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FDI in India's Retail

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Abstract: *The retail industry in India is being hailed as one of the sunrise sectors in the economy. According to AT Kearney, international management consultancy identified India as the "second most attractive retail destination" .According to Deloitte report Jan 2013, The Indian retail industry is expected to be around 850 billion USD by 2015 and is expected to be over 1.3 trillion USD by 2020. The share of organized retail is estimated to be 20% by 2020. The recent wave of reforms by the Government of India to intensify FDI in retail has brought about a new outlook on the business climate in India. This paper attempts to outline the government's policy on FDI in retailing and tries to examine its pros and cons while examining the voices of small retailers on the government's decision. This paper is based on the Department of Industrial Policy and Promotion (DIPP, Government of India, Ministry of Commerce & Industry's) Press Note on the 'guidelines and policy as to FDI in Single brand and multi brand retail, various journals, relevant news articles and opinion of experts and press reports in' The Hindu Business Line'. This paper analyses the issues involved in effective implementation of the policy. A SWOT analysis has been made on the FDI policy.*
Key words: *FDI , retail, policy*

I. Introduction

World Bank has defined FDI as "Foreign direct investment (FDI) or foreign investment can refer to the net inflow of funds to acquire a long-term management interest in an enterprise operating in a foreign economy. It is the accumulation of equity, re-investment of retained earnings , other long-term sources of capital and short-term funds as presented in the balance of payments". FDI plays a very vital role in India's growth and development. FDI to a great extent aids in expansion of markets, reducing costs through improved supply chains and would be a catalyst in the economic development. This paper brings forth the FDI policy in retail in India and analyses the issues, challenges , opportunities and threat that it poses and the impact it has on the small retailers.

Objectives Of The Study

1. The main objective of the study is to analyse the FDI policy
2. The strength, weaknesses, threats and opportunities of FDI
3. To study the issues and challenges involved in implementation of the FDI policy
4. The impact of FDI on small retailer

II. Research Methodology

This paper is based on the Department of Industrial Policy and Promotion (DIPP) , Government of India, press noteon the 'guidelines and policy as to FDI in Single brand and multi brand retail, various journals, relevant news articles and opinion of experts and press reports in' The Hindu Business Line'.

III. Indian Retail Sector – An Over View

The Indian retail sector is fragmented, consisting of small independent owner managed shops, accounting for 92% of the retail sector and the remaining 8% constitutes the organized sector. Rising disposable incomes, urbanization, dominance of younger generation in spending, nuclear families, advancement in science and technology (ICT) are various factors contributing to the growth of retail in India. The organized retail is poised to grow at the rate of 20% by 2020. The policies of the Government of India , namely FDI in single brand and Multi-brand retail have opened up the gates for foreign investment in retail in India.

IV. FDI Policy

FDI was initiated around the year 2005 by the Government of India, though the liberalization and globalization started in 1990s. Initially GOI had allowed 100% investment in the cash and carry or wholesale trading. The single brand retailing in 2006 was initially restricted to 51% but later it was enhanced to 100% subject to 30% sourcing from within India. Currently, the Committee of Secretaries (COS) has given nod to 51% investment in multi-brand retail , but with stringent conditions like mandatory investment of at least 50%

in the back- end infrastructure , minimum sales of 30% to come from small traders and 30% mandatory sourcing from micro, small and medium enterprises. but it is left to the discretion of the State Governments to implement it in the respective states of India.

The Ministry of Commerce and Industry, GOI is the nodal agency for reviewing the FDI policy on continued basis and changes in sectoral policy or sectoral equity cap. The FDI policy is notified through press notes by the secretariat for Industrial Assistance (SIA) , DIPP. The salient features are:

1. India will allow FDI upto 51% in multi-brand retail.
2. Single brand retailers can own 100% of their Indian stores.
3. FDI upto 100% for cash and cary wholesale trading and export trading allowed under the automatic route.
4. Both single and MBR will have to source at least 30% of their goods from small and medium sized Indian suppliers.
5. MBR (Multi brand retailers) must bring minimum investment of USD 100m. % of which must be invested in back-end infrastructure such as cold chains, transportation, packaging etc to reduce remunerative prices to farmers and also to reduce post-harvest losses.
6. The opening of retail competition (policy) is left with the State Governments of the respective states.
7. All retail stores can open up their operations in cities having population of over 1 million.

