IMPACT OF FOREIGN DIRECT INVESTMENT IN INDIAN RETAIL SECTOR

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ABSTRACT

The Retail Industry is the sector of economy which is consisted of individuals, stores, commercial complexes, agencies, companies, and organizations, etc., involved in the business of selling or merchandizing diverse finished products or goods to the end-user consumers directly and indirectly. Goods and products of the retail industry or sector are the finished final objects/products of all sectors of commerce and economy of a country. The International Monetary Fund defines FDI as when one individual or business owns 10 percent or more of a foreign company capital. Every financial transaction afterwards is considered by the IMF as an additional direct investment. If an investor owns less than 10 percent, it is considered as nothing more than an addition to his/her stock portfolio. This paper describes the overall impact of FDI in the Indian Retail sector.

Keywords: *Foreign Direct Investment, Retailing, Wall Mart, Globalization, Indian Economy*

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INTRODUCTION

Retailing in India is one of the pillars of its economy and accounts for 14 to 15 percent of its GDP. The Indian retail market is estimated to be US$ 450 billion and one of the top five retail markets in the world by economic value. India is one of the fastest growing retail markets in the world, with 1.2 billion people. India's retailing industry is essentially owner manned small shops. In 2010, larger format convenience stores and supermarkets accounted for about 4 percent of the industry, and these were present only in large urban centers. India's retail and logistics industry employs about 40 million Indians (3.3 percent of Indian population). Until 2011, Indian central government denied foreign direct investment (FDI) in multi-brand retail, forbidding foreign groups from any ownership in supermarkets, convenience stores or any retail outlets. Even single-brand retail was limited to 51percent ownership and a bureaucratic process.

In November 2011, India's central government announced retail reforms for both multi-brand stores and single-brand stores. These market reforms paved the way for retail innovation and competition with multi-brand retailers such as Walmart, Carrefour and Tesco, as well single brand majors such as IKEA, Nike, and Apple. The announcement sparked intense activism, both in opposition and in support of the reforms. In December 2011, under pressure from the opposition, Indian government placed the retail reforms on hold till it reaches a consensus.

In January 2012, India approved reforms for single-brand stores welcoming anyone in the world to innovate in Indian retail market with 100% ownership, but imposed the requirement that the single brand retailer source 30 percent of its goods from India. Indian government continues the hold on retail reforms for multi-brand stores. In June 2012, IKEA announced it has applied for permission to invest $1.9 billion in India and set up 25 retail stores. Fitch believes that the 30 percent requirement is likely to significantly delay if not prevent most single brand majors from Europe, USA and Japan from opening stores and creating associated jobs in India.

On 14 September 2012, the government of India announced the opening of FDI in multi brand retail, subject to approvals by individual states. This decision has been welcomed by economists and the markets, however has caused protests and an upheaval in India's central government's political coalition structure. On 20 September 2012, the Government of India formally notified the FDI reforms for single and multi brand retail, thereby making it effective under Indian law.

RELATED LITERATURE

Nandi Kumar Taney and Saher Ritankar (2007) in their work made an attempt to study the Foreign Direct Investment in India with a special focus on the retail trade. This paper uses the augment that FDI is allowed in multiple sectors and the effects have been quite good without harming the domestic economy.

Gupta Rupali (2012) conclude that there will be initial and desirable displacement of middleman involved in the supply chain of farm produce, but they are likely to be absorbed by increase in the food processing sector induced by organized retailing.

RESEARCH METHODOLOGY

The study is based on secondary sources of data. The main source of data is various economic survey of India, various journals, websites or newspaper etc.

DISCUSSION ON TOPIC

The opening of retail industry to global competition is expected to spur a retail rush to India. It has the potential to transform not only the retailing landscape but also the nation's ailing infrastructure. A Wall Street Journal article claims that fresh investments in Indian organized retail will generate 10 million new jobs between 2012–2014, and about five to six million of them in logistics alone; even though the retail market is being opened to just 53 cities out of about 8000 towns and cities in India.

The direct FDI impact in the short term from retail chains will be modest. Large retail chains when they venture abroad do so in three phases. In Phase One, they often set up a test case/pilot project. This can be done through a partnership with local chains (with risk and revenue sharing), or a few flagship stores that serve as brand broadcasters. The chains employ this initial-phase entry strategy to learn lessons about the local markets. They assess demand, test merchandizing strategies and set up operational capabilities. In this phase, they bring in some investment to cover their set-up costs and for establishing their sourcing (supply) footprint. This usually takes 18-to-24 months.

