

FDI IN INDIAN RETAIL: FOOD AND GROCERY INDUSTRY

T.Vijaya^{1*} and Usha Munipalle²

¹Department of Management, Nizam College, Hyderabad, Andhra Pradesh, India.

²Professor, Department of Management, Nizam College, Hyderabad, Andhra Pradesh, India.

Corresponding Author

T.Vijaya

Email: vijji_tiru@rediffmail.com

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ABSTRACT

Indian retail industry is one of the sunrise sectors with mammoth growth potential. The recent wave of reforms by the Government to incentivize Foreign Direct Investment (FDI) in various sectors is bringing a new zest to the investment climate in India. One of the most debated reforms is the policy for allowing 51 per cent FDI in multi-brand retail. Organized retail sector considers 8% of total retail sector, which is expected to grow 20% by 2020 by various estimates. The Indian retail industry has experienced growth of 10.6% between 2010 and 2012 and is expected to increase to USD 750-850 billion by 2015. Food and Grocery is the largest category within the retail sector with 60 per cent share followed by others. The demand-push impact of a young consuming class with growing disposable incomes, India offers significant investment opportunities in the food and agri-business sector. This paper explains the impact of FDI in Multi-Brand Retail Trade (MBRT) in relation to food and grocery sector, by balancing the interests of different stake holders like farmers – corporate – government- consumers. The change in some of the policy conditions indicates government intention to “move food from farm to plate”. With its backward and forward linkages, MBRT can act as wealth and health creator for the nation. Some of the thrust areas of the MBRT are to develop Infrastructure, to enhance productivity and quality, development of SME sector, taming inflation and others. The first part of the paper contains the introduction about the FDI in retail segment of food and grocery, continued by evaluation of various opportunities and challenges with the entry of FDI which can be buoyed by a favorable policy environment by government to protect the basic standard of the industry.

Key words: FDI, MBRT, Food and Grocery.

INTRODUCTION

The government allowing FDI of up to 51% in multi-brand retail, as part of moves aimed at encouraging investment in the country. Categories such as mass grocery and apparel will emerge as the two most favored destinations following the government allowing foreign direct investment (FDI) in multi-brand retail. In both these segments there are large domestic retailers who could be potential joint venture partners for foreign retailers. Retail sector in India is the second largest employer after agriculture. Almost 33 million people involved here. India is the second largest producer of fruits and vegetables. Foreign retailers could enter India by forming a new joint venture company, which shall have multi-brand retail stores in India. Alternatively, the foreign investor may also consider acquiring 51% stake in the existing business set-up of the potential Indian joint venture partner. The Indian retail industry has seen growth of 10.6% between 2010 and 2012 and is expected to reach \$750-850 billion by 2015, according to the report. Food and grocery is the largest category within the retail sector with a 60% share, followed by the apparel and mobile phones. Existing mass grocery retailers in India already source many products directly from producers and “small” food processing units, which is why they are likely to be a draw for overseas investment. Organized retail, which constitutes 8% of the total retail market now, will grow much faster than traditional retail, according to the report. Its share of the growing retail market in India is also expected to expand. Various estimates put the share of organized retail at 20% by 2020. There was large pandemonium about this issue regarding the opportunities and challenges but at the same time we should be in equal footage with the changing times of the dynamic world. The recent allowance of FDI in multi brand retailing will allow global retail powerhouses like Wal-Mart, Carrefour and Tesco to tap the above market in India [1-3].



Objectives

- To analyze the prospects and constraints faced by the retail sector in relation to food and grocery sector, by the entry of FDI.
- To study the various policies framed by the government, to protect the basic Indian sectors.

METHODOLOGY

The methodology is designed with an intention to make a critical appraisal of the challenges and opportunities, faced by the Indian populace and foreign MNC'S while creating a conducive business environment. The study is based on secondary source of data.

Prospects and constraints faced by the retail sector in relation to food and grocery sector, by the entry of FDI. There are many spillover effects with the entry of FDI into the Indian economy, as such there may be demanding situations for the Indian government and populace, which should be attacked in a proper manner.