The proposal of GOI to allow 51% FDI in MBR comes with riders.

a. Approval should be taken from the FIPB(Foreign Investment Promotion Board) for investments.
b. The policy also states that fresh agricultural produce including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products may be unbranded. Small and medium units for FDI means units which have a total plant and machinery investment not exceeding Rs. 1.25 crores. This investment refers to the value at the time of installation, without providing for depreciation. The foreign retail chains will be required to comply with self-certification. They have to keep all records and the government will have the first right to procure agricultural produce.

V. SWOT Analysis Of The FDI Policy In Retail

1. Strengths

a. Effective control of wastage of farm produce
b. Flow of foreign exchange into the country
c. Generates revenue through tax
d. Variety to consumers

2. Weaknesses

a. State Governments to decide on implementation of FDI
b. Relaxation of mandatory local sourcing criteria in case of FDI in single brand retail.
c. Investment in back-end infrastructure not including costs of land etc.

3. Opportunities

a. FDI in retail will drive consumption and provide capital to the retail sector.
b. Small manufacturers can expand their business operations.
c. Elimination of middle men , greater transparency and direct procurement from farmers is likely to benefit farmers to a great extent.
d. New technology, improvement in supply chains, packaging, storing is expected to greatly reduce wastages.
e. Brings in best management practices and training to youth.

4. Threats

a. Manufacturing sector at its low, unprepared to absorb population likely to be displaced.
b. Ambiguity on the definition of small scale industries.
c. Poses a great threat to unorganized retailers, which constitutes 92% of the retail sector.
d. Predatory pricing, monopolistic practices and cartelization.

Now, let us analyse the impact of FDI on the various stakeholders.

Positive Aspects

1. For the Government

Modern trade players are very large tax payers and are tax-compliant. There is certainly going to be increase in tax receipts . By building effective and sophisticated supply chain, there is going to be a great impact on the logistics, warehousing and related sectors. This will definitely lead to increase in direct and indirect tax collections. FDI in retail is expected to generate 16.2 billion USD in the form of VAT etc by 2021 . According to CRISIL Research Estimate, FDI investment will be between 5 to 6 bn USD (FICCI) to 10 bn USD over the next five years. Thus FDI in retail will help in improving the balance of payments (BOP) position, generate employment opportunities, increase in tax collection.

2. For the MSMEs

The interests of the MSMEs have been protected with the clause of 30% sourcing from MSME mandatory, the Government has tread cautiously, to protect and promote the MSMEs. The presence of global players is likely to boost exports , through the distribution networks, market position and brands of the foreign players. This is likely to enhance sourcing and exports from India. Thus, FDI in retail provides great export opportunities for the MSMEs. Large volumes can be sourced from MSMEs. This will have an impact on the manufacturing sector through improvement in quality products being manufactured to compete with the global brands, innovation, new technology adoption, which will have a cyclical effect on the economy in terms of employment generation and consequent GDP growth.

3. For the Consumers

Big box retailers will be in a position to offer products at low cost with fabulous discounts, as they have a well developed supply chain , smart procurement and effective inventory management. Thus consumers will get products at lower prices, better shopping experience, greater varieties of products, latest products and designs and quality products.

4. For the farmers

Indian economy is predominantly an agrarian economy . FDI in retail is likely to transform the lives of whole chains of human beings and the operations of the agricultural sector as a whole. Though the agricultural marketing dates back to 1928 colonial regulations to protect the poor farmers, yet agricultural marketing in India has not come a long way. Distribution of food items involves multiple intermediaries by the time the produce reaches consumer from the farmer. Millions of tons of fresh fruits and vegetables is wasted due to inadequate post-harvest storage, handling, processing facilities. Farmers have very little choice but to sell to the traders on the latter's terms. Farmers unjustifiably get very low prices for their produce. Thus, FDI in retail in India will help the farmers in better price realization due to elimination of intermediaries. It will also educate farmers in improving crop yield and crop selection as per consumer's requirement. Due to improved supply chain and back-end infrastructure, there is going to be a significant reduction in wastage of tons of agricultural produce. There is likely to be greater transparency and dissemination of information on food stocks and thus facilitate planning and preparing for any contingencies.

