FOREIGN DIRECT INVESTMENT (FDI) IN INDIAN RETAIL SECTOR

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Abstract

India is one of the major growing marketplaces in the world, together with a population of over one billion. It is considered as one of the prominent nations in the world in terms of purchasing power. After the market reform in the year 1991, India gradually opened up its economy to Foreign Direct Investment (FDI) in a wide range of sectors. At present, India can breath fresh oxygen coming out from such a suffocating situation. India is the top most eye-catching country for FDI among the rest of the markets in the world. As a matter of fact, FDI in the vibrant Indian retail sector should it be without restraint permitted and should it be significantly inspired. Indian retail sector is one of the rising sectors which have an enormous opportunity for attracting FDI. It is predictable that FDI will speed up the growth of organized retail and will bring many more foreign retailers to India. The current revolutions brought in the retail sector by the government has made the retail sector to have many retailers for India. A number of concerns were squeezing out with respect to the partial beginning of the retail sector (multi-brand retail) for FDI. Whether it would lead to partial competition and finally result in the large-scale walking out of domestic retailers, especially the small family managed outlets, foremost to large scale movement of persons working in the retail sector or will create more employment. Moreover, the structure and procedure of foreign direct investment in the retail sector have improved a lot since India has opened ready for world markets. This has powered high prospects that FDI in retail may help as a channel for the better economic growth of India.

Keywords: Foreign Direct Investment (FDI), Retail, Sector, India, Economy, Brand, Store, Government, and world etc.

Introduction

Foreign direct investments have been very helpful for developing countries in the last two decade. There are various sectors in which foreign player are interested to enter and the retail sector is one the most attractive sectors for them. It makes available 9% employment to the total workforce and contributes about 15% to the Indian GDP. It could have been a welcome step in strengthening India’s FDI regime with making it in tune with the country’s needs. India is a growing economy and it is considered as an attractive market to invest in, especially in a rapidly growing retail market. India is the founder member of the World Trade Organization and signatory to its General Agreement on Trade in Services (GATS). This agreement includes wholesale and retailing
services and all member countries are required to open up the retail trade sector to foreign investment. There were initial reservations with regard to opening up of the retail sector get up from fear of job losses, procurement from the international market, competition, and loss of business opportunities. However, there are some policy issues and restrictions on foreign direct investment in the retail sector in India. Even after so many years of debate, the government in a series of moves has opened up the retail sector slowly to Foreign Direct Investment (FDI) in India. The regulations are still changing slowly with lots of uncertainties. Foreign investors are having close eyes on India and ready to enter into Indian retail sector.

The Indian Government believes that the opportunity of FDI in multi-brand retail and further liberalization of single-brand retail trade will facilitate greater FDI inflows providing new opportunities and benefits besides quality improvement. At a time when decreasing investments have led to slower GDP growth, on the other hand, a strong competition, between the large domestic retailers and those with FDI, should be maintained. Impressive socially desirable restraints on FDI funded retailers would lead to unfair competition. In spite of the current developments in retailing and its enormous impact on the economy, retailing continues to be the least developed industries and the growth of organized retailing in India has been far slower as compared to the rest of the world. One main reason for this is that retailing is one of the few sectors where foreign direct investment is not permissible.

According to the report made by FICCI and ICICI Property Services in Feb 2005, FDI can be a powerful catalyst to spur competition in the retail industry. It can bring about improvement in various areas such as:

- Supply Chain Improvement
- Investment in Technology
- Manpower and Skill development
- Tourism Development
- Greater Sourcing From India
- Up gradation in Agriculture
- Efficient Small and Medium Scale Industries
- Growth in market size
- Greater Productivity
- Benefits to the government through greater GDP, Tax income and employment generation
The influence of the consequential rise in FDI in Indian retail is probably to not just develop sound backward links but also build a domestic supply chain of international standards. What is inspiring now for these international majors is the new policy driving force, which aims to further liberalize the FDI regime in Indian retail. The Indian Government has a more liberal policy with regard to wholesale trade, franchising, and commission agents’ services, thus preparing the ground for FDI in retail as well. Foreign retailers have already initiated operations in India through different routes:
1. Joint ventures where the Indian firm is an export house
2. Franchising (e.g. Kentucky Fried Chicken, Nike)
3. Sourcing of supplies from small scale sector
4. Cash and carry operations (Giant in Hyderabad, Metro in Bangalore)
5. Non-store formats – direct marketing (Amway)

