ANWESHAN, Vol. 1, No. 1, March 2013

FDI IN MULTI BRAND RETAIL: COST BENEFIT ANALYSIS

Debabrata Mitra, Amlan Ghosh***

Abstract

The decision of the UPA Government to allow FDI in multi-brand retail is a highly controversial issue though the government has opened the retail sector to FDI in cash and carry with 100 percent ownership and 51 percent investment in single brand category. There are various issues that need to be addressed by the policy makers while allowing FDI in multi-brand retail. It can hardly be denied that entry of big giants in the retail sector may adversely affect a large section of population employed in the unorganized retail. Proper regulatory measures should be imposed to protect the vulnerable sections of the society.

Keywords: *FDI, Multi-brand retail, organized retail, Wal-Mart.*

Introduction

The decision of the Government to allow multi brand foreign direct investment (FDI) in India has fetched a lot of arguments from both the sides who are supporting the decision and who are opposing the same. But there is a lack of conscientious debates about this issue and there is a need for basic understanding of the subject from the view point of its cost and benefits. Before we come to any conclusion about the benefit or negative implications of this proposed decision we need to understand the retail sector in India and then FDI in retail along with its impacts in present situation. The primary objective of this article is to analyse the present retails

**Professor, Department of Commerce, University of North Bengal, email: debabrata_nbu@yahoo.co.in, **Assistant Professor, IBS Hyderabad, Hyderabad, India, e-mail: amlanpost@gmail.com*

scenario in India and we can arrive at a mutual consensus on this particular issue which has greater implications on large section of population.

The term 'retail' can be defined as a sale for final consumption in contrast to a sale for further sale or processing (i.e. wholesale). That is *sale to the ultimate consumer*. The retail industry in India is mainly divided into Organised Retailing and Unorganised Retailing. Organised 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 hypermarkets and retail chains, malls and also the large retail businesses managed by the people privately. Unorganised retailing, on the other hand, refers to the traditional formats of low-cost retailing available to our nearest places. For example, the local *'kirana shops',* general stores, '*paan/beedi shops'*, footpath vendors, etc. The Indian retail sector which is the largest source of employment after agriculture in India, is highly fragmented with only 5 per cent of its business being run by the organized retailers as compared to 80% in USA, 40% in Thailand and around 20% in China.

India is a signatory member of World Trade Organisation (WTO) and its General Agreement **on Trade in Services** (GATS) advocates of removal of trade and tariff barriers, include wholesale and retailing services to open up the retail trade sector to foreign investment. The government in a series of moves has opened up the retail sector 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. Wal-Mart is already in India with 50:50 cash and carry joint ventures with Bharti Group while Tesco has tied up with Tata group. It means that the FDI in retail sector is already there in India. Only FDI in Multi-Brand retailing (MBR) was prohibited in India. Let us elucidate both the term single brand FDI and multi brand FDI in retail.

FDI in 'Single brand' retail implies that a retail store with foreign investment can only sell one brand. For example, if Nike were to obtain permission to retail its flagship brand in India, those retail outlets could only sell products under the Nike brand. Nike has opened its outlet in Delhi, Kolkata, Mumbai, Hyderabad, Bangaluru and other cities in India selling nothing but Nike shoes, Nike wrist watches, Nike T-shirts etc. Since the outlet is selling only one brand products to end consumers it is called single brand retail. Similarly, we have Reebok, Adidas, Nokia, Sony, Cannon, LG, Samsung outlets in India. On the other hand we can define multi brand retail as and when an outlet sells products of different brands under one roof. For example if an outlet sells the shoes of Nike, Adidas, Reebok, ID or T-shirts/Shirts of Puma, Reebok, Nike, Levis, Crocodile, Lacoste, Allen Solley, Van Huesen, Peter England etc under one roof then that retail is called multi brand retailing. We have these kinds of retail outlets in India but are owned and managed by Indian prompters and not by any foreign promoters, e.g., Big Bazar, Pantaloons, Westside, Reliance Fresh, Shoppers Stop etc.

