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FDI IN INDIAN RETAIL SECTOR: OPPORTUNITIES AND CHALLENGES

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ABSTRACT

Foreign Direct Investment (FDI) is considered to be the lifeblood of economic development especially for the developing and underdeveloped countries. It plays an important role in the long-term development of a country not only as a source of capital but also for enhancing competitiveness of the domestic economy through transfer of technology, strengthening infrastructure, raising productivity and generating new employment opportunities. Allowing FDI proves good as improvements in supply chain technologies and informational externalities to local players and competitive dynamics that could benefit consumers and suppliers. Competition is best for consumers as it gives them variety, better prices and better quality. It may give domestic producers an incentive to become more efficient. FDI in retail sector can expand markets by reducing transaction and transformation costs of business through adoption of advanced supply chain and benefit consumers and suppliers. FDI in multi-brand retail will support the government's role of achieving remunerative prices for farmers and will also increase quality and choice for India's increasingly sophisticated consumer base. An incredibly high percentage, 40% of food is lost in India due to the lack of cold storage and the lack of quick transportation. This is one of the very important benefits of multi-brand retail that they brought across the world in supply chain. FDI is expected to bring the investment and expertise necessary to modernise and develop the farm and manufacturing sector. The prospect of higher growth in the food and grocery is particularly attractive because over fifty per cent of India's workforce is employed in the farm sector. FDI increases the level of competition in the host country. Other companies will also have to improve on their processes and services in order to stay in the market. FDI enhanced the quality of products and services. FDI has also ensured a number of employment opportunities by aiding the selling up of industrial units in various corners of India.

INTRODUCTION

FDI

Generally speaking FDI refers to capital inflows from abroad that invest in the production capacity of the economy and are "usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors. FDI also facilitates international trade and transfer of knowledge, skills and technology." It is furthermore described as a source of economic development, modernization, and employment generation, whereby the overall benefits (dependant on the policies of the host government)....triggers technology spill overs, assists human capital formation, contributes to international trade integration and particularly exports, helps create a more competitive business environment, enhances enterprise development, increases total factor productivity and, more generally, improves the efficiency of resource use.

HISTORY OF FOREIGN DIRECT INVESTMENT (FDI) IN INDIA

Foreign direct investments (FDI) are a major driving force behind the growth of Indian financial markets. Post liberalisation in 1990s, the country is being viewed as a strategic destination by foreign majors to park their investments and benefit from the economic growth. In India, FDI is considered as a developmental tool, which can help in achieving self-reliance in various sectors of the economy. With the announcement of Industrial Policy in 1991, huge incentives and concessions were granted for the flow of foreign capital to India. India is a growing country which has large space for consumer as well as capital goods. India's abundant and diversified natural resources, its sound economic policy, good market conditions and highly skilled human resources, make it a proper destination for foreign direct investments

India remains the world's third most attractive destination for investment by transnational corporations (TNCs) during 2013-15, stated a recent survey by UNCTAD. The country was ranked after china and the US in the survey based on responses of 159 companies. As per the recent survey done by the United National Conference on Trade and Development (UNCTAD), India will emerge as the third largest recipient of foreign direct investment (FDI) for the three-year period ending 2012 (World Investment Report 2010). As per the study, the sectors which attracted highest FDI were services, telecommunications, construction activities, and computer software and hardware. In 1991, India liberalised its highly regulated FDI regime. Along with the virtual abolition of the industrial licensing system, controls over foreign trade and FDI were considerably relaxed. The reforms did result in increased inflows of FDI during the post reform period. The volume of FDI in India is relatively low compared with that in most other developing countries.

Moreover, this economic segment enjoys high attention from top officials of the Government, owing to its strategic importance. The Government keeps making efforts to provide impetus to FDI flows in the country and hence undertakes numerous reform initiatives. FDI norms were further liberalised after September 2012 in sectors like civil aviation, power exchanges and retail. The Ministry of Finance has also suggested modifications in FDI caps for various sectors, including tea, media, natural gas and petroleum.

