



## INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE, IT AND MANAGEMENT

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- Chandel K.S. (2009): "Ethics in Commerce Education." Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19-22 June.

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**FDI IN THE INDIAN RETAIL SECTOR- PROBLEMS AND PROSPECTS****BULBUL SINGH****ASST. PROFESSOR****SRI AUROBINDO COLLEGE OF COMMERCE AND MANAGEMENT****LUDHIANA****SUVIDHA KAMRA****ASST. PROFESSOR****SRI AUROBINDO COLLEGE OF COMMERCE AND MANAGEMENT****LUDHIANA****ABSTRACT**

*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, identified India as one of the most attractive retail destinations globally from among thirty emergent markets in 2010. The government has allowed FDI in the single brand segment upto 51% and has also allowed 100% FDI in the wholesale segment. However, as of now, FDI in the multi brand segment wherein foreign giant retailers like Wal-Mart operate are not allowed to enter India. This is because the government wanted to ensure that the entry of global retail giants does not displace the existing population of millions of people employed in the local retail business. The retail sector in India is largely dominated by the unorganized players (mom and pop stores/ kirana or neighbourhood stores with 100- 500 square feet floor area). Organised sector forms just 5% of the market. The retail sector in India is under- invested and according to a study by McKinsey, almost Rs 50,000 crores worth of food is wasted because of poor supply chain management. These drawbacks can be removed if the modern foreign retailers are allowed to enter the Indian markets as they shall bring their technical know how and help in cutting prices by removing intermediaries from the supply chain. The paper discusses the problems and benefits of allowing FDI in the Indian retail sector and recommends how it may be gradually introduced when inevitably it must.*

**KEYWORDS**

FDI, Retail, Organised Retail, Wal-Mart

**INTRODUCTION**

Retailing is the interface between the producer and the individual consumer buying for personal consumption. This excludes direct interface between the manufacturer and institutional buyers such as the government and other bulk customers. A retailer is one who stocks the producer's goods and is involved in the act of selling it to the individual consumer, at a margin of profit. As such, retailing is the last link that connects the individual consumer with the manufacturing and distribution chain.

Retailing is the largest private sector industry in the world economy with the global industry size exceeding \$6.6 trillion and a latest survey has projected India as one of the top destination for retail investors. The government had opened up 51% FDI in the single brand retail outlets which led to an upsurge in retailing business in India. The government is cautiously exploring the avenues for opening FDI in multi-brand segment. The Government is seeking these options keeping in view the existing social framework of India and wants to ensure that the entry of global retail giants do not displace the existing employment in the retail business.

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, identified India as the 'third most attractive retail destination' globally from among thirty emergent markets in 2010. India has consistently featured in the top three positions of the Global Retail Development Index conducted by AT Kearney for the last five years. It has made India the cause of a good deal of excitement and the cynosure of many foreign eyes. With the market worth \$410 billion, the retail industry is definitely one of the pillars of the Indian economy.

**OBJECTIVES OF THE STUDY**

1. To study the factors that make India an attractive destination for retailers
2. To analyze benefits and problems of allowing FDI in India in the multi brand segment
3. To make recommendations on how and under what conditions can FDI be allowed in the Indian Retail Sector so as to reduce the risk of lifting restrictions on the multi brand segment

**METHODOLOGY**

The study involved extensive collating, summarizing and synthesizing of secondary data available online by AT Kearney (Global Management Consultants), reports prepared by the Indian Council for Research on International Economic Relations (ICRIER), reports prepared by Centre for Policy Alternatives. All of these reports formed informative studies on some of the key issues with FDI in Retail. To obtain up to date information and opinions on the research topic it was necessary to refer to domestic and international news articles and gather a variety of industry reports and papers, for example reports by Price Waterhouse & Coopers, McKinsey, India Knowledge at Wharton, articles published in the International Retail Digest and several newspaper reports. All of these helped to provide a wide and balanced understanding of the key issues of this research.

**PROBLEMS OF THE STUDY**

We noted that data available, particularly in relation to India's retail sector, was often inconsistent. However, for the purposes of this research being more of an exploratory nature, this did not have too much impact on the findings. Up-to-date data was also hard to source. Also, the nature of the research being internet/online based, it was inevitable that it lacked primary data/ findings.

**RETAILING IN INDIA**

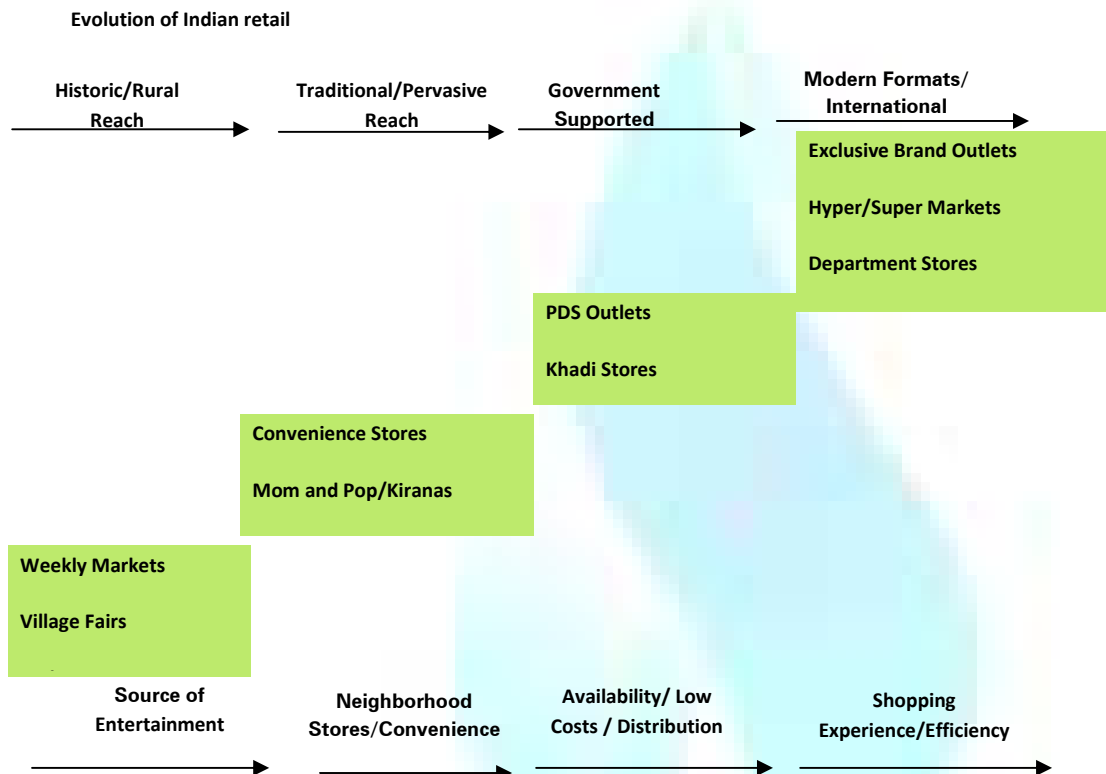
Trade or retailing is the single largest component of the services sector in terms of contribution to GDP. Its massive share of 10-11% is double the figure of the next largest broad economic activity in the services sector. Retailing is the largest private sector in India and second to agriculture in employment. After farming, retailing is India's major occupation (8% of total population). It employs 40 million people.

