



## The FDI permit for multi brand retail trading in India - Green signal or Red signal

### Abstract

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The Indian consumers have undergone a remarkable transformation. Just a decade or two ago, the Indian consumers saved most of their income, purchased the bare necessities and rarely indulged themselves. Today, armed with a higher income, credit cards exposure to the shopping culture of the west and a desire to improve their standard of living, the Indian consumers are spending like never before. Organized retail with its variety of products and multitude of malls and supermarkets is fueling their addiction. Their new mentality, in turn, is fueling the growth of organized retail in India. This paper firstly speaks about the global giants' entry to India and their myths and realities. The second part shows the status of organised food retailing in India with SWOT Analysis and highlights on farmer's issues towards FDI in multi brand retailing. The third part overviews the two faces of retail sector – Challenges and key success factors. The fourth part reviews the impact of Organized Retailing on the Unorganized Sector. The last part reveals the recommendations before allowing FDI in Multi brand Retailing.

### Introduction

Organised/Modern retailing refers to trading activities undertaken by licensed retailers and includes formats such as hypermarkets and supermarkets, and retail chains. Organised Retail, valued at INR 96500 Crores in 2008, accounts for around 5% of the total retail market. Organised Retail has been growing at an impressive rate of 35% to 40% Y-O-Y in the last few years compared to 9-10% growth in the overall retail industry.

Retail in India is essentially "unorganized." 98% of the retail industry is made up of counter-stores, street markets, hole-in-the-wall shops and roadside peddlers. The term "unorganized retail" is better understood when comparing this form of retail to the organized retail that one is familiar with in developed countries. Unorganized retail is characterized by Family-run stores, lack of best practices when it comes to inventory control and supply-chain management, lack of standardization and essentially a sector populated by anyone who has something to sell.

Unorganized Retail is essentially the next-step above agriculture for those seeking to climb the ladder of affluence in search of a higher income. Recognizing the short-term

and long-term growth of retail in India, a number of domestic business giants have entered the retail industry or are planning to do so in the near future. Some like Pantaloon Retail, Shopper's Stop and Pyramid Retail have been in the industry for a decade. Others like Reliance Retail Ltd. (RRL) (RRL is part of the Mukesh Ambani run Reliance Industries Ltd., one of India's largest industrial houses) have entered and Birla (Also known as the Aditya Birla Group, another large industrial house with various business interests) and Bharti (India's largest cellular service provider) opened up a number of stores across the country.

French supermarket giant Carrefour has opened its first cash and carry store in India, hoping the government will soon relax restrictions on foreign investment in its massive retail sector. The 5,200 sq. m. wholesale store in the east of the capital New Delhi and is open to food companies, institutions, restaurants and retailers. The arrival in India of Carrefour - the world's second-largest retailer - comes some years after its main rival in the sector. US giant Wal-Mart has already opened two wholesale stores and plans to open 10 more within four years. India agreed in 2006 to allow foreign investment of up to 51 per cent in the retail sector but only for shops selling single-branded products like Reebok, forcing

overseas companies to sign franchise agreements with Indian firms. Wal-Mart signed a partnership agreement in 2006 with India's Bharti Enterprises while Britain's Tesco formed a tie-up with the giant Tata Group conglomerate. The arrival of foreign companies into the Indian retail sector is a sensitive issue, as small shopkeepers fear being driven out of business by multinationals. Industry bodies want the retail sales sector to be liberalised gradually but calls for the market to be opened up to foreign competition have increased in recent months, notably during visits by Western leaders. Both US President Barack Obama and his French counterpart Nicolas Sarkozy urged India to remove restrictions on foreign trade and investment.

Each of these domestic and international retail giants have or will introduce a number of modern retail formats like malls, hypermarkets and supermarkets. Initial consumer response to these novelties in the retail sector has been very promising and as the middle-class continues to grow, organized retail in India is sure to see large returns. In fact, organized retail is growing at a staggering 35% per year.

As organized retailers enter the Indian market, however, they must be mindful of the unique status of retail in the country. Retail in the country has been dominated by millions of unorganized retailers who have used consumer proximity and home-delivery as their operating ideals to cater to the Indian consumer that has become accustomed to this convenience. Unorganized retail has both shaped the mentality of the Indian consumer and been shaped by it.

