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FDI Logjam

What's in Store

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FDI Logjam: What's in Store

THE RETAIL INDUSTRY WAS ECSTATIC WHEN THE GOVERNMENT ANNOUNCED LIBERALIZATION OF THE FDI REGIME IN NOVEMBER. HOWEVER, THINGS QUICKLY GROUND TO A HALT IN THE TEETH OF OPPOSITION FROM POLITICAL PARTIES AND INTEREST GROUPS. THE FDI DECISION IS IN A LIMBO AT THE MOMENT, BUT WHEN CAN SOME PROGRESS BE EXPECTED? HOW MUCH DOES THE DOOMSDAY SCENARIO BEING PAINTED AGAINST FDI IN RETAIL JUSTIFIED? FINALLY, WHAT CAN THE GOVERNMENT DO TO BREAK THE LOGJAM? AN 'IMAGES RETAIL' REPORT.

Late evening on November 24, 2011, with the Parliament's winter session in full bloom, the government took an executive decision to allow 51 percent foreign direct investment (FDI) in multi-brand retail and 100 percent in single brand retail. The unexpected move from the governing UPA coalition, long suffering from scams and policy paralysis, came as a delicious shock to the organized retail industry which had been waiting 16 years to hear the news.

The mood among the retail honchos and CEOs was ecstatic – FDI was their chance to quickly get money to expand their footprint across the country, reduce high-cost debt, lower the interest burden, benefit from the mass-retailing expertise of the likes of Tesco and Wal-Mart and book some profits by selling equity. One industry watcher described it as the coming of the second independence for the organized retail players.

WELCOME CHANGE

Stalwarts of the Indian retail industry were quick to appreciate the move, arguing that FDI will be a big game-changer due to the massive inflow of funds and other benefits to accrue over the years. Foreign capital will help expand organized retail in India, which currently accounts for less than 10 percent of the total retail market, compared to 80 to 90 percent in some Western countries. FDI can help ease the burden on Indian retailers grappling with rising expenditure and interest costs, which are squeezing profit margins in a very competitive environment.

Raj Jain, MD & CEO, Bharti Walmart, called FDI in multi-brand retail an important step which will positively impact the Indian market. "We are willing to invest in back-end infrastructure that will help reduce wastage of farm produce, improve the livelihood of farmers, lower prices of products, and ease supply-side inflation," he said.

Shoppers Stop Vice Chairman BS Nagesh pointed out that all SME and SSI vendors of the Indian automobile industry have became billion-dollar market cap companies, and FDI will ensure the same benefits come to the retail industry vendors too. "IKEA is already sourcing from several Indian vendors for exports; with FDI in multi-brand retail, they will start sourcing for selling in India too," he said.

FDI in retail will create an ecosystem where consumers will have a wider choice, producers can achieve better realizations, wastage in the agricultural supply chain can be reduced, and fresh employment can be generated amongst the lesser educated, said Bijou Kurien, President and CEO, Lifestyle, Reliance Retail. "For the cash strapped domestic retailer, it provides a new opportunity for inducting fresh capital into the business or retiring high-cost debt. The policy change will also support the development of retail real estate," he added.

Aditya Birla Retail CEO Thomas Varghese felt that FDI in multi-brand retail will introduce much-needed capital to fuel the growth of modern retail and create a huge employment opportunity for the Indian youth. The FMCG companies will collaborate to fuel the domestic consumption story. "With a partnering approach, we can reduce prices for consumers and help them get more product choices. It will also boost investment in commercial properties and encourage development of well-thought retail spaces," he said. Sanjiv Goenka, Chairman of the RP-Sanjiv Goenka Group was of the view that FDI will lead to disintermediation of the supply chain and bring substantial investments and technology in the back-end, thereby reducing wastage and helping soften the rampaging inflation.

For Vinay Singh, MD, Max Hypermarkets India, the immediate impact of FDI, once allowed, would be to expand organized retail across India in a win-win scenario. The efficiencies of retail will increase and there will be a positive impact on the back-end support, since most of the investment will be focused there. This will benefit farmers, small manufacturers and even the vendors. The consumers will get better choices, quality, and comparative prices. "With FDI, global retail players who already have formed alliances with Indian partners will move faster to scale up their businesses. And those who are not present will become more interested in investing in India," he said.

Anirudh Dhoot, Director, Videocon Industries, said FDI will help consumers get a wide range of

