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IMPACT OF FDI RETAIL POLICY ON BIG BOX FOREIGN RETAILERS IN INDIA

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Abstract
The Indian retail has immense potential to contribute towards the Indian economy. Retailing alone generates more than 10 per cent of India's GDP and employs around 8 per cent of the total work force. Despite being the largest industry and second largest employer (after agriculture), unorganized retail dominates the distribution sector and suffers from poor access to capital and lack of management skills. Yet, retail reforms in India are lagging behind other Asian countries that have immensely benefitted from liberal FDI reforms. In India, the much talked about FDI reforms finally saw the light of the day on 14th September 2012. Despite a warm welcome extended by the then UPA government in the form of further liberating the retail sector by allowing 51% FDI in Multiple Brand Retail and a more or less status quo maintained by BJP led current government, foreign multi brand retailers aren't queuing up for entry in India. This paper aims to examine the impact of the FDI Retail Policy on multi-brand foreign retailers also referred to as big box retailers.

Key Words: Foreign Direct Investment (FDI), Retail, Multi Brand Retail, Single Brand Retail, Organized Retail, Big Box Retailers.

Objectives of the Study

1. To track the changes in policy relating to FDI in Multi Brand Retail in India
2. To examine the impact of FDI policy implementation on foreign big box retailers in India

Methodology

This research is based on secondary sources of data. Books, journals, newspapers, survey reports & websites have been extensively used. The conclusions and recommendations of this study are based on analytical, descriptive and comparative analysis of secondary sources.

Introduction

In 2004, The High Court of Delhi defined the term 'retail' as a sale for final consumption in contrast to sale for further sale (Wholesale) or processing. Thus, retailing involves transfer of goods and services from the seller directly to the end user in small quantities for personal, family or household consumption and is the final link in the distribution channel. The goods or services may be sold in stores or by mail, telephone, vending machine, on the street or on internet. India has a long history of retail starting with the barter system to modern formats that offer a variety of products.

The retail sector is classified as organized and unorganized. The two coexist in different proportions in countries across the world. Organized retailing refers to trading done under license. In India, any trading activity conducted with registration under sales tax and income tax, forms a part of the organized retail. Typical features of organized retail are professional management and high levels of centralization in merchandise and manpower planning, technology integration, accounting standardization, an organized supply chain management and alignment of visual merchandising. Unorganized retail refers to the traditional forms of retailing in India where the businesses are run by owners or trusted employees/relatives. This includes local kirana stores, sole ownership clothing stores, Paan/beedi shops, convenience stores, road side vendors and hand carts. These retailers are highly unstructured but have a cost advantage against organized retail stores. They usually operate in only one city.

In India, the organized retail emerged around 1980's when manufacturers started exploring alternative channels of distribution. The results of this search were retail chains like Raymond, SKumar, Grasim, Bombay Dyeing and Titan. The next wave of growth in this sector started with the process of liberalization in the 1990's as new entrants in this sector were entities with no interest in manufacturing. Many Indian and International players have entered the market and are spread across product categories which included FMCG, apparel, music, books, gems & jewelry, pharmaceutical, consumer durables etc. The sector is once again in spotlight with the entry of e-retailers and m-retailers that may completely change the rules of the game.

Single and Multi-Brand Retail

The Government has not categorically defined the meaning of "Single Brand" anywhere neither in any of its circulars or any notifications. However, 'single brand' implies that foreign companies would be allowed to sell goods sold internationally under a 'single brand', viz. Promod, Reebok, Nokia, Adidas. Some preconditions to qualify as single brand retail are mentioned in Press Note 3[8] as under;

a. 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),
b. Products should be sold under the same brand internationally,
c. Single-brand product retail would include products which are branded during manufacturing and
d. Additional product categories to be sold under "single-brand" would require fresh approval from the government.

However, it should be noted that the retailers would be able to sell multiple products under the same brand.
Multi Branding in Retail – Multi Brand is also not specifically defined by the government of India. It generally refers to selling multiple brands under one roof. The company decides to further introduce more brands into an already existing category.