**Meaning and Definition of Foreign Direct Investment (FDI)**

Dictionary of Economics (Graham Bannock et.al) defined FDI as is an investment in a foreign country through the acquisition of a local company or the establishment thereof an operation on a new (Greenfield) site. In simple word FDI (Foreign Direct Investment) refers to the capital inflows of investment for acquiring a lasting management interest (more than 10%) in an enterprise operating an economy other than that of the investor.

Foreign direct investment is the amount of equity capital, reinvestment of returns and other long or short term capital as shown in the balance of payments. It generally takes in participation in management, joint venture, transfer of technology and expertise, merger or acquisition and includes Greenfield and Brownfield projects. Thus, foreign direct investment is an investment made by a foreign company or entity into a company or entity based in a different country. Foreign direct investments change substantively as of indirect investments for example portfolio flows, in which overseas institutions invest in equities listed on a nation's stock exchange.

In addition to the different forms of foreign investment, foreign direct investment (FDI) flows are usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their incomes depend on the performing of projects financed by the investors. In fact, FDI provides a win-win situation to both the host and the guest countries. The “guest” countries want to take advantage of the vast markets opened via policy initiatives that led to industrial growth. Alternatively, the “host” countries want to get technological and managerial skills and improve domestic savings and foreign exchange. Furthermore, in order
to overcome the deficiencies of all kinds of resources viz. capital, financial, entrepreneurship, technological expertise, skills and practices, access to markets abroad in their economic development. Developing nations accepted FDI as an exclusive visible way out for all their scarcities.

According to International Monetary Fund, FDI is defined as “investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor, the investor’s purpose being to have an effective voice in the management of the enterprise”.

OECD has defined FDI as “investment by a foreign investor in at least 10% or more of the voting stock or ordinary shares of the investee company”.

**Meaning and Definition of Retail**

Retail is a French word which means to “cut it again” and basically mean a sale to the consumer for direct consumption. Retailing is a linkup between the producer and the consumer for accomplishing personal needs. It is defined as all activities participating in selling goods or services directly to the final consumer for their personal, non-business use via shops, market, door-to-door selling, and mail-order or over the internet where the buyer means to consume the product. In basic terms, it implies a first-hand transaction with the customer. Retailing can be described as the buying and selling of goods and services. It can also be defined as the timely supply of goods and services demanded by consumers at prices that are economical and reasonably priced. Retailing contains a direct interface with the customer and the coordination of business pursuits from end to end- right from the concept or design stage of a product or offering, to its supply and post-supply service to the customer.

The industry has promoted to the economic growth of various countries in the world and it is absolutely one of the fastest changing and dynamic industries in the world today.

According to a definition recognized to Philip Kotler, “retailing includes all the activities involved in selling goods or services directly to the final consumers for personal, non-business use”. Even though selling goods or services directly to the final consumers is the primary activity in the retailing, there are a number of supplementary activities that are associated with it. Retailers are engaged in the delivery phase of an integrated supply chain and are in direct interface with consumers.

In 2004, The High Court of Delhi referred to Black’s Law Dictionary to define the term “retail”. The term “retail” is defined as a sale for final consumption in contrast to a sale for further sale or processing (i.e. wholesale) a sale to the ultimate consumer.
As a result, retailing consist of a direct crossing point with the customer and the coordination of business activities from end to end- right from the concept or design phase of a product or offering to its supply and post- supply service to the customer. This excludes direct line between the manufacturer and institutional buyers such as the government and other wholesale customers. Retailing is the end relation that connects the individual consumer with the manufacturing and distribution chain. A retailer is involved in the act of selling goods to the individual consumer at a surplus of profit. The industry has participated in the economic growth of various countries in the world and is definitely one of the most rapidly changing and dynamic industries in the world today.