Reduction in wastage to goods: According to industry estimates, 35-40% of fruits and vegetables and nearly 10% of food grains in India are wasted; at the end of the day total 60% of the goods reach the consumer. Though FDI is permitted in cold-chain to the extent of 100%, through the automatic route, in the absence of FDI in front-end retail, investment flows into this sector have been insignificant [1].

Reinforcing the efficiencies of supply chain:

FDI act as a catalyst between many lacunae for Indian farmers to make farming again a profitable business activity with better supportive infrastructure. Metamorphosis of food supply chain with the entry of FDI helps in enhancement of cold storages, warehousing facilities is pivotal to the incomes of hundreds of millions of those employed in rural and urban areas as farmers, wholesalers, truckers, processors, and retailers participating in these supply chain.

A typical example of Himachal apple illustrated above, that the farmer only fetches 30% in place of 70-75% (excluding transport cost) because of absence of direct buyers and presence of mediators. Currently about two thirds of the total value share is hooked by the middlemen and traders in the commodity trade business.

Analysis: In the above example, if middle people in the supply chain are removed, it will be a win-win situation for both the farmer and the consumer. Farmer will be benefited up to $(30+8+10+20= 70\%)$ and at the same time consumer will get a benefit of 5-10%.

The low return to the primary producer restricts the quality received by the end consumer and the presence of unnecessary mediatory increases the end produce price. At the brim it is the producer and the consumer who carries the agony, FDI in retailing can be the path breaker indulging benefits for primary produce and the end consumer [2].

Advantage for farmers

In the interim process of production and marketing of commodities, Indian farmer deals with a pile of challenges, like, low productivity, shrinking land holdings, less availability of farm inputs, depleting share of income, and the list is endless, remaining pawns in the hands of big landlords. Current state of supply chain of perishables adds up to the end price of commodities. Lack of proper transport and storage facilities increases the wastage level and lowers the availability of produce. Augmentation of international retailers operations will encourage farmers to utilize better storage and transportation facilities. With a huge geographical area, there are many admirable exotic commodities which are restricted with local markets. The upgraded supply chain interventions will improvise the reach of these commodities a producers will fetch better returns. Not only this when Indian farmers enter the Supermarket Channel of food supplies (either directly or through agents) their source of income will increase substantially. So we can that end-to-solutions are provided by these retail chains and will benefit one and all [3].

- **Check on inflation:** In the past few years the food inflation has shot up by a double digit growth and whenever the control measures have been suggested, they pertain to the supply side of the food chain. FDI in retail will give impetus to the backward linkages which is essential for controlling food inflation. Players in the organized retail sector will create adequate infrastructure facilities, thereby reducing wastages and increasing the supply of commodities, bringing down their prices considerably.

- **Development in MSME sector:** Upliftment of MSME sector with the entry of FDI, in the areas of food processing sector and other related areas.

- **Impact on end consumers:** The strongest impact of organized retailing would be seen on the consumers. Along with the increase in disposable income and increased discretionary expenditure, the consumers will get better choice of dimensions. Indian Customer has a win-win situation with this FDI policy in multi branding retailing. With opening of supermarkets in India Indian customer will experience a world class standards of retailing.

Employment generation: Huge investments in the retail sector will see gainful employment opportunities in *agro-processing, sorting, marketing, logistic management and the front-end retail business*. Industry estimates suggest employment of one person per 350-400 sq. ft of retail space, which means nearly 1.5 million jobs, will be created in the front-end alone in the next 5 years. Assuming that 10% extra people are required for the back end, the direct employment generated by the organized retail sector in India over the coming 5 years will be close to 1.7 million jobs. Indirect employment generated on the supply chain to feed this retail business will add millions of jobs. From an Indian perspective, the advent of international retailers



would mean an FDI infusion of \$5 billion over the next five years. Retail joint ventures are actually going to hire a lot of people. So, in the short run, there will be a spurt in jobs. Eventually, there's likely to be a redistribution of jobs with some drying up (like that of middlemen) and some new ones sprouting up entire new supply chain system where jobs are being created not in selling physically to people but in upgrading the supply. Unless you take that into account this comparison is meaningless. Not only would consumers be further spoiled for choice, Indian retailers, by partnering with international players such as Wal-Mart and Carrefour would be able to adopt global best practices and become more efficient [4].