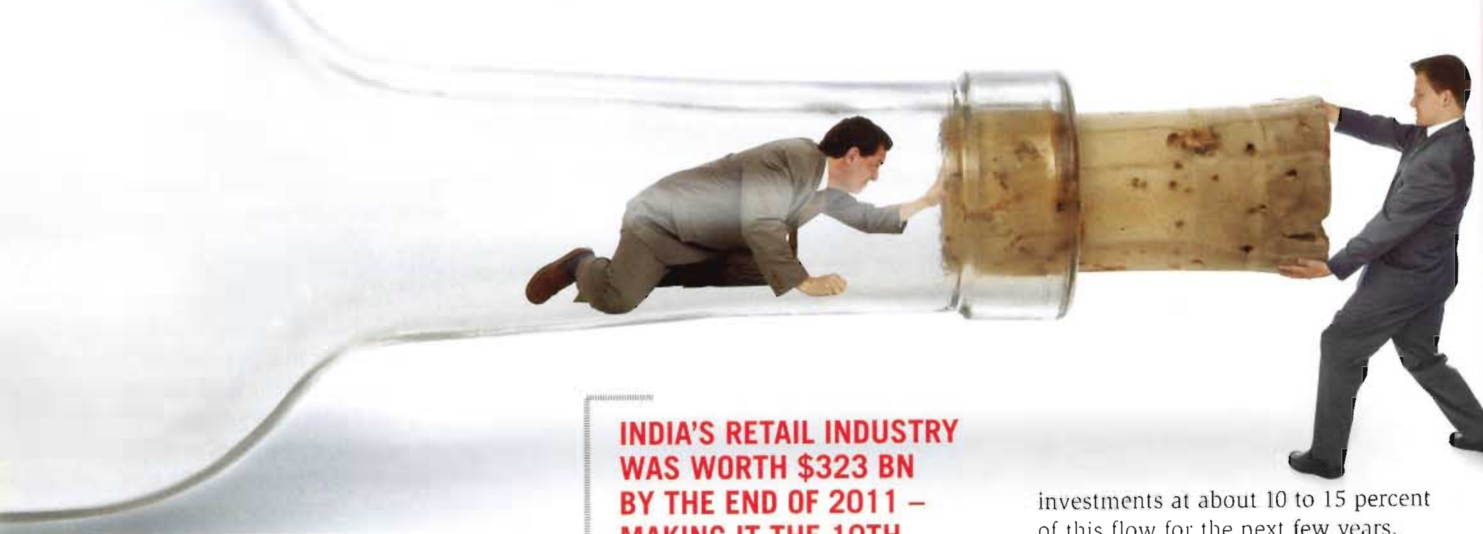
Clive Woodger
Chairman,
SCG London

Hemchandra Javeri
Executive Director,
Forum Synergies

Shrinivas Rao
CEO–Asia Pacific,
Vestian Global

competitively priced products. The entry of large international retailers will create a huge employment opportunity and global standards of technological know-how will enter India. This will be followed by collaborations which will create a healthy competition among Indian retailers.

Industry watchers too were upbeat about the FDI announcement. Parita Chitakasem, Research Manager (India), Euromonitor, said foreign funds will be useful for Indian retailers to wriggle out of massive debts. "Players such as Pantaloon Retail and Vishal Retail need to ease their current debt levels. Vishal Retail has around Rs 70 bn of debt; as of June 2011; Pantaloon Retail has a debt burden of Rs 40 bn. FDI will support them in reducing this."



CAPITAL INFLOWS

Industry players and researchers differed over the exact quantum of foreign investment that will pour into the Indian retail industry after the FDI tap has been turned on, but they were unanimous that the inflow would be quite significant considering that India currently offers a very lucrative proposition to global retail chains.

According to Chitakasem of Euromonitor, the Indian market is a potential gold mine for foreign retailers. "India's retail industry was worth an estimated $323 bn by the end of 2011 – making it the 10th biggest retail industry in the world in value terms. It will grow by 7.7 percent over the next five years to reach $469 bn. There is no doubt that foreigners will be looking to invest in India's high potential growth and offset some of the struggles they face in their home countries."

India's biggest retailer, Kishore Biyani, Founder and Group CEO of the Future Group, reckoned that a total of $10 bn can enter India's retail sector over the next 5-10 years if FDI is allowed.

An IMAGES-ASIPAC report has estimated that by 2015, urban India will have a population of 423 million people. They will need 635 million square feet of total space for food retailing (including grocery, pharma, beauty and FMCG) at 1.5 square feet of per capita food retail space, compared to about 511 million square feet today, including space occupied by modern trade as well as traditional retailers and neighborhood kiranas. The Western world has an average of 3.1 square feet and South-East Asia 1.82 square feet. Assuming that the organized sector (including the existing players) will capture only 7.5 percent of the market share in four years, India will have an estimated 47.63 million square feet of hypermarkets, supermarkets, convenience stores, pharmacies and drug stores by 2015, compared to about 15.3 millon square feet today.

Nimesh Shah, Director, Equirus Capital, said that If we exclude the investments coming through the public markets and only consider the PE and inbound M&A transactions over the last four years, the inbound M&A investments would be around $8 bn to $10 bn and the PE investments would be an additional $8 bn to $10 bn. "If we take retail sector investments at about 10 to 15 percent of this flow for the next few years, we may see capital flows in the non-public space into retail to be around $2 bn to $3 bn per annum," he estimated.

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WILD OVER WALMART

Olivier Bernheim, President and CEO, Raymond Weil Genève, whole-heartedly welcomed the government's announcement about FDI in retail. "It's a bold decision keeping in mind the local pressures, but a very late one," he told "Images Retail." Alas! The local pressures became too hot for the government to handle and soon the FDI decision was put on hold by the powers that be.

Small traders and retailers form an important pool of voters for India's principal opposition party, the right-wing BJP. Within hours of the government's announcement on retail FDI, its politicians came out openly against the move. BJP leader Murli Manohar Joshi said the party is dead against FDI in the Indian retail sector and would protest it inside and outside the parliament. He charged that foreign investment will kill India's domestic retail industry and small traders will become jobless because they will not be able to compete with international retailers.

Nothing symbolizes global retail industry and Western capitalism more than Wal-Mart, and the mercurial BJP leader Uma Bharati – with her penchant for grandstanding – threatened to personally burn to the ground the first-ever store the retailer opens in India.

Protests against FDI in retail spanned the entire political spectrum, from the right to the left and even the UPA allies, the DMK and the Trinamool Congress. For once the BJP and the communists were speaking in the same voice. Senior Communist Party of India (CPI) leader Gurudas Dasgupta demanded that the government completely roll back the decision of permitting FDI in retail trade and call an all-party meet to resolve the issue.

There was a deadlock in the Parliament and almost half the winter session was wasted in slogan shouting by opposition members, mainly over FDI in retail. Against the combined onslaught of small traders and hostile politicians, Finance Minister Pranab Mukherjee told leaders of political parties that the FDI decision will be kept in abeyance until unanimity is reached among the stakeholders. West Bengal Chief Minister Mamata Banerjee, a key ally of the Congress party, too announced the union government's decision to keep FDI in retail on hold until a consensus has emerged.

The government had relented, but just. A few days later, Commerce and Industry Minister Anand Sharma said that fresh talks with the stakeholders on FDI in multi-brand retail will start soon. He said there had only been a suspension of the FDI decision, not a roll-back. "We will be talking once again," Sharma added.

Prime Minister Manmohan Singh said there was a need to evolve a broad-based consensus about FDI in retail and the Government would work towards it. Congress leader Rahul Gandhi in a speech said the government is determined to implement its decision. He argued that FDI in retail would help farmers save their produce from rotting because of increased investment in cold storage facilities, and get the right price. "About 60 percent of vegetables go waste in India and FDI would enable farmers to directly sell their produce to retailers," he stated.

COMMERCE AND INDUSTRY MINISTER ANAND SHARMA SAID THAT FRESH TALKS WITH THE STAKEHOLDERS ON FDI IN MULTI-BRAND RETAIL WILL START SOON. HE SAID THERE HAD ONLY BEEN A SUSPENSION OF THE FDI DECISION, NOT A ROLL-BACK.