Figure: A simple supply chain

Division of Retail Industry

Retailing is the largest private industry in India. The Indian retail industry is usually separated into two main sections

1) Organized and
2) Unorganized Retailing

Organized Retailing

It represents trading activities started by licensed retailers, that are, those who are registered for sales tax, income tax, etc. These consist of the corporate-sponsored hypermarkets and retail chains, and also the privately maintained large retail businesses. It covers only 3% of retail business in the country.

Unorganized Retailing

It indicates to the old-style formats of low-cost retailing, such as the local kirana shops, owner operated general stores, paan/beedi shops, convenience stores, hand cart (street sellers) and footpath/roadside vendors etc. and it covers nearly 97% of the retail business in India. This sector is the prevalent source of employment next to agriculture, and has deep
penetration into rural India and generating more than 12 percent of India’s GDP. The performance of this sector has a great effect on consumer welfare.

**Perspective of FDI in Indian Retail**

By tradition, most of the Indian family circle have enjoyed the convenience of calling up the grocery "kirana" store, which has advantages of understanding with their brand preferences, flexibility in returning and exchanging goods and also offers credit. In spite of this in most cities today, shopping centre based shopping formats are gaining popularity but still, the price-sensitive Indian shopper prefers Big box stores such as Big Bazaar particularly for the steep discounts and bulk prices. The majority of the customers go for the convenience and get into offered by the local grocery store and thus, retail chains such as Reliance Fresh, Subhiksha and more have closed down their operations in certain locations. These retail giants will have to focus on several operations even though reaching out to the Indian consumer. Firstly, they have to efficiently build their expertise with cold storage technologies to attract customers with fresh and exotic vegetables and organic produce. Secondly, they want to build a range of inspiring global foods and household brands and therefore generate access for the consumers. Thirdly, they have to ensure interval free supplies of necessary raw materials by supporting domestic farmers.

In India, retailing is developing rapidly, with consumer expenditure increasing by unique rates and with encouraging a number of global players investing in this sector. Organized retail in India is going through a change and is probably to scale up to meet universal standards over the next five years. India’s retail market has practiced enormous growth over the past decade.

The Indian retail industry is the fifth largest in the world which consist of organized and unorganized sectors. The retail industry is of late often being welcomed as one of the fastest growing industries in India. It offers 9% of employment to the total labor force and contributes about 15% to the Indian GDP. It could have been a welcome step in building up India’s FDI regime with making it in tune with the country’s needs. The FDI policy has been shifting away from the license approach of protection against imagined foreign dictators towards a more open, healthy and competitive environment. This policy would have offered a window for the world-class retailer Hermes, Tiffany & Co and Wal-Mart, etc. to set their foot in the prosperous Indian retail sector.

The Government of India trust that the opportunity of FDI in multi-brand retail and farthest liberalization of single-brand retail trade will facilitate more FDI inflows offering new
opportunities and benefits besides quality upgrading. At a time when declining investments have led to slower GDP growth, however, a healthy competition, between the large domestic retailers and those with FDI, should be maintained. Imposing socially desirable constraints on FDI funded retailers would lead to unfair competition. Notwithstanding the current developments in retailing and its great contribution to the economy, retailing continues to be the least progressed industries and the growth of organized retailing in India has been much slower as compared to rest of the world. One main cause for this is that retailing is one of the few sectors where foreign direct investment is not permitted. Within the country, there have been objections by trading associations and other stakeholders against permitting FDI in retail.

In 1991, Indian Economy was liberalized it's Foreign Direct Investment (FDI) policy, that has made most business sectors in India eligible to welcome foreign investment has opened up front doors to many a multinational corporation. Although the policy framework for the retail and the trading sector has continued to be highly restricted. Ever since the multinational corporations have been excitedly coming up for the opening of the Indian retail sector for the FDI. Debates relating to FDI in retail trade in India have always brought in a mixed bag of reactions. In recent times FDI in retailing has been the most heard buzzword in the Indian Corporate World.

