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Address

- Vikram Nagar, Boudhi Chouk, Latur.
- Tq. Latur, Dis. Latur 413512
- (+91) 9922455749, (+91) 9158387437

Email

- editor@aiirjournal.com
- aiirjpramod@gmail.com

Website

- www.aiirjournal.com

CHIEF EDITOR – PRAMOD PRAKASHRAO TANDALE

Role of FDI in Indian Economy

Author**Mr.Suhas S.Pawar**

B.Com, M.B.A.

Co-Author**Ms. Shital D.Hangargekar**

M.sc (CM), M.B.A.

Retailing in India:-

Is one of the pillars of its economy and accounts for 14 to 15 percent of its GDP. The Indian retail market is estimated to be US\$ 450 billion and one of the top five retail markets in the world by economic value. India is one of the fastest growing retail markets in the world, with 1.2 billion people. There are two types of retailing in India:

a. Organized retailing b. Unorganized Retailing.

Organized retailing:-

In India refers to trading activities undertaken by licensed retailers, that is, those who are registered for sales tax, income tax, etc. These include the publicly traded supermarkets, corporate-backed hypermarkets and retail chains, and also the privately owned large retail businesses. E.g. Carrefour, Wal-Mart, K- mart, Spencer's, Tesco and so on.

Unorganized retailing:-

Refers to the traditional formats of low-cost retailing, for example, the local corner shops, general stores, paan/beedi shops, convenience stores, hand cart and pavement vendors, etc. India's retail industry (organized and unorganized in combination) employs about 40 million Indians (3.3% of Indian population). The typical Indian retail shops are very small. Over 14 million outlets operate in the country and only 4% of them being larger than 500 sq ft (46 m²) in size. Vast majority of the unorganized retail shops in India employ family members, they do not have the scale to procure or transport products at wholesale level, have no training on safe and hygienic storage, packaging or logistics. The unorganized retail shops source their products from a chain of middlemen who mark up the product as it moves from farmer or producer to the consumer. The unorganized retail shops do not offer after-sales support or service. Finally, most transactions at unorganized retail shops are done with cash. Organized retailing was absent in most rural and small towns of India in 2010. Supermarkets and similar organized retail accounted for just 4% of the market.

Until the 1990s, regulations prevented innovation and entrepreneurship in Indian retailing. Farmers and producers had to go through middlemen monopolies. The

logistics and infrastructure was very poor, with losses exceeding 30 percent. Through the 1990s, India introduced widespread free market reforms, including some related to retail. Between 2000 to 2010, consumers in selected Indian cities have gradually begun to experience the quality, choice, convenience and benefits of organized retail industry.

Foreign direct investment :-

FDI refers to capital inflows from abroad that are invested to enhance the production capacity of the economy. However, FDI in retail is different from the investment in corporate, manufacturing, or infrastructure sectors. Retail can be single or multi brand and may be described as a sale to the ultimate consumer at a margin of profit. While the FDI in single-brand retailing was allowed earlier, FDI in multi-brand retailing is being allowed now; meaning a retail store with a foreign direct investment can sell multiple brands under one roof. So it is the link between the producer/manufacturer and the individual consumer.

Proposals to permit FDI in multi-brand retail trading in all products, in a calibrated manner, are likely to be subject to the following conditions:

- 1.FDI in multi-brand retail may be permitted to the extent of 51 per cent with government approval.
- 2.Minimum amount to be brought in as FDI by a foreign investor would be around \$100 million.
- 3.At least 30 per cent of the procurement of manufactured processed products shall be sourced from small industries, in the country, that have total investment in plant and machinery not exceeding \$100 million.
- 4.The government will have the first right to procurement of agriculture products.
- 5.Fresh agricultural products, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meal products may be unbranded.
- 6.At least 50 per cent of the total FDI brought in shall be invested in back-end infrastructure. Back-end infrastructure will include investment made towards processing, manufacturing, distribution, design improvement, quality control, packaging, logistics.
- 7.This valuation refers to the value at the time of installation without providing for depreciation.
8. Further, if at any point in time, this valuation is exceeded the industry shall not qualify as a small industry for this purpose.
- 9.Expenditure on land cost and rental, if any, will not be counted for purposes of back-end infrastructure.
10. Self-certification will be done by the company to ensure compliance of all the conditions.
11. Retail sales locations may be set up only in cities with a population of more than 10 lakh (1 million) as per 2011 Census and may also cover an area of 10 km around municipal urban agglomeration limits of such cities.

12. Retail locations will be restricted to areas as per the master zonal plans of the cities concerned and provisions will be made for requisite facilities such as transport connectivity and parking.

FDI: Growth over 1997-2012:-

In 1997, India allowed foreign direct investment (FDI) in cash and carry wholesale. The automatic permission was granted in 2006. Between 2000 to 2010, Indian retail attracted about \$1.8 billion in foreign direct investment, representing a very small 1.5% of total investment flow into India. Single brand retailing attracted 94 proposals between 2006 and 2010, of which 57 were approved and implemented. For a country of 1.2 billion people, this is a very small number. Some claim one of the primary restraints inhibiting better participation was that India required single brand retailers to limit their ownership in Indian outlets to 51%. China in contrast allows 100% ownership by foreign companies in both single brand and multi-brand retail presence. Indian retail has experienced limited growth, and its spoilage of food harvest is amongst the highest in the world, because of very limited integrated cold-chain and other infrastructure. India has only 5386 stand-alone cold storages, having a total capacity of 23.6 million metric tons that is grossly inadequate during peak harvest seasons. This leads to about 30% losses in certain perishable agricultural output in India, on average, every year. Until 2010, intermediaