Foreign Direct Investment In Multi-Brand Retail : Opportunities And Threats

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INTRODUCTION

In the era of liberalization, globalization and privatization, the whole economy is opening up gradually. The Indian retail sector has also not remained untouched. India has already allowed 51 percent FDI in single-brand retail and 100 percent FDI in cash-and–carry or wholesale trading and now, there is a proposal by the Department of Industrial Policy and Promotion (DIPP) to allow 51 percent FDI in multi-brand retailing (Hindustan Times, 30th August, 2010). India has 15 million-plus retailers, who account for $350 plus billion of annual sales. The retail space is dominated by the unorganized sector, that contributes to 94 percent of the sales (Shrikhande, 2010). The retail sector is the largest sector in India after agriculture, accounting for over 10 percent of the country's GDP and around 8 percent of the employment. India has the most unorganized retail market in the world (DIPP, 2010). Most retailers of the unorganized retail market have their shops in the front or at the back of their houses.

The Indian retail sector is one of the fastest growing sectors, with several players entering the market. Currently, the organized sector accounts for only 2 percent, indicating a huge potential market opportunity. India is being seen as the most attractive market by retail investors from all over the world. A.T. Kearney, the well-known international management consultancy, recently identified India as globally, the *'second most attractive retail destination'* from among thirty emergent markets. The Asian Development Bank in its recent report has estimated the size of the burgeoning Indian middle class at 418 million, and the country's private consumption expenditure has been growing at an average rate of 8.3 percent per annum, which touched ₹ 26,51,786 crore ($589 billion) in 2008 -09, from ₹ 19,26,858 crore ($428 billion) in 2004-05 (Sify Finance, 2010).

Trade is an important segment in India's Gross Domestic Product (GDP). As per the National Accounts, released by the Central Statistical Organization (CSO), GDP from trade (inclusive of wholesale and retail in the organized and unorganized sector), at current prices, increased from ₹ 4,33,963 crore in 2004-05, to ₹ 7,91,470 crore, at an average annual rate of 16.2 percent. The share of trade in GDP, however, remained fairly stable at a little over 15 percent in the last four years (CSO, 2008-09). The share of the private organized sector in total GDP from trade was 23.2 per cent in 2008-09, and it grew at 15.0% during the year. The share of the retail trade in GDP remained stable at 8.1 per cent during this period (DIPP, 2010). The Department of Industrial Policy and Promotion (DIPP) in its discussion paper has proposed 51 percent FDI in Multi-Brand Retailing. There are several stakeholders who are for and against this proposal. Global retailers like Wal-Mart & Carrefour, US-India Business Council, Confederation of Indian Industry, Federation of Indian Chambers of Commerce and Industry, etc. are for the proposal. They are of the view that FDI will eliminate the middleman from the supply chain, increase the returns to the producers, and lower the prices for consumers. On the other side, farmers group like *Kisan Jagriti Manch, Trade Unions like Bhartiya Mazdoor Sangh*, BJP, Left Parties and various trade/ shopkeeper associations are against this proposal. They say that FDI in multi-brand will force small-scale manufacturers and farmers to sell their products at cheaper rates and uneconomic prices will be dictated by the MNC retailers (Hindustan Times, 30th Aug., 2010). In this paper, an attempt has been made to analyze the possible opportunities that may emerge after FDI in multi –brand –retail and also the threats that it may pose to our retail sector.

OPPORTUNITIES

FDI has certainly benefited the country in telecom, automobile and insurance sectors, and with large-scale investments in each of these sectors, customers are getting the best of the services and products, and the resultant competition is spurring the players to improve further (Shrikhande, 2010). In the retail sector too, it is expected that

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FDI in multi-brand-retail will help in shaping up the Indian retail sector.

1) Strengthening The Supply Chain : Inefficient supply of the commodities at the back-end has been leading to inflation. Lack of investment in the logistics of the retail chain is leading to an inefficient market mechanism. India is the largest producer of fruits and vegetables (about 180 million mt). It has a very limited integrated cold storage chain infrastructure. Lack of infrastructure has resulted in the decaying of the bumper food and vegetables. It has resulted in high inflation, even after a good production. Lack of adequate storage facilities causes heavy losses to the farmers in terms of wastage in quality and quantity of produce in general, and of fruits and vegetables, in particular. Post-harvest losses of farm produce, especially of fruits, vegetables and other perishables, have been estimated to be over ₹ 1 trillion per annum, 57 per cent of which is due to avoidable wastage and the rest is due to avoidable costs of storage and commissions (CRISIL, 2007). As per some industry estimates, 25-30% of the fruits and vegetables and 5-7% of the food grains in India are wasted (Annual Report 2006-07, MoA). The DIPP in its paper has highlighted the non-compositeness of India's horticulture produce, primarily due to its weak supply chain. FDI in multi – brand retail seems to be the perfect answer to tackle this situation, as it would speed up the development of cold storage chains and back-end infrastructure facilities.