In political economy terms, the entry of foreign retailers affects different stakeholders on the demand and supply side. Improvement in supply chain, especially for food items, across the country benefits low income groups because their major part of the consumption basket is food. Secondly, it will increase surplus to small and medium farmers. Low income consumers on the demand side and small and medium scale farmers on supply side are less cohesively organized in influencing government policies than wholesalers, middlemen, and Indian large retailers. Indian large retailers (such as the newly entrenched interests like the Reliance fresh) may block the entry of foreign players with short-term calculations of their interests. However, they can benefit from externalities arising out of the entry of foreign players if the foreign players invest significant resources in developing the supply chain and improve the know-how of large number of vendors. This took place in the case of the automobile sector. Some of the wholesalers and small Kirana stores adopted innovative practices in procuring and selling goods in response to competition from the large retailers which will improve the overall organization of the markets. The main losers would be the middlemen rather than small traders. Small traders retain the advantage of low overhead costs and take advantage of geographic distribution and density of consumers. Any technological and organizational changes have disruptive effects - some losers in the short run and larger number of gainers in the long run. As the presence of large retailers increases, government tax revenues will increase which can be used to compensate the losers. The main role of government is to establish and implement effective and autonomous regulatory institutions- restraining anti-competitive conduct by firms, labour and environmental regulation. The government has to make credible commitments of its policies.

FDI in "Single-Brand" Retail

FDI in single-brand retail implies that a retail store with foreign investment can only sell one brand. For example, if Adidas were to obtain permission to retail its flagship brand in India, those retail outlets could only sell products under the Adidas brand. For Adidas to sell products under the Reebok brand, which it owns, separate government permission is required and (if permission is granted) Reebok products must then be sold in separate retail outlets.

Up to 100% in Single Brand Retail Trading

By only one non-resident entity whether owner or the brand or otherwise 30% domestic sourcing requirement eased to preferable sourcing rather compulsory Further clarification on FDI companies that cannot engage in B2C e-commerce.

FDI in "Multi-Brand" Retail Up to 51% in Multi-Brand Retail Trading

- At least US$100m as equity into Indian company.
- At least 50% of the total FDI is to be invested in back end infrastructure within 3 years.
- At least 30% of the value of procurement of processed product shall be sourced from Indian "Small Industries".
- Fresh agricultural produce is permitted to be sold unbranded.
- Indian states have been given the discretion to accept or refuse to implement FDI. More than 8 states have already given their consent.
- Retail outlets can be set up in cities having a population of at least 1 million.

Application needs to be approved by two levels at Department of Industrial Policy and Promotion (DIPP) and Foreign Investment Promotion Board (FIPB). With this, a plethora of business opportunities in India has been thrown open to the foreign investors. India has seen an eightfold increase in its FDI in March 2012, at a time when the aforesaid norms were not even approved – a sign that suggests India is set to be one of the favoured destinations for foreign investors in the retail sector. The table given below shows the statement on sector-wise FDI equity inflows from April, 2000 to June, 2013.

Table 1: Statement On Sector-Wise Fdi Equity Inflows From April, 2000 To June, 2013

S. No.	Sector	Amount of FDI Inflows		%age with total FDI Inflows(+)
		(in Rs crore)	(In US $ million)	
1	Services Sector*	177,594.62	38,179.78	19.22
2	Construction Development: Townships, Housing, Built-Up Infrastructure And Construction-Development Projects	101,994.86	22,247.50	11.20
3	Telecommunications	58,785.79	12,865.83	6.48
4	Computer Software & Hardware	53,757.60	11,862.37	5.97
5	Drugs & Pharmaceuticals	54,321.68	11,318.32	5.70