In the second phase, firms expand their demand footprint; they open more stores and increase both the scale of operations (volume of products sourced) and scope of products that they feature. There is considerable investment in this phase in the form of real estate acquisition, putting in operational infrastructure, establishing sourcing relationships, establishing supply chains and massive logistics capabilities. This is volume-independent investment -- that is, investment meant to gear up for volumes of business to come, but not calibrated to the current volume of business.

In the third phase, the investment keeps pace with the rate of expansion. As volumes grow and urban and semi-urban retail locations get saturated, companies look for new locations and bring in investment that is calibrated to growth in volumes. It is in the second phase and the third phase -- which come after the initial 18-to-24 months -- that large investments manifest themselves.

FDI is often opposed on the grounds that it will put mom-and-pop stores out of business. This is very unlikely for several reasons. The big-box retailers, when they venture into developing markets, do not use the same business model as they do in the U.S. Walmart -- the most iconic of these companies and the one most often cited as a threat to Indian mom-and-pop stores -- is by no means the lowest-price retailer in China. Walmart U.S. is based on "everyday low prices." The firm has an activity system that is meant to help Walmart compete as a cost leader. The company began by locating in rural areas and then moved to suburban and semi-urban areas in the U.S. In China, the rural areas and semi-urban areas are not where the money is. Consumers in China -- unlike their American counterparts living in suburbia - do not drive miles and do bulk purchasing, nor do they have massive storage facilities at home. In India, China, Brazil, Indonesia, Thailand and Mexico, the vast majority of educated middle and upper classes live in the cities (and not in semi-urban and rural areas) where real estate is very expensive and population density is high.

The foreign retail chains will need to make very expensive real estate investments. They will have a very high variable cost of operation. Their fixed, volume-independent costs are also likely to be much higher than the mom-and-pop convenience stores. These chains will operate with price points that are much higher than those featured by the mom-and-pop shops.

These firms' real competition will be the domestic multi-brand retailers. A recent study by the CII and Boston Consulting Group estimated the size of organized retail of US$28 billion in 2010 to be 6 percent to 7 percent of the total retail market in India. The study predicted that the size of retail – total retail sector size, not just organized retail – would grow to US$1.25 trillion by 2020 if the efficiencies that typically come from greater competition and modernization of retail supply systems were to be unleashed. Under this scenario, the study predicts that the size of organized retail could grow to US$260 billion or about 20.8 percent of the total market. So even under this scenario, the idea that a fractional segment that accounts for 20.8 percent of the total economic activity of a sector can drive the remaining 79 percent of that sector out of business does not stand the scrutiny of reason.

The foreign retail chains will have a more significant impact on traders that dominate procurement of commodities and perishables, including grains and cereals. It is not surprising that these traders are the most virulent opponents of FDI in retail (the main opposition party that derives its support from the trading castes and traders has openly stated that “traders’ interests will be harmed by FDI in retail”). Indian farmers and many other rural producers are at the mercy of large and well-organized monophony buyers. Very often these traders dominate geographies and account for nearly all procurement in their geographies. In many states, the food ministry determines who it will buy from and this is usually a small number of traders who in turn dominate direct procurement from farmers in their geographies. These are economic fiefdoms that they dominate and exploit. When the Carrefours, Walmarts and Tescos set up direct procurement mechanisms where sophisticated procurement systems are put in place and information about demand (prices, product varieties and quantities demanded) becomes more easily available, it becomes more difficult for the middlemen to dominate local geographies and restrict competition. The emergence of these supply chains that drive transparency of information will bring significantly more competition in sourcing.

CONCLUSION

At last we can say that the Retail sector of India is vast, and has huge potential for growth and development, as the majority of its constituents are un-organized. The retail sector of India handles about $250 billion every year, and is expected by veteran economists to reach to $660 billion by the year 2015. Small retailer are not appreciated about the big stores, they oppose allowing FDI in retailing in India. This may because they are not well informed about the advantages and disadvantages of the proposed policy change. Moreover, FDI in retailing should not be seen as just another policy decision because it has a direct impact on agricultural sector as well. Allowing FDI may not be as bad as some of us feel. But the policy must be well drafted for which a country wide perceptional study of the stakeholders of retailing is solicited.

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