The Retail Sector in India
The retail industry in India has emerged as one of the fastest growing industry. In 2012, the retail sector was said to be at UD$ 5 billion (approx) and was expected to grow at CAGR of 13% to touch USD$ 741billion by 2015. By 2020 it is expected to touch US$948 billion**.** According to research by CRISIL, Organized retail is also expected to touch 10.2% and to 20% by 2021 of total share of the retail market in India.

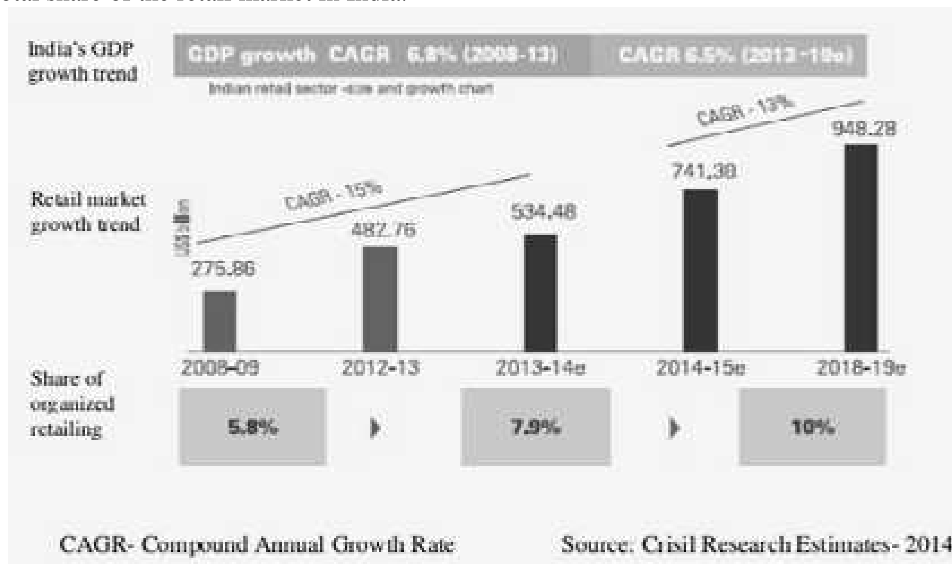

Fig-1: Size of Indian Retail (in US$ bn)

Several players, both Indian and global have evinced interest in entering the Indian markets, however, the wait for ideal conditions for entry continues.

Fig-2: Indian Retail Industry Break-Up by Revenues
Food and grocery is the largest segment followed by Apparel, Consumer Durables and IT and Jewellery are the other major contributors to this segment. The uniqueness of the Indian Market lies in the high proportion of unorganized sector.

This is a typical characteristic of a market in its nascent stage of development.

Table 1: Quantum of Retail Trade		
Country	**Organized**	**Unorganized**
India	6	94
China	20	80
Indonesia	30	70
Thailand	40	60
Malaysia	55	45
Taiwan	81	19
Source: Booz & Company analysis, FICCI, 2012		

Organized retailing in India is limited to the urban areas with huge rural markets still remain untapped. The share of organized retail has gone up from 3% in 2007 to almost 14% in 2014. India has over 14 million stores; 11 stores per 1000 persons, the highest density of stores in the world.

FDI - Significance for Developing Economies
It is important to note that FDI has emerged as an important source of investment funds for a number of developing countries like India due to decline in development assistance earlier considered a reliable source. As against other forms of external finance, Foreign Direct Investment (FDI) flows are usually preferred because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by investors. FDI also facilitates international trade and transfer of knowledge, skills and technology. In a world of increased competition and rapid technological change, their complementary and catalytic role can be very valuable.

In addition to being a source of badly needed funds, FDI brings with it other tangible and intangible benefits like new technology, organizational and managerial skills, marketing networks, stimulus to competition, modernization, innovation, savings due to efficient use of resources /minimizing wastage and capital formation, and through these, job creation. Supported by major reforms in domestic policies and practices, FDI can turn around a slow-moving economy into a growing economy.

Almost every country be it China, Russia, Brazil, Chile, Thailand, Indonesia and Argentina have benefitted in some way from liberalized reforms in retail in terms of improved infrastructure, better returns to farmers and manufacturers, creation of jobs etc.