6	Chemicals (Other Than Fertilizers)	41,118.29	8,993.12	4.53
7	Automobile Industry	42,015.28	8,810.07	4.43
8	Power	36,805.41	7,953.93	4.00
9	Metallurgical Industries	35,448.07	7,620.73	3.84
10	Hotel & Tourism	33,819.35	6,731.89	3.39
11	Petroleum & Natural Gas	24,950.25	5,406.70	2.72
12	Trading	19,243.58	4,063.79	2.05
13	Information & Broadcasting (Including Print Media)	16,163.91	3,406.19	1.71
14	Electrical Equipments	14,826.59	3,211.43	1.62
15	Non-Conventional Energy	13,425.78	2,683.72	1.35
16	Cement And Gypsum Products	11,941.58	2,656.29	1.34
17	Miscellaneous Mechanical & Engineering Industries	11,432.46	2,477.18	1.25
18	Industrial Machinery	11,504.84	2,388.12	1.20
19	Construction(Infrastructure) Activities	10,332.94	2,198.77	1.11
20	Consultancy Services	9,928.46	2,136.36	1.08
21	Food Processing Industries	9,534.62	1,964.32	0.99
22	Hospital & Diagnostic Centres	9,169.24	1,914.28	0.96
23	Port	6,717.38	1,635.08	0.82
24	Agriculture Services	7,866.74	1,620.65	0.82
25	Electronics	5,986.51	1,292.48	0.65
26	Textiles (Including Dyed,Printed)	5,871.60	1,258.91	0.63
27	Sea Transport	5,504.15	1,196.57	0.60
28	Fermentation Industries	5,263.53	1,163.46	0.59
29	Rubber Goods	5,944.50	1,154.61	0.58
30	Mining	4,385.34	1,001.38	0.50
31	Paper And Pulp (Including Paper Products)	4,096.21	872.83	0.44
32	Prime Mover (Other Than Electrical Generators)	4,196.03	860.24	0.43
33	Education	4,106.87	820.58	0.41
34	Medical And Surgical Appliances	3,185.03	653.45	0.33
35	Machine Tools	3,037.00	635.08	0.32
36	Soaps, Cosmetics & Toilet Preparations	3,115.55	632.40	0.32
37	Ceramics	2,780.98	611.63	0.31
38	Air Transport (Including Air Freight)	2,066.14	456.82	0.23
39	Glass	2,122.17	420.35	0.21
40	Diamond,Gold Ornaments	1,891.81	405.06	0.20
41	Vegetable Oils And Vanaspati	1,898.45	385.79	0.19
42	Railway Related Components	1,682.64	348.64	0.18
43	Agricultural Machinery	1,659.26	337.21	0.17
44	Fertilizers	1,536.11	318.24	0.16
45	Printing Of Books (Including Litho Printing Industry)	1,270.42	274.66	0.14
46	Commercial, Office & Household Equipments	1,183.63	255.17	0.13
47	Earth-Moving Machinery	770.54	175.21	0.09
48	Leather,Leather Goods And Pickers	554.92	112.35	0.06
49	Tea And Coffee (Processing & Warehousing Coffee & Rubber)	476.63	104.97	0.05
50	Scientific Instruments	534.30	101.51	0.05
51	Retail Trading (Single Brand)	468.37	96.96	0.05
52	Timber Products	433.20	85.19	0.04
53	Industrial Instruments	310.56	67.06	0.03
54	Photographic Raw Film And Paper	269.26	66.54	0.03
55	Boilers And Steam Generating Plants	306.75	62.00	0.03
56	Sugar	242.32	51.82	0.03
57	Coal Production	119.19	27.73	0.01
58	Dye-Stuffs	87.32	19.50	0.01
59	Glue And Gelatin	71.31	14.69	0.01
60	Mathematical,Surveying And Drawing Instruments	39.80	7.98	0.00
61	Defence Industries	24.36	4.94	0.00
62	Coir	10.37	2.17	0.00
63	Miscellaneous Industries	36,206.17	7,976.00	4.01
Sub-Total		**926,408.62**	**198,678.62**	**100.00**
64	Rbi's- Nri Schemes (2000-2002)	**533.06**	**121.33**	-
Grand Total		**926,941.68**	**198,799.95**	-

* *Services sector includes Financial, Banking, Insurance, Non-Financial / Business, Outsourcing, R&D, Courier, Tech. Testing and Analysis*
FDI inflows data re-classified, as per segregation of data from April 2000 onwards.
„+" Percentage of inflows worked out in terms of US$ & the above amount of inflows received through FIPB/SIA route RBI‟s automatic route & acquisition of existing shares only.
FDI Sectoral data has been revalidated / reconciled in line with the RBI, which reflects minor changes in the FDI figures (increase/decrease) as compared to the earlier published sectoral data

OBJECTIVES OF THE STUDY

1. To study the emerging challenges in FDI in Indian Retail Sector.
2. To study the opportunities in FDI in Indian Retail Sector.
3. To recommend certain suggestions for growth of FDI in Indian retail sector.

RESEARCH METHODOLOGY

This study is descriptive in nature. The study is based on secondary data which has been taken from case studies, books, journals, newspapers and online databases and websites of DIPP (Department of Industrial Policy and Promotion), RBI (Reserve Bank of India) and FICCI (Federation of Indian Chambers of Commerce and Industry) and UNCTAD (United Nations Conference on

Trade and Development). The main focus of the study is to highlight the emerging challenges and opportunities of FDI in retail sector.