5. For the Economy/ Society

Supply chain will be a critical factor for the retail. FDI in retail will lead to improvement in transportation, logistics, warehousing and other allied service sectors and a greater improvement in the infrastructural facilities in the country. This will be a major employment generation sector. Also, FDI in retail is likely to provide to better salaries, better work environment and will contribute to increase in the living standards of the people.

Negative aspects

*1. **Is FDI a debt inflow or a liability foreign exchange ?***

Foreign exchange is either an asset or liability, depending on its repatriability. If it is repatriable (ie), to be repaid in the form of foreign exchange, it is a liability. The profits or returns will have to be repatriated in foreign exchange, it is a liability. All the men, material, merchandise imported will have to be paid in foreign exchange. Also, at the time of winding up, the sale proceeds will flow out of the country in foreign exchange. Thus, foreign exchange is both a boon and bane. FDI would impact our already fragile foreign exchange position, with imports gaining ascendancy and the fact that foreign retail giants view the world as their oyster.

2. **Impact on small traders**

Entry of foreign retailers will to a great extent affect the livelihood of small traders. Experience with Wal-Mart in the country of its origin shows that, as Walmart's business continued to grow and the stores began to expand, communities lost their local retailers. Small retailers were forced to close their shutters. The growth of Walmart has resulted in decreased wages, shrinking middle class and increase in working poor. The savings due to shopping at Walmart cannot compensate for the loss of job opportunities and income. The need of the hour is to protect the interests of millions of traditional retailers , whose livelihood depends on this trade. We need to protect, strengthen, modernize traditional retailers through institutional credit to attain inclusive growth.

3. **Impact on the manufacturing sector**

Big box retailers,, through their effective supply chain and distribution networks, will import low cost products, which will have a direct impact on the manufacturing sector. This would result in closure of industries, loss of jobs and consequent impact on the economy as a whole. Various research articles suggest that US is being transformed from a technologically advanced manufacturing economy to a mere consuming economy on account of higher imports. Studies have shown that retail giants like, Walmart contribute to poverty, which would prove costly for a developing nation like India. Instead of allowing foreign capital to set up shop in India, we should import technology, if needed and set up the same industries with domestic capital. This would enable domestic consumers getting the same products at the same time improving the manufacturing sector and resultant employment generation.

Thus FDI in retail is allowing them to reap profits here and taking them back. Historically, no country has ever developed on foreign capital. Indigenous mobilization of resources, domestic technological development and application, support from Government, strategic management were the important factors in the industrial revolution of various nations. These are lessons India must learn from developed countries.

4. **Impact on the small farmers**

Complaints are made by agro- ecologists who observed that farmers working under contract gain more price security, but forfeit their freedom to make decisions. Another class of bonded labor is getting evolved. The poultry farmers in the US turned into regimented assembly lines, from being independent entrepreneurs due to the transformation. This not only undermines the self-esteem of the farmers but also have a serious impact on the land, resources, soil degradation, as the farmers are directed to work only for commercial gains, with no long-term consequences in mind.

Also, when contracts are made in advance, market prices will have no relevance. In addition, as FDI retailers are very keen on size, shape of the farm produce, and farmers are forced to supply as per the specifications, there is likely to be huge rejections due to stringent quality checks and resultant huge wastage of farm produce.

VI. Conclusion

There are regulatory hitches, high cost of real estate are serious issues the foreign retailers are facing and cannot be lost sight of. Companies, even with strong lobby teams are wary of red-tapism, bureaucracy. Also, the FDI policy of allowing the State Governments to decide on the entry, will have serious consequences with the change in the political climate.

The question here is "Does India need FDI in retail"? The advocates of FDI have probably put too much emphasis on it. India stands different from other countries. We have a large pool of entrepreneurs, tech savvy, have access to global technology. Large retail giants due to their huge buying power will procure cheap goods and import them into the country , which would be an impediment for the growth of manufacturing sector. Not only will the small traders bring their shutters down but also the manufacturing industries will have to shut down their business.

For the small and traditional retailers to compete with large retailers and to stay in the business, they need to change their business model and should embrace technology. They need to leverage the increasing trend of people opting for credit card payments and ensure safe cashless transactions. To conclude , whether the entry of FDI in retail in India lead to overall economic development remains to be seen.

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