Another factor that major retailers must be wary of is the lack of infrastructure to support supply chains and efficient retail operations in India. Companies like Wal-Mart that grew from the ground-up leveraged the infrastructure of U.S.A to build a large supply-chain which has been the backbone of its success. The story in India is very different. Inadequate highways, the absence of cold storage facilities, an underdeveloped supply chain, limitless bureaucracy and the lack of regulations created a situation where the local corner-stores and hawkers thrived. What was the street-vendors gain will be a major hurdle for large-scale organized retailers. They will have to demonstrate unprecedented innovation, adaptation and experimentation to succeed in the Indian retail industry.

## Review of Literature

Organized retail, one of the most notable emerging sectors of the Indian economy, continues to attract significant investments and interest from leading national and international retail players. It has also generated considerable opposition from small traders and shopkeepers who are worried about the impact of large-scale organized retail on their businesses. As a result, the government has been forced to carefully examine the long-term implications of organized retail in India.

Indian traditional retailers have a number of inherent strengths which helped them not merely survive the competition from organized retail but flourish. These include proximity to consumers, consumer goodwill, credit sales and amenability to bargaining, sale of loose items, convenient timings and home delivery. The Indian Council for Research on International Economic Relations (ICRIER) study (M. Joseph and N. Soundararajan, 2009) 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.

A study conducted by 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.

India stands out as an example for the late coming of modern organized retail in emerging markets and also for the kind of

restrictions placed on foreign investments in retail. The arrival of modern retail in developing countries occurred in three successive waves (Reardon and Hopkins, 2006; Reardon and Berdegue, 2007). The first wave took place in the early to mid-1990s in South America, East Asia outside China, North-Central Europe and South Africa. The second wave happened during the mid to late 1990s in Mexico, Central America, Southeast Asian countries, Southern-Central Europe. The third wave began in the late 1990s and early 2000s in parts of Africa, some countries in Central and South America, Southeast Asia, China, India, and Russia.

According to the authors, the main reason why the third wave countries which include China, India and Russia lagged behind was the severe restrictions on foreign direct investment (FDI) in retailing in these countries. The demand side features of these countries, such as income, size of the middle class, urbanization, and the share of women in workforce, etc., have been similar to countries in the second wave. In China and Russia these restrictions were progressively relaxed in the 1990s and in India only partially in the 2000s. In January 2006, India allowed foreign companies to own up to 51 per cent in single-brand retail joint ventures (JVs), but multiple brand foreign firms are still barred in retail although they can set up wholesale operations.

The domestically driven organized retail expansion in India is facing difficulties. The food inflation in the country has stayed high for some time now. The gap between the farm level prices and consumer prices is very high in India which has not come down with the expansion of organized retail. Why? While the number of domestic restrictions on the operation of organized retail in India is partly responsible for this, the ban on foreign entry into multi-brand retailing is also partly responsible.

India permitted foreign direct investment in cash-and-carry wholesale trade up to 100 per cent through the automatic route and in single-brand retail up to 51 per cent in 2006. The former brought in US\$ 1.8 billion during April 2000 to March 2010 and the latter just US\$ 195 million during April 2006 to March 2010. India perhaps remains the only exception in emerging economies in barring the multi-brand retail for foreign investment. The reason why India has not allowed FDI in multi-brand retail is the fear that it will harm the traditional small retailers.

## Research Objectives

Having presented the immense potential and current status of the entry of the global giants to Indian retail industry, this paper continues to flesh out the Indian retail story with the objective of highlighting some of the major concerns that organized retailers will have to consider as they venture into the Indian market.

The objective of the paper has five dimensions:

- Discussion about the myths and realities of global giant's entry to India.
- Status of organised food retailing in India with SWOT Analysis and highlights on farmer's issues towards FDI in multi brand retailing.
- Overview the two faces of retail sector – Challenges and key success factors.
- Review the impact of Organized Retailing on the Unorganized Sector.
- Recommendations before allowing FDI in Multi brand Retailing.

## Global Giants in India

### Wal-Mart

Wal-Mart has emerged as one of the largest corporations in the world, and definitely the largest in retail. It started only fifteen years ago. In May 2009, Wal-Mart was ready to open its first store in India. The reason for Wal-Mart's entry in India was clear – The Indian middle class. The world's biggest retailer had been silently working on its strategy for India for around two years. Mom-and-pop stores and traditional distribution networks dominated the \$375 billion Indian retail market. Wal-Mart's first outlet was set to launch in the city of Amritsar, Punjab in North India. The first store air-conditioned and built over 50,000 sq. ft. was on the outskirts of the city, Amritsar. The store employed 200 locals and was likely create 500 indirect jobs. In the first few weeks itself, the company had managed to sign on close to 35,000 members.

