

Impact Of Foreign Direct Investment In Indian Retail Sector With Reference To Andhra Pradesh

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Abstract

The Government of India was initially very apprehensive of the introduction of the Foreign Direct Investment in the Retail Sector in India. The unorganized retail sector as has been mentioned earlier occupies 98 per cent of the retail sector and the rest 2 per cent is contributed by the organized sector. Hence one reason why the government feared the surge of the Foreign Direct Investments in India was the displacement of labour. There are different viewpoints on the impact of FDI in the retail sector in India, According to one viewpoint, the US evidence is empirical proof to the fact that FDI in the retail sector does not lead to any collapse in the existing employment opportunities. There are divergent views as well. According to the UK Competition Commission, there was mass scale job loss with entry of the hypermarkets brought about by FDI in the UK retail market. This paper highlight is Introduction & Definition of Retail, Division of Retail Industry, FDI Policy in India, and impact of FDI in various dimensions.

KeyWord: FDI, Labour, GDP, Competition, Retail sector.

1. Introduction

India being a signatory to World Trade Organization's General Agreement on Trade in Services, which include wholesale and retailing services, had to open up the retail trade sector to foreign investment. There were initial reservations towards opening up of retail sector arising from fear of job losses, procurement from international market, competition and loss of entrepreneurial opportunities. However, the government in a series of moves has opened up the retail sector slowly to Foreign Direct Investment (FDI). In 1997, FDI in cash and carry (wholesale) with 100 percent ownership was allowed under the Government approval route. It was brought under the automatic route in 2006. 51 percent investment in a single brand retail outlet was also permitted in 2006. FDI in Multi-Brand retailing is prohibited in India.

2. Definition of Retail

In 2004, The High Court of Delhi defined the term 'retail' 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.

Thus, retailing can be said to be the interface between the producer and the individual consumer buying for personal consumption. This excludes direct interface between the manufacturer and institutional buyers such as the government and other bulk customers retailing is the last link 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 margin of profit.

Division of Retail Industry: The retail industry is mainly divided into:

- 1) Organized and
- 2) Unorganized Retailing.

Organized retailing refers to trading activities undertaken by licensed retailers, that is, those who are registered for sales tax, income tax, etc. These include the corporate-backed hyper markets and retail chains, and also the privately owned large retail businesses.

Unorganized retailing, on the other hand, refers to the traditional formats of low-cost retailing, for example, the local *kiranashops*, owner manned general stores, *paan/beedi* shops, convenience stores, hand cart and pavement vendors, etc.

The Indian retail sector is highly fragmented with 97 per cent of its business being run by the unorganized retailers. The organized retail however is at a very nascent stage. The sector is the largest source of employment after agriculture, and has deep penetration into rural India generating more than 10 per cent of India's GDP.

3. Indian FDI policy

FDI as defined in Dictionary of Economics (Graham Bannock et.al) is investment in a foreign country through the acquisition of a local company or the establishment there of an operation on a new (Greenfield) site. To put in simple words, FDI refers to capital inflows from abroad that is invested in or to enhance the production capacity of the economy. Foreign Investment in India is governed 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 regard 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 amended from time to time.

The Ministry of Commerce and Industry, Government of India is the nodal agency for motoring and reviewing the FDI policy on continued basis and changes in sectoral policy/ sectoral equity cap. The FDI policy is notified through Press Notes by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP). The foreign investors are free to invest in India, except few sectors/activities, where prior approval from the RBI or Foreign Investment Promotion Board ('FIPB') would be required.

4. FDI Policy with Regard to Retailing in India

It will be prudent to look into Press Note 4 of 2006 issued by DIPP and consolidated FDI Policy issued in October 2010 which provide the sector specific guidelines for FDI with regard to the conduct of trading activities.

1. FDI up to 100% for cash and carry wholesale trading and export trading allowed under the automatic route.
2. FDI up to 51 % with prior Government approval (i.e. FIPB) for retail trade of 'Single Brand' products, subject to Press Note 3 (2006 Series)
3. FDI is not permitted in Multi Brand Retailing in India.

5. Foreign Investor's Concern Regarding FDI Policy in India

For those brands which adopt the franchising route as a matter of policy, the current FDI Policy will not make any difference. They would have preferred that the Government liberalize rules for maximizing their royalty and franchise fees. They must still rely on innovative structuring of franchise arrangements to maximize their returns. Consumer durable majors such as LG and Samsung, which have exclusive franchisee owned stores, are unlikely to shift from the preferred route right away. For those companies which choose to adopt the route of 51% partnership, they must tie up with a local partner. The key is finding a partner which is reliable and who can also teach a trick or two about the domestic market and the Indian consumer. Currently, the organized retail sector is dominated by the likes of large business groups which decided to diversify into retail to cash in on the boom in the sector – corporate such as Tata through its brand Westside, RPG Group through Food world, Pantaloon of the Raheja Group and Shopper's Stop. Do foreign investors look to tie up with an existing retailer or look to others not necessarily in the business but looking to diversify, as many business groups are doing?