The retail industry is divided into organized and unorganized sectors. **Organized retailing** refers to trading activities undertaken by licensed retailers, that is, those who are registered for sales tax, income tax, etc. These include the corporate-backed hypermarkets and retail chains, and also the privately owned large retail businesses. Modern format retailers which include Supermarkets like Foodworld, Hypermarkets like Big Bazaar, HyperCity; Departmental Stores like,



Shoppers Stop, Lifestyle, Pantaloons, Piramyds, Westside and Trent, Specialty chains like Ikea the retail furnishing house and entertainment chains like Fun Republic, Fame Adlabs, Inox and PVR. Some of the biggest Indian corporate houses like the Future Group, Raheja Group, Reliance, TATA's, Aditya Birla Group, Bharti etc. have made massive investments in India's organized retail business. **Unorganized retailing**, on the other hand, 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. Unorganized retailing is by far the prevalent form of trade in India – constituting 95% of total trade, while organized trade accounts only for the remaining 5%.

Organized retail trade employs roughly 0.5 million people and unorganized 39.5 million. The Indian retail industry is highly fragmented. According to AC Nielsen and KSA Technopak, India has the highest shop density in the world. In 2001, it was estimated that there were 11 outlets for every 1000 people. India today has approximately 15 million retail outlets. The entire retail trade contributes about 10-11% to India's GDP and is valued at an estimated Rs. 9,30,000 crores. Out of this, organized retailing industry is around Rs. 35,000 crores. Organized retailing is primarily urban centric, its share as represented in urban scenario is projected to be 12 to 20%. Growing at more than 30%, the organized sector is driving the retail growth in India and contributes significantly to the growth of the economy. This economic growth comes primarily from increased consumer spending.



#### THE CHANGING INDIAN CONSUMER

There has been an increase in the disposable income of the middle class households in India. Between 1993 and 2003 there was a 20.9% growth in the real disposable income of the Indians. Besides, that, there has been a 10% growth in the middle and high income populations in the last decade. Add to that, the falling interest rates, easier consumer credit and a greater variety and quality of goods available at all price points has increased the momentum of consumerism in India. Consumers in particular, the urban consumers are getting exposed to international lifestyles. They are inclined to own more assets and thus there is an increased tendency to spend. Therefore, contrary to the olden times, shopping is no longer need based. The greater education levels have increased the awareness levels of consumers and they are becoming more demanding and discerning. The age segments of 17- 21 year olds, (which number more than a 100 million in India) tend to spend freely and are highly influenced by international lifestyles.

As the contemporary retail sector in India is reflected in sprawling shopping centers, multiplex- malls and huge complexes offer shopping, entertainment and food all under one roof, the concept of shopping has altered in terms of format and consumer buying behavior, ushering in a revolution in shopping in India. This has also contributed to large scale investments in the real estate sector with major national and global players investing in developing the infrastructure and construction of the retailing business. The trends that are driving the growth of the retail sector in India are

- Low share of organized retailing
- Competitive real estate prices
- Increase in disposable income and customer aspirations
- Increase in expenditure for luxury items

Another credible factor in the prospects of the retail sector in India is the increase in the young working population. Hefty pay-packets, nuclear families in urban areas, along with increasing working-women population have also contributed to the growth of retailing in India. These key factors have been the growth drivers of the organized retail sector in India which now boast of retailing almost all the preferences of life - Apparel and Accessories, Appliances, Electronics, Cosmetics and Toiletries, Home and Office Products, Travel and Leisure and many more. With this the retail sector in India is witnessing a rejuvenation as traditional markets make way for new formats such as departmental stores, hypermarkets, supermarkets and specialty stores.

The retailing configuration in India is fast developing as shopping malls are increasingly becoming familiar in large cities. When it comes to development of retail space specially the malls, the Tier II cities are no longer behind in the race. If development plans till 2007 are studied it shows the projection of 220 shopping malls, with 139 malls in metros and the remaining 81 in the Tier II cities.

#### ANTICIPATED GROWTH RATES

As foreign investors exploring their potentials in the retail sector, are keen on developing malls in India, the size of organized retailing is expected to touch \$30 billion by 2010 or approximately 10 per cent of the total GDP. This has initiated market-entry announcement from some retailers and has signaled to international retailers about India's seriousness in promoting the sector. While international retailers like Wal-Mart have entered the wholesale cash-and-carry business in an equal (50: 50) joint venture with Sunil Bharti- promoted Bharti Enterprises for; Reliance, the largest Indian conglomerate has invested \$3.4 billion to become India's largest contemporary retailer. There are also reports of investments for 'Hypercity Retail' by K.Raheja Group to establish 55 hypermarkets by

2015. Bharti Enterprises is likely to spend \$5 billion by 2015 in their retailing business; they are expected to occupy 10 million sq. ft. of retailing space and employ about 60,000 people in their retailing venture. All these factors will contribute in taking Indian retail business to unexpected growth based on the consumer preference for shopping in congenial environs and also availability of quality real estate.

#### INDIA AS AN EMERGING DESTINATION FOR FDI

India today represents the most compelling investment opportunity for mass merchants and food retailers looking to expand overseas. According to AT Kearney's Annual Global Retail Development Index for 2010 – an annual study of retail investment attractiveness among 30 emerging markets – India is placed at third rank ahead of countries like Saudi Arabia, Brazil, Chile and Russia and just behind China and Kuwait (see table 1 and Figure 1).

TABLE 1: TOP 10 RETAIL INVESTMENT COUNTRIES

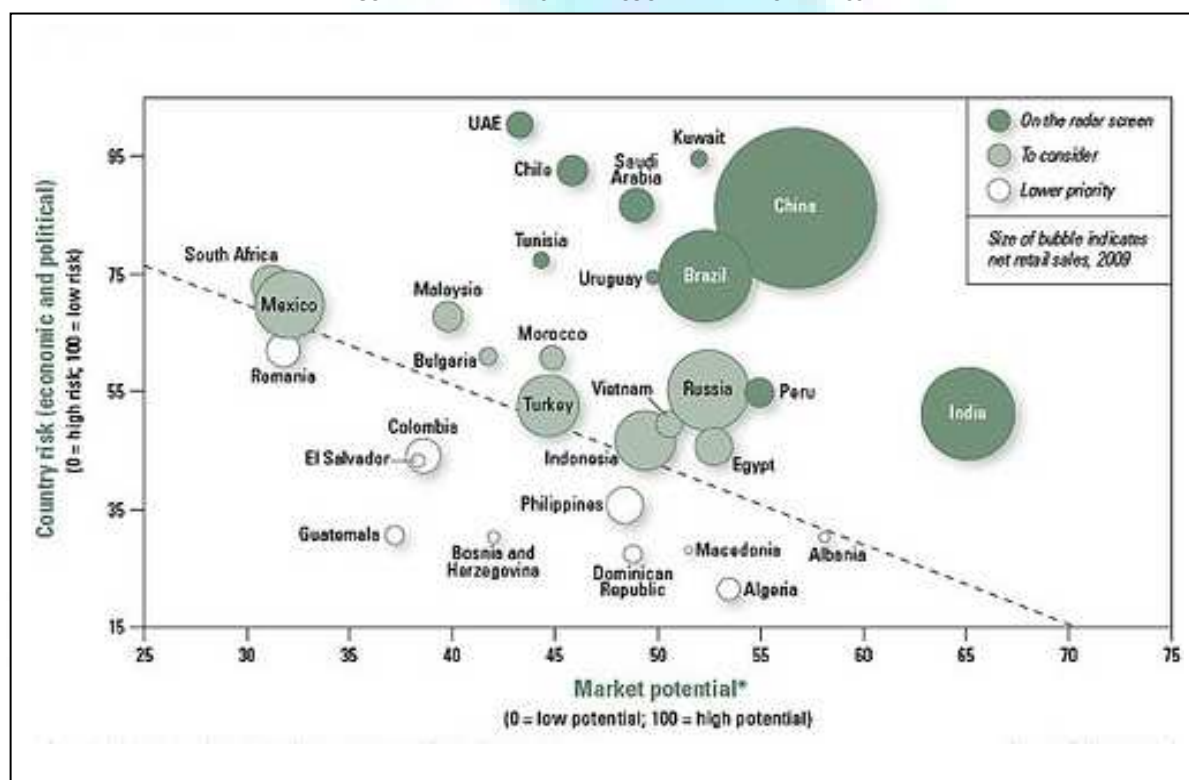
| 2010 Rank | Country      | Market Attractiveness (25%) | Country Risk (25%) | Market Saturation (25%) | Time Pressure (25%) | GRDI Score |
|-----------|--------------|-----------------------------|--------------------|-------------------------|---------------------|------------|
| 1         | China        | 50.6                        | 85.8               | 32.9                    | 86.6                | 64.0       |
| 2         | Kuwait       | 75.4                        | 94.3               | 56.2                    | 24.5                | 62.6       |
| 3         | India        | 35.4                        | 51.3               | 62.2                    | 97.8                | 61.7       |
| 4         | Saudi Arabia | 65.3                        | 86.5               | 50.7                    | 31.0                | 58.4       |
| 5         | Brazil       | 73.5                        | 74.3               | 46.6                    | 36.9                | 57.8       |
| 6         | Chile        | 71.8                        | 92.3               | 27.5                    | 38.3                | 57.5       |
| 7         | UAE          | 79.1                        | 100                | 18.8                    | 32.0                | 57.5       |
| 8         | Uruguay      | 67.7                        | 74.3               | 58.6                    | 23.1                | 55.9       |
| 9         | Peru         | 43.4                        | 54.6               | 72.2                    | 49.2                | 54.9       |
| 10        | Russia       | 63.5                        | 55.1               | 32.0                    | 61.8                | 53.1       |

Source: 2010 Global Retail Development Index 2010, AT Kearney Analysis

The Indian retail market is worth \$410 billion but only 5% sales are through organized retail, meaning opportunity in India remains immense. Retail should continue to grow rapidly – upto \$535 billion in 2013, with 10% coming from organized retail, reflecting a fast growing middle class demanding higher quality shopping environments and strong brands.

Store growths and consumer insights have been the focus for the past few years. The market is maturing as most retailers are now focusing on profitable growth (see figure 2). Several domestic retailers filed for bankruptcy or exited the market during downturn, like Subhiksha and Magnet, while others optimized their operations, including store labour, rent renegotiations and strategic cost management. Expansion plans did not slow however: Bharti Retail strengthened its position by 59 stores, Bharti- Walmart is expected to open 10 to 15 wholesale locations in the next three years, and Marks & Spenser is considering plans to open additional outlets in the next few years.