WTO & FDI Reforms in India
At this stage it would be interesting to explore whether FDI in retail was inevitable. Is India obliged under WTO to allow FDI in Retail?
The Uruguay Round into effect in 1995 with deadlines ending in 2000. Most developing/Asian countries implemented sweeping changes in their FDI policy due to WTO implications. India's major trading partners such as the United States, Japan and the European Union made "requests" in this regard to New Delhi to allow FDI in retailing during the Doha Round negotiations of the WTO. As a result, India opened up the retail space in a phased manner.

FDI Reforms in India - The Milestones
In continuation of the economic liberalization process set in place by the Industrial Policy of 1991, the Government of India opened the retail sector to FDI through a series of steps taken over a period of time.
Under mentioned is the sequence followed by the government until finally allowing Multi Brand Retailing -
1997: FDI in cash and carry (wholesale) with 100% rights allowed under the government approval route;
2006: FDI in cash and carry (wholesale) was brought under automatic approval route;
Upto 51% investment in single brand retail outlet permitted, subject to Press Note 3 (2006 series).
2011: 100% FDI in Single Brand Retail allowed.
2012: The Government of India allowed further liberalized FDI in retail as under:

- **Up to 100% FDI in Single Brand Retail Trading**
    1. By only one non-resident entity whether owner or the brand or otherwise.
    2. 30% of the procurement of the value of products sold would have to be done from Indian small industries (defined as industries which have a total investment in plant & machinery not exceeding US $ 1.00 million at

the time of installation and any point in time in the future)/village and cottage industries, artisans and craftsmen'.
3. Companies are not allowed to operate a mix of fully owned stores and franchisees or engage in wholesale trading. They cannot engage in B2C e-commerce business.

- **Up to 51% in Multi-Brand Retail Trading**
    1. Minimum amount to be brought in by foreign retailers should be at least US$100m as equity into Indian company.
    2. At least 50% of the total FDI is to be invested in back end infrastructure within 3 years. (Back end infrastructure will include all investments made towards all activities like processing, manufacturing, distribution, design improvements, quality control, packaging, logistic, storage, warehousing, agricultural market produce infrastructure etc. However will exclude the following- Expenditure on land costs, rentals.
    3. At least 30% of value of procurement of processed product shall be sourced from Indian "Small Industries" (Same as above). Fresh produce won't count as part of this 30 percent.
    4. Fresh agricultural produce is permitted to be sold unbranded.
    5. Indian states have been given the discretion to accept or refuse to implement FDI.
    6. Retail outlets could be set up cities having population of at least 1 million.
    7. Application needs to be approved by two levels at Department of Industrial Policy (DIPP) and Foreign Investment Promotion Board (FIPB).

2013: In August, 2013 the following reforms were announced:
1. Change from compulsory to preferable sourcing of 30% from SME's.
2. Redefining MSME: Also, companies with a total investment of up to $2 million as against $1 million in plant and machinery will be included in the definition of MSME(Micro, Small and Medium Enterprises). The 'small industry' status would be reckoned only at the time of first engagement with the retailer.
3. Change in 50% investment in infrastructure: 50 per cent investment will be restricted only to the first tranche of $100 million, the mandatory initial investment amount, while subsequent investments into back-end will depend on the retailer.
4. Allowed to invest in cities with less than 1 million populations

The above FDI changes were brought about by the previous UPA government. Since a BJP-led new government came to the power in May 2014, the hope of further liberalization in FDI being allowed in the multi-brand retailer has taken a backseat. The present government has maintained its opposition to FDI in multi-brand retail, fearing such a step would hurt Indian traders.

Impact on Global Big Box Retailers
The following contentious issues in FDI MBR policy in India have been identified.
- Ambiguity in defining FDI for subsidiaries.
- Indian partner necessary due to 50% FDI in MBR.
- Mandatory 30% sourcing norms from MSME.
- Minimum investment of $100 million in new facilities.
- State-wise approval to FDI in retail.

These issues have lead to either delay, or cancellation of the entry of global big box retailers in India.