An arrangement in the short to medium term may work wonders but what happens if the Government decides to further liberalize the regulations as it is currently contemplating? Will the foreign investor terminate the agreement with Indian partner and trade in market without him? Either way, the foreign investor must negotiate its joint venture agreements carefully, with an option for a buy-out of the Indian partner's share if and when regulations so permit. They must also be aware of the regulation which states that once a foreign company enters

into a technical or financial collaboration with an Indian partner, it cannot enter into another joint venture with another Indian company or set up its own subsidiary in the 'same' field' without the first partner's consent if the joint venture agreement does not provide for a 'conflict of interest' clause. In effect, it means that foreign brand owners must be extremely careful whom they choose as partners and the brand they introduce in India. The first brand could also be their last if they do not negotiate the strategic arrangement diligently.

6. FDI in Single Brand Retail

The Government has not categorically defined the meaning of "Single Brand" anywhere neither in any of its circulars or nor any notifications. In single-brand retail, FDI up to 51 per cent is allowed, subject to Foreign Investment Promotion Board (FIPB) approval and subject to the conditions mentioned in following

1. Only single brand products would be sold (i.e., retail of goods of multi-brand even if produced by the same manufacturer would not be allowed)
2. Products should be sold under the same brand internationally,
3. single-brand product retail would only cover products which are branded during manufacturing and
4. Any addition to product categories to be sold under "single-brand" would require fresh approval from the government.

7. FDI in Multi Brand Retail

The government has also not defined the term Multi Brand. FDI in Multi Brand retail implies that a retail store with a foreign investment can sell multiple brands under one roof. In July 2010, Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce circulated a discussion paper on allowing FDI in multi-brand retail. The paper doesn't suggest any upper limit on FDI in multi-brand retail. If implemented, it would open the doors for global retail giants to enter and establish their footprints on the retail landscape of India. Opening up FDI in multi-brand retail will mean that global retailers including Wal-Mart, Carrefour and Tesco can open stores offering a range of household items and grocery directly to consumers in the same way as the ubiquitous 'kirana' store.

Talking about the organized sector, which consists of big Indian players who have entered in retail sector just to take advantage of diversification and expand their business, they will also be affected but from different prospects. Major challenges that lie ahead are:

1. **Economies of scale:** the global players have economies of scale and are perfect in cost cutting and providing the consumer the best at lowest price

which still is a major challenge for Indian retail firms. The way they perform their process itself builds an entry barrier for other new firms

2. **Brand name:** They bring with them world class products which have high quality and a highly valued brand name. The domestic brands don't have that charm and attracting power as of global brands.
3. **Technology:** Global players are highly advanced in technology. The tools, equipments, kind of warehouses they use, their way of performing processes are highly advanced and cannot be compared with those used by Indian retail firms, which in turn provides better services and better quality products even in categories like perishable food etc.
4. **Attract skilled employees:** The work culture of global players is quite different from those of Indian players. They believe in earning profits by cutting costs as much as possible and at the same time are conscious towards career of their employees. Their approach is more oriented towards achieving ends rather than means. Attractive salary and high incentives can also attract skilled employees towards global players which is also a threat for big Indian retail firms.
5. **Better infrastructure:** Better storage facilities, better transportation medium and high investment can pose another threat to Indian retail firms which can hardly match the capabilities of giants own their own.
6. **Joint ventures:** Global players may not prefer to enter into joint ventures with Indian firms and may also close down the existing ventures in wholesale and single brand which may adversely affect the Indian firms.

8. Impact of FDI in various Dimensions

8.1 Impact of Government decision to allow 51% FDI in multi-brand retail

The study shows that the 65 per cent of the people of Andhra Pradesh society supported the government decision to permit 51per cent FDI in multi-brand. This means that they liked to have foreign brands in India. The rest 35per cent people of Andhra Pradesh society were not supporting the government decision to permit 51per cent FDI in multi-brand. This means that they were having the fear of the foreign trade and were of the view that it can repeat the history where East India Company came to India in the past and captured India through the business.