FIGURE 1: RETAIL INVESTMENT COUNTRY ATTRACTIVENESS



Source: 2010 GRDI, A T Kearney Analysis

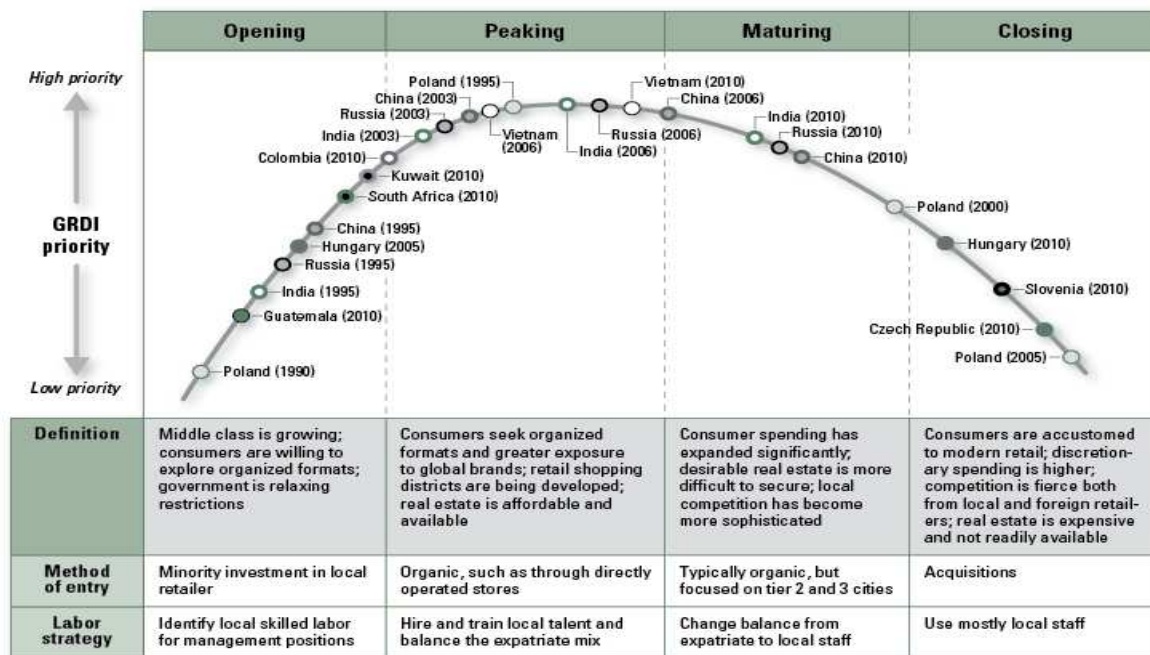
Established retailers are tapping into the growing retail market by introducing innovative store formats, such as community shopping, village malls and destination shopping stores for example, Future Group set up a first of its kind Community Family Shopping Centre in Bangalore. Another innovative concept, wedding malls devoted to nearly every aspect of weddings, are making a splash in the Indian market.

While rising commodity prices hit Indian consumers in all segments (including cereals, grains, fruit and vegetables), retailers launched a wide range of private labels. More profitable for retailers, these brands are gaining customer acceptance in categories beyond staples. Future Group plans to add 10 to 15 new private label categories every year; this year, it expanded its Tasty Treat label to the breakfast cereal, noodle and soup categories. Beyond private labels, Wal-Mart is working to change the agricultural supply chain model in India to improve productivity and the quality of goods by launching a direct farm produce sourcing system.



Foreign players continue to demonstrate strong interest in India- most major hypermarket retailers either have a presence or are studying the market for entry. In apparel, Zara (owned by Spain's Inditex Group) opened its first store in 2010, while Polo Ralph Lauren and Diesel are expanding. Desirable real estate is a lingering challenge for retailers. Mall rental rates are lower because of an oversupply of space, but there is still a lack of quality street locations. Given these challenges, many retailers see tier 2 cities as the next frontier. Customers in these locations are proving similar to those in tier 1 cities, meaning that retail models translate well- even increasing profitability because of lower operating costs. Spencer's Retail, More (owned by Aditya Birla Group) and Shoppers Stop (owned by K Raheja Group) already plan to expand. Regulations pose another challenge to retail growth in India, particularly the foreign investment restrictions for multi brand retail, which will probably not change anytime soon. As a result, cash-and -carry formats will thrive, as foreign companies are allowed full ownership. Wal-Mart and Metro have already successfully entered through this route, and Carrefour and Tesco plan to follow.

FIGURE 2: THE RETAIL INVESTMENT OPPORTUNITY ANALYSIS



Source: A.T. Kearney analysis

### FDI IN INDIAN RETAILING

FDI rules in India do not permit foreigners to set up retail stores directly as this threatens small store owners. 100% FDI is however, permitted in the cash and carry (wholesale or B2B format) business. Cash and carry is a form of trade that allows sale to offices, hotels and retailers who become its members. The government has opened up 51% FDI in single brand segment but does not allow foreign entry in the multi- brand segment. There are certain other exceptions also, where foreign players are allowed. These are:

1. Private labels
2. High- Tech items/ items requiring specialized after sales service
3. Medical and Diagnostic Items
4. Items sourced from the Indian small sector and manufactured with technology provided by the foreign collaborator.

### STRATEGIES ADOPTED BY INTERNATIONAL PLAYERS TO ENTER INDIAN MARKETS CURRENTLY:

**Franchise:** here an international company gives name and technology to local partner and in return gets a royalty. Examples of international retailers operating through franchises in India are- Nike, Pizza Hut, Tommy Hilfiger, Marks & Spencer and Mango.

**Manufacturing-** Here a foreign company sets up an Indian arm for production and also has permission to set up retail outlets for sale. For example, Bata India.

**Distribution-** in such cases an international company sets up local distribution offices and supply products to Indian Retailers for sale. These international companies can also set up franchise for exclusive brand outlet. For example, Swarovski and Hugo Boss.

**Wholesale trading-**these are cash and carry outlets and at present 100% FDI is permitted in wholesale trading. Metro of Germany is an example of such a company.