A typical Wal-Mart store sells 60,000 different items; a super centre sells 120,000 items. Wal-Mart is one of the best beneficiaries of corporate led globalization, and has made communities dependent on supplies from thousands of miles away for everyday items – including the food we eat

and the clothes we wear. If Wal-Mart and other retail chains get a foothold in India, it will mean displacement of small retailers and farmers. Yet Wal-Mart is spreading myths about its corporate reach and its predatory growth. These myths have been totally exposed in the best seller “Wal-Mart effect” by Charles Fishman.

#### **Myth I “Localization”**

In an article Wal-Mart’s vision of India published in the Financial Express, 1st June 2007, Raj Jain, President, emerging markets, Wal-Mart has stated: “One key reason for Wal-Mart’s success is localization. We carry local products from local suppliers that appeal to local tastes, needs and fashions.”

#### **Myth II: “An ally of small retailers”**

Wal-Mart is presenting itself as an ally of the small retailers it will destroy. “The Joint Venture will sell quality merchandise directly to retailers – big and small, including ‘mom and pop’ or kirana stores. The purpose is to establish an efficient supply chain linking farmers and small manufacturers – who have limited infrastructure or distribution strength.”

#### **Myth III: “Provide Quality Jobs”**

“Provide quality jobs to India’s unskilled workforce. We expect to provide direct and indirect jobs to thousands of Indians.”

#### **Myth IV: “Help develop and grow local suppliers”**

Wal-Mart’s profits are based on destroying local production and local retail. In 2004, Wal-Mart bought products from fifty three hundred factories in sixty countries around the world. This is not local supply. Wal-Mart pushes prices so low that local producers cannot supply. In 1991, Ridlen Adhesives was abandoned by Wal-Mart because they could not lower the prices further. As Nancy Ridlen, the owner reports, Wal-Mart said: “We don’t want to pay 50 cents for these glue sticks. We’ll pay 45 cents. Either you take it or we’ll go elsewhere.” This is what has happened to every product, from locks to lawn movers from shirts to jeans. And every producer who was destroyed had been tempted by Wal-Mart’s large volumes. As Jim Wier, who said no to Wal-Mart states: “They had the lure of the Wal-Mart volume? Once they get hooked on the volume, it’s like getting hooked on cocaine. You’ve created a monster for yourself.” Let us not fall into the trap of Wal-Mart’s myths. Let us not create a

monster for India’s small producers and retailers.

#### **Carrefour**

French retail major Carrefour, the second-largest in the world in terms of revenue (euro 90 billion) after Wal-Mart, is going slow in India, even as its rivals are chalking out bold expansion plans in the country.

Ever since Carrefour launched its first store in India, a cash-and-carry wholesale format store at Seelampur, East Delhi on 30<sup>th</sup> December 2010, the retailer has maintained an awkward silence on its expansion plan for the country. Interestingly, Carrefour’s only cash-and-carry store in Asia at present is in India. The group has a total of 151 cash-and-carry stores - 137 in France, 13 in Europe (excluding France) and 1 in Asia.

Experts point out three specific reasons why Carrefour is quiet on its India expansion. First, it wants to be clear about the country’s FDI policy on multi-brand retail before it formulates a concrete cash-and-carry strategy here. (Currently, FDI is not permitted in multi-brand retail, but the government is said to be in a review mode. And, Carrefour has kept its potential Indian partner for multi-brand retail guessing). Second, the French retailer set up shop in India only towards the end of December last year and it may still be watching the market before embarking on an expansion plan. Third, economic slowdown, cost cuts and related business decisions in many of its European markets have forced it to turn more than cautious.

#### **Status of Organised Food Retailing in India – before and after global giant’s arrival**

Organised retailing in food is poised to grow from about Rs.150 billion to about Rs.620 billion by 2020. The share of organised players within total food retail is likely to grow from the current 1.5% to around 2% over these years.