Case 1: Carrefour: Early 2011 saw Carrefour, a French wholesaler, opened its first cash and carry store in Delhi and eventually four more stores in Agra, Jaipur, Meerut and Bangalore. In 2014, however Carrefour announced its exit from Indian markets after reporting losses of $17 million (about Rs 102 crores) in 2012, on a turnover of Rs 190 crores. Carrefour is said to have invested a total of about Rs 300 crores in India since its entry. Many factors have played a part in its unsuccessful Indian foray. The company failed to rope in an Indian partner for its multi-brand retail plans; the mandatory sourcing from small and medium sector units added to its worries; cash-and-carry operations in India had been running into losses and to top it business had slowed down in Europe where it is the largest retailer. India was the only Asian country in which Carrefour operated cash-and-carry stores. Wholesale was not a part of the group's overall strategy for emerging markets but a vehicle to stay invested in India; and, more important, the NDA government indicated it won't clear any new FDI proposal in multi-brand retail, as that will hurt local traders. This left little hope for Carrefour to continue its India operations and has finally left Indian shores.

Thus after struggling to find its ground, one of the world's largest retailer quit India. This clearly indicates the negative impact of FDI retail policy on foreign retailers.

Case 2: Wal-Mart Store Inc: India has allowed 100% foreign direct investment (FDI) in the cash-and-carry segment since 1997. Yet, Wal-Mart chose to partner with Bharti Enterprises for its India foray.

In 2007, Wal-Mart announced a joint venture with Bharti Enterprises. Bharti Wal-Mart Pvt. Ltd runs Best Price Modern Wholesale stores in cities such as Amritsar, Jalandhar, Bhopal, Kota, Raipur, Ludhiana, Agra, Vijayawada, Lucknow, Meerut, Jammu, Guntur, Aurangabad, Amravati, Hyderabad and Rajahmundry. That same year, the Bharti group formed Bharti Retail Holdings Ltd, which in turn owned a subsidiary called Bharti Retail Ltd which operated supermarkets and hypermarkets under the Easy Day marquee. In December 2009, Bharti Retail Holdings changed its business description from retail to consulting services. Later, the name of Bharti Retail Holdings was changed to Cedar Support Services. In 2010 Wal-Mart Stores Inc took the first step by investing $100 million through convertible debentures in Cedar Support Services, a consultancy with no profit, no employees and a scant $14,000 in revenue. Indian law at the time wasn't explicit on whether such investments if made through convertible debentures in holding companies, amounted to FDI in subsidiaries. This investment was probed by the Enforcement Directorate for alleged violations by Wal-Mart of the Foreign Exchange Management Act (FEMA) for putting money into retail before the government threw open the sector to global players in 2012. When Wal-Mart made the investment in 2010, it was legal for foreigners to invest in consultancy but not retail, so the shift in Cedar's business description raised eyebrows. This caused delay in opening of the first Bharti Wal-Mart cash and carry store in India.

Finally, in 2012 the 1st Bharti Wal-Mart store came up in Amritsar under the brand Best Price Modern Wholesale. In the same year, Wal-Mart admitted to have shelled out $25 million lobbying the Congress in India, which is considered bribery in India and sparked a fresh debate surrounding the issue of multi brand FDI.

The Bharti Wal-Mart joint venture opened 20 cash and carry stores in India. They ended their 50/50 joint venture in 2013 after seven-years of partnership. The JV had 20 stores across the country and was running losses pegged at Rs 372 crores as of December 2012. Bharti group's retail venture EasyDay, to which Wal-Mart gave back-end support had 212 stores in the country. Bharti Retail had accumulated losses of Rs 1,522 crores as of December 2012 and had reported net loss of Rs 538 crores on revenues of Rs 1,528 crores for the year ended December 2012. Earlier Wal-Mart was contemplating buying into Bharti Retail's EasyDay to operate the stores jointly. With the amendments announced in September 2012, allowing 51% FDI in Multi brand retail along with a string of preconditions, Wal-Marts long awaited hope of entering the lucrative Indian retail sector took a beating.