### WHAT INDIA MEANS TO THE WORLD'S TOP 10 RETAILERS

| COMPANY. COUNTRY OF ORIGIN | RETAIL SALES - 2003 (\$ BILLION) | INTEREST IN INDIA   |
|----------------------------|----------------------------------|---|
| Wal-Mart, USA              | 256.33                           | Very Keen to enter India; has already entered in B2B format a 50-50 JV with Bharti Enterprises  |
| Carrefour, France          | 79.80                            | A prominent global retailer in the world; among the first to enter China; has entered even small countries like Oman. Should be interested in India |
| Home Depot, USA            | 64.82                            | Has not ventured beyond the American continents yet; may not find immediate traction here   |
| Metro, Germany             | 60.50                            | Cash and Carry format is already present in India; likely to roll out other formats if FDI is allowed   |
| Kroger, USA                | 53.75                            | Present only in USA; India may not be on its radar  |
| Tesco, UK                  | 51.54                            | Quite keen in India; is in touch with the Govt.   |
| Target, USA                | 46.78                            | Present only in USA; India may not be on its radar  |
| Ahold, Netherlands         | 44.58                            | Has some experience in Thailand; India may not be top priority  |
| Costco, USA                | 41.69                            | Is in touch with the Govt.; very keen to enter  |
| Aldi Einkauf, Germany      | 40.06                            | No Asian presence so far; India may not be Priority   |

**PROBLEMS OF ALLOWING FDI IN RETAIL IN INDIA IN THE MULTI BRAND SEGMENT****(1) ADVERSE IMPACT ON THE EMPLOYMENT**

In the absence of any substantial improvement in the employment generating capacity of the manufacturing industries in our country, entry of foreign capital in the retail sector is likely to play havoc with the livelihood of millions. Let alone the average Indian retailer in the unorganized sector, no Indian retailer in the organized sector will be able to meet the onslaught from a firm such as Wal-Mart when it comes in full swing. With its incredibly deep pockets Wal-Mart will be able to sustain losses for many years till its immediate competition is wiped out. This is a normal predatory strategy used by large players to drive out small and dispersed competition. This entails job losses by the millions.

A back-of-the-envelope calculation can substantiate the point. If we take the case of India, it has 35 towns each with a population over 1 million. If Wal-Mart were to open an average Wal-Mart store in each of these cities and they reached the average Wal-Mart performance per store—we are looking at a turnover of over Rs 80330mn with only 10195 employees. Extrapolating this with average trend in India, it would mean displacing about 432000 persons and if we suppose that the large FDI driven retailers take up 20% of the retail trade in India, it would mean a turnover of Rs 800 billion and displacement of eight million persons employed in the unorganized retail sector.

**(2) THREAT ON ORGANIZED RETAIL PLAYERS**

Entry of global players would increase internal rivalry among the players than promoting business of overall industry. Their economies of scale will allow them to reduce their margin to provide value for money products in the beginning to grab the market share which is not possible for domestic players to reduce in comparison to global players because of huge investment. Majority of the Indian players have not attained even break even point as organized retail is still at the nascent stage in India.

**(3) HUGE SPREAD OF RETAIL CHAIN STORES**

Financially strong giants will spread their function at multiple location to cater to maximum markets with full fledged infrastructure which is not possible for domestic player to cater.

**(4) PREDATORY PRACTICES OF THE MULTINATIONAL RETAIL CHAINS**

FDI in retail is often supported on the basis of the need to develop modern supply chains in India, in terms of the development of storage and warehousing, transportation, logistic and support services, especially in order to meet the requirements of agriculture and food processing industries. While the infrastructure and technology needs are undeniable, the belief that the entry of multinational food retailers is the only way to build such infrastructure is unfounded. Moreover, the pitfalls of relying upon an agrarian development strategy driven by food retail chains and giant agribusinesses have already become clear through the experience of several developing countries like Malaysia, Thailand and Vietnam. Farmers experience many problems in supplying their produce to the food retailers and many get eliminated under the "preferred supplier" system. Farmers also face problems related to depressed prices due to cutthroat competition among the food retailers, delayed payments and lack of credit and insurance. The emergence of such problems in India, especially in the context of the deep crisis that has engulfed the agrarian economy is totally avoidable.

It is often argued that the Indian farmers and manufacturers are going to enjoy access to international markets by supplying commodities to these multinational retailers. However, the experience of the producers, especially those producing primary commodities in the developing world, is not encouraging in this regard. According to a source, while a cocoa farmer in Ghana gets only about 3.9% of the price of a typical milk chocolate bar, the retail margin would be around 34.1%. Similarly, 54% of the final price of a pair of jeans goes to the retailers while the manufacturing worker gets around 12%. The International market access available to the global retailers do not benefit the producers from the developing countries since they are unable to secure a fair price for their produce in the face of enormous monopsony power wielded by these multinational giants.

**(5) MONOPOLY IN THE CUSTOMER MARKET AND CREATION OF CARTELS BY THE GLOBAL PLAYERS**

Foreign players may create monopoly by providing products at discounted rates in the beginning to grab the market share by displacing domestic giants and after getting good market or monopoly in the market may create a cartel of global giants to exploit the customers by inducing price hike and customers would not get any option than to purchase at the available prices.

**(6) SETBACK TO THE TRADE BALANCE**

FDI in retailing can upset the import balance, as large international retailers may prefer to source majority of their products globally rather than investing in the local markets.

**(7) TOWERING EFFECT ON REAL ESTATE PRICES**

The entry of global players may have towering impact on the real estate prices. With intensified fight for space in cities, the race may result in steep rise in real estate prices which could be counter productive for the domestic players.

**(8) DISTORTION OF URBAN DEVELOPMENT AND CULTURE**

The promotion of large retail stores with huge retail space also fosters a different kind of urban development than what we have followed in India till date. Large shopping malls with all known retail chains with their showrooms as a part of urban development is familiar in the US where the consumers live in suburbs, drives long distances for his/her shopping and lives in a community that hardly knows each other. The problem with this model is that it neglects the simple Indian reality where most households do not have cars and need local markets. The myth of a huge and fast growing affluent middle class is counter to the reality that this section is still too small to support the remodeling of the urban landscape as is being planned with malls, large retail chains and branded products.