Benefits/Opportunities of FDI

➢ **Benefits to Indian Economy**

FDI in retail would have been an opportunity to attract inflow of funds which would have resulted in major benefits for the Indian economy:

- **Growth in allied industries:** The inflow of funds into retailing would have simultaneously led to the growth of allied industries as happened in the case of automobiles, which led to the growth of auto components sector. Likewise FDI in retail would assist growth in supplier industries such as food-processing and textiles moreover, growing demand for retail space, construction of real estate would have also taken place.
- **Improvement of Government Revenues**: Another significant advantage of organized retailing is its contribution to government revenues. Organized retailers, by virtue of their being corporate entities need to file tax returns periodically whereas in the unorganized sectors there have been leakages in the collection of central and state taxes.
- **Supports the growth of Indian small industries**: If the consumers in India buy goods at foreign single-brand outlets, established in India and enjoy the shopping experience, in reality, they would be actively contributing towards significant money transfer to a multinational based out of the USA, which after retaining profits, would end up sending majority of this money to China, where most goods are being manufactured. The government appears to be cognizant of this very issue, which is why they proposed that at least 30 per cent of the procurement of manufactured / processed products shall be from "small industries" (presumably this refers to "small industries" in India). This aspect will lead to support the growth of the small industries in the country.
- **Supports Improved Standard of Living**: Allowing FDI in Indian Single-Brand Retail will certainly bring in more sophisticated and luxurious goods and services to the country. Availability of such goods backed with good promotional support will definitely motivate / induce the Indian buyers to buy and consume them. It will be certain that the standard of living of the consumers will be improved. In addition to the above, the people who shall be employed in the multi-national retail enterprises will be paid attractive salaries and wages that will also stand for their increased affordability. The organised retail also provides other add-on services along with the products sold. All these new changes, that shall be resulted by allowing FDI in single-brand retail will surely support improved standard of living.
- **Enhanced Competition and Reduced Prices**: Entry of the many other multi-national corporations will obviously promise intensive competition between the different companies offering their brands in a particular product market. When the manufacturing companies will take efforts to increase their market share or to accomplish their other marketing objectives, competition among them will be activated. Such a competition will result in the availability of many varieties, reduced prices, and convenient distribution of the marketing offers.
- **Enhanced Shopping Environment and Experience**: Consumers in India mostly suffer from unhygienic experiences, erratic price and irregular availability in daily food and FMCG products. Many established foreign retail giants that are known for low pricing, creation of pleasant shopping environment, maintenance of hygienist, better customer care, effective inventory management and storage facilities shall efficiently contribute for eradicating the said problems and make the shopping very productive and a happy experience to the customers in India.
- **Efficient Enforcement of Laws:** The presence of International companies in Indian Retail will facilitate effective enforcement of Tax Laws and increase in tax revenue. Tax evasion could be stopped when more of the retail is in organised format.
- **Overall Growth of The Country:** FDI in Indian retail will obviously result in the growth and expansion of the market and change in consumer spending pattern and also increase in their spending that eventually lead to higher GDP in the country.
- **Efficient Supply Chain Systems:** The Government believes that FDI in retail is the silver bullet solution to all issues regarding the inefficient supply chain system in India. This belief rests on the premise that a component of the capital inflow into the retail sector will go into developing an extremely efficient and organised supply and logistic system that will take care of collection, storage and transportation of food produce, seamlessly. The government cannot expect the Wal-Mart's and the Tesco's to build good roads, without which the supply systems cannot be optimized. This is one of the constraints that Indian retail players are already struggling with. Globally, logistics account for around five per cent of total cost retail players incur, while it is as high as ten per cent in India, thus making a dent in its attractiveness.
- **Higher Profits for Farmers:** The section in the Indian Government that supports foreign investments in retail, believes that such a move has the potential to boost up the lives of our farmers. The underlying rationale is that with the giant retailers setting up shops and investing in fully integrated supply chain from farm gates to supermarket shelves, middlemen in the chain will be cut out. Without the intermediaries, food producers would get higher prices for their produce.
- **Large-Scale Employment Generation**: Proponents of FDI in retail have declared that there will be large-scale job creation in the economy. Union Minister for Commerce and Industry Anand Sharma went one step further by quoting a figure of 10 million as the number of new jobs to be created, with bulk of that supposedly coming from the logistics sector. For example, the Wal-Mart, whose global turnover is close to size of India's entire retail industry, employs only 2.1 million people. Assuming that the Wal- Mart and other retailer giants will extend their highly profitable model in the Indian retail sector as well, it is highly unlikely that 10 million jobs will be created. On the other hand, there is a possibility of loss of employment for several small retailers once foreign retailers establish themselves in the market, as seen in developed nations. In the Indian context, a study conducted by the Indian Council for Research on International Economic Relations in 2008 observed that unorganised retailers operating in and around organised retailers have witnessed a drop in business turnover and profits after the entry of large

organised retailers. The entry of foreign players into the Indian retail market may or may not result in huge loss of jobs, but income reduction of marginal retailers and intermediaries is highly likely.