The policy of FDI in single-brand retail was basically adopted to allow Indian consumers access to foreign brands. Since Indians spend a lot of money shopping abroad, this policy enables them to spend the same money on the same goods in India. Between 2006 and 2010, a total of 94 proposals have been received. Of these, 57 proposals have been approved. An FDI inflow of Rs 196 crore under the category of single brand retailing was received between April 2006 and September 2010, comprising 0.16 per cent of the total FDI inflows during the period in India. But there were no such protest was visible as it is now in case of multi brand retail. Neither the politician nor the un-organised retailers raised their voices, why? Because these outlets are going to sell to the brand conscious upper middle class or rich people mostly sportswear, fashion clothing, life-style products. Now government allowed FDI in multi brand retail. This would open the doors for global retail giants such as Wal-Mart, Tesco etc to enter into the organised retail sector of India. This would enable global retailers to open stores in India offering a range of household items and grocery directly to consumers in the same way as the Big-Bazar or ubiquitous '*kirana*' stores are offering today. Now we have seen protests against this decision of the government by few political parties and by un-organised retail sector. Every decision has its merits and demerits and we need to assess those and find out which would be beneficial for the society, as a whole, in the long run.

Cost Benefit Analysis of FDI in retail in India

One of the most important arguments in favour of FDI in multi brand retail is the need to develop an efficient supply chain. India is the second largest producers of fruits and vegetables (more than 180 million MT) in the world but it has very limited integrated cold storage facility (less than 6000) to support its production. Importantly, out of the total available cold storage facility, 80% is used to store potatoes only. Because of this less developed supply chain management, India is not a big exporter of farm produce in the world. More than Rs 1 trillion worth of farm produce and other perishables are wasted due to lack of storage and transport facility. That is one of the major reasons of inflation in food items in India. More than 50% of this production can be saved if we have proper cold storage facility along with necessary transport support system. Though FDI is permitted in cold-chain to the extent of 100%, through the automatic route, in the absence of FDI in retailing, FDI flow to this sector is almost insignificant. It is advocated that FDI in multi brand retail will bring MNCs and they will invest in Cold storage chains which will reduce the wastage and increase the supply of food grains to the market through their improved logistics and lowers the inflation. Farmers are also going to be benefited as the logistics would improve along with reduction in wastage. Improved logistical support along with cold storage facility will give more money to the farmers for their produce.

Presently intermediaries (middle men or agents) dominate the complete supply-chain management system in India. Without these middle men or agents, it is very difficult for the farmers to sell their produce at the *'Mandis'* which are basically controlled by the middle agents. These Mandis, governed by the State Agriculture Produce and Marketing Committee Acts (APMC), have developed a non-transparent character over the years. According to a study of World Bank, Indian farmers receives for a typical horticulture product is only 12-15 percent of the price which final consumers end up paying at the retail outlets. It is expected that the FDI in multi brand retail will remove the intermediaries and farmers will be benefited by getting more price for their produce as the MNCs will buy straight from them. This will create a chain of producer-retailer-consumer where there is no space for intermediaries and the benefit of removing the middle agent will be shared by both the producer and the consumers. This would definitely reduce the price of goods in the market.

According to the CII Survey (2012), on the impact of FDI of Retail on SMEs, (based on a large sample size of 250 companies covering different categories of SMEs) is in favour of the government's decision to allow 51% Foreign Direct Investment (FDI) in multi-brand retail and 100% in single brand retailing as this would benefit the sector with more sales, capacity addition, quality improvement, supply chain efficiency and creation of employment opportunities.

There is no doubt that the country needs a wide spread and efficient supply chain system but it is highly improbable that few multi brand retail outlets in few cities would serve the purpose. As we can see that the total share of organised retail market in India is just 5% of the total retail market. The sheer size of our country and the unique character of the market would be requiring a huge effort by the MNCs to have some impacts. Therefore, the unorganised sector will still be playing a dominating role in the retail market. As food grains are the major component of the inflation index (WPI) in India, it is argued (The Economic Times, 23/07/2011) that by reducing wastage and improving the supply of food grains and also lowering the price would impact the inflation. But it needs to be understood that the entire process of setting up of the supply chains and for organised retail (domestic and MNCs) to have any impact on inflation will take few years and that too its share in the total retail market needs to be more than 50 percent. Thus the theory of less food inflation with the advent of MNCs in retail sound good on paper but hold very difficult in the practical scenario as the investments and the work needed to develop such supply chain network to be effectively link the entire country cannot be carried out by few MNCs and domestic retailers.