Economic development, increase in purchasing power, developing consumerism and brand proliferation has led to retail modernization in India. With high economic progress, per capita income increases; this, in turn, leads to a shift in consumption pattern from essential items to discretionary consumption. Moreover, as the economy liberalizes and globalizes, different international brands arrive in the domestic market. Consumer consciousness increases and consumers have a tendency to experiment with different international brands. The proliferation of brands leads to an increase in retail space. Retail modernization in India depicts a similar story.

According to A.T. Kearney’s Annual Global Retail Development Index (GRDI) for the year 2012, India has been placed at fifth rank (after Brazil, Chile, China, and Uruguay) on the basis of retail investment attractiveness. The emergent Indian market has to pay attention to a number of foreign retailers and domestic corporate to invest in this sector. Being helped by India’s growing retail boom many multinational companies also started to arrive in India’s retail market.
According to the Investment Commission of India, the retail sector is expected to grow almost three times its current levels to $660 billion by 2015. FDI can expand markets in the retail sector through diminishing exchange and change costs of business throughout the taking up of advanced supply chain and benefit consumers, and suppliers (farmers). Opponent to relaxing FDI policy in this sector raise points on employment losses, raise of unhealthy competition among organized domestic retailers resulting in the departure of small local retailers from the market and alteration of urban cultural development.

In India, only a few companies with a strong retail background exist. Retailing is the largest employer in India after agriculture. Over the last few years, India has been witnessing a transformation of the retail sector such as departmental stores, hypermarkets, supermarkets, and stores. Earlier, FDI inflows in infrastructure, manufacturing and natural resources were high in India. It is evident that now FDI inflows are increasing in the sectors like retail, hospitality, tourism, and other service-oriented industries. This is a positive sign for the economic development of the country.

**Top Players of Retail in India**

1. Pantaloon Retail
2. Raheja Group
3. Tata
4. RPG Group
5. Landmark
6. Piramal Group
7. Subhiksha
8. Bharati – Walmart
9. Reliance Group
10. AV Birla Group

**FDI Policy in India**

Foreign investment in India is regulated by the FDI policy announced by the Government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. The Reserve Bank of India (RBI) in this respect had issued a notification, which contains the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000. This notification has been modified from time to time. Department of Industrial Policy and Promotion (DIPP) under the Ministry of Commerce and Industry, Government of India is the nodal agency for monitoring and reviewing the FDI policy on a
continuing basis and changes in sectoral policy/sectoral equity cap which goes from 26% to 100% at present. The FDI policy is notified throughout Press Notes/Policy Circulars by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP) Ministry of Commerce & Industry, Government of India. FDI is permissible under Direct Route and Government Route in India. The foreign investors are free to invest in India, except few sectors/activities, wherever prior approval from the RBI or Foreign Investment Promotion Board (FIPB) would be prerequisite. FDI in the retail sector is allowed through Government Route only.

FDI in cash and carry (wholesale) with 100 percent ownership was allowed in 1997. Investment in a single brand retail outlet was also permitted 51 percent in 2006. FDI in multi-brand retailing is prohibited in India. The central Government of India dispossessed of foreign direct investment (FDI) in multi-brand retail, critical foreign groups from some ownership in supermarkets, convenience stores or several retail outlets up to 2011. In December 2011, under pressure from the opposition, the Indian Government placed the retail reforms on hold till it reaches a consensus. In January 2012, the Government of India permitted reforms for single-brand stores welcoming any person in the world to invest in Indian retail market with 100% proprietorship but fulfilled the requirement that the single brand retailer supplier 30% of its goods from India. Indian Government remains the hold on retail reforms for multi-brand stores. Indian Parliament approved of the central government’s decision to allow foreign direct investment (FDI) in multi-brand retailing in December 2012. This smooth the way for foreign retailers to open retail stores with 51 percent ownership in major cities to sell a large variety of products under one roof (For the time being, the foreign retailers will be permitted only in cities with the population of above one million). On the other hand, the state governments will have the rights to avoid foreign retailers from opening up stores in their particular states. It may be noticed that foreign capital has already been allowed in single-brand retailing. However, there are various indirect channels, for example, cash and carry wholesale agreements, franchise agreements, strategic licensing agreements, manufacturing and wholly owned subsidiaries, through which foreign companies consist of large retailers have already had called up to the Indian market.