**BENEFITS OF ALLOWING FDI IN RETAIL IN INDIA IN THE MULTI BRAND SEGMENT****(1) IT WILL IMPROVE COMPETITION AND BRING PRICES DOWN**

Retail trade in India is fragmented, unorganized, un-networked, inefficient and individually small. An all too visible manifestation of the inefficiencies is the huge disparity between the price which the producer gets and the price which the consumer pays— sometimes as high as 10-20 times! Clearly, what is needed is an efficient supply chain backed by improved infrastructure, cold storages, packing and transportation. The traditional system of distribution, ending with the mom and pop or the street-side vegetable seller, is just not capable of creating it.

**(2) INVESTING IN TECHNOLOGY AND BETTER SUPPLY CHAIN MANAGEMENT**

The cold storage chains set up by international retailers will solve the perennial problem of wastages. As much as 40 % of India's fruits and vegetables rot due to lack of processing facilities. The foreign retail giant houses like Wal-Mart and Carrefour can bring better managerial practices and IT- friendly techniques to cut wastages and set up integrated supply chains to gradually replace the present disorganized and fragmented retail market. According to McKinsey, India wastes nearly Rs. 50,000 crore in the food chain itself. With IT application, the modern retail store can cut transaction costs such as due to inventory, delivery and handling. That is precisely how the US based Wal-Mart grew to be a giant because it reduced its distribution costs to 3% of sales compared to 4.5% of others. These international retail outlets can help develop the food processing industry which requires \$28 billion of modern technology and infrastructure. Also a more advanced and efficient production and distribution cycle shall evolve. An improved distribution system and better supply chain management shall make an improvement in the product basket from India for exports.

**(3) CONTROLLING INFLATION**

Industry trends for retail sector indicate that organized retailing has major impact in controlling inflation because large organized retailers are able to buy directly from producers at most competitive prices.

**(4) INCREASE IN EXPORTS**

There are likely to be greater levels of exports due to increased sourcing by major players. Sourcing by Wal-Mart from China improved multifold after FDI was permitted in China.

**HOW MUCH FOREIGN RETAILERS EXPORTED OUT OF CHINA**

- Wal-Mart: \$15 billion - \$18 billion
- Metro: \$2.4 billion
- Carrefour: Over \$2 billion
- Total sourcing of global retailers from China: approx \$60 billion

Wal-Mart sourced products worth \$600 million from India in 2006, its fifth year of sourcing operations. In 2010, Wal-Mart sourced goods worth \$125 million from Punjab alone comprising mainly of cotton. Wal-Mart officials are hoping that if world's top 10 retailers start buying from India, exports could go up by tens of millions of dollars.

Foreign players can generate positive inflow of cash through export of trade items or cutting down expenses of trade can increase the margin of profit. After 1994, there was a sudden influx of foreign investment in China which helped the country to attain a surplus in its balance of trade. Similarly, India can also benefit from foreign investment.

#### (5) MANPOWER AND SKILL DEVELOPMENT

By allowing market-savvy, market-intelligent and best management practices of corporations such as Wal-Mart, Carrefour, Ahold, JC Penny, etc to enter India the know-how and professionalism of Indian employees shall increase. Also there shall be a greater managerial talent inflow from other countries which add to transfer of knowledge and technical know-how.

#### (6) BETTER ENFORCEMENT OF TAX LAWS

While there will be increased tax revenue on the one hand, on the other hand there will be better enforcement of tax laws on the organized sector and international players. Tax evasion by players of the organized sector will not be possible like those of the unorganized sector. Thus, the exchequer of the Govt. shall increase.

#### (7) INCREASE IN EMPLOYMENT LEVELS

Employment shall be generated at various levels and across the entire value chain. Retailing industry doesn't need very high level skill sets. Graduates and school pass outs shall be suitable for the jobs and this is a major unemployed demographic group. It is projected that job generation will be similar to that of the ITES industry. More employment generation shall lead to an increase in the tax paying population.

#### (8) BETTER LIFESTYLE

Greater levels of wages are paid by most international players. The increasing purchasing capacity of consumers shall lead to better lifestyle. International retailers shall offer a better product variety with many new product categories emerging. Also the quality of products shall improve. The newer supermarkets in urban/metropolitan India offer a produce which is cleaner, fresher, well-packed and often cheaper than the vegetable seller on the street.

Modern retailing is designed not only to provide consumers with a wide variety of products under one roof, but also of assured home delivery and information feedback between consumers and producers. A modern retail outlet will also make it easy to buy on credit and provide for servicing and repair of products sold.

#### (9) TOURISM DEVELOPMENT

The Singapore and Dubai shopping festivals were examples of the possibilities for improving tourism thanks to the retail industry.

#### (10) OVERALL GROWTH AND EXPANSION

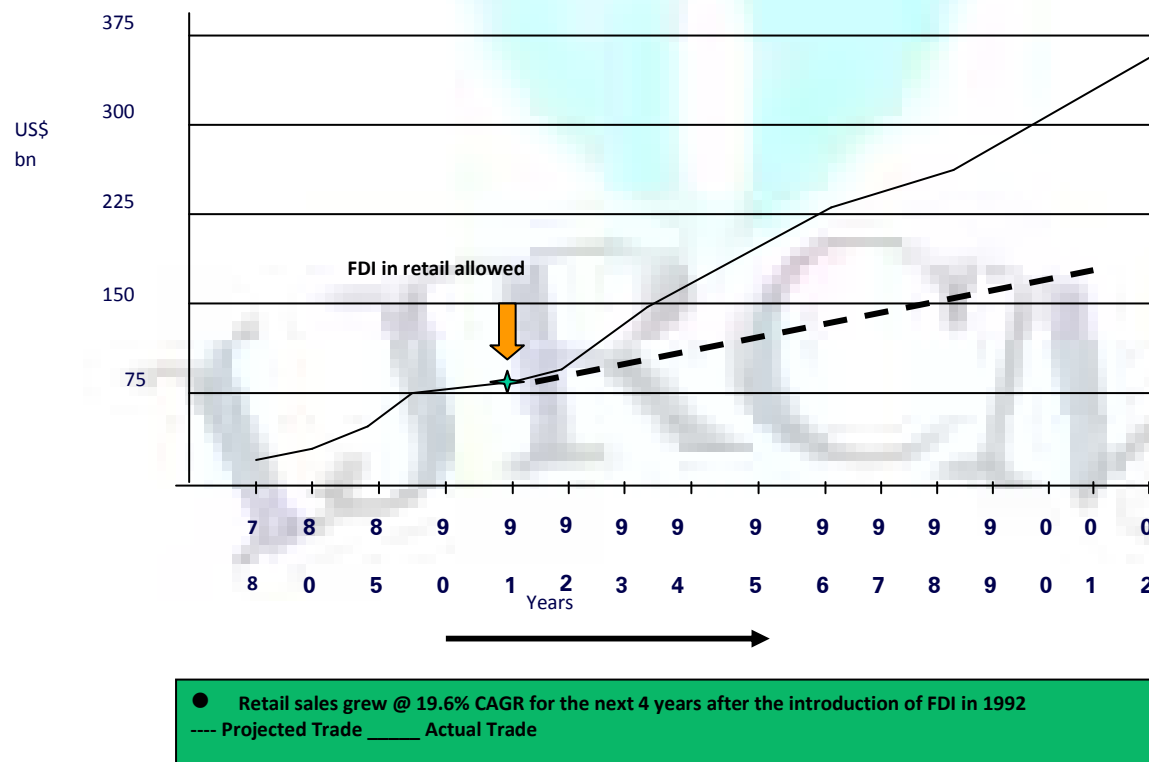
FDI would result in market growth and expansion. A greater consumer spending shall lead to greater GDP growth.