There is a fear that the introduction of MNCs in the multi brand retail would pave the way for the end of *'Kirana'* shops in India along with all other existing retail shops which will create a mass unemployment in the country. The people who advocate in favours of MBR they argue that it will eliminate the middle men from the channels of distribution. If it becomes so, then around four crores of people at this moment will lose their earnings (Arun Jaitely, Dec 6, 2012) and it will create a socio-economic imbalance in the society. Moreover, it is also argued that the total elimination of middle men from the channel of distribution is not at all possible and it may so happen that these middle men may create a "cartel" and can go for strengthening their position. Generally, it is quite natural that these multinational companies, e.g, Wal-Mart, have got huge resources at their helm of affairs and they may resort to dumping tactics for capturing the Indian retail market at the initial stage. After eliminating the middle men completely from the channels of distribution they will manipulate both the procurement and selling price for maximising their profit which will lead towards maximum exploitation of masses.

We think this has been exaggerated by everyone those who are protesting the FDI in multi brand retail and the political parties are pondering on it to use this issue for their benefit. Let us elucidate in a lucid manner. Multi brand retailers are mostly operate on large scale format and in the cities only. We haven't seen any outlets of Big-Bazar or Pantaloon retail in villages. Because they are not going to get enough customers having more disposable income to spend on those shops. Therefore, you will never see a 'Wal-Mart' shop in countryside. So MNCs have to open in the cities where real estate prices are quite high. First they have to procure enough area to establish their retail malls and that too should be in nearby area so that consumers are able to come for shopping. In present days you can't fool any customers as they are very much aware of the market place. Customers think of traffic, time and petrol cost before visiting any of the multi brand retail outlet such as Wal-Mart. No one would go 7-8 kilometres just to avail few small discounts on beverages/ biscuits etc. because the conveyance cost would negate the benefit of discounts. Again, Wal-Mart can't open malls in every corner of the India. Their running cost of malls (staff, electricity, security etc) will surpass the profit margin. Therefore, people will still be buying daily requirements from the local *Kirana* shops or from un-organised retailers. The importance of these local un-organised retail shops will remain in the society because of their customised services such as monthly credit system and home delivery system. More importantly, it may possible that in few circumstances they may end up being suppliers to the MNC retailers. We need to remember that the organised domestic retailers have failed to displace the un-organised retailer, and they will not be able to, because of the labour cost factor. According to the Indian Council of Research in International Economic Relations (ICRIER, 2011), a premier economic think tank of the country, which was appointed to look into the impact of BIG capital in the retail sector, has also come to conclusion that investment of 'big' money (domestic corporate houses and FDI) in the retail sector would in the long run not harm interests of small, traditional, retailers. Moreover, if the FDI in multi brand is allowed, then the retail MNCs requires man power to run its business in all the areas from logistic supply to customer care to security. So there will be more employment opportunity. So the theory of mass unemployment does not stand tall.

To open a mall MNCs require to purchase land and construct their premises which will spur more demand for other industries such as cement, steel, along with more labourers, masons, plumbers, electricians etc. In the same way farmers are going to get more money in absence of middle agents. This will provide money to the people who will create demand in the economy for more goods and services. There will be a trickledown effect on the economy. The share of organised retail in India is just 5% whereas the same is 20% in China, 30% in Indonesia, 66% in Japan. The FDI in multi brand retail would induce competition in the market which might bring down the farm price and retail selling prices and would ultimately benefit the consumers as well as producers.