**FDI in Single Brand**

FDI in single brand retail means that a retail store with foreign investment would be allowed to sell goods only one brand. Such as, if Adidas were to get approval for retail its flagship brand in India, those retail outlets could only sell products under the Adidas brand and not the
Reebok brand, for which separate approval is mandatory. If given permission, Adidas could sell products under the Reebok brand in separate outlets. The meaning of single brand has not categorically defined by the government anywhere neither in any of its circulars nor any notifications.

Foreign investment in single brand product retail trading is aimed at inviting investments in production and marketing, get better the accessibility of such goods for the consumer, stimulating better sourcing of goods from India, and enhancing the competitiveness of Indian enterprises through access to global designs, technologies, and management practices. The Foreign Investment Promotion Board (FIPB) has allowed 100% in retail industry which will contain only those classified during manufacturing. Only one brand can sell with foreign investment in a retail store.

**Conditions for Investing in Single Branding**

- Only single brand products would be sold.
- Products should be sold under the same international brand.
- Single Brand product-retail trading would cover only products which are branded during manufacturing.
- The retailers have to get at least 30% of goods from SMEs.
- All stores can open where there is a population of over one (1) million.
- The foreign investor should be the owner of the brand.
- Self-Certification In for the company is needed.
- Checking by statutory auditors is necessary.

**Procedure for Approval**

- Application to Secretariat for Industrial Assistance, DIPP, Ministry of Industry.
- Approval from the government for any additional products or products categories if any to be added.
- Processed in DIPP before approval from FIPB.

**FDI in Multi Brand**

FDI in multi brand retail involves that a retail store with foreign investment can sell multiple brands under one roof. The government has also not described the term multi brand. 51% FDI in multi brand retail indicates that a retail store with foreign investment can sell various brands under one roof. Opening up FDI in multi-brand retail will mean that international retailers including Wal-Mart, Carrefour, and Tesco can open stores in India and offering a
variety of household articles and grocery directly to consumers in the similar method as the ubiquitous “Kirana” store.

**Conditions for Investment in Multi Branding**

- Minimum investment of US $100 Million to be brought in by foreign investors.
- 50% of investment to be borne by infrastructural development.
- 30% of raw material to be taken from Indian SME’s.
- Permission is given to set up malls in cities with a minimum population of 10 lakhs.
- The Government will first procure materials from farmers.
- Products should be sold in the same brand.
- Foreign investor should be the owner of the brand.

The approval for single and multi-brand contains a set of provisos for the foreign investors, intended at confirming that the foreign investment makes a genuine contribution to the development of Indian infrastructure and logistics, at the same time helping the integration of small retailers into the upgraded value chain.

**States in Favour of FDI in Multi Brand Retail**

- Maharashtra
- Haryana
- Andhra Pradesh
- Rajasthan
- Jammu and Kashmir
- Uttarakhand
- Manipur
- Assam
- Delhi

Uttarakhand, Manipur, and Assam have no cities with a population of one million but capital cities of these states can be considered for opening multi-brand retail stores. These states cover 19 cities like Delhi, Mumbai, Pune, Nagpur, Jaipur, Hyderabad, Vijayawada, and Srinagar.

**States Opposing FDI in Multi Brand Retail**

- Gujarat
- Uttar Pradesh
- West Bengal
- Bihar
FDI Policy in multi brand retail though approved by the Cabinet yet the final authority for permitting the trade license rests with the states under the irrespective Shops and Establishment Acts. Similarly, foreign retailers will only be permitted to set up shop in cities with a population of more than one million.

Indian retail sector holds a vast employment potential and hence, attracts the attention of government and foreign major retailers. Boosting efficiency and improving the food retail sales would have a cascading effect on employment and economic activity in the rural areas for the marginalized workers. Even without any significant involvement of FDI, the corporate-owned sector in retailing is expanding wildly at a high rate. The face of the Indian retail industry will change with the entrance of major’s global retail in the country who are known for their quality, service, and technology of the highest standards.