#### **SWOT analysis of organised food retailing**

In any strategic planning process, two factors namely internal and external environmental factors play an important role. A scan of these factors is important for future planning. The environmental factors, which are internal to the retail sector, can be classified as strengths

#### **4.3 Myths and Realities about the Global Giants arrival to India**

	<b>Myths</b>	<b>Realities</b>
<b>Price</b>	Prices of different items are less here.	The rates at which the vendors sell are less as those in the corporate retail shops.
<b>Middlemen</b>	Corporate retail is throwing away middlemen.	They are becoming the new mega middlemen and creating monopolies by becoming the wholesaler, distributor and the retailer.
<b>Employment</b>	They are creating employment. The employment potential projected is 2 million jobs.	They are robbing livelihoods many more times than the number of jobs they are going to create. For creating 2 million jobs they are going to destruct 40 million livelihoods in retail sector.
<b>Better deal or Best deal</b>	Farmers are getting better deal. Corporations are friends of farmers and consumers.	Corporations are buying from existing mandis and not straight from farmers at this point of time, so there is no question of farmers getting a better deal. In future when the corporation will have control over the whole supply chain of food, farmers will have no place to sell other than these corporations. Then our farmers will face monopsony as the farmers of the west are facing now.
<b>Fresh Products</b>	Corporate retail sell fresh.	The hawker sells much fresher than any of these shops. Long distance supply chain and refrigeration means stale fruits and vegetables.
<b>Local Economy Promotion</b>	Corporate retail is promoting local economy.	They have destructed local economy wherever they have gone, and are doing the same in India. Attacks on the reliance stores in Ranchi and Indore are preemptive action by people dependent on local economy.
<b>Efficient Supply Chain Management</b>	Corporate entry will make the supply chain more efficient. They are more scientific than the existing system.	The supply chain gets more centralized, and the average distance traveled by food increases manifolds. In scientific, social and ecological terms this is inefficient compared to our hawkers.
<b>Push or Pull Strategy</b>	There is huge consumer demand for corporate retail.	The corporations are pushing the agenda, never have people in India demanded for corporation led retail.
<b>Grow without Kill</b>	There is room for all, as Indian economy is growing at an enormous pace.	The corporate retail chains cannot prosper without killing the small businesses. The experience of west shows us the truth.
<b>Money saving or money</b>	Corporation led shops sell	Corporations are propagating

wasting shopping	cheap and consumers save the habit of wasteful money shopping there. consumerism among the Indian consumers.
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Organised Food Retailers	Started in the year
Nilgiris	1905
Trinethra Super Retail Limited	1986
Foodworld	1994
RPG Enterprises - Foodworld (In 2005 Spencers)	1994
Pantaloon Retail India Limited (PRIL) - Food Bazaar	2001
Tata Trent Ltd. - Star Bazaar	2004
Wadhwan Group formed Retail Food & Grocery Business	2005
Reliance industries ltd	2006
Aditya birla, Group's foray into the retail sector	2006
Landmark group formed SPAR	2008
Bharti Retail Pvt Ltd launched Easy day	2008

and weakness. The factors, which are external to the sector, can be opportunities and threats. The strategic analysis of environmental factors is referred as SWOT analysis. This analysis provides the information that is helpful in understanding the retail sector resource mobilization and capabilities to the competitive environment in which it operates. Finally, this will be an instrumental in formulation of strategies for future growth and development of the sector.

### Strengths

➤ Most of the organised food retailers have diversified into retailing from other businesses. These highly diversified business groups are able to support the investment requirement of organised retailing business as well as absorb business losses through their own funds.

➤ The parent groups normally have a robust balance sheet, which acts as a strength of the group giving them ability to negotiate funds with banks and institutions.

### Weaknesses

➤ The industry does not have an established business model. Most of the organised food retailers are not making sustainable profits. This has forced all the players to experiment to get an understanding of a viable model for survival and growth.

➤ India has a huge diversity in the food habits, buying pattern, customer attitude, and

the supply chain related issues. This creates hurdles for all organised food retailers to scale up and realize the much necessary economies of scale.

➤ Food retail has retained its commodity nature without any clear brand differentiation among players operating in the market. Hence, customer loyalty to a particular type of organised retailer is very low.

➤ Lack of trained and motivated manpower remains one of the main weaknesses of the organised food retailers. While initially there were some attempts to provide quality training to employees, at present, the players are not keen on such investments. As a result, customer expectation on the quality of staff has come down. Odd hour work, monotonous nature of the work and low salary levels among employees (relative to other comparable urban ventures such as BPO, IT) lead to high employee churn and attrition.

➤ There are genuine problems in demand management and associated planning in case of food retail. Initially, it was thought that proper demand planning could be done with the help of IT. However, it was realized later that a larger issue is that of response time from the supply side, which has to do with suppliers as well as logistics and warehouse management.

➤ The retail sector depends heavily on rented infrastructure. Inability to have a control on the rental cost element is a weakness that the industry has to encounter.