#### A CASE STUDY OF WAL-MART'S EXPERIENCE IN FOUR OTHER COUNTRIES

##### HOW CHINA BEAT THE FEARS

- Since China allowed foreign investment in retail in 1992, it has progressively increased the FDI cap from 26% in 1991-92 to 49% in 2002
- It allowed 100% foreign equity only in 2004
- Initially, China had allowed entry in only a few selected cities
- It actively encouraged domestic retailers to merge and become large enough to balance the global retailers.
- Percentage of Workforce employed in Retail: 6%
- No. of workers employed by top 100 retailers: 8,10,000

Figure 3: Total wholesale and retail trade



#### RESULTS IN CHINA

##### FOREIGN RETAILERS PRESENT IN CHINA

Four out of top 10 global retailers, 35 out of top 50 and 78 out of 250 are already operating in China.

The Combined Market Share of top 17 foreign retailers in China is as follows:

\$13.8 billion out of China's retail sales of \$628 billion or a mere 2.2%

China not only beat the fears but was successful in increasing the overall size of the business (See Figure 3).

HOW MUCH FOREIGN RETAILERS EXPORTED OUT OF CHINA

Wal-Mart: \$15 billion - \$18 billion

Metro: \$2.4 billion

Total sourcing of global retailers from China: approx \$60 billion

#### LESSONS LEARNT FROM THE CHINESE CASE

- There is strong evidence in favor of FDI
- FDI has improved the entire size of the industry
- Retailing in China has grown at a compound rate of 15% per annum after FDI inflow
- There has been an employment growth
- There has been evolution of modern formats
- Most importantly, local players can survive and even beat foreign competition

| Type         | No. of stores in 1996 | No. of stores in 2001 |
|--------------|-----------------------|-----------------------|
| Traditional  | 1,920,604             | 2,565,028             |
| Supermarkets | 13,079                | 152,194               |
| Convenience  |                       | 18,091                |
| Hypermarkets |                       | 593                   |

- Modern formats have grown after FDI
- But so have traditional players

#### WAL-MART IN JAPAN

Wal-Mart had acquired a majority stake in Japanese retail chain Seiyu and by early 2005 opened several big size outlets in busy streets of Japan. The global stores offered a wide variety of Japanese products. However, the initial poor decisions made by Wal-Mart put them in bad taste among Japanese consumers. The global retailer fired 25 percent of the staff, which included 1500 employees and managers of Seiyu. As mass firings are not common occurrences in Japan, the country as a whole felt offended. As a result, Wal-Mart received negative press publicity causing the retailer to lose customers. The unique proposition of Wal-Mart is to sell products at "everyday low price". This strategy helped Wal-Mart to achieve success in under-related markets such as Mexico and China. However, Japanese consumers equate low prices with inferior goods. They are willing to pay high prices for quality goods. Hence, failure to understand consumer behavior severely impacted sales. Industry observers in Japan believe that social harmony and a distaste of foreign control are heavily ingrained in the social and business environment of the country. Hence, American companies would always be far from ever achieving success in Japan.

#### WAL-MART IN SOUTH KOREA

Wal-Mart ventured in South Korea in August 1998. Wal-Mart had relied on its proven business model and its strategy in offering low prices for products. However, "everyday low prices" alone were insufficient to make Wal-Mart successful in South Korea. Similar to the United States, most Wal-Mart outlets in South Korea were placed outside city limits. South Koreans are used to easily accessible shopping facilities without the need to travel much. Some individuals felt that Wal-Mart should have been located in the central location of the cities where consumers felt more comfortable to shop. South Koreans are visually oriented customers, appreciating aesthetically pleasing displays and shopping environment. South Korean ladies did not like the warehouse like atmosphere of Wal-Mart, which the American consumers seem not to mind since the products are still cheap. They prefer the department store-like, neat, clean, and sophisticated atmosphere. Wal-Mart struck to Western marketing strategies that concentrated on dry goods, from electronics to clothing, while their local rivals' focused on food and beverages, the segment that attract South Koreans to hypermarkets. As a result, on May 22, 2006, Wal-Mart, added its name to a list of multinationals like Nokia, Nestle, and Google that had failed to adjust to the taste of South Korean Customers.

