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Impact of Foreign Direct Investment on Retail Sector in India

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ABSTRACT

Foreign direct investment (FDI) plays an important role in India's growth dynamics. There are several examples of the benefits of FDI in India. FDI in the retail sector can expand markets by reducing transaction and transformation costs of business through adoption of advanced supply chain and benefit consumers and suppliers (farmers).

India being second most-populous country has immense scope for retail expansion as along with time urbanization and consumerism has also been increasing. Initially India was conservative regarding FDI; it imposed restriction on foreign companies to limit their share in equity capital of their Indian subsidiaries but over the time Government of India gradually liberalized foreign investment in various sectors. Recently in 2011 India permitted 100% FDI in single brand retail and in 2012, 51% FDI permitted in multi brand. In this paper we are analyzing the impact of such decision on various sectors like food retail sector, farmers, traditional & employment and food inflation. In this context the present work makes an attempt to study the likely impact of FDI on Indian retail sector whether good or bad, opportunities & challenges. It analyses the reasons why foreign retailers are interested in India and their prospects in India and also find out the suggestions for the future growth of the retail industry.

Keywords: *Foreign Direct Investment, Liberalization, Retail, Economic Growth, Opportunities & Challenges, Globalisation, Strategic Issues and Prospects.*

INTRODUCTION

FDI (Foreign Direct Investment) is a process which enables the residents of one country to directly invest their funds in another country and acquire ownership of assets and exercise control over the investment in terms of production, management, distribution, effective decision making, employment etc. ***"FDI is an international financial flow with the intension of controlling or participating in the management of an enterprise in a foreign country."***

Retail sector is one of the biggest supports of the Indian economy and accounts for 15 percent of its GDP. The Indian retail market is estimated to be US$ 450 billion and one of the top ten retail markets in the world by terms of economic value. India is one of the fastest emerging retail markets in the world, with 1.2 billion people. In simple words retailing is making the final product directly available to the final consumers of the product or a sale to the ultimate consumer.

The Indian retail industry is the fifth largest in the world which is comprised of organized and unorganized sectors. The Retail industry is of late often being hailed as one of the fastest growing industries in India. With growing market demand, the industry is expected to grow at a pace of 25-30% annually. The Indian retail industry is expected to grow from Rs. 35,000crores in 2004-05 to Rs. 109,000crores by the year 2010. AT Kearney, the well known international management consultancy recently identified India as the second most attractive retail destination globally from among thirty emergent markets. In 2007, the retail trade in India had a share of 8- 10% in the GDP (Gross Domestic Product) of the country. In 2009, it rose to 12%. It is also expected to reach 22% by 2010(Kearney, A.T). The organized sector is expected to grow to $100 bn and account for 12-15% of retail sales by 2015(Singhal 1999). The latest moves taken by Indian government suggest that this may be about to change and global supermarket chain stores such as Wal-Mart (United States), Carrefour (France), Marks & Spencer and Tesco (United Kingdom), and Shoprite (South Africa) may finally be allowed to set up shop in India. 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.

The impact of entry by large retail chains on employment and incumbent mom-and-pop stores is mixed. There can be substantial benefits to consumers in the form of lower prices and lowered food price inflation. Moreover, by employing improved distribution and warehousing technologies, large retail chains are in a position to provide better price signals to farmers and to serve as a platform for enhanced exports.

This paper discusses about the likely impact of FDI on Indian retail sector whether good or bad, opportunities & challenges and also the contribution of FDI in retail in economic growth of the country. It also explains about the trends in FDI inflows in various emerging market economies.

REVIEW OF LITERATURE

M. Joseph and N. Soundararajan, (2009), The Indian Council for Research on International Economic Relations (ICRIER) study has shown that hardly 1.7 per cent of small shops have closed down due to competition from organized retail. They have competed successfully against organized retail through adoption of better business practices and technology. FDI has positive spillover effects on the economy as its ownership advantages get disseminated to locally owned enterprises, enhancing their productivity. All these benefits of foreign direct investment have been well proven in India in sectors such as automobiles, telecom and consumer electronics.