➤ High level of wastage and losses including store level shrinkage remains an important area of concern.

### Opportunities

- The overall retail sector including food retail is poised for an impressive growth in the next 10 years owing mainly to high income growth measured by per capita GDP.
- Researchers have placed the growth of overall retail between 18-40%.
- The progressive decline in customs duty and other non-tariff barriers under the WTO regime liberalization policy of the Government would enable the organised food retailers to import premium foods and international brands. Global sourcing would create more choices for the consumers and improve the attractiveness of organised retailing.
- The proportion of Indian residents who seek international food products is increasing. This is owing to increasing exposure of many Indians towards foreign products by their visits abroad and through the increasing NRI population.
- The consumer attitude in India is changing. This change is marked by an attitude towards saving, debt and deferred payment (credit card etc.). This is in favour of organised food retailers as they can develop schemes to purchase on debt (credit card, payment in installments etc).
- The idea of 'India as a consumer' has been accepted globally in the last 10 years. The result has been strong MNC product flows into India and our doors have just opened up.
- The openness of the government to review some of its policies such as policy on FDI investment in multi-brand retail, policy on reforming agricultural marketing systems is an important opportunity in the present context which is going to favour

huge capital investment in the sector. The FDI investments from the countries where the organised retail has attained steady phase can bring the experience, knowledge and also strategies for India.

- Government also have initiated schemes like Terminal markets to create rural infrastructure. This could bring competitive marketing advantage for farmers produce.
- Unexplored rural organised retailing is a great opportunity in front of the retail sector.
- In the existing supply chain, a considerable portion of the produce is wastage due to handling and bruises damages caused. Particularly in case of perishable commodities like Fruits and Vegetables, the direct procurement can reduce such losses to 7% by increasing efficiency up to 17% at the same time. Currently the prices of commodities are skyrocketing; tapping such wastage by investment in supply chain could be an opportunity.

### Threats

- Regulatory threats- Unfortunately, many growth levers for organised retail are outside the industry. Be it clarity on FDI in organised retail, implementation of agricultural reforms by the states facilitating direct procurement and so on. In a functional democracy such as India, decision-making on such vital issues is often long-drawn.
- Policy threats- Government is deeply concerned with food inflation in the last 12 months. One of the areas that economists point out is the widening difference between wholesale prices and retail prices. The general perception in this regard is tilted against organised retailing and thus, it might slow down growth.
- Competition from FMCG-backed unorganized retailing could reduce the appeal of organised retail. This is expected to have a more profound effect in case of the food-retailing category.
- Our primary survey with organised retailers reveal that in the existing supply chain, the retailers are

uncomfortable in handling perishable commodities. This is due to multiple handling and the lack of rural infrastructure facilities.

- Decreasing turnover due to mushrooming of unorganised outlets is posing threat for the sector as a whole and is affecting both unorganised and organised food retail. The competition in the sector is increasing and could impact turnover and profits.
- Lack of uniform tax system for retailers is a burden which constrains the establishment of an efficient pan India supply system. The goods and services tax is expected to stream line the tax structure. However, it is facing many hurdles in its final implementation.
- Amendment to APMC act in inviting private partners to establish a direct marketing system is mooted. But there is an opposition from majority state governments fearing that they may lose market fee. The progress in the direction of implementing second-generation agricultural marketing reforms is very slow.

The organised food retail sector does not have much strength except the back up of the promoters. The sector should look for the upcoming opportunities to develop a competitive advantage between strengths and opportunities. At the same time the sector can overcome the weakness in order to prepare itself to take up the compelling opportunity. Thus, along with the strengths and opportunities the defensive mechanism for threats and weakness are to be countered through a balanced strategy. The Government support is needed for the sector in a balanced way by taking steps such as opening up the FDI in multi-brand retail, initiating second-generation reforms in the agricultural marketing with adequate safeguards to ensure that the interests of the producers and the consumers are not harmed in the process.

#### **FDI in Organised Retail industry-Farmers' perspective**

Multi-brand global retail giants like the Wal-Mart, Metro and Carrefour have entered and may enter into multi brand retail in Indian retail markets if this bill gets approved.

However, the expansion of supermarkets in developing countries is expected.