**Major Players Expected to Enter in Indian Retail Sector**

- WAL-MART STORES INC
- CARREFOUR SA
- TESCO PLC
- METRO AG
- IKEA

Even though the organized retail sector in India is at the infant stage, India has today become a budding target for FDI. India today offers the most persuasive investment opportunity for mass merchants and food retailers looking to expand overseas as the Indian economy is growing at a rapid pace with consumers having high purchasing power. With a robust economy experiencing unrelenting growth, India has exerted a pull and an irresistible enticement to companies looking to expand their scope of operations. FDI is a strong source for the strengthening of retailing and will generate enormous opportunities for innovation in the retail sector in India but at the same time, it is relatively likely that a unit of the local retailing industry will be severely unhappy due to the entry of foreign retailers.

Amongst other benefits, the opening up of multi-brand retail will have a positive impact on the overall economic growth owing to increased employment opportunities; increased
demand of real estate; healthier infrastructure; decrease in prices of the final product; reasonable remuneration to the farmers.

According to the news-paper Indo-Asian News Service, Washington, (dated December 09, 2011), the U. S. has said that they respect India for opening retail stores. The United States has said that foreign direct investment in retail trade would be beneficial to both India and the U. S. The U. S. is happy for getting the opportunity of retail business in India, the world’s second largest market.

Impact and Benefits of the Country

- Growth of Infrastructure
- Franchising Opportunity for Local Entrepreneurs
- The inflow of Funds and Investments
- Implementation of IT in Retail
- Investment in Supply Chain, Cold Chain, and warehousing
- Increase the number and Improve Quality of Employment
- Reduced Cost and Increased Efficiency
- Provide better value to end Customer

Hence it will lead to overall economic growth and create a Benchmark.

FDI in retail will ultimately lead to increased income to farmers because of increased sourcing by the companies from them. Farmers are probable to get benefited through investments in infrastructure such as cold storage and other machinery so that they can diminish their post-harvest loss and thereby get guaranteed and higher income. Micro, Small and Medium Enterprises are predictable to be benefited since the foreign companies will move toward them for the know-how, local tastes, and merchandise preferences. Investments in back-end infrastructure will lead to more competent retail trade and as a result, it can be felt that FDI in multi-brand retailing will definitely help in developing the world-class supply chain for the retail sector in India.

Conclusion

In India, retailing has been a key service industry. In particular, with faster growth of the overall economy, higher disposable incomes, and rapid urbanization in recent years, there has been an acceleration in the growth of this sector. Actually, it has been recognized as a sunrise industry with infinite future growth potential. Last decade has indeed witnessed tremendous growth in the Indian retail industry and has integrated our Indian economy with the world. Retailing in India is progressively inching its way for becoming the next boom industry. The
growth of the retail industry will be tapped which will allow foreign players to play a major role in upbring this industry as an emerging sector. Foreign investors are extremely eager about charisma in the Indian retail sector. Without a doubt, foreign direct investment in retail is promising as a kind of litmus trial to the government's pledge to liberalization. Approval of FDI in retail sector will not only fulfill India’s commitment to WTO’s GATS agreement but will also encourage the local players to be more competitive and quality oriented. Consumers will also get the benefit as they will have a variety of products to choose from at the competitive prices. In brief, FDI in retail sector may boost the socio-economic development of the whole country if implemented wisely carefully while signing the agreements with the Foreign Investors. Allowing foreign direct investment in multi-brand retail trading is an important reform in the Indian economy. This has made ground for Joint Ventures in multi-brand retail trading and expected to bring improvement in infrastructure, technology, the price for agricultural produce and generate employment opportunities. In spite of the ongoing improvements in retailing and its extraordinary effect on the economy, retailing keeps on being the least developed industries. The advancement of this industry will be tapped which will allow foreign companies to play a key role in upbring this industry as an emergent sector. Allowing FDI may not be as bad as some of us feel. But the policy must be well-drafted for which a general perceptional study of the stakeholders of retailing is solicited.

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