Mukherjee and Patel (2005), found that foreign retailers are working with small manufacturers for in-house labels and are providing them technologies like packaging technologies and bar coding. Sourcing from India has increased with the advent of foreign retailers and they also bring in an efficient supply-chain management system. Joint ventures with foreign retailers are helping the Indian industry to get access to finance and global best practices. Besides, retailing being a non-tradable service there is no possibility of improved efficiency through import competition and foreign investment is the way forward. The aspects of foreign direct investment i.e. political scenario and trends are analyzed by most of the studies and they are, Alvin and Wint(1992) Reviews the liberalization of FDI regulation in ten developing countries and concludes that there can be a disconnect between formal liberalization and the actual implementation of the screening process.

Dornbusch and Park(1995) observe that foreign investors pursue a positive feedback strategy, which makes stocks to overreact to change in fundamentals.

Borensztin et al (1998) examine absorptive capacity of recipient country, which is measured by stock of human capital required for technological progress; it takes place through 'capital is deepening' associated with new capital goods brought into an economy by FDI.

Tanay Kumar Nandi and Ritankar Saher (2007) in their work made an attempt to study the Foreign Direct Investment in India with a special focus on Retail Trade, This paper stresses the need of FDI in India in retail sector and uses the augment that FDI is allowed in multiple sectors and The study also suggests that FDI in retail sector must be allowed.

Jaya Gupta (2007) in a paper made an attempt to review the change in sectoral trends in India due to FDI inflows since liberalization. This paper also examines the changed policy implications on sectoral growth and economic development of India as a whole.

John Andreas32 (2004) in his work "The Effects of FDI Inflows on Host Country Economic Growth" discusses the potential of FDI inflows to affect host country economic growth. The paper argues that FDI should have a positive effect on economic growth as a result of technology spillovers and physical capital inflows. Economic growth increases the size of the host country market and strengthens the incentives for market seeking FDI. This could result in a situation where FDI and economic growth are mutually supporting. However, for the ease of most of the developing economies growth is unlikely to result in market – seeking FDI due to the low income levels. Therefore, causality is primarily expected to run from FDI inflows to economic growth for these economies.

OBJECTIVES OF THE STUDY

1. To analyze the Impact of FDI on Retail Sector
2. To know the trends of FDI inflows in various Emerging Market Economies
3. To discuss about the Opportunities & Challenges faced by the Retail Sector
4. To discuss about the suggestions for the growth of Indian retail industry.

GROWTH OF INDIAN RETAIL

1. According to the 8th Annual Global Retail Development Index (GRDI) of AT Kearney, India retail industry is the most promising emerging market for investment. In 2007, the retail trade in India had a share of 8-10% in the GDP (Gross Domestic Product) of the country. In 2009, it rose to 12%, 22% in 2010 and is expected to reach 35% by 2011-12.

2. In 2011-12 over 1,000 hypermarkets and 3,000 supermarkets are projected to come up. India will need additional retail space of 700,000,000 sq ft (65,000,000 m2) as compared to today. Current projections on construction point to a supply of just 200,000,000 sq ft (19,000,000 m2), leaving a gap of 500,000,000 sq ft (46,000,000 m2) that needs to be filled, at a cost of US$15–18 billion

3. According to the ICRIER report, the retail business in India is estimated to grow at 13% from $322 billion in 2006-07 to $590 billion in 2011-12. The unorganized retail sector is expected to grow at about 10% per annum with sales expected to rise from $ 309 billion in 2006-07 to $ 496 billion in 2011-12.

TRENDS OF FDI INFLOWS IN EMERGING MARKET ECONOMIES

The liberalization of trade, capital markets, breaking of business barriers, technological advancements, and the growing internationalization of goods, services, or ideas over the past two decades makes the world economies the globalised one. Consequently, with large domestic market, low labour costs, cheap and skilled labour, high returns to investment, developing countries now have a significant impact on the global economy, particularly in the economics of the industrialized states. Trends in World FDI flows depict that developing countries makes their presence felt by receiving a considerable chunk of FDI inflows.