2) More Variety For The Consumers : FDI in retail will have a far-reaching impact on the various aspects of the economy. Customers will get a wide assortment of quality goods at reasonable prices. They will be able to buy the best brands across various categories. The entry of the global retail giant like Wal-Mart, Tesco, etc. will certainly provide a large variety of products to the Indian customers. Commodities from all over the world can be collected from one store, which will help customers to save time and energy. International brands that were not available due to non accessibility by domestic retailers could easily be made available through these global players.

3) Control On Inflation : FDI would help consumers, supplies and farmers. It would help in controlling inflation by offering more competitive and rationalized prices of products to consumers and reduction of wastages across India's farms –to- fork supply chain (Sify Finance, 2010). The Indian economy has been facing the acute problem of high inflation in recent times. The main reasons for inflation are excess supply of money or shortage of supply of goods in the market. Supply of money can be regulated by the Reserve Bank of India (RBI). It has its own mechanism to control the supply of money. Scarcity of supply of goods can either be due to less manufacturing/production, or it could be created artificially by malpractices like hoarding, etc. FDI can help in removing both types of scarcity by arranging for goods from the global markets or creating competition at the domestic level. The retailers can procure the supply directly from farmers or manufacturers, who will help in strengthening the supply chain as well as help in reducing the prices.

4) Employment Generation : Large investment in infrastructure would lead to a rise in farm productivity, manufacturing and food processing as well as cold storage facilities. This would cut down wastages and spur growth in employment, exports and GDP (Business Standard, 14th July, 2010). Retail is the largest sector in India after agriculture, accounting for over 10 percent of the country's GDP, and employs over 4 crore people. Within this, unorganized retailing accounts for 97 percent of the total retail trade (People Democracy, 2007). FDI in multi-brand-retail is certainly going to create employment opportunities for the youth. Setting up of retail outlets by big retailers from all over the world in different parts of the country will help in removing regional inequalities by providing avenues for the employment.

5) Farmers Will Get Their Due From Their Produce : In the Indian trading system, there are different types of intermediaries at different stages. Some of the intermediaries procure products from the farmers and sell it to *artiyas* (middleman), who collect products from different small middlemen and then *artiyas* sell products to various small retailers, who then sell the products to different customers at different localities. In this system, at every stage whenever middlemen are involved, they get a fixed commission. Commission at each level adds to the prices of commodities. Generally, when the traders get the products from the farmers or small manufacturers, they pay very little money to them and grab the maximum part of the price, which they charge from the final customer. Involvement of organized sector and allowing FDI in multi-brand retail can help in ousting these intermediaries, and help farmers to get their due from their produce. FDI in the supply chain can help in diverting the commission from intermediaries to the farmers. According to some reports, Indian farmers realize only 1/3rd of the total price paid by the final consumer, as against 2/3rd by farmers in nations with a higher share of organized retail (ICRIER Report, 2008).

THREATS

There are certain threats which may emerge after allowing FDI in multi-brand- retail that are required to be studied and analyzed in detail.

