

FDI in Retail

A Much Awaited Decision!

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FDI (Foreign Direct Investment) assumes a space of immense significance in a country's development and assists in establishing an open and effective international economic system. It is done as direct investment into production in a country by a company located in another country, either by buying a company in the targeted country or by

expanding operations of an existing business in that country. The Indian retail industry, though with huge growth potential (studies validating a contribution of 14% to the national GDP and employment of 7% of the total workforce) is estimated to be one of the five retail markets in the world by economic value but unfortunately it remains one of the least evolved

industries in India as compared to the rest of the world. Retail is the largest source of employment in India after agriculture. According to Indian Staffing Federation (ISF), an apex body of the flexi staffing industry in India, FDI in retail can create around 4 million direct jobs and almost 5 to 6 million indirect jobs including contractual employment within a span of 10 years.

The much debated decision of the Government to allow 51% FDI in multi brands (like Wal-Mart, Carrefour and Tesco) and 100% in single brands like IKEA, Nike, and Apple to encourage an organised retailing in the country was recently taken. It has also been specified that retailers (both single and multi brand) will have to source at least 30% of their goods from small and medium sized Indian suppliers. Multi-brand retailers must bring a minimum investment of US\$ 100 million. Retail chains will be allowed only in cities with a population of more than 10 lakh as per 2011 Census.

This decision has met with much varied views from the Indian Industry. For International retailers it is definitely a boost who are presently in India through their cash and carry model (selling to other retailers and business establishments), where 100% FDI is allowed.

Former Union Minister **Arun Shourie** while in a recently held global conference remarked, "FDI in retail will neither hurt people more nor benefit companies much. It is not of much use to either side (businessmen and consumers). It will also not affect

the small retailers. Big MNCs are not going to come here in large numbers as they know it is not easy for them to establish here in India."

The Upside

FDI is done for many reasons – to take advantage of cheaper wages in the country and special investment privileges such as tax exemptions offered by the country as an incentive to gain tariff-free access to the markets of the country or the region.

Union Minister **Kamal Nath** in defence of FDI in multi-brand retail feels that the agricultural sector would benefit from the move in a big way. He adds, "As many as 40% of vegetables are rotting as there is no backend. Multi-brand retail is a model that will work and the advantages outweigh the risks. Advantages of a backend and cold-chains being formed, sourcing, quality standardisation, etc is going to mainly help our agricultural sector". Stating that the real issue was not about the FDI but about the big versus the small, he adds, "We have allowed FDI only in cities with over 1 million population. I think only 21 cities in all the states will be able to avail of this."

A comprehensive survey by CII's (Confederation of Indian Industry) conducted during Dec 2011-Jan 2012 on the effect of FDI in retail on the SME sector shows an approval by the SME industry. Though the entry of MNC retailers has been acknowledged both as a threat and as an opportunity, the survey has validated that a majority feel that such a decision would bring about substantial growth of sales of their products, a growth in the size of their industry, a positive impact in the form of new orders and contracts generated, qualitative improvements and branding of products, improvements in the supply chain efficiencies in the sector and a positive impact on the employment.

By attracting foreign investments in the Indian market, the introduction of FDI in retail is looking at improving the back-end storage and procurement process, creation of infrastructure facilities following the establishment of multi chain retailers, the reduction of prices for consumers on account of elimination of the intermediate channels in the procurement process and bringing in of technical expertise in the country. Some experts are also of the view that this will strengthen India's inefficient food distribution system, which causes food wastage, leading to high food inflation.

It is envisaged that small farmers will be the biggest beneficiary of this decision since they will be able to improve their productivity and realise higher remuneration by selling their produce directly to large organised players, thus shortening the chain from farms to consumers. Farmers in Punjab have expressed that this will ensure sourcing of farm produce in bulk and better pricing and will encourage the much needed crop diversification in the state.

This decision also looks at inviting an increase in the demand





for commercial space in the market, which will evidently increase the demand of residential space which will help in boosting the real estate sector in the country, also leading to a rise in the demand of steel, cement and other building materials and construction equipment.

Points to Ponder!

FDI in retail has not been a sudden decision by the government, but an idea which has been toyed with, for over 14 years and has undergone various discussions with stakeholders, experts and has been the theme of many commissioned studies based on international experiences of organised retailing.