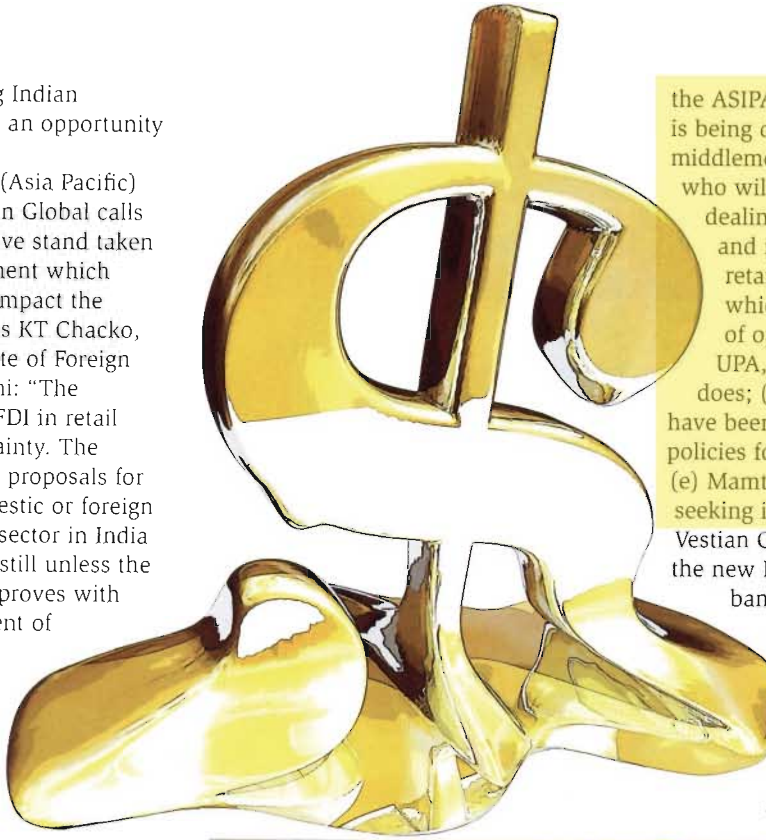
Today, it does seem that the government is biding its time over FDI due to the announcement of elections in five states – Uttar Pradesh, Punjab, Uttarakhand, Goa and Manipur. These are to be held in the first two months of 2012, with the results to be released on March 4. But the FDI issue will surely be revisited in a few months to build a broad consensus with the stakeholders, especially the political parties.

THE OPPOSITION

The intensity of the backlash against opening Indian retail to foreign capital left a bad taste in the mouth for many. Fumes Prof. Rodney Fitch, founder of British design consultancy Fitch: "*The Times* of London has reported that Tesco and IKEA have postponed any plans for investment in India, citing not a lack of demand but 'political hostility.' For the vested interests

in India to deny young Indian homemakers access to an opportunity like IKEA is criminal."

Shrinivas Rao, CEO (Asia Pacific) of advisory firm Vestian Global calls the holdback a defensive stand taken by the central government which is likely to negatively impact the reforms process. Agrees KT Chacko, Director, Indian Institute of Foreign Trade (IIFT), New Delhi: "The decision to hold back FDI in retail would result in uncertainty. The likely impact is that all proposals for investment either domestic or foreign in the organized retail sector in India would come to a standstill unless the policy environment improves with the essential requirement of predictability. Further growth of this sector and new initiatives would be adversely affected. Global investors would certainly keep off the Indian market while the Indian Investors also would wait for the policy to evolve."



Hemchandra Javeri, Executive Director of PE fund-managers Forum Synergies, says the holdback of the FDI decision is a regressive move from an international retailer's point of view, but from an Indian businessman's viewpoint, depending on which side of the issue you are, it is mixed. "Sometimes big changes do create fears in the minds of the people, real or otherwise. The problem in this issue is the lack of adequate information with most people involved," he explains. "Most Indian consumers just want great retail products and services, Indian and foreign, in the right environment and at affordable prices."

The arguments against FDI are all well known, but the people offering them are not looking at the picture comprehensively and are driven only by the motive to oppose, according to Harminder Sahni, Managing Director of management consultants, Wazir Advisors. "This is politics and thus beyond business logic," he adds.

Many commentators think the opposition to FDI in retail is being led by forces which profit handsomely from the existing disorganized nature of retail trade. Says M Krishna Reddy, founder and CEO of supermarket chain Apna Bazaar: "In India, 90 percent of retailing is unorganized. Many retailers are not registered under central or any state government and do not pay taxes. Middlemen in today's system are getting more advantage than farmers, producers, and consumers. It is the middlemen who play a major role in Indian retail sector."

According to Amit Bagaria, Chairman of the retail consulting firm, the ASIPAC Group, the opposition is being driven by five forces: (a) middlemen with vested interests who will lose out if retailers start dealing directly with farmers and manufacturers; (b) small retailers (kiranas); (c) BJP, which is following the policy of opposing everything that UPA, the governing coalition, does; (d) the left parties which have been opposing all free-market policies for the last three decades; and (e) Mamta Banerjee who is "always seeking importance." Says Rao of Vestian Global: "The opposition to the new FDI policy is due to vote bank politics. Almost all other political parties other than Congress are opposing it."

All is not lost though and it does seem that there will be some progress regarding FDI soon. Shah of Equirus Capital says that nobody can predict the politics of India and it is quite possible that we may see retail FDI in some form or other within the next 12 months. Agrees Rao of Vestian Global: "FDI in retail may be delayed, but it will eventually be approved as it is a major reform which will have a positive impact on the economy." Sahni of Wazir Advisors and Javeri of Forum Synergies are convinced that FDI in single brand will be approved soon, though it will be a while before FDI in multi-brand is permitted. Clearly, FDI in retail is an idea whose time has come.

WILL KIRANAS DIE?

A powerful albeit emotional argument against FDI in retail is that it will lead to the certain demise of millions of kirana stores and road-side shops as they will be unable to compete with the organized onslaught of global retailers. Are the fears being overstated, or there actually will be a mass closure of small shops? Says Harish Bijoor, CEO of consulting firm Harish Bijoor Consults: "Small retailers of India will definitely be affected by FDI, particularly in the big cities which will be the playground of new entrants. We will have a kind of 'Retail Darwinism' at play. The big fish will shake and stir the small ones for a start."

Regional retailer Rajiv Thakur, who runs the 7 to 9 Bazaar chain in Guwahati, says opening up of FDI for multi-brand retail will definitely impact his company's business. "Maybe big chains can balance their stakes, but if a player like Wal-Mart or Carrefour enters Guwahati, it will definitely attract more footfalls and affect our business adversely."