In India, growing middle class with changing consumption patterns are ideal for supermarkets to prosper. The total size of Indian retail sector, including organized and unorganized sector is \$300 billion, where currently the organized sector accounts for 2% only but near future the supermarket retail chains are going to play major role in agro-food sector in India. The supermarkets concerns are stable, year around supply with high quality and competitive prices. Supplying to large chain supermarkets gives both potential and large opportunities to our Indian farmers. The biggest challenge is to follow the strict guidelines by the retail groups in terms of quality and safety standards since most of the farmers usually deliver their goods to open markets or to local wholesalers. Mainly Indian farmers are marginal and small who are having average farm size of 3.3 acres, lack of infrastructure and poor post harvesting practices.

In India 40% of harvests are lost in storage and transportation. India is the second largest producer of fruits and vegetables but the country is losing Rs.1 trillion per annum, (estimated 50% of produce) going waste due to lack of storage facilities and difficult to link to far-away markets. We need large investments to improve our agriculture infrastructure in terms of seed supply, agrichemicals, processing, machinery, storage facilities, rural transportation and supply chain linkage to support the current retail trends. This could be achieved through private investors preferably by organized retailers whether domestic or Global. If it truly improves the farmer's income, agriculture growth and food security, there is no need to be concerned about FDI or domestic.

Before bringing the global retailers into the multi brand retailing in India, the following points should be considered.

- a) First and foremost... the multinational retailer's trade practices should not dampen the spirit of Indian farmers and consumers. FDI – Retail should be a process of integrating Indian economy to the global economy as well as farmers can be integrated into the world class retail market not on the mercy or control of global retail giants.

- b) The Government should make sure that the farmers will receive the remunerative price should be between 60% - 70% (based on product category) of the price paid by the consumer.
- c) International retailers should be mandated to work with farmers to improve yields by enabling them provide quality inputs, best farm technologies, timely credit and remunerative prices for their produces.
- d) Government needs to identify the trends and ways of supporting farmers to meet the needs of modern supply chains and marketing systems to enable with the supermarket sector.
- e) Government should ensure that the agro produces should be procured from the local producers and local people must be given priority in employment opportunities in processing and supply chain.

### Overview of the Two Faces of Retail Sector

The one side of the Retail mirror is challenges and the other side is Key success factors which boost up the Retail Sector.

### Challenges faced by the Retail Sector

#### Supply chain

Finance Minister Pranab Mukherjee had in his 2010-11 budget speech said "... the second element of the strategy relates to reduction of significant wastages in storage as well as in the operations of the existing food supply chains in the country. This needs to be addressed."

India is the seventh largest country (land mass: 3.2 million sq. kms.) with varying climatic conditions over the country. Taste and preferences of people vary strongly all across the country. Catering to people in 35 states and union territories is equivalent to catering to people in 35 countries, leading to complexities in merchandise/ inventory management. Infrastructure has been developing at a rapid pace over the past decade but has still a significant ground to cover; the planned expenditure of US\$ 1 trillion in the 12th five year plan will help bridging this gap. There exists a need for retail to concentrate on developing a strong back-end support especially for perishable

products to help reduce wastages which is estimated to be at 40 percent of national produce.

### Channel conflicts

Globally, retailers maintain a direct relationship with their suppliers. Due to the complex taxation structure and geographic spread of the country, most FMCG companies have developed regional distribution and re-distribution network. Cutting out the distribution network will hurt operating structures of distributors, who as an industry body in the past have opposed FMCG companies selling directly to retailers. There exists a need for a retailer to work closely with the suppliers in an attempt to shorten the supply chain network resulting in saving time and money.

### Location and rental

Finding the right location with the right rental for stores has been a challenge for all retailers. Rent forms a large portion of the total expenditure (6 to 11 percent of the revenue) in retailer's income statement and can more often than not convert a profitable store into loss making. The challenge for a retailer would be to find the right location for their stores either in malls or as a standalone store to be able to generate enough footfalls. A retailer could evaluate option of setting up a property development/ management arm that would be able to source/ develop stores at lower rentals.

### Unique Indian customer

The Indian consumer experiencing modern retail has now warmed up to this idea. Buying habits have still not changed, where people prefer to buy most of the fruits and vegetables on a daily basis. The Indian consumers have a strong preference for freshly cooked food over packaged food mainly attributed to dietary patterns, poor electricity supply, low penetration of refrigerators and a family structure where one of the primary roles of the housewife is feeding the family. There is also an impact on the basket size because of non-availability of personal transport facilities, due to which the consumers prefer to buy smaller quantities from stores conveniently located near their homes.