According to the Department of Industrial Policy and promotion (DIPP), after the implementation of 51% FDI in single-brand retail, FDI inflows, between April 2000 to April 2010, stood at only US $ 194.69 million to India, constituting barely 0.03% of total FDI inflows. Indian retail sector is expected to grow to US $ 535 billion by 2013 (A. T Kearney, 2010). Some studies such as, A.T. Kearney (2011), McKinsey & Company (2007) and A C Nielsen (2008) have predicted that the modern retail will grow in double digit in India and pointed out that it is the right time to enter the Indian retail market as it is not saturated (A.T. Kearney (2011). Therefore, there is a huge investment gap is visible and FDI in multi brand retail may attract reasonably good amount of FDI. The reason why we say may attract FDI because MNCs are not going to find the Indian retail market very smooth ground to operate (as stated earlier) and they have to face tough competition and conditions to be in the vast and unique retail market of India. If we look at the successful implementation of FDI in retail policy in 1992 in China, we can see that its retail sector is the second largest (in value) in the world with global retailers such as Walmart, 7-Eleven and Carrefour comprising 10% of the total merchandise. In case of Indonesia, even after many years of emergence of multi-brand retailing and supermarkets, 90% of fresh food and 70% of all food is still controlled by traditional retailers.

Conclusion

There is a great possibility that with the introduction of MBR will create serious disruptions in the total socio-economic scenario of our country by thronging out a huge population from their current employment. So introduction on MBR will definitely hit the large section of marginalised population to a considerable way.

FDI is permitted in all the major developing countries such as Brazil, China, Argentina, Indonesia, Thailand etc. This would benefit both the farmers and consumers with lower prices due to competition and removal of middle agent and good quality of goods. This would also generate employment in the economy. Micro Small and Medium Enterprises (MSMEs) are going to be benefitted with the introduction of more malls as they would get another market to supply their products. But all the anticipated benefits may not be materializing without changes in other laws such as APMC Act. Therefore, FDI in multi-brand retailing must be dealt with cautious approach as it has direct impact on a large section of population. We need an effective regulatory framework to look into the fact that the FDI in the multi brand sector actually contributing towards the building up of back end infrastructure and logistics in the retail sector and effectively reducing the wastage of farm produce and the producers and the end consumers are benefited.

References

- D/o IPP File No.: 5/12//201O-FC-I dated: 20th September, 2012; accessed on 02/02/2013, http://dipp.nic.in/English/acts_rules/Press_Notes/pn5_2012.pdf.
- D/o IPP File No.: No. 5/12/201O-FC-I dated: 20th September, 2012; accessed on 02/02/2013, http://dipp.nic.in/English/acts_rules/Press_Notes/pn4_2012.pdf .
- "The Impact of FDI in Retail on SME Sector: A survey report", (2011), CII.
- Michel Chossudovsky, (1997) The Globalisation of Poverty: Impacts of IMF and World Bank Reforms, Indian edition.
- Reports on Investments Approval and FDI in India, Academic Foundation, New Delhi (2003) ISBN - 81-7188-337-0.
- S. Narayan, (2012) "FDI in Multi Brand Retail in India: Signs of new resolve", ISAS insights, Vol. 192, December, 2012.
- "Impact of the Retail FDI policy on Indian consumers and the way forward", (2011) ICRIER Policy Series, No. 5, August, 2011.
- "Organized retail in India to triple by 2010: CRISIL", www.domain-b.com
- A.T. Kearney (2010): "Expanding Opportunities for Global Retailers-2010 Global Retail Development Index", A.T. Kearney, http://www.atkearney.com/images/global/pdf/2010_Global_Retail_Development_Index.pdf
- AC Nielsen (2008): Consumer and Designer Brands. AC Nielsen, April 2008 http://id.nielsen.com/news/documents/

GlobalNielsenLuxuryBrandsMay08.pdf.

- A.T. Kearney (2011): "Retail Global Expansion: A Portfolio of Opportunities-2011 :Global Retail Development Index", A.T. Kearney, http://www.atkearney.com/images/global/pdf/Retail_Global_Expansion-GRDI_2011.pdf
- McKinsey & Company (2007): "The 'Bird of Gold': The Rise of India's Consumer Market", McKinsey Global Institute, http://www.mckinsey.com/mgi/reports/pdfs/india_consumer_market/MGI_india_consumer_full_report.pdf.
- "FDI in multi brand will kill manufacturing jobs", Arun Jaitely, (2012) . http://www.niticentral.com/2012/12/06/fdi-in-multibrand-will-kill-manufacturing-jobs-26631.html. December 6, 2012.
- The Economic Times, dated, 23rd July,2011, http://articles.economictimes.indiatimes.com/2011-23/news/29806618_1_ajit-kumar-seth-cabinet-secretary-small-retailers/2.