Impact on corporate taxes

There is a direct relationship between the increase in tax receipts and the increasing share of corporatized retail. Most retail transactions take place in India are in cash. This provides a significant headway for a parallel economy to mushroom. There are tax (VAT) leakages via under-invoicing or non-reportage of sales. The framework of independent retail also provides enabling conditions for the trade of phony and counterfeit goods. With an expanding share of corporatized retail, the probability of such leakage shrinks and the certainty of tax receipts surges [5].

Manifold Challenges

▪ **Unemployment**

A major debate in this whole section of FDI entry is the creation of unemployment which has to be compensated in other related areas with its forward and backward linkages.

▪ **Different structure of sales tax in different states**

Lack of uniform tax system for organized retailing is also one of the obstacles. Inadequate infrastructure is likely to be an obstacle in the growth of organized retails, with multi-point octroi collection.

▪ **Problems of supply chain intermediaries and logistics**

It is feared that foreign retailers will directly impact existing supply chain intermediaries that are being fed by SME's. Since sourcing from domestic SME's is not mandatory, foreign retailers may source the products from countries like China which is known as manufacturing hub of the world and it may put Indian SME sector in great danger. There may be a possibility of large scale unemployment if not checked. The current provision of 30% sourcing from Indian SME's should be made mandatory and should be strictly monitored. Due to predatory pricing strategies, vast class of India's merchants. For perishables, the system is too complex. Government regulations, lack of adequate infrastructure and inadequate investment are the possible bottlenecks for retail companies. The supply chain for staples is less complicated than the net groceries. But staples have a unique problem of no standardization

▪ **Competition between the local kiranas**

The local kiranas, small shopkeepers, hawkers, peddlers still form major section of Indian economy. Retail sector acts as a shock absorbing sector, providing opportunities for self employment in case of economic slowdown. The local shopkeepers in the vicinity of big retailers might find it difficult to compete. The prices will be determined by modern retailers and small shopkeepers may have to loose their profit margin due to predatory pricing strategy. The entry of large global retailers such as Wal-mart would kill local shops and millions of jobs, since the unorganized retail sector employs an enormous percentage of Indian population after the agriculture sector; secondly that the global retailers would conspire and exercise monopolistic power to raise prices and monopolistic (big buying) power to reduce the prices received by the suppliers; thirdly, it would lead to asymmetrical growth in cities, causing discontent and social tension elsewhere

▪ **Not – catering to all the economic classes**

Will mainly cater to high-end consumers placed in metros and will not deliver mass consumption goods for customers in villages and small town.

▪ **High cost of real estate**

The most important ingredient for a modern trade retailer is real estate in the right catchment area. A retail store would require anywhere between 50,000 and 100,000 sq ft of retail space. The biggest challenge in the India retail story is availability of quality real estate. Instead of setting up large stores within the city, retailers in most mature markets set up a 100,000 sq ft plus store, on the outskirts, saving on expensive real estate. But the average Indian prefers picking up groceries from a nearby kirana store rather than navigate through heavy traffic on bad roads. This leaves the retailer with little option but to look for real estate within the city. But one rarely finds big box retail stores on High Street, Linking Road, Mumbai and South Ex in Delhi don't have a single big-box retail store. There is no space in these areas to accommodate a 50,000 sq ft store and the costs are exorbitant—Rs 300-400 per sq ft. It will be difficult to sustain at those prices.

Cost of big-box retail stores in India are located in malls, which are mostly in the suburbs. For example, almost 80% of the malls in Mumbai are located in suburbs such as Malad, Vashi and Mulund. At Rs 100-120 a sq ft, the rentals here are not cheap either. And there's a shortage of quality malls—there are around 150 malls in the country, of which only 30-40 are making money.

▪ **Repatriation of profits:** FDI inflows should be balanced with the outflows accordingly, in the form of profits remittances on the investments made, that are repatriated to the home country. This could have implications in economic downturns where net FDI could decrease sharply without a corresponding decrease in profit remittances and thus worsen the balance of payment contribution of the



- FDI course. This has special relevance now given the scale and the extent of the ongoing financial crisis in the globe.
- The negative effect on the domestic private sector: Government should frame the policies to protect the new born industries and plan some incentives for these, to umbrella these from the FDI [6-8].