8.2 Impact on farmers over FDI in retail

The study shows that the 68per cent of the people of Andhra Pradesh society were of the view that the Indian farmers will be benefitted by the FDI in retail. This means that they are of the view that Indian farmers will get good payment for their produces, without the agent in between the two parties. There will be good storage techniques and transportation techniques. The rest 28per cent of the people of Andhra Pradesh society were of the view that the Indian farmers will not be benefitted by the FDI in retail because they were of the view that

Indian farmers will not get the advantage as it is a myth. There will be some irregularities. The left over 4per cent were not having the adequate information about the recent issue.

8.3 Impact of Foreign big retails will reduce the purchase from local stores

The study shows that the 69per cent of the people of Andhra Pradesh society disagree that foreign big retail will reduce the purchase from local stores. This means that they are of the view that foreign big retail will have their own market while local stores will continue with their available market without much change in it. The rest 26per cent of the people of Andhra Pradesh society were of the view that foreign big retails will reduce the purchase from local stores because the market of local stores will make a switch over to foreign big retails. The left over 5per cent were not having the adequate information about the recent issue.

8.4 Impact on consumers over FDI in retail

The study shows that the 88per cent of the people of Andhra Pradesh society were of the view that the Indian consumers will be benefitted. This means that majority were of the view that Indian consumers will get lot of opportunities in terms of purchasing the products. The rest 10per cent of the people of Andhra Pradesh city were not of the view that Indian consumers will be benefitted because they were highly satisfied with the swadesh products in terms of price and availability. The left over 2per cent were not having the adequate information about the recent issue.

8.5 Impact on other Indian industries over FDI in retail

The study shows that the 35per cent of the people of Andhra Pradesh society were of the view that the other industries will be benefitted over FDI in retail. This means that they were of the view that other industries will get good business through partnership, supply of raw material, giving of land or building and other means which will lead them good profits. The rest 24per cent of the people of Andhra Pradesh city were of the view that the other industries will not be benefitted by this action. They were of the view that it is a false because the foreign big retail will try to depend on their people for business. The leftover was in majority with 41per cent saying it is a very difficult situation to say whether FDI in organized sector will benefit or not. One reason can be as usual that they are not having the adequate information about the recent issue. The other can be that consumers can give information's better about purchasing than business because there can be job holders and house-wives.

8.6 Impact on un-organized retail sector over FDI in retail

The study shows that the 76per cent of the people of Andhra Pradesh society were of the view that the un-organized retail sector will not be benefitted by the FDI in retail. This means that majority of the people of Andhra Pradesh society were of the view that the organized retail sector will capture the un-organized

retail sector. The rest 18per cent of the people of Andhra Pradesh city were of the view that there will be no major impact of organized retail sector over the un-organized retail sector in India. The left over 6per cent were not having the adequate information about the recent issue.

9. Conclusion

The future of foreign retail players is also uncertain like that of Indian retail players. Apprehensions were raised on many such occasions in the past on virtually every measures of liberalization of Indian economy but most of the apprehensions proved wrong while many others come true. It is better to act and watch than not to act at all. The government has added an element of social benefit to its latest plan for calibrated opening of the multi-brand retail sector to foreign direct investment (FDI). Only those foreign retailers who first invest in the back-end supply chain and infrastructure would be allowed to set up multi brand retail outlets in the country. The idea is that the firms must have already created jobs for rural India before they venture into multi-brand retailing.

It can be said that the advantages of allowing unrestrained FDI in the retail sector evidently outweigh the disadvantages attached to it and the same can be deduced from the examples of successful experiments in countries like Thailand and China where too the issue of allowing FDI in the retail sector was first met with incessant protests, but later turned out to be one of the most promising political and economic decisions of their governments and led not only to the commendable rise in the level of employment but also led to the enormous development of their country's GDP. Moreover, in the fierce battle between the advocates and antagonist of unrestrained FDI flows in the Indian retail sector, the interests of the consumers have been blatantly and utterly disregarded. Therefore, one of the arguments which inevitably need to be considered and addressed while deliberating upon the captioned issue is the interests of consumers at large in relation to the interests of retailers.

The Industrial policy 1991 had crafted a trajectory of change whereby every sectors of Indian economy at one point of time or the other would be embraced by liberalization, privatization and globalization. FDI in multi-brand retailing and lifting the current cap of 51% on single brand retail is in that sense a steady progression of that trajectory. But the government has by far cushioned the adverse impact of the change that has ensued in the wake of the implementation of Industrial Policy 1991 through safety nets and social safeguards. But the change that the movement of retailing sector into the FDI regime would bring about will require more involved and informed support from the government. One hopes that the government would stand up to its responsibility, because what is at stake is the stability of the vital pillars of the economy- retailing, agriculture, and manufacturing.

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