1) FDI Will Jeopardise The Existing Retailers : Indian unorganized retailers have been facing stiff competition from the organized sector. Due to financial strength and professional dealing with the parties, organized retailers have got the competitive edge over the unorganized retailers. Unorganized retail accounts for 97 percent of the total retail trade. Allowing FDI in multi-brand retail will certainly affect the survival of the unorganized sector. Unorganized retailers who have already been facing tough competition from the domestic organized retailers will have to face retailers like Tesco, Walmart, etc. Small traders, shop owners and farmer organizations find the proposal shocking and say it would endanger the livelihood of four crore (40 million) people directly engaged in retailing food and non-food items, and twenty crore people depend on them (Sify Finance, 2010). England which allowed MNCs and FDI into multi brand retail sector in 1980 saw over 4.5 lakh people lose employment and over 25,800 retail shops shutting down owing to this decision. The impact was similar in the Asian countries of Thailand and even in Japan (Jagadeeran, 2010).
Employment generation, which is expected from FDI in multi-brand retail shall be nullified as many retailers will lose their business owing to tough competition. India has 35 towns, each with a population of over one million. If Wal-Mart were to open a store in each of these of these cities, and they reach the average Wal-Mart performance per store, we are looking at a turnover of over ₹ 80,330 mn with only 10,195 employees. Extrapolating this with the average trend in India, it would mean displacing about 4,32,000 persons if large FDI driven retailers were to take 20 percent of the retail trade, as the now somewhat hard-pressed Hindustan Lever Limited anxiously anticipates, this would mean a turnover of ₹ 800 billion. This would mean an employment of just 43,540 people, displacing nearly a million people employed in the unemployed sector (Guruswamy, Sharma, Mohanty & Thomas, 2005).

2) Unfair Trade Practices : Due to their financial strength and technical expertise, the organized retailers have got a competitive edge over small unorganized retailers. Moreover, they are in a position to get the produce from farmers and small manufacturers at the price that they want to pay. Farmers and small industries in India are not organized. They do not have any bargaining power and after FDI in multi-brand retail, they will be at the mercy of their buyers. Small producers organized into something like Amul, are a different kettle of fighting fish altogether. Then again, without rural electricity and large scale new investment in surface water management, farmers would be hard put to produce more, even with technical inputs from big retail (The Economic Times, 8th July, 2010).
The organized retailer would be on the dictating terms. Allowing FDI in multi-brand retail means further strengthening of organized retailers. Organizations like *Kisan Jagriti Manch, Bhartiya Majdoor Sangh*, and merchant associations from across the country, said that small-scale manufacturers and farmers would be forced to sell their products at cheaper and uneconomic prices dictated by the Multi National Corporation (MNC) and create oligopolistic market conditions in retail trade. There are merely 10 crore (100 million) enterprises (SME & Traders) in India, and it is believed that they are growing at the rate of 15 percent annually. MNCs with their predatory pricing policies and large cash reserve will crush our retailers (The Financial Express, 6th Sep., 2010). Praveen Khandelwal, General Secretary, Confederation of All India Traders Association said that global retailers owing to their outsourcing skills, resources and facilities from the government, will be able to crush competition and charge monopolistic prices (Khandelwal, 2010). In the paper presented by DIPP, the main focus was on value chain intermediaries. It was mentioned that due to intermediaries, the farmers are getting only 1/3rd of the total price paid by the customers, and 2/3rd of total price are retained by small retailers. Since 2005, big corporate houses have been engaged in retail operations, and their prices are either higher than, or are at par with the market price. This establishes that two thirds of the total margin is kept by these big retailers, and they are not ready to sell their products at a lower price. Nick Robbins wrote in the context of the East India Company, *"by controlling both ends of the chain, the company could buy cheap and sell dear."*(Robbins, 2004).

CONCLUSION AND SUGGESTIONS

The Indian retail sector has been a great source of employment. With a lack of employment opportunities in other sectors, this sector has been proving to be a panacea for the employment seekers. The retail sector is the largest sector in India after agriculture, accounting for over 10 percent of the country's GDP and around 8 percent of the employment. India has the most unorganized retail market in the world. Most retailers of the unorganized retail market have their shops in the front and at the back of their houses. The owners of these retailing outlets are non-professionals. Generally, these types of retailing outlets are inherited from parents. With the passage of time, the face of Indian retail has been changing. There are new types of retailing businesses, which are being run by professionals and are in the organized form. Textile companies like Raymond, Grasim, Bombay Dyeing, etc. witnessed the opening up of retail chains. Later, Titan came up by opening showrooms selling watches, creating and organizing the retailing concept successfully. Since late 1990s, new companies like – Big Bazar, Food World, Subhiksha, Crossword, Planet- M, etc. have come up with the modern retailing concept. It is the era of liberalization, globalization and privatization, where the whole world has become a global village. The whole economy has been opening up. The Indian retail sector has not been an exception to this. India has already allowed 51 percent foreign direct investment (FDI) in single-brand retail and 100 percent FDI in cash-and-carry or wholesale trading. Now, there is a proposal from DIPP to allow 51 percent Foreign Direct Investment (FDI) in multi-brand retail. There are lots of discussions going on as to whether FDI in multi-brand retail is to be allowed or not. A lot has been said in its favour and against it. It is quite sure that FDI in multi-brand retail has to be allowed, sooner or later. The G- 20 mandates its member countries to open up to FDI in retail. We are under an international obligation to open up for FDI in retail (Sharma, 2010).