Policies of government

FDI monitoring and reviewing agencies [8]

1. The Ministry of Commerce and Industry, GOI is the nodal agency monitoring and reviewing FDI policy on continuous basis.

2. RBI (Reserve Bank of India): RBI administers FEMA along with Directorate of Enforcement under the Ministry of Finance. Its main objective is to facilitate external trade and payment and promote orderly development and maintenance of foreign exchange market in India.

3. FIPB (Foreign Investment Promotion Board): FIPB is a board, set up under Dept. of Economic Affairs, Ministry of Finance, and GOI. It is a government body that offers single window clearance for proposals on FDI in India that is not allowed an access through automatic

routes. FIPB has powers to consider recommendations up to Rs. 1200 crores. Proposals more than Rs. 1200 crores require the approval of cabinet committee on economic affairs (CCEA). It is mandated to play important role in the administration and implementation of governments FDI policy.

4. DIPP (Dept of Industrial Policy and Promotion)

Established in 1995, reconstituted in 2000, this board mainly looks after the formulation and implementation of industrial policies and strategies for industrial development of the country.

Now the Committee of Secretaries had given their nod to 51% FDI in multi brand retail, but with stringent conditions like mandatory investment of at least 50% in the back-end infrastructure.

1. 50% investment in back - end infrastructure, but also generate the employment to the country.

2. Minimum sales of 30% to come from small traders, it will create a very good opportunity for small traders and they will competitive enough.

Table 1. Percentage of Losses Estimated for Major Produces for the Year 2010

| Crop | Percentage of Losses Estimated for Major Produces (Cumulative Wastage - %) |
|---------------------|--|
| Cereals | 3.9 - 6.0 |
| Pulses | 4.3 – 6.1 |
| Oil seeds | 6.0 |
| Fruits & vegetables | 5.8 – 18.0 |
| Milk | 0.8 |
| Fisheries | 2.9 – 6.9 |
| Meat | 2.3 |
| Poultry | 3.7 |

Source: A study of CIPHET, 2010

Table 2. Inefficiencies of Supply Chain

| Supply Chain Stakeholder | Price Break Up/Kg | % Share | Gross margin % |
|--------------------------|-------------------|---------|----------------|
| Farmer | 27 | 28-30 | |
| Transporter | 5 | 5-8 | 12-15 |
| Commission agent | 7 | 8-10 | 18-20 |
| Aggregate cum wholesaler | 11 | 12-13 | 20-25 |
| Transporter | 5 | 5-8 | 8-10 |
| Distributor | 16 | 18-20 | 20-25 |
| Retailer | 20 | 20-25 | 20-25 |
| | 90 | 100 | |

Source: Technopak analysis

Table 3. Expected Employment Status on FDI Entry

| Year | 2001 | 2012 | 2021 |
|---|-------------|-------------|-------------|
| GDP (USD bn) | 450 (US bn) | 1958 (USbn) | 3310 (USbn) |
| Estimated merchandise consumption | 120 | 490 | 810 |
| Share of independent retail (mn) | 115 | 455 | 648 |
| No of direct employees in independent retail (mn) | 18 | 22 | 31 |
| Shares of corporatized(usd bn) | 5 | 34 | 162 |
| No of direct employees | 0.1 | 0.7 | 3.3 |

Source: Technopak analysis



Table 4. Estimates Showing Increase in Corporate Taxes After FDI Entry

| year | 2001 | 2012 | 2021 |
|---|------|------|------|
| Total merchandise retail(USDbn) | 120 | 490 | 810 |
| Share of organized retail | 4% | 7% | 20% |
| Size of organized retail(USDbn) | 5 | 34 | 162 |
| Tax revenue @weighted avg tax rate 10% (USDbn) | 0.5 | 3.4 | 16.2 |