Dr. Sukhpal Singh, Associate Professor, Center for Management in Agriculture, IIM-Ahmedabad, says there is no doubt that traditional retailers will be impacted by the entry of foreign retail chains. "Some studies done by us have shown a 10 to 30 percent decline in sales of kiranas located within a kilometer of modern stores," he explains. According to him, the solution is not to block FDI but to provide

FDI IN RETAIL – A VIEW FROM AFAR

Prof. Rodney Fitch
Founder of design firm Fitch

I have often heard China and India compared. This is understandable since they have much in common including huge populations, growing economies, and a burgeoning middle class. There are, of course, substantial differences too: China believes in infrastructure investment, India does not; China is developing a modern, efficient retail sector; India is not.

Infrastructure and modern shopping go hand in hand – you cannot have one without the other. New shops, no matter who owns them, are nothing if there are no roads, chilled plants, and distribution centers to support the supply chain. Infrastructure is not only about capital projects; it is also about the infrastructure that helps toward building a civil society that can enjoy and share in the nation's success. FDI would help to deliver this since a healthy retail environment is high on the consumers' list of expectations and aspirations.

I have heard plenty of voices, all with vested interests, raised against FDI in retail – indeed at the last India Retail Forum in Mumbai, I even heard one of these voices liken FDI to a "backdoor recolonization of India." Get real! In Asia's largest democracy, I wonder if the consumer's interests are being ignored. Does an Indian polity really imagine that Indian people will be best served by the kirana industry and its variants for the foreseeable future? If it does, then this polity is misjudged because the tectonic plates of the Indian retail landscape are shifting. The modern shopping experience calls for choice, quality, value and convenience, and much of this is delivered by technology. Shopping everywhere is perhaps the most democratic of activities in which the citizen-consumer can engage – look at what is happening in Russia, China, and Brazil. Does India really feel it should stand apart and deny its own citizens those benefits? If those vested interests do, they should ask the people. I am quite confident that modern India would vote for as good a shopping environment as exists elsewhere in the world, and FDI would help deliver that experience.

I wrote all this mindful of the following: The Indian economy is slowing down from 9 to 10 percent to an optimistic 7.5 percent. Economy watchers expect this figure to be nearer 6.5 percent. Exports are also slowing. India is running considerable deficits and desperately needs foreign investment. There have been 13 interest rate rises in the last year alone, with the effect of making the price of goods, particularly food, more expensive, which hurts the poorest sections of the community the hardest.

FDI in the retail sector would go a long way to address some of these problems, by encouraging foreign investment, not least in distribution infrastructure and technology; creating a more competitive environment that would help drive down inflation; provide the citizen consumer with a much wider choice.

In the last decade, FDI across all sectors in India totalled around $130 bn. In contrast, China attracted FDI of $100 bn in 2010-11 alone! Vested interests talk about "stakeholders." In this debate. The only stakeholder who really matters is the citizen consumer. I do not hear much of a dialogue with them, notwithstanding the claims for democracy in India.

some kind of protection or support mechanism for small retailers to move on or better bear the impact of big international chains setting stores in their area. Small sellers have to be given space in the wider scheme of things.

While there is bound to be some change in any industry when large players come in with new paradigms and business models, what the actual impact will be on small retailers is anyone's guess, thinks Javeri of Forum Synergies. "The consumer will always gain with competition; the vendor will gain from a larger market and investment. A small retailer can stand up to the bigger retailer with better service and product planning. Some of the fears are real but others are definitely exaggerated."

Sahni of Wazir Advisors says that the negative impact of FDI on traditional retailers will be as much as has been with the arrival of Reliance or the Future Group in organized retail. "The policy change is about FDI, not about large or modern retail that has already existed in India for some years. With the restrictions that are proposed in the new FDI policy, I think there are enough measures to control any major disruption in the overall market," he adds.

Bagaria of the ASIPAC Group has calculated that there would not get created more than 300 new "foreign-owned" hypermarkets in 50-odd cities of India with a million plus population, in case FDI in multi-brand retail becomes a reality. At an average, one hypermarket will sell around Rs 30 mn worth of goods each month, which would otherwise be sold by the kiranas in the same neighborhood. As the average kirana store in these cities does business of around Rs 12 lakhs per month, a hypermarket displaces an average of 25 kirana stores. "Therefore, 300 hypermarkets will displace a maximum of 7,500 kirana stores. All the hullaballoo is only for these 7,500 kiranas all over India," he argues.

In contrast, the benefits of allowing FDI in multi-brand will be immense, Bagaria says, such as the following:

(a) The 300 new hypermarkets that are estimated to be established post-FDI will sell farm produce (including unprocessed meat, fish and seafood) worth Rs 48 bn per annum (at current prices). This will benefit more than 2 million farmers and fishermen.

(b) FDI in multi-brand retail will not be restricted to these 300 hypermarkets alone. There will be investments in non-food retail space as well, which does not affect kiranas that much. Overall, about 330 million square feet of new retail space will get created in cities with a million plus population, which will generate more than 4.58 million new jobs.

(c) The 330 million square feet of space will generate annual revenues of Rs 7.92 trillion and taxable profits of Rs 238 bn. This translates to Rs 1,092 bn in GST collections (@ 16% GST), Rs 73.5 bn in corporate income tax, and Rs 82.5 bn in personal income tax collections. This amounts to an increase of over 7.6 percent in the tax collection of the centre and states.

"Additionally, in the estimated five years that it will take for these new 300 hypermarkets to be built in the post-FDI scenario, the population of those 50 cities will grow by another 16 million – this extra population will

need more than 30,000 new kiranas to service them. So, it is 30,000 new kiranas versus 7,500 displaced kiranas," Bagaria says.

Sahni of Wazir Advisors too rejects the notion that FDI will result in the death of kiranas, arguing that most of the global large retailers are used to running large format stores and are not too keen on being present in every street. He says: "Indian chains like Food Bazaar, More and Reliance Fresh have tried to replace the kiranas

but haven't succeeded in the last five years. So will a fresh entrant like Walmart, facing a new country and a new set of customers, be able to beat the kiranas? I don't think so."