The Indian retail sector has been facing the problem of back-end infrastructure. There are lots of gaps in the supply chain. It is expected that the FDI in multi-brand retail will build up the supply-chain infrastructure, remove the artificial scarcity of goods, help the farmers and small manufacturers get their due for their produce, curb inflation, remove the intermediaries, provide better assortment to the consumers at cheap price, global market accessibility, etc. In the discussion paper by DIPP, the example of Indonesia, Chile, Russia, Thailand and China, who allowed FDI in retail, has been given. Our economic structure, policies, preferences are quite different than of those countries. Allowing FDI in multi-brand retail straight away would not be appropriate on this basis. India has already allowed 100 percent FDI in the cash-and-carry system or wholesale retailing. However, it has not shown much improvement on back-end infrastructure, where the Indian retailing sector is struggling. It was also found that supermarkets that are supposed to create back-end infrastructure chains also get their supply for fresh produce from the same *mandis* that feed hawkers and efforts to procure directly from farmers remain largely on paper (Subramaniam, 2010). Nothing prevents foreign investment from flowing into the back-end logistics business, which is vital for wholesale, the ground reality, however, is that not much overseas investment is flowing into the wholesale and back-end (Sharma, 2010).

It is the assumption that the FDI in multi-brand retail will help in getting good prices of the produce to the farmers and small manufacturers by removing the middlemen. In fact, big retailers do not squeeze out middlemen from the food chain. Middleman by definition means someone who is between the producers and the consumer. Wal-Mart claims that it removes the middleman. In fact, it only replaces the plethora of small middlemen. Wal-Mart is itself a middleman. The drop in the farmer's income is ,therefore, shared by the new batteries of middlemen, who replace the traditional middleman, who are the quality controller, certification agencies, packaging industry, processors, wholesalers, etc.. Therefore, the removal of middlemen is not possible, but the nature of middlemen can be replaced. Further, Union Minister for Food Processing Industries, Government of India, is of the view that FDI will help farmers' produce to be sold in the world market through linkage with FDI companies. The big chain will not go to the small and rural markets, so the fear that *artiyas* (middleman) and small vendors will be hurt is unfounded (Sahai, 2010). Increased corporate control over food and agriculture has meant that profits are being shared among the traders, processors, wholesalers and retailers. This is not only limited to the developing countries, it can also be seen in developed countries. In the US until 1990, a farmer used to receive about 70 percent of every dollar spent on food. Today, it is no more than 3 to 4 percent (Sharma, 2005). Moreover, once it is supposed that the FDI in multi-brand retail will help in removing the middlemen from the system, it will gain the monopoly in the market and act according to its interest. The diversion of commission from middlemen to the farmers would become impossible, but certainly it would go to the retailers themselves as our farmers are unorganized and they do not have the bargaining power. With regards to creation of employment opportunities, FDI in multi-brand retail will certainly create job opportunities for those people who are skilled and trained. However, there is a lot of workforce in India, who is unskilled. Skilled and trained persons have never been the problem for our policy makers. Therefore, it is not going to help in removing our basic problem. Further, stiff competition from the global retail giants like Wal-Mart, Tesco, etc. are certainly going to oust our small and unorganized retailers. Providing employment to the displaced persons would be a further challenge for our policy makers as they are either unskilled or semi-skilled. Further, growth in the manufacturing and agriculture sector has not been enough to absorb the displaced ones.

