to open many doors for the employees and thereby enhance their employment potential.
v) Entry of new corporates in retailing may enable a world-class market segmentation and wide range of products classification.
vi) Influx of new retails may indirectly benefit the rural markets for their product procurement.
vii) Because of the advent of newer technological concepts in this arena, cost efficiency can be handled smoothly.

HICCUPS FOR INDIAN RETAIL SEGMENT

i) **Fragmentation**: Among the retail sector as an entity, unorganized retailing accounts for 96% of the total retailing and as the organized sector shares only less than 5% of the total workforce in India and millions are forced to seek their livelihood in the informal sector, retail trade being an easy business to enter with low capital and infrastructure needs, acts as a kind of social security net for the unemployed.

ii) **Over dominance of unorganized retail players**: When compared to the other developed countries, India has its major share towards the unorganized players which contribute around 95% of the total market share.

iii) **Invasion of multinational chain retail outlets and low share of organized retailing:** This may reduce the sale of unorganized sector.

iv) **Ambiguity in explaining the term "single brand"**: The existing policy does not clearly codify whether retailing of goods with sub-brands bunched under a major parent brand can be considered as single-brand retailing, and is accordingly, eligible for 51 per cent FDI.

v) **Phenomenon of disturbing the Hornet's Nest**: Even though, opening new retail outlets in urban and suburban places, avenues more employment opportunities, it indirectly paves way for dislocating millions of population from their existing occupation, and dropping our GDP from the current level as our country is predominantly based on agriculture. However, economists opined that it won't promote the employment opportunities for semi-illiterate people, which forms a majority of Indian population.

vi) **Fear of Predatory pricing**: If FDI is allowed for retailing, there may be chances of lowering of prices because FDI will result in good technology, supply chain etc. If prices were to reduce, then it may hamper the margin of the unorganized local players.

vii) **Increase in real estate prices:** Because of the invasion of foreign players, there may be a chance for spurt in the real estate prices and also an increase in the price per unit area.

viii) **Chance for the dominance of counterfeit and fake goods:** Since retailing is considered as an intermediate process, supply of genuine and high quality goods may not be ensured. So there may be chances for the explosion of counterfeit goods through foreign entrants.

ix) **Predominance of xenocentrism:** If FDI is being increased by the foreign entrants, desi people may shift towards the foreign culture in their eating, dressing habits and other living trends. In other words, a xenocentrism is being followed rather than the ethnocentrism.

STRATEGIC ALLIANCE AS THE KEY FACTOR

Any foreign entrant, either through the open policy or the backdoor entry, can find its niche position only through the strategic alliance with an Indian firm as a part of their merger and acquisition (M&A).

i) As India does not allow FDI into multi-brand retail, foreign entrants as US Wal-Mart have entered the country only for wholesale trading known as 'Cash-and-Carry'.

ii) The tie-up between Bharti and the world's largest retailer, Wal-Mart, for a cash-and-carry wholesale trade joint venture coupled with the Indian company's plans for front-end retail business have drawn attention to the "grey areas" in government's FDI policy.

iii) Carrefour of French origin, is considering to enter the Indian market through multiple licenses for its wholesale cash-and-carry business and Carrefour India Master Franchise Company Pvt. Ltd., for the direct-to-consumer front end retail in partnership with the Reliance Retail.

iv) The entry of foreign companies into retailing has been restricted so far to single brand stores such as Reebok and Benetton.

v) Renault-Nissan Automotive India, a 50:50 joint venture floated for a passenger car project in Chennai, is eyeing 5.7 per cent of the market share in India by 2012, according to Colin Dodge, Executive Vice President, Nissan.

DISCUSSIONS & CONCLUSION

Organized retailing has gained its momentum in the last decade only. This propensity of organized sector propels the small retailers to migrate to unorganized sector and affects their livelihood. This needs to be kept in mind while discussing the impact of FDI in retail trade. The main lacuna for the FDI in retailing is that FDI is still not permitted for a multi-brand retailing concept. The only option to the foreign players is through the franchisee method. The entry of some of the MNC retail outlets seems to be a backdoor entry for such concerns, which in due course may drive out the local kiranas as well as small sellers. However, this entry can be purely viewed as a strategy of merger and acquisition. When we talk of the unorganized Indian retailers, they are comparatively lesser in dimensions in terms of average retail area, their turnover and thereby their return on assets and return on equity. Hence the invasion of foreign retailers as a behemoth which may be able to sustain their initial losses, may in due course definitely litigate the Indian markets and intensify the job losses.

Even though the McKinsey report on 'Indian Growth' projects a whooping addition of 70 lakhs job in the retail sector between 2000 to 2010, with a projected GDP growth of 10%, this trend is not favorable in the current scenario, where we evinced around 7% GDP growth rate.

During the Union Budget for 2010-11 announced by Mr. Pranab Mukherjee, the Union Finance Minister, some of the initiatives were laid to spurt the FDI inflows which include the reduction in complexity process of FDI, clear cut methodological approach for indirect foreign investment in Indian companies and the complete liberalization of pricing and payment of technology transfer fee and trademark and brand name etc. Also the Central Government, has come out with allowing 100% FDI in defense sector. Same way, permitting a 100% FDI in retail is always a boon for our fund inflows, despite some bottlenecks.

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