Sahni argues that Indians have a habit of buying fresh and cheapest food – preferably on credit – which works in favor of the small neighborhood shops. "It will be long time before all Indians become savvy enough to drive to an air-conditioned supermarket to buy vegetables and fruits. Also, food and grocery value chain is so complicated in India, most global retailers will likely stay away from it due to back-end issues. Most of them derive their majority sales from value-added processed and packaged food, not from fresh fruits and vegetables. And even if retailers like Auchan and M&S sell a lot of fresh food, their supply chain in their home countries is all well set and they need not go to the farm to collect produce. I don't see them doing that In India either," he adds.

Organized retail already exists in

ORGANIZED RETAIL ALREADY EXISTS IN INDIA AND HAS BEEN GROWING AT A CAGR OF 35 PERCENT, THE "THREAT" TO KIRANAS IS ALREADY ACTING IN THE COUNTRY THROUGH DOMESTIC RETAILERS, SO WHAT WILL CHANGE WITH THE FDI?

India and has been growing at a CAGR of 35 percent – the perceived "threat" to kiranas is already acting, so what will change with FDI? Explains Shah of Equirus Capital: "When we talk about retail FDI, in one way what we are talking about is the access to deep pockets which global companies enjoy and their ability to take huge initial losses. With retail FDI, two things will happen: organized retail will grow faster with injection of large capital, and they will have the willingness and deep pockets to continue operations despite incurring huge operating losses." It is this new-found ability of big retail chains in India to continue incurring losses that will have an impact on other players like kiranas. This is common phenomenon whenever an aggressive player comes in and works on a loss-leadership strategy.

Shah says that when this happens, the kiranas will evolve. The products mix sold by them will undergo a change – sale of intangibles like SIM cards and pre-paid vouchers will increase and so will service-based selling such as home delivery, just-in-time needs, fresh preparations like idli mix, daily bread and eggs. "India is a land of entrepreneurs and small retailers will survive. If you see the US – the land of organized retail – many such small shops are profitably run by the Indians. Why cannot they do the same in India?" Shah asks.

According to him, the farmers are set to benefit too with FDI, as presently the procurement system is stronger than them and is taking up a big slice of the end consumer price. "Even more importantly, the improvement in logistics and supply chain which organized retail is likely to bring in will benefit the farmers by reducing wastage and given them an ability to get a better price. The retailers are also likely to benefit as their purchasing costs will go down somewhat due to the competitive pressures within the entire procurement system brought about by organized retail," says Shah.

Javeri of Forum Synergies says FDI will not result in the death of traditional retailers. "It will actually result in the death of any retailer who cannot meet the service and product needs of consumers. If that retailer works more efficiently and with new-age tools for success, he will win. Again the issue is about big versus small, not Indian versus foreign," he adds.

Considering the conveniences offered by the kiranas for particular income groups both in the metros, tier II and III cities and in rural areas, they will continue to co-exist with supermarkets and hypermarkets, asserts Rao of Vestian Global. "China allowed FDI in retail 20 years ago, but that has not affected its local retail shops. The number of kiranas has actually gone up in China, rather than decline," says he.

Reddy of Apna Bazaar points out that the traditional kirana shops have very deep roots in the Indian society. "An important social segment of India needs kirana stores, and FDI cannot make this segment disappear. So nothing will happen and kiranas will keep on flourishing. This no challenge and even if it is there, it is very limited," he says. Agrees Singh of Max

Hypermarkets India: "In India there is space for both, the bigger format stores of organized retail and the traditional retail stores, as each caters to a different set of customers and there will be no major clash between the two."

CARTELISATION AND PRICE MANIPULATION

Critics of FDI allege that big global retailers can gain control of both the back-end and front-end of operations and get the ability to control prices of essential products such as grocery. Can this cartelization and price manipulation become a reality?

Says Dr. Sukhpal of IIM-Ahmedabad: "There is a possibility that foreign retail chains can monopolize the distribution of agricultural produce over the longer term. For example, in some European countries – where supermarket retail has been in existence for 50 years – just three or four supermarket chains account for around 80 percent of all food sales."

Bagaria of ASIPAC points out that India has enacted the MRP (Maximum Retail Price) law exactly for such a purpose – no one can sell a product higher than the MRP anywhere in the country. "European countries have populations of just 30 to 60 million and such small markets cannot be compared to India. Did FDI in telecom and insurance create monopolies? Did it increase prices?" Agrees Sahni of Wazir Advisors: "Even after the alleged monopolies, is the food more expensive in Europe than in US or Japan? European farmers – are they better off or not than their Indian counterparts? If both the consumers and farmers are happy, then who is left for us to bother about?" Reddy of Apna Bazaar says: "We must strengthen the MRTP Act to prepare for such an eventuality, and see that a few companies don't monopolize our system."

Argues Clive Woodger, Chairman of the strategic consulting group, SCG London: "Manipulation due to strong monopolies does not happen in Europe. In the UK, the major grocers have kept food prices and the cost of living low. The danger of over-protecting suppliers produces inefficiency with potentially poor quality and certainly does not allow competitive prices. In Russia, the supplier lobby is trying to persuade the government to bring in protective legislation, but the retailers are making the point that they have to be more attractive to consumers in an increasingly competitive market. This creates higher standards to the benefit of customers."

Rao of Vestian Retail says that the retail sector in India has completely different challenges as compared to Europe or the US due to the vast cultural differences as well as the strong urban-rural divide. "It may not be possible for a few foreign players to monopolize food distribution in India," he says.

"How big is food expenditure as a proportion of income of an average European or US family?" questions Shah of Equirus Capital. "It is quite small, compared to that of an average Indian family. Over time, food expenditure in India will come down in proportion on the lines of the West. Once that happens, how does it matter if there are five players or fifty? What is important is that there should be sufficient competition within those players."

WILL UNEMPLOYMENT RISE?