### Regulatory

Currently, indirect taxation structure is complex in India with varying tax rates, multiplicity of taxes and multiple tax enforcement authorities. Goods and Service Tax likely to be implemented in 2011 will replace a host of levies like excise, sales tax, value-added tax, entertainment tax and luxury tax. This is likely to have an impact on the supply chain model and cost structure of distributive trade, followed by consumer packaged goods companies. Opening a new store requires a lot of licenses, which have to be obtained from different government departments leading to considerable lead time in opening up of the stores. A push has been made by existing retailers to get the government to have a single window clearance for getting all the licenses at one place to speed up the process.

### Private Labels

Private labels enable retailers to offer products at a better price point attracting footfalls to the store. This, in turn, not only translates to better margins by cutting out middlemen but also enhances retailers bargaining power with supplier. Penetration of private labels in emerging markets is expected to be about 6% of retail sales which in India is estimated to be about 10 – 12%. The concept is still at a very nascent stage in India given the age of modern retail in India. Few players have introduced private labels in the category of Food & Grocery, Apparels, Consumer Durables etc. but reservations still exists towards acceptance of these products with the Indian consumer. Private labels offering competitive pricing proposition has helped to generate interest and a slow but steady acceptance from the Indian consumer.

### Key Success Factors

#### Efficient Supply Chains

Highly fragmented supply chains coupled with infrastructure issues and the vast geographical spread of the Indian market pose huge challenges to the retailers. Indian retailers have to enhance their supply chains to succeed in the cost conscious market. Segments such as food and grocery have to cope with very highly unorganised supply chains. Also, the rising customer expectations would necessitate supply chains with quick reaction times.

### Ability to penetrate rural market

The urban area has been the focus of Organised Retail which has led to increased competition. Rural India is home to 72 Crores consumers across 6 lakh villages. 17% of these villages account for 50 % of the rural population as well as 60 % of rural wealth. Hariyali Kisan Bazaars (DCM) and Aadhars (Pantaloon-Godrej JV), Choupal Sagar (ITC), Kisan Sansars (Tata), Reliance Fresh, and others such as the Naya Yug Bazaar have already ventured into the retail market.

### Leveraging Technology

The Organised Retail layers have to leverage IT and technology to sustain business growth through innovation and differentiation. A numbers of retail players like DLF Retail, Khadims, Diamexon Diamonds have expanded their SAP footprints to simplify business processes, reduce costs and adapt to the changing industry landscape. GPS and RFID technology can help in logistics and inventory management.

### Customized solutions

The Indian retail market is very heterogeneous in nature. The dynamics for various segments change with the geography and other cultural factors. The challenge for the retailer is to keep this heterogeneous nature of the target market in mind and to balance it with other issues like economies of scale.

### Investing in retail brand (store brand)

A strong retail brand is a critical success factor. The retailers should invest in brand building activities which would help them in attracting new customers as well as retaining the existing ones. The strong retail brand will allow the retailers to push through “private labels” which would strengthen their bottom line.

### Customer Relationship Management (CRM)

The retailers have to come up with innovative CRM activities to retain their customer base and to add on to their brand value. CRM activities like loyalty programs have been received well by the customers in the past.

### Impact of Organized Retailing on the Unorganized Sector

Unorganized retailers in the vicinity of organized retailers experienced a decline in their volume of business and profit in the initial years after the entry of large organized retailers. The adverse impact on sales and profit, however, weakens over time. There was no evidence of a decline in overall employment in the unorganized sector as a result of the entry of organized retailers. The rate of closure of unorganized retail shops in gross terms was found to be 4.2 per cent per annum, which is much lower than the international rate of closure of small businesses. The rate of closure on account of competition from organized retail was found to still lower, at 1.7 per cent per annum. There was competitive response from traditional retailers through improved business practices and technology up gradation.

Consumers definitely gained from organized retail on multiple counts. Overall consumer spending has increased with the entry of the organized retail. While all income groups saved through organized retail purchases, the lower income consumers saved more. Thus, organized retail is relatively more beneficial to the less well-off consumers. Proximity is a major comparative advantage of unorganized outlets.

There was no evidence of an adverse impact by organized retail on intermediaries. There is, however, some adverse impact on turnover and profit of intermediaries dealing in products such as, fruit, vegetables, and apparel. Over two-thirds of the intermediaries planned to expand their businesses, in response to increased business opportunities opened by the expansion of retail.