- **Elimination of Food Wastage:** Presently the highly unorganised and inadequate supply chain in India is considered responsible for the wastage of about a quarter of the total produce between the harvest and the consumption stages. In theory, development of an efficient end-to-end cold chain will make it possible to eliminate this wastage during the collection, storage and transportation of fresh produce from farms to supermarket shelves. The increase in supply base of food items due to elimination of waste will supposedly translate into higher income for farmers and lower prices for consumers. However, data from countries where retail is highly organised convey a different story. In the US and UK, anywhere between 20 and 30 percent food is wasted by retail giants between the stages of production and consumption. A huge quantity of fresh produce is thrown away by the supermarkets during the sorting process since they have a policy of accepting products that conform to strict standards in shape, size and appearance. Hence, fresh fruits and vegetables which are otherwise edible are thrown away from supermarket shelves for their unappealing looks. The Environment Agency estimates that the total UK retail food waste is 1.6 million tonnes per year.

➢ **Benefits to consumers**

- Consumers have increased the competitiveness of domestic players.
- The growth in the sector assisted the development of the auto component industry which not only produces products of global standards but has also resulted in increased employment.
- The productivity levels within the sector have improved as a result of following globally recognized models of manufacturing.
- The technological capability of Indian firms has also seen improvements over the years.
- FDI bought the required capital into the sector which assisted players in scaling up their supply thereby assisting their overall efficiency and growth.
- Consumer choices have increased by many folds both in terms of product range within a price range as well as across price range.
- The Indian consumer today has access to global brands
- The quality of products in terms of customer experience as well as other parameters such as safety, accessories have improved tremendously.

Over the years there have been new product categories that have been created keeping in mind the change in customer preferences. The recent surge in demand for luxury and high end automobiles has been noticed by various international brands which have now started looking at India as a future growth driver.

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 neighborhoods. The informal system of credit adds to their attractiveness, with many houses 'running up a tab' with their neighborhood 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 neighborhood 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 neighborhood 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.

SUGGESTIONS FOR THE GROWTH OF RETAIL INDUSTRY

FDI since 1991 has proved to be game changer for wide segments of Indian industry. FDI has changed quality, productivity, and production in areas where it has been allowed.

1. India needs to invest in infrastructure development because India is lacking only in this which will affect our Retail Industry majorly.
2. India should increase the investment absorption capacity.
3. India should make FDI policies little bit more liberal so that it can face competition with other emerging economies.
4. Bureaucratic delays and various governmental approvals and clearances involving different ministries need to be fastened.
5. Restrictions on sector caps and entry route to sectors other than those of national importance need to be liberalized further and constant reviewing of policies must be done.
6. Government must ensure consistency of policy so as to improve the business and investor confidence.

CONCLUSION

In light of the above, it can be safely concluded that allowing healthy FDI in the retail sector would not only lead to a substantial surge in the country's GDP and overall economic development, but would also help in integrating the Indian retail market with that of the global retail market in addition to providing not just employment but a better paying employment, which the unorganized sector (kirana and other small time retailing shops) have undoubtedly failed to provide to the masses employed in them. Thus, as a matter of fact FDI in the buzzing Indian retail sector should not just be freely allowed but should be significantly encouraged. Allowing FDI in multi brand retail can bring about Supply Chain Improvement, Investment in Technology, Manpower and Skill Development, Tourism Development, Greater Sourcing from India, Up-gradation in Agriculture, Efficient Small and Medium Scale Industries, Growth in market size and Benefits to Government through greater GDP, tax income and employment generation.

Despite the current policy and regulatory environment not being 'perfect' for foreign investors, there are clearly moves towards improving the current position and facilitating FDI inflows without having a detrimental impact on various sectors of the economy. The current policy is trying to encourage Joint Ventures in multi-brand retailing so as to boost the domestic retailer's growth in this area. However, there is also the risk that some foreign retailers will not be interested in investing unless they have 100% ownership and that the current policy will prevent them from choosing India as a Retail destination. In our view, the advantages outweigh the disadvantages of allowing unrestrained FDI in the retail sector, as successful experiments in countries like Thailand and China demonstrate. In both countries, the issue of allowing FDI in the retail sector was first met with incessant protests, but allowing such FDI led to GDP growth and a rise in the level of employment.

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