The government claims there will be 4 to 5 million new jobs created in the country if FDI in multi-brand retail is allowed. The critics on the other hand warn of major job losses in the traditional retail industry. What is the truth? Says Dr. Sukhpal Singh of IIM-Ahmedabad: "A lot of people are involved in retail in India. We have to see if we are

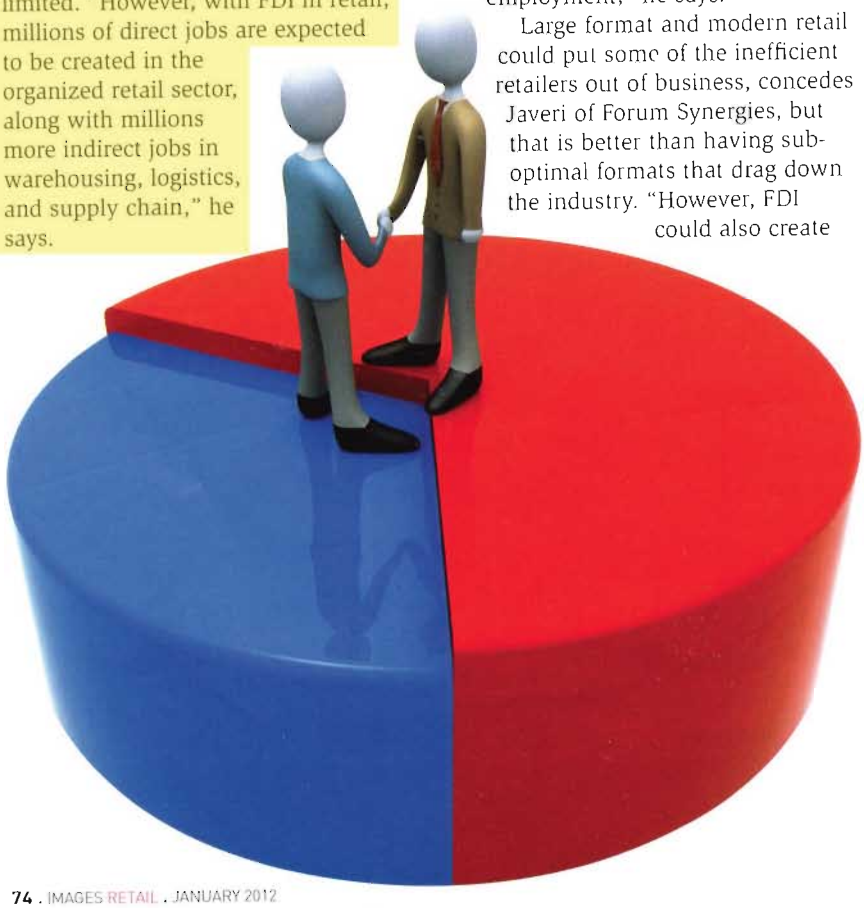
going to damage the already existing employment capability in our quest for generating new jobs through FDI in retail. Definitely the new FDI-driven retail system will generate some employment, but we have to carefully consider if it will displace the existing employment such as push-cart vendors, roadside stalls, small shops, etc."

Shah of Equirus Capital argues that with FDI, the days of cheap labor and exploitation of labor by retailers, traders and middlemen will get over. "Youth (both urban and rural) will have more avenues to seek employment, and the talented will be able to earn more. The traders and middlemen will feel the pinch as they will have to work hard to attract and retain good people in the post-FDI scenario," he adds.

Bagaria of ASPAC says for every job lost in the unorganized sector, a new job will be created in the organized one. "One should ask the politicians which out of the two would be the better job," he retorts. According to Rao of Vestian Global, the job loss in the unorganized market will be limited. "However, with FDI in retail, millions of direct jobs are expected to be created in the organized retail sector, along with millions more indirect jobs in warehousing, logistics, and supply chain," he says.

Reddy of Apna Bazaar contends that if one looks at the Chinese policy, they have allowed only the highly technical expatriates into the organized retail industry, that too for a limited time. "There will be some layoffs in the unorganized sector, but the organized sector will need manpower to function. So there will be a transition of jobs from unorganized sector to the organized sector, creating local employment," he says.

Large format and modern retail could put some of the inefficient retailers out of business, concedes Javeri of Forum Synergies, but that is better than having sub-optimal formats that drag down the industry. "However, FDI could also create massive opportunities for young people to be vendors or employees, as also the huge supplier base for retail," he says.



RESTRICTIONS ON GLOBAL PLAYERS

Many countries in the world impose restrictions on big-box retail to protect small players. These can come in many forms, such as zoning regulations, barring the supermarkets from selling certain items (such as breads and eggs), mandating a minimum distance between two supermarkets, and the type of stores that can be opened. The Indian government has also proposed some restrictions on large foreign retail chains in its FDI announcement, but critics say these do not go far enough in protecting the interests of small retailers.

There is nothing in the government's new FDI policy to protect the front-end, charges Dr. Sukhpal Singh of IIM-Ahmedabad, saying that once the bigger global players enter India, the kirana stores are going to lose sales because everybody will be taking a chunk of the same market. He explains: "The new policy mandates that foreign players can open shop only in 53 Indian cities with a million-plus population. But these together account for 42 percent of the total urban population of India! So, half of the urban market is already opened to the global players. In fact, the intensity of traditional retail is higher in such places."

Secondly, Dr. Sukhpal argues, there is no provision in the policy specifying the locations in a city where foreign retailers can open stores. In many countries, big retailers are often prevented from setting up stores within the municipal limits of a city. Sometimes, these can only be located a particular distance away. The policy does not say what kind of a store a foreign player can open and where. "Small retailers are understandably worried that some big-box store of a foreign retailer will open in their neighborhood and cut into their sales," says he.

Chacko of IIFT however doesn't think that the FDI policy announced by the Indian government for organized retail could be considered lenient on the global investors in any way. He points out that most of the countries in the world, including large economies having major agricultural interests, have gone for 100 percent FDI in retail. "In fact, the requirement in our FDI policy for 50 percent investment in back-end operations and 30 percent of the procurement from the SME, etc., viewed from the perspective of global investment would appear as unwelcome riders. Given that FDI is being allowed in principle only in 53 cities and towns and that too in states where the local governments are welcoming global retailers, the overall impact of FDI in retail in India would anyway have been not very significant," says Chacko.

Bijoor of Harish Bijoor Consults supports the government in imposing reasonable restrictions on global retail players. "I love the riders in the policy. We are talking of serious players with deep intent in the market coming in. The $100 mn investment that has been mandated in the back-end infrastructure ensures this," he says, adding that the 30 percent local-sourcing clause will ensure health

FDI IN RETAIL IS A CRYING NEED

Sanjiv Gupta
CEO,
GKB Opticals

Economically we are facing a tough situation in the country at the moment. The food inflation is very high at 9 percent and is refusing to come down despite a good monsoon. The main reason is that we are not organized in the food sector in terms of retail strength and supply chain. We need huge investments in food storage facilities (warehousing, cold storage, etc.) and professional managers to run them. The currently existing facilities – most of them government-owned – are so inadequate and in such a pathetic condition that almost 50 percent of all the food produced in India gets wasted, even as food consumption continues to rise.