#### WAL-MART IN GERMANY

In 1997, Wal-Mart acquired Wertkauf, a leading German retail chain. Later it acquired another leading retail major, Interspar in 1998. Wal-Mart stores are designed for customers who are willing to spend lots of time in shopping. But in Germany, the shopping hours are limited: Shops close by 5 pm on weekdays and no shopping on Sundays. This implies that German customers are not in the habit of spending lots of time in a store- wandering around for the things that they need. The German customers do not like to be assisted by Wal-Mart's friendly store assistants for shopping. They prefer to do their own search for bargains. Wal-Mart got its merchandise placement wrong: Germans like to see the advertised discount products upfront- without having to ask the store assistant. This implies that the discount products must placed at the eye level. However, Wal-Mart followed its US style merchandise display strategy- where premium priced products are kept at eye level and the discount products are kept at higher shelf or in the bottom racks. This irritated the German shoppers. Wal-Mart also got its store inventory wrong. Products like clothes, hardware, electronics and other non- food products were given much bigger floor space than food products. Germans shop in big outlets mainly for food products. Hence, other German retailers like Metro stock more of food products which constitute more than 75% of their revenue. As a result of constituent mistakes, Wal-Mart suffered consistent losses to the tune of \$ 1 billion and exit Germany in 2006 by selling its 85 stores to Metro.

#### RECOMENDATIONS

India is poised to grow as a Retail hub. It is estimated that the market would grow to \$635 billion by 2015. It is imperative to sustain the modernization of the retail sector and cater to the growing taste of the Indian consumer and dispel the myth that the game is *big vs. small* or *traditional vs. modern* or *organized vs. unorganized* or *local vs. foreign*. What is needed is to promote consumption- which will ultimately lead to economic growth of the country. For the Indian consumer, the gradual and step wise entry of foreign companies in retail involves three pivotal changes- modern technology, better transparency in dealings and sharing best practices. To date, through the franchising route, foreign retailers have already entered India. Pizza Hut, Lacoste, Mango, Chanel, Louis Vuitton, Nike and Marks & Spenser have all entered via franchise agreements. The big multi-brand retailers have expressed keen desire to enter India and are looking forward the government's green signal. Metro of Germany, Shoprite Checkers of South Africa and Wal-Mart of US have already started to operate in the wholesale segment. Today, as far as multi-brand retailing is concerned, the question is not of whether "**Should India be open to FDI**" but "**when to open**" and "**how to open**" as under the WTO regime it is inevitable.

##### (1) WHEN AND TO WHAT EXTENT SHOULD FDI BE ALLOWED

The capital formation needed to develop retail trade in India will take at least 2 to 3 year's time. FDI should be opened up in a gradual phased manner, allowing a lead time for the Indian retailers to create a level playing field for all. FDI should be allowed in three stages which are as follows:

**First Stage** of 2-3 years wherein only 26% FDI is allowed

**Second Stage** of another 2 years wherein 49% FDI is allowed and

The **Third stage**, when markets are completely ready and developed 100% FDI may be allowed.

The government may additionally consider opening FDI first in relatively less sensitive sectors- like garments, lifestyle products, house ware, entertainment etc.

##### (2) CITY RESTRICTIONS



Another objective of FDI is to enhance infrastructure. While there is no dearth of potential investors in metro cities, the Tier-2 and lesser cities are getting sidelined. FDI should be initially allowed in Tier-2 and lower cities to facilitate infrastructure building. The more such investment, the more incentives may be granted to operate in Metro cities. Models similar to airline operators need to be explored. With this the focus would be on incremental business and create a level playing field for all and not on cut throat competition.

### (3) ZONING LAWS AND AREA RESERVATION FOR FOOD PRODUCTS

The government is already considering a host of conditions for bringing in FDI. One of them is to impose a minimum limit of 10,000 sq ft on the floor space of foreign retail chains and limit the number of stores to one per million once FDI in retail is allowed. These huge retail stores should be located outside the city area and thus be subjected to certain zoning restrictions. Giant shopping centers must not add to our existing urban snarl. This also serves to create level playing fields for all players. Also, inclusion of a clause for reserving at least 500-600 sq ft (out of 10,000 sq ft) of retail space for foods and processed foods alone will further help to protect the interests of certain sectors like agriculture and integrate them with the organized retail supply chain. These measures may be applicable for a short while only, and the Department of Industrial Policy (DIPP) may consider easing some of these restrictions with time.

### (4) CONDITIONS ON SOURCING

India should take lessons from the Thailand story. In Thailand and Malaysia, global retailers spelt doom for the traditional mom and pop stores. In fact, the Thai government had to step in to save local retailers from annihilation. It set up Allied Retail Trade, a network of franchised stores, which brought small stores together to fight the big chains. One solution to this problem is to put a restriction on sourcing of products locally. Thus foreign companies must be encouraged to form linkages with local producers and packages. For example, tie ups with Companies such as Amul, Vita, Verka for dairy may be made.

### (5) SET UP AN AGRICULTURAL PERISHABLE PRODUCE COMMISSION (APPC)

The government should set up Agricultural Perishable Produce Commission to ensure that procurement prices for perishable commodities are fair to farmers and that they are not distorted with relation to market prices.

### (6) FORMATS

Stores like Wal-Mart which is one the world's most successful retail organizations operates through many business formats- large departmental stores, all-under-one-roof 'super centers' and members-only 'cash and carry' stores that cater to small business and bulk consumers. Being an efficient retailer, it offers quality merchandise across all product categories at low prices. Its logistics, IT and sourcing efficiency are one of the best in the world. And the chain's efficient business operations depend on it. The government may initially allow only supermarkets to be set up so that retailers cannot immediately indulge in 'predatory pricing'.

### (7) IMPROVE MANUFACTURING SECTOR

In order to address the dislocation issue, it becomes imperative to develop and improve the manufacturing sector in India. There has been a substantial fall in employment by the manufacturing sector, to the extent of 4.06 lakhs over the period 1998 to 2001, while its contribution to the GDP has grown at an average rate of only 3.7%. If this sector is given due attention and allowed to take wings, then it could be a source of great compensation to the displaced workforce from the retail industry

## CONCLUSION

Given the WTO regime India is a party to, the entry of FDI in the retail sector is inevitable. Bit with the instruments of public policy in its hands, the government can create conditions that slow down their entry. Japan has done this quite effectively. In this fashion, the Government can try to ensure that the domestic and foreign players are approximately on an equal footing and that the domestic traders are not at an especial disadvantage. While it is true that some dislocation of traditional retailers will be felt, the government must ensure that retail does not remain concentrated in a few foreign hands.

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