The Government has given the state governments the right to implement or reject the policy in their own respective states following which Governments in West Bengal, Gujarat, Tamil Nadu, Kerala, Bihar and Chhattisgarh have decided to not allow FDI in retail. A number of Bandhs in the country have also been held to oppose the same.

A grim situation has been witnessed where the opposition

parties have opposed the Union Government's decision. Accusations have also been cast that the measures taken by the government should not be called 'economic reforms' because these are mere administrative decisions being taken. It has been felt that the 'Government and some sections of the media are being unnecessarily upbeat about multibrand retail which would cater only to 5-10% of the population interested in branded products and in turn cause harm specially to agro based products.

Invariably, the main fear of this decision rampant is the disruption of the livelihood of the poor people engaged in this trade, the disruption of the 'unorganised retail sector' which is responsible for employing a large percentage of Indian population.

The decision to allow multi retailing could also give rise to an asymmetrical growth in the cities, thus generating a lot of social tension. The import balance can also be affected since international retailers would prefer to source majority of their products globally than wanting to invest in local products. Concern

has also been outpoured on the fact that due to higher lending rates in India, Indian retailers' especially small retailers are at a disadvantage compared to foreign retailers who have access to international funds at lower interest rates.

On the government's comment that foreign investors will build large storage warehouses which would lead to a drastic curbing of wastage of agriculture produce, there have been questions whether 'assuming that the foreign investors will come in and create cold storage facilities to sell agricultural products which make up 10% of the overall sector is correct?'

According to some, while foreign direct investment may bring down prices in the first few years, it will increase inflation, once foreign retailers gain a large share of the retail market. This is because large retailers do not remove middlemen but only replace small middlemen. The continued presence of middleman might hamper the retail prices from coming down by a large extent.

Looking Forward

Foreign Capital has been an important part in the Indian economy and hence its entry into multi-brand retailing has to be directed in a way which would be beneficial for the country. This could be achieved by incorporating certain rules and regulations for FDI in multi brand retailing. To take care of the rural stagnation, 50% of the jobs in the retail outlet can be reserved for rural youth and procuring a certain amount of farm produce from the poor farmers should be made mandatory. It might also be a good step to first strengthen the Indian retail sector before opening it to foreign retailers.

The huge gap between the real price paid by a consumer and the price at which the product is procured from the farmers is also set to be reducing



with this decision-the large retailers could save on commission cost by buying the food produce directly from the farmers. These claims of FDI helping the farmers is again being questioned since the process of obtaining raw materials from the farmers can be standardised only if organised retail becomes the largest part of retail which will take a while to happen in India. Right now it occupies only 2% of the retail sector.

However advantageous or disadvantageous this decision might be, it is true that its implementation is set to remain a challenge. Rating agency India Ratings feels that 'FDI in retail will help retailers de-leverage their balance sheets, but the complexities involved could delay the process, with benefits not expected to accrue in the next two to three years'. Consulting firm Pricewaterhouse Coopers (PwC) have said in a report that 'though FDI will help the Government bring down fiscal deficit from the current 6 per cent to 4 per cent, if implemented at the earliest, retailers will face challenges in re-organising their corporate structure at state-levels and create separate legal entities before attracting FDI investments'.

What is of supreme importance is also the interest of consumers at large in relation to the interest of the retailers. The Delhi Government has wanted to incorporate views of

traders, supermarkets and provision store owners on the decision so that these could be discussed at length at their Cabinet Meeting. Senior Congress Leaders are also trying to ensure that Delhi 'becomes the first to implement FDI in retail'.

The country still stands divided with the opposition parties not in favour of this decision but majority of the retail industry happy with it who feel that FDI in retail is the first critical step for the growth of the retail segment. Some experts feel that the Government needs to build infrastructure first since this decision would need large warehouses/storage facility which is again a challenge in India given the paucity of land. Also the sorry state of roads would make it even more challenging for goods to be transported in huge semi-trailers

either from the docks or from local sources. But what is also true is that India obviously needs a huge capital to build its infrastructure especially for the Indian economy that is small and has limited surplus capital.

We must remember that we live in an age of globalisation and allowing a healthy FDI in retail sector can help in integrating the Indian retail market with the global retail market. This decision will allow domestic retail firms to form joint ventures with foreign retailers as has already been conveyed by brands like Shoppers Stop and Foodworld. The need of the hour is to skilfully balance the opportunities and prospects attached to FDI and look forward to a steady economic development of the country.