Big global retailers will bring in investment along with management expertise and technology. Indian organized retailers such as the Future Group have been able to bring the share of organized food and grocery retail in the overall food retail segment to 3 percent. But we need to make this share grow to at least 15 to 20 percent in the next few years to ease out inefficiencies in the backend and substantially reduce wastage. This will in turn help bring down food inflation. The government can then afford to lower the interest rates leading to more economic growth, which can again rise to 9 percent from the current 6.9 percent.

Due to the high interest rates currently prevailing in India, the stock market has taken a beating, leading to an outflow of funds from the country. The Indian economy has suddenly turned quite weak and the Rupee has depreciated 18 percent against the Dollar, while other Asian currencies have depreciated by only about 8 percent. We need more foreign funds coming into India through FDI and FII. In the absence of this, Indian growth can slow down to a level from where it will be difficult to recover.

The government does not have the resources in terms of money or better governance to support Indian industry. Indian retailers have invested heavily over the last few years by incurring huge debts and they are running out of resources to grow at the same pace. With 51 percent FDI in multi-brand retail, foreign retailers can join them for further growth and bring the much-needed funds into India. In the FDI retail policy announced by the government, it is mandated that 30 percent of sourcing by global retailers have to be done from the micro and small-scale sector. This will be a big boost to our farmers who comprise 40 percent of our population. FDI will bring a huge change in the economic condition of the country. We Indians envy ourselves when we see neighboring countries such as Indonesia and China develop so much in the last 20 years while we have not. Maybe the reason is that they allowed FDI in retail 10 to 15 years back.

GIVE US A CHANCE TO SAY "THANK YOU!"

Shailesh Chaturvedi
CEO,
Tommy Hilfiger India

We celebrated the Retail Employees' Day on 12th Dec last year, and wholeheartedly said "Thank You" to our colleagues in the stores. We committed ourselves again to supporting them and helping them in further improving their lives. For this to happen, however, the Indian retail industry needs "enabling environment" which can help efficient organizations run profitable businesses. This is because without healthy bottom lines, it may be impossible for the retail industry to take care of its own people and generate quality employment.

So what are these enabling factors?

The cost structure in India has turned so hostile in recent times that even efficient organizations can lose money. Let us look at the cost blows on industry in the last few months:

- Cotton prices increased towards the early 2011, pushing the landed cost of garments in India by 10 to 15 percent.
- High inflation in India has impacted consumer sentiments. Despite increase in bank rates, government decided to impose excise duty on branded garments in the Union Budget of Feb 2011, pushing costs up further by 10 percent.
- The Rupee overall plunged by 15 percent in 2011, with more than 10 percent drop occurring only in the month of September. This has pushed the cost of imported garments and trims skywards.
- The liberalization of FDI in retail would have helped the investment climate, but the logjam there has made foreign investors cautious.

Basically, there has been one bad news after another for the Indian industry. It needs enabling factors such as the following to help it regain its health:

- Reduction of Import Duties: The government's stated policy is to bring import duties towards the ASEAN level, which is 20 percent. However, the duties in India are at least 15 percent higher. There is a need to drop the total import duties in the country to the 20 percent mark.
- Excise Duty: This duty is MRP-led. Given the high level of discounting, the garment industry ends up paying excise duty on discounts given to customers! The current level of abatement is not sufficient or realistic.
- Implementation of GST: This is urgently needed to streamline input costs and bring simplicity in operations.
- Octroi/Entry Tax: This should be totally abolished in important cities like Mumbai, to reduce the cost of doing business.

for the SME manufacturing sector of India.

Zoning restrictions are already in place by limiting the global players to million-plus cities only, points out Rao of Vestian Global. "The new policy has addressed a lot of issues by restricting FDI in multi-brand retail to 51 percent. Further, the condition of 30 percent local sourcing will safeguard interests of the smaller local producers and improve efficiency in the existing Indian eco-system," he says. "These conditions will give sufficient time to the government to understand the effects of FDI on the Indian retail market before allowing it in regions where local population is more dependent on domestic economy and less open to changes."

Sahni of Wazir Advisors believes there should indeed be restrictions on global players, mainly to assure the stakeholders that there would not get a free run of the market. "My whole argument is that big retailers are not interested in small stores, and also are not too keen on selling fresh fruits and vegetables. So zoning or no zoning, Walmart is not coming to every street in India. Global retailers will not go all the way to the farms either to buy their produce. It will actually be the big consolidators of food like Cargill and Sysco which will do the collection from farms and then supply to the retailers. These big suppliers will come to India only when there are farm-level policy changes to facilitate their investments," he says.

Javeri of Form Synergies, on the other hand, says there should be no restrictions at all on the global retail players in India.

"We should not differentiate between Indian and foreign retailers, but create an environment where the small entrepreneur thrives and wins," he suggests.

THE WAY FORWARD

Industry watchers and organized retail players are unanimous that once the FDI policy has been announced, the government should not backtrack under political pressure. Instead, it should try to create a consensus around the issue and ensure more effective

protection for small retailers, so that their opposition to the entry of global retailers gets diluted.

If the FDI announcement is rolled back, it will be quite a serious setback for foreign direct investments in India, warns Chacko of the Indian Institute of Foreign Trade. India would be seen in the world as a country that is not able to provide a suitable and liberalized framework for investment. The credibility of the government itself would be a factor in attracting large-scale investments from foreign investors. Even the Indian industry would be wary of taking decisions involving major investments.

Woodger of SCG London says his experience of international markets such as the UK, Europe and particularly Russia (another BRIC economy) is that governments should not frustrate competition and restrict consumer choice. Protecting inefficiency and poor quality is ultimately counterproductive for everyone. "Encouraging international operations to bring more efficient logistics, processes and practices would stop the incredible current waste of existing systems and operations in India. It cannot be morally and environmentally right to produce food and then see so much waste due to the inefficient product procurement that India experiences today," he argues.

Javeri of Forum Synergies feels the issue is large, but so is the opportunity. People have to look at the issue as an economic and political matter; one dimension cannot succeed without the other. "My view is that the issue is not understood correctly by most people and as a result, there is confusion all around. For me the issue is about big versus small and traditional versus modern, not Indian versus foreign," he stresses.