The JV was called off more due to external factors than internal factors like incompatibility among partners. Stringent policy conditions, such as mandatory 30 per cent sourcing from Indian small and medium enterprises, have been the main hurdle. This may be possible in textiles and handicrafts, but not in products like electronics. Later, in 2013, the 30 per cent requirement was waived for those retail brands whose products cannot be sourced from the small and medium scales.Other clauses like a minimum investment of $100 million in new facilities (50 per cent of that in building back-end infrastructure), too, have played a spoiler. The clarifications issued by the Department of Industrial Policy and Promotion state that this must be entirely for green-field assets, meaning Wal-Mart's investments in India thus far did not count toward meeting that mandate.

State-wise approval to FDI in retail was also seen as a stumbling block. Since the NDA government took over Rajasthan and Delhi have opted out of the list of states & union territories open to FDI in retail.

Retail business is not seen as an area of expertise of Bharti Retail. After struggling for two years post its break up with Wal-Mart, Bharti Retail has merged with Future group in May 2015. Given the 51% limit in MBR, Wal-Mart, too will have to find another Indian partner. This will be difficult due to fewer choices in the Indian market. The MBR FDI retail policy had negative impact on the entry on the world's largest Big Box retailer. However, Wal-Mart has decided to continue on its own in its current cash and carry business with the only addition being its online foray in the same business model. Wal-Mart may reenter the multi-brand retail market when the regulations are relaxed further.
Case 3: Tesco: Tesco was the first global retailer to apply for multi-brand retailing after the government allowed 51 per cent FDI in the segment in September 2012.

Conclusion
The Retail FDI policy has caused delays and losses for the foreign retailers. Apart from dealing with cultural diversity of Indian consumers, political instability, high rental and real estate costs, lack of skilled manpower, infrastructure challenges and red tapism, the retail FDI policy is only adding to the woes of the foreign retailers.

Domestic capital in India is not adequate to support expected growth in retail hence FDI is the only stable source of achieving growth. Various studies show that productivity can be enhanced by adopting modern retailing. FDI in retail sector can prove to be a key driver of productivity in India. Simplification, removal of unnecessary restrictions and proper implementation of the Retail FDI policy will help generate employment and enhance quality of life of consumers. Also, the Indian retail chains would get integrated with global supply chains since FDI will bring in technology, quality standards and marketing. Many sectors including agriculture, food processing, manufacturing, packaging and logistics will reap benefits of FDI in India.

Recommendations

- The government should allow MBR in a phased manner by allowing FDI in lifestyle products first before allowing the foreign big box retailers to spread their wings in other segments like grocery. This will reduce the opposition from fractions who think FDI in MBR will negatively impact mom and pop stores in India. It was also lead to growth in retailing by creating additional customer segments for lifestyle products.
- The big box retailers should not be allowed to enter small formats which will further restrict direct competition with small mom and pop stores.
- Further restriction on the distance of location of these MBR especially big box retailers from heavily concentrated residential areas which are well serviced by small retailers can be included. This may not have any impact on the big box retailers as these areas are very congested and space may not be available. Even if it is available acquiring or renting such space may not make financial sense. However, it will further ease the opposition from small retailers since they will retail their USP of convenient location as against big box retailers.
- If the aim of the government is to boost manufacturing in India through the 30% sourcing from MSMEs' clause, instead may be 50-60 % sourcing over a period of time can be made compulsory from manufacturing in India which will encourage organizations like IKEA to set up their own manufacturing facilities and will also boost exports. By being stuck on the 30% sourcing clause from MSMEs', in effect the government is driving away job creations by thousands as foreign companies may want to set up their own manufacturing facilities. There may be fear of cheap exports from countries like China but foreign retailers cannot be held responsible for the same as toys, mobiles, garments, festival decorations etc are all being imported already. Besides imports can be curbed by tariff and non-tariff barriers.
- To run a sustainable retail business scale of operations is the key. State level approval of FDI should be abolished as this will cause bottleneck in achieving the desired scale and increasing the perceived uncertainty by foreign companies on the political front. State wise approvals will cause further delays and uncertainty further complicating implementation.
- Retail needs to be given an Industry status which is still lacking in India despite its size, complexity and potential.
- The policy needs simplification and ease in implementation. One stop permissions as has been done in China will give a boost to FDI.

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