Industry-Captains Speak

Mr Navin M Raheja, CMD, Raheja Developers Limited and President NAREDCO

"The Government's decision to allow 51% FDI in multi brand retail has cheered both retail and real estate sectors. From the real estate point of view, it will open up multiple opportunities in the medium and long term, as the demand for quality real estate would rise. Presently, some retailers are cash strapped and this will provide a sort of bail out option to them.



With flow of fresh investment into the retail sector, it will trigger investment in real estate, both at the front end and back end. In front end, retail store spaces will see investments and in the back end, better quality warehouses will be seen.

Vacancy in malls across the board ranges between 15-20%. Opening of FDI in multi brand retail would surely improve the uptake of present vacant retail spaces and vacancies should improve by at least 5 to 7 percent in the next 2 to 3 years. There should be



Mr Lalit Kumar Jain, National President of CREDAI

“The awaited policy of introduction of FDI into retail sector is a move in the

of employment. India needs bold decisions to help the nation progress with new vigour and enthusiasm and we are happy that the government has at last begun to move in the right direction.”



Mr Sachin Sandhir, Managing Director, RICS South Asia

“It has been a long standing demand of the real estate sector that in addition to pure development financing that was initiated in 2005, an evolution to ‘FDI in investment financing’ would truly help in providing for a vibrant investment environment in India. The recent move by the Government to open multi-brand retail to FDI is definitely welcome, considering it will go a long way in strengthening organized retail in the country.

For long now, the retail sector in India has been facing numerous on-going challenges with respect to processes, technology, supply chain, real estate etc., resulting in fewer investments in the sector as compared to others, which have seen growth occur at a much faster pace. While there are still some policy hurdles that need to be overcome in the implementation of this directive, FDI will definitely prove to be a powerful catalyst for the much required growth in the retail sector. This will have a positive spill over on real estate as well, as the demand for retail property will witness renewed demand and uptake along with improved investor confidence in the sector”.



an increase in demand for commercial real estate and increased investor confidence as presently there is a mismatch in lease rates and capital values.

All this would motivate developers to build quality shopping centres with a clear vision to long term profit. This decision has come at a time when business sentiments have taken a beating, GDP growth is near decade low and inflation remains high. It will help the economy as a whole to gain momentum, depth and size with great employment opportunities getting created.”

right direction as it will give a new fillip to the development of retail sector in the country. The government has also opened up doors for development of logistics and infrastructure like cold storage's in the rural areas which will help change the village economy positively. This is a praiseworthy move as it will help create jobs across the country and thus check large scale migration of people from rural areas to urban centres in search of employment and I am quite sure that all the right thinking people will wholeheartedly support the government initiative.

The overall policy will also contribute to the equitable distribution



Mr Irfan Razack, CMD, Prestige Group

I will like to definitely encourage FDI in retail, as this will only benefit both the consumer and the country at large, apart from the increase of capital inflows into India and creating thousands of job opportunities. This is also a good step from the India growth story perspective as this is likely to overhaul our entertainment and shopping experience altogether, while giving customers more choice.”



Anuj Bhandari, CREDAI, Pune Metro

The introduction of FDI into retail industry would bring about multifold improvements in the sector. The introduction of foreign systems of working in the functioning of the Indian markets will help the Indian markets to get to learn new and innovative methods of working that they can introduce here in India. Also due to FDI, a lot of employment will be generated. All of this will lead to enhancing the turnover of the retail industry. Other businesses associated with the retail sector, directly or indirectly, will also witness a boom. Talking specifically about the realty sector, this decision will bring about some liveliness in this zone. Constructions of commercial complexes will increase. Finally, goods will become cost effective which will be beneficial to all.”



Mr Kishore Pate, Hon. Jt. Secretary, CREDAI, Pune Metro

“The decision has been a positive move in building a strong economy of our country with which funds would be raised in huge amount which will be favourable for the economic growth. Some people believe that due to the introduction of the FDI, only malls and big shopping complexes will see a rise and small shop owners will get adversely affected in their business. But we must realize that the mall culture is limited to the cities and most of the small towns in our country are not really aware of it. They still have only the small shops at their service. Hence, the overall effect of FDI is definitely going to be good on our economy. As far as realty sector is concerned, the effect of this decision is definitely going to be optimistic. Construction of commercial complexes like malls, hotels, multiplexes will enhance and help the sector expand.”