Javeri's advice to the government: Welcome FDI up to 51 percent in modern multi-brand retail and encourage modern Indian groups in retail, but also aggressively support small retail. He offers a five-point action plan:

- Support small Indian retailers with low-cost finance for capital expenditure and working capital. Provide finance to the allied and feeder businesses which supply to retailers to build the ecosystem of modern retail.
- Provide key retail associations with a government-backed mandate and resources to train and develop retail entrepreneurs and retail employees, who can build either careers or businesses.
- Provide infrastructure and government-backed channels for direct sourcing from foodgrain, fruit, vegetables, flowers and cash-crop farmers, as also fishermen and other agriculturists to improve price realization and product quality.
- Provide tax exemptions for small retailers on real-estate costs which are the biggest costs for them today.
- Allow 100 percent FDI for feeder and supplier businesses immediately, even if you do not want to give international retailers access to the Indian consumer.

"Such a retail initiative could be the showcase of a government's desire to be progressive, modern, and yet Indian. This five-point plan should ensure a win-win success story for the retailer who satisfies his customers, whether big or small," says Javeri. According to him, the government should at least open FDI to supplier, vendor and feeder businesses immediately.

Shah of Equirus Capital suggests the government should reduce the percent of FDI allowed to soften the impact. To begin with, the government should have only up to 49 percent FDI in multi-brand retail, but reduce the FDI investment limit to $50 mn. "This will

BENEFITS OF FDI IN MULTI-BRAND RETAIL

Sanjiv Goenka
Chairman, RP-Sanjiv Goenka Group

FDI will propel the growth of organized retail in India. This will be good for the consumers as it will lead to disintermediation of the supply chain and bring substantial investments and technology in the back-end. It in turn will reduce wastage and improve efficiencies, which will have a softening impact on inflation in the long run.

Other benefits of FDI:

- Capex (investments) in any industry is most welcome. FDI or domestic, it will create additional capacity and hasten the growth of modern trade.
- Fifty percent of the FDI investment is to be in the back-end (cold storage, etc.), which will help reduce wastage and help contain inflationary pressures. This in turn will improve accessibility and affordability for the shopper as modern trade will be within his reach.
- Modern retail stores will become a viable option for SMEs to represent their range of merchandise which is critical to the inclusive growth of the economy.
- As more and more business gets monetized it also helps the government recover taxes fairly.
- Today, about 90 percent of the children in India do not pursue education beyond schooling. With large number of new stores opening up, modern trade will become a preferred choice of employment for them. This has its own positive impact on the economy.

For all of the above to gain momentum, the government needs be an enabler.

make it easier for many players to come in, thereby giving only the large players an upper hand. Competition will make it equally tough for all players, thus ensuring survival of the fittest," he says.

The best way forward according to Sahni of Wazir Advisors will be to allow 100 percent FDI in single-brand retail initially. "Also, if the government can allow foreign institutional investors (FIIs) to invest in Indian retail, it will be fantastic because I believe the first need of the retail sector is capital and not necessarily the foreign brands and retailers," he says. According to him, another thing the government can do is to keep the food and grocery category out of bounds for the global retailers but allow them to trade in things like electronics, furniture and apparel.

"It is all about communication and that is not going to happen overnight. It will be a long drawn process and having put the FDI on hold once, the government has in a way legitimized the resistance and it would be harder to overcome this soon. I believe any policy change as big as this should not be forced through and all stakeholders need to be taken along. Thus the government has to do lot more convincing and make the opposition see the merit of allowing FDI in the sector," he says.

Thakur of 7 to 9 Bazaar suggests that the global retail chains should only be restricted to the metros to make their presence more palatable, otherwise in the smaller towns, things will get very tough for small retailers. Reddy of Apna Bazaar says the solution to the FDI logjam is to form a restricted policy, and the government should involve consumer bodies as well as farmers and retailers associations in the decision-forming process.

Javeri of Forum Synergies points out that India has a rich heritage in retail, driven primarily by service excellence and cost efficiencies, and there are several Indian-origin retailers all over the world. With almost 14 million retail outlets existing in India, the country has around 60 to 70 million people directly dependent on retail. They in turn have hundreds of millions of satisfied and loyal customers who get proper service and even credit. Another 30-40 million people would be involved in the ecosystem of allied businesses related to retail.

According to Javeri, what is needed is an Indian solution for an Indian opportunity. "The opportunity is to create new-age entrepreneurs who offer new products and services

THE GOVERNMENT SHOULD IMMEDIATELY ALLOW FOREIGN INSTITUTIONAL INVESTORS (FIIS) TO INVEST IN INDIAN RETAIL BECAUSE THE FIRST NEED OF THE RETAIL SECTOR IS CAPITAL AND NOT NECESSARILY THE FOREIGN BRANDS AND RETAILERS

to the new-age Indian consumer. The opportunity is to support new businesses feeding into retail and provide them with finance, tax breaks and support to win," he says. "FDI in retail should be welcome, but for the right reasons relevant to us Indians and with the right parallel actions. FDI will come in with huge infrastructure creation, including significant sourcing enhancement and vendor development, establishment of an efficient supply chain, warehousing and logistics, as well as massive opportunities for the youth in the front-end of retail and several allied and support businesses."

There are lessons to be learnt from other countries and how they have benefitted from FDI in retail. For example, in China, employment in retail has almost doubled between 1992 and 2001. In other developing countries such as Brazil, Poland and Thailand, FDI in retail has been a key driver in increasing productivity, resulting in lower prices and higher consumption. "Global retailers in these countries are forcing wholesalers and food processors to improve quality and bring down prices. Further, these retailers are also emerging as important sources of exports. For example, Tesco in Thailand and Walmart in Brazil are sourcing local products for their global supply chains," says Shrinivas Rao of Vestian Global.

Chacko of the Indian Institute of Foreign Trade has the last word: "In my view, the announced FDI policy in organized retail should be implemented. Learning from the experience and lessons of its implementation, the policy could be fine-tuned in three to five years. In all probability, such fine-tuning would result in further liberalization of FDI in retail as the overall impact would be highly positive."

If managed well, FDI can be a very powerful resource for modernizing India's organized retail industry. The only thing the government has to do is to protect the underside and cushion its impact on the fortunes of small Indian retailers. ☒