Source: Technopak analysis

Figure 1. India in retail report 2013, images group

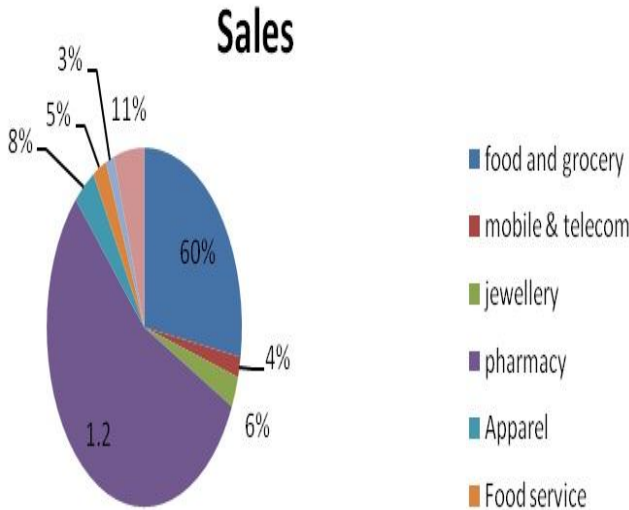
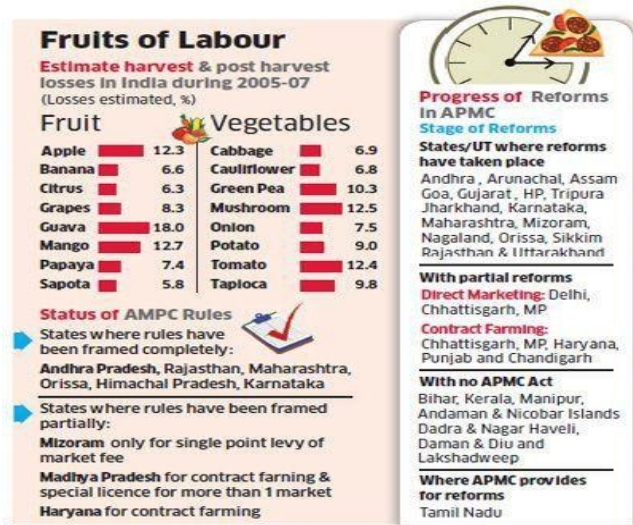


Figure 2. Percentage of Harvest & Post Harvest Losses of Fruits for the Year 2005-2007



3. 30% mandatory sourcing from small and medium enterprises will give an opportunity to small and medium enterprises to be competitive and improve their quality because whoever will come in India they will be very quality conscious. FDI multi-brand retail clears the deck for multi-national chains such as Carrefour, Tesco and Wal-Mart to set up shop in India, but with riders [9].

4. Zonlisation of the FDI limits, in the urban and rural areas. A strong legal framework in the form of the Competition Commission is available to deal with any anti-competitive practices, including predatory pricing to meet the policy guidelines on sourcing and to have better margins, foreign retailers would need to cultivate relationships with local manufacturers to drive strong private label brand. However, some conditions could delay the entry of multi-brand retailers, the report said. Land cost and rentals for warehousing are not included in the definition of backend infrastructure, the report said. The stipulation of a minimum investment of Rs250-220 crore in the first three years in back-end infrastructure may be a concern for the mass grocery segment, it said in conformity with developmental needs and national objectives. It also plays key role in the formulation of FDI policy, approval and facilitation of FDI. It also plays a role in resolving problems faced by foreign investors in implementation of

their projects through Foreign Investment Implementation Authority (FIIA), which interacts directly with ministries/state Governments concerned. framework on FDI. Industrial Assistance in DIPP, under Ministry of Commerce and Industry, is another facilitation body as regards to FDI in India [10].

CONCLUSION

Even though this a controversial issue, after balancing both the prospects and constraints, prospects outweigh the constraints, which can be overcome with time. Entry of FDI help in improvements in supply chain management, product quality, decreasing wastage, taming the inflation by improving the supply side of products, last but the key argument in this whole issue is unemployment created by the FDI can be outweighed by the jobs in food processing and allied sectors. Paucity of quality retail space, soaring rentals, different consumer mindsets, unfriendly policies and the volatile political climate are bound to scare away any international retailer with India aspirations. But with low growth rates on their home terrain, international retailers are desperately looking at emerging markets to fuel further growth. Exclusive regulatory framework is necessary in order to keep the basic standards of the industry. So, that there will be a win-win trading situation for everybody.



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