CURRENT PICTURE OF FDI IN RETAIL SECTOR

According to the announcement, FDI up to 51 per cent in retail trade would be subject to the following conditions

1. Products to be sold should be of a single brand only
2. Products should be sold under the same brand internationally
3. Single brand product retailing would cover only products which are branded during manufacturing.
4. FDI would be allowed only with prior approval of the Government, conforming to prescribed norms and conditions
5. Processing will be done by the dept. Of industrial policy and promotion for government Approval.

The guidelines would, however, ensure that the food and grocery segment of Indian retailing would not face competition from capital because this sector in India tended to be multi-stock keeper units and multi-brands.

MAJOR CHALLENGES FOR RETAIL DEVELOPMENT IN INDIA

Organized retail in India is little over a decade old. It is largely an urban phenomenon and the pace of growth is still slow. Some of the reasons for this slow growth are: -

- The Existence of Traditional KIRANA stores - The first and foremost challenge facing by the organized retail industry in India is competition from the unorganized sector. Retailing is not new concept for India; it has been established here since centuries. It is a low cost structure, mostly owner operated, has negligible real estate and labor costs and little or no taxes to pay. Consumer familiarity that runs from generation to generation is one big advantage for the traditional retailing sector. On the other hand, organized sector have big expenses to meet and yet have to keep prices low enough to compete with the traditional sector.

- Lack of Recognition as an Industry – Lack of recognition as an industry hampers the availability of finance to the existing and new players. This affects growth and expansion plans.
- High Cost of Real Estate – Real estate prices in some cities in India are amongst the highest in the world. Lease rent of the property is so high that it reduces the profitability of the project.
- High Cost of Stamp Duties– Stamp duties on transfer of property are also very high which varies from state to state e.g, 12.5% in Gujarat and 8% in Delhi. The problem is compounded by problems of clear titles to ownership, while at the same time land use conversion is time consuming and complex as is the legal process for settling of property disputes.
- Lack of Infrastructural Facilities- Poor roads and transport facility hampers the development of food and grocery retail in India. The existing supermarkets and foods retailers have to invest a substantial amount of money and time in building a cold chain network.
- Multiple and Complex Taxation System –The sales tax rates vary from state to state and organized retail players have to face a multiple point octroi with the introduction of value added tax (VAT) which causes disruption in supply chain management.
- Price War-There is price war between different retail organizations. Each and every one is saying to provide goods at low cost and offers various promotional schemes. In such a case it is difficult to keep one's customers with oneself.

OPPORTUNITIES FOR RETAIL DEVELOPMENT IN INDIA

Retail marketing gets various opportunities to grow up in the Indian market. Not only retailing but Manufacturers as well as suppliers, and buyers have various opportunities, some of which are mentioned below-

- Provides visibility to Brands- Organized retail provides needed visibility to brands and a platform for customer interaction. It also helps in launching of new product or product variant and in market penetration. It has wider product range and more frequent, speedier deliveries.
- Urbanization– As large percentage of population has now been shifted to urban areas due to more job opportunities and more facilities for their children and family, they know the importance of brands and moreover they want everything under one roof, thus a single retail can catch more customers.
- Nuclear Family- As the time passed away joint families came in a new form i.e. nuclear family. Again the income level of these nuclear families increases because both members started earning. This results into increased power of purchase and lack of time. Now they want everything under one roof. This brought the concept of organized retailing.
- Plastic Revolution– Increased use of credit cards is in favor of retail marketing. It creates requirement even when it is not necessary.
- Indian Consumers– Organized retail stores put stress on proper infrastructure like well maintained building, air conditioning, trained employees, electronic machine, parking facilities and proper display of goods category wise. The customers feel good to see everything displayed in front of them which make purchase easier for them. They need not to wait for anybody to show them the products. Self-selection saves time and gives more opportunities and satisfaction. Fix cost removes the threat of misleading. They avail various discounts and promotional schemes presented by the manufacturers. They also get product of different varieties and of proper quality.
- High Availability of Jobs - There will be huge job opportunities in the country (in crores) as there will be opening of malls and store houses. The entry of modern retailers will expand the market creating large amount of additional jobs in retail. Opportunities will vary from ordinary workers to specialized officers. The employment opportunities will be in retail sales, retail floor manager, cold chains,

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warehousing and logistics. The jobs will be for urban as well as rural youth. There will be huge scope of MBA's as they will cherish working with world class chain of retailers.