SUGGESTIONS

The Indian retail sector in multi-brand retail is not ready to open up in the present situation. However, surely, it is going to open up in the near future. By the time it opens up, enough improvements are to be done at the front and back- end infrastructure. Instead of waiting for FDI to create infrastructure in this sector, it is time for Government and various trade associations to take initiatives for creating infrastructure for themselves. Just waiting for foreign investors to come and invest would not be appropriate. However, whenever FDI is allowed in multi-brand retail, they may certainly be compelled to utilize a certain percentage of the amount towards upgradation /creation of back-end infrastructure facilities, such as development of post-harvest and cold-chain infrastructure near the farmers' field, logistics or agro processing facilities. Initially, the cash-and-carry business was opened with the intention of allowing FDI in wholesale trading. There are instances where these businesses actually become a retail trade in the garb of cash and carry. Thereafter, single brand retailing was allowed through outlets. The next step in this direction was to allow Indian companies to set up retail stores ostensibly without FDI, but actually granting permission for Indian companies to be in front office, with a foreign investor at the back office, in the garb of cash and carry (The Financial Express, 6th Sep., 2010).

The Indian retail sector is in its nascent stage and ,therefore, it is important that the domestic retail sector would be allowed to grow and consolidate first before opening this sector to foreign investors. FDI in multi-brand retail may be allowed after giving full opportunity to the unorganized retailers and small manufacturers to unite or be competitive. It would not be possible for the unorganized retailers to transform themselves into organized retailers at a large scale, therefore, cluster approach must be adopted for this. A breathing space of 5 to 10 years should be given to the unorganized retail sector so as to enable it to re-orient its strategies. Further, technical assistance and proper training must be provided to retailers for handling storage, transport, grading, sorting, maintaining hygiene standards, packing, etc. The Government comes up with the certain tax policies time to time, focusing on developing certain areas. This time too, the Government has come up with a tax exemption scheme, under which if ₹ 20,000 is invested in certain infrastructure bonds, such an investment shall be free from tax. Such types of policies can also be initiated in creating and developing back-end infrastructure or cold chains. Besides issuing bonds, the banks and other financial institutions must be encouraged to sanction credit at low interest rates for the development and creation of infrastructure.

There is a fear that if big foreign retailers enter the market, they can create tough competition for the small retailers. Thus, survival of these retailers would only be possible if they become competitive. Even after proper opportunity, if it is not possible for the small retailers to be in the competition, they certainly have to leave the arena. If this is the case, then avenues for their settlement will have to be looked into. For that, we have to see other areas where employment opportunities are present. Our manufacturing and agriculture sector has not shown that much progress. Service sector is the only sector where there is some spurt. We have to strengthen our agriculture and manufacturing sectors so that more and more employment opportunities can be created, and the displaced from the retail sector could easily be absorbed in them.

With their financial strength, the foreign players may be involved in unfair trade practices. They have the capacity to influence the market. At the early stage, when they have to access the market, they can fix the prices at the lowest level, as they have the ability to face loss for even a longer time as compared to small retailers. As and when they oust those small retailers from the market, they will be in a position to dictate the terms. The same situation can prevail with farmers. For eradicating traditional intermediaries, they can fix the prices higher than the market rate, but when they succeed in removing intermediaries, they will start to pay a lesser amount for the procured produce. High unemployment, especially unskilled unemployment rates made it imperative that mom and pop stores be allowed to function. Therefore, it is needed to make certain changes in the legislation that help in controlling the unfair trade practices. The focus should not be only on making of laws, but strict adherence to laws must be encouraged. Therefore, there should be some effective mechanism to control the unfair trade practices. Countries like China, Malaysia and Thailand, who opened their retail sector to FDI in the recent past, have been forced to enact new laws to check the

prolific expansion of the new foreign malls and hypermarkets (Tarun, 2004).
Creating employment opportunities for rural youth is the main concern of our government since independence. FDI in multi-brand retail can provide employment opportunities to these rural youth. It is upon the government agencies and various organizations to frame certain policies with the help of which these rural youth can be encouraged and trained as per the requirement of these big retailers.
There are a number of people in India, who are living below the poverty line. If every thing is controlled and let free as per the prevailing market conditions, these people are certainly going to be affected. Therefore, besides allowing FDI, the public distribution system also needs to strengthen itself to safeguard the interests of these people. Small scale industrial sector has great significance in the development of our economy due to its high employment potential, small gestation period, relatively limited financial requirements and also has the capacity to balance regional development. It constitutes 95 percent of industrial units, contributes 40 percent of industrial output and 35 percent of national export. Looking at the importance of this sector, it needs to be protected. Therefore, there must be some provisions that retailers will be encouraged to buy their supplies from the small and medium enterprises. There must be certain amount of purchases made by big retailers compulsorily from the small and medium manufacturers. However, there should not be any compromises in regards to the standards of produce.

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