Farmers were found to benefit significantly from the option of direct sales to organized retailers. The average price realization for cauliflower farmers selling directly to organized retail was about 25 per cent higher than their proceeds from sale to regulated government *mandis*. The profit realization for farmers selling directly to organized retailers was about 60 per cent higher than that received from selling in the *mandis*. The difference was even larger when the amount charged by the commission agent (usually 10 per cent of sale price) in the *mandi* is taken into account.

Large manufacturers have started feeling the competitive impact of organized retail through price and payment pressures. Manufacturers have responded through building and reinforcing their brand strength, increasing their own retail presence, 'adopting' small retailers, and setting up dedicated teams to deal with modern retailers. The entry of organized retail is transforming the logistics industry. This will create significant positive externalities across the economy. Small manufacturers, however, did not report any significant impact of organized retail.

### Major Recommendations

- i. Modernization of wet markets through public-private partnerships.
- ii. Facilitating cash-and-carry outlets, like Metro, for sale to unorganized retail and procurement from farmers, as in China.
- iii. Encouraging co-operatives and associations of unorganized retailers for direct procurement from suppliers and farmers.
- iv. Ensuring better credit availability to unorganized retailers from banks and micro-credit institutions through innovative banking solutions.
- v. Facilitating the formation of farmers' co-operatives to directly sell to organized retailers.
- vi. Encouraging formulation of "private codes of conduct" by organized retail for dealing with small suppliers. These may then be incorporated into enforceable legislation.
- vii. Simplification of the licensing and permit regime for organized retail and move towards a nationwide uniform licensing regime in the states to facilitate modern retail.
- viii. Strengthening the Competition Commission's role for enforcing rules against collusion and predatory pricing.

### The road ahead

The sentiment towards 100 percent FDI in retail sector is gathering pace. Currently, the UPA has a majority in the house and it seems quite possible that they will be able to pass

the bill, making FDI in multi-brand retailing, a reality. Moreover, with state governments like Punjab working with modern retailers in furthering improvement of trade, there is a possibility that support will flow in from other state governments as well. However, the opposition led by the BJP is not in favour of this move and has presented a report recently to the Parliament recommending a complete ban on FDI in retail.

The proposed FDI norms will open up strategic investment opportunity for global retailers, who have been waiting to invest in India. This may have a significant impact on the current arrangement of foreign players. This policy will require investment from retailers in areas of supply chain, especially for perishable products, thus helping farmers to get better income leading to an inclusive growth in the country. Given the large number of SKU's that retailers stock Small and Medium Enterprises (SME) sector is also set to gain from this move due to preference given by retailers to private label brands. The move will also encourage smaller suppliers to take their products to a national platform that they could not previously manage due to lack of an organised supply chain of their own. This policy will also open up avenues for attracting, developing and retaining talent. Contract manufacturers would also benefit from these policy changes. With the global economy still recovering, investment in India is lucrative to a retailer attributable to strong consumerism, rising disposable income, growing middle class population, favorable macro and micro economic indicators supplemented by a stable government.

### Conclusion

The objective is modernization of Indian retail. To achieve it we need to move on three fronts: first, the government has to proactively assist traditional retailers in competing successfully with the organized retail by modernizing themselves; second, remove the domestic regulatory and interstate movement restrictions on retail; and third, allow foreign entry into multi-brand retail.

Corporate retailing in India is witnessing considerable growth. The share of corporate retail in overall retail sales is projected to jump from around 3% currently to around 9-10% in the next three years. A number of large domestic business groups have entered the retail trade sector and are expanding their operations aggressively. Several formats of corporate retailing like

hypermarkets, supermarkets and discount stores are being set up by big business groups besides the ongoing proliferation of shopping malls in the metros and other large cities. This will have serious implications for the livelihood of millions of small and unorganized retailers across the country. Large organized retail is controlled across the world by many governments. An appropriate regulatory framework for the organized retail sector in India has to be framed keeping in mind the Indian specificities. India has the highest shop density in the world with 11 shops per 1000 person. If the corporate retail starts spreading in India without any control and if the Government brings in Foreign Direct Investment in the sector, the potential social costs of the growth and consolidation of organized retail, in terms of displacement of unorganized retailers and loss of livelihoods will be enormous. Regulation needs to be more stringent and restrictive.

Retailers entering the Indian market need to ensure that they have considered the opportunity along with the challenges to maximize their returns. Retailers will need to bank on the local knowledge brought in by their partners/employees/ service providers to be able to reduce the lead time required by them to set-up operations and get a foothold in the Indian market.

**Catering to people in 35 states and union territories is equivalent to catering to people in 35 countries, leading to complexities in merchandise/ inventory management...**

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