- Indian Farmers: The main benefits of FDI in retail would be to farmers who will be able to get good returns of their harvest by supplying to organized retailers by tying up long term contracts with them which they are not able to sell in the local mandi. The payments will be directly credited into bank accounts and will be free from commission agents. The large retailers will also save 10-15% in comissions by purchasing fruits and vegetables directly.
- Reduces Supply Chain Management - The big players of retail marketing and the Manufacturing companies directly come in contact thus reducing many intermediary chains. Manufacturers also give many promotional schemes for their product that is beneficial for consumers.
- Proper tax system: Tax revenue will increase like VAT and service tax. The organized sales with computerized billing system will also yield more revenue through commodity taxes like VAT and service tax to the government. Thus tax buoyancy of the economy would increase.
- Inflation control: Inflation will be curbed.

CONCLUSION

The concept of FDI is now a part of India's economic future but the term remains vague to many, despite the profound effects on the economy. FDI means Foreign Direct Investment in which foreign investors can make investment in India. FDI in India's retail sector has both advantages as well as disadvantages. It is advantageous to the government as the tax revenue collected can be used for infrastructure development, not only this it will be beneficial to the farmers and consumers also to a large extent. It will also provide job opportunity which is a crucial factor for developing countries. On the other hand it will cause cut throat competition specially in the organized retail sector promoting cartels, creation of monopolies, increase real estate prices etc. Increased competition will be beneficial as everyone will try to make its product better from others to increase their profits which will ultimately result in quality products at reasonable prices. Opponents of FDI in retail argue that it will bring major job losses but frankly it will cause only redistribution of jobs with some drying up (like middlemen) and new ones sprouting up. The argument that farmers will suffer due to creation of monopolies is weak. Stores like Wal-Mart and Tesco are very few, on the outskirts of cities (to keep real estate costs low) and can't intrude in the local territory of local kiranas.

FDI is advantageous and disadvantageous both but it depends only on the way we implement it in our country so that FDI does not have a bad impact on India's Business. Government must make some rules so that it is beneficial for Indian market, retailers and the customers get the required benefit from this. May be by this Indian economy may rise which is helpful in the employment field. The experience of successful ASEAN countries amply demonstrates how FDI can play a leading role in bringing about rapid, export-led growth. In the retail sector changes are very frequent therefore survival in retail will depend upon the ability to adapt to change. The Indian retailers need to develop proper systems and processes keeping the unique nature of the country in mind. FDI would lead to a more comprehensive integration of India into the worldwide market and as such, it is imperative for the government to promote this sector for the overall economic development and social welfare of the country. So FDI should be implemented in a limited way so that it releases a good impact on India market. If done in the right manner, it can prove to be a boon and not a curse.

The performance of foreign direct investment till date is round about the satisfactory level baring the certain issues and challenges. Today we have more than $303.48 billion as a foreign exchange reserves and above foreign debts are around about $297.5 billion which we can further improves through export promotions, liberal opportunities of investment for foreign investors.

The future of foreign retail players is also uncertain like that of Indian retail players. No doubt the opening of the investment opportunities for the foreign investor will make the Indian industries more competitive and some of them may have to struggle for the survivals such as small retailers and shop keepers. It has been observed from the above analysis that FDI approval given by the government will benefit almost all the sectors of the economy. There are some people who are trying to mislead people for their own benefit and are opposing the entry of foreign retailers into India. FDI in retail sector not only benefit the society but also helps in the economic growth of the country. The India Retail Industry is gradually inching its way towards becoming the next boom industry.

SUGGESTIONS FOR THE GROWTH OF RETAIL INDUSTRY

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

1. India needs to invest in infrastructure development because India is lacking only in this which will affect our Retail Industry majorly.

2. India should increase the investment absorption capacity.

3. India should make FDI policies little bit more liberal so that it can face competition with other emerging economies.

4. Bureaucratic delays and various governmental approvals and clearances involving different ministries need to be fastened.

5. Restrictions on sector caps and entry route to sectors other than those of national importance need to be liberalized further and constant reviewing of policies must be done.

6. Government must ensure consistency of policy so as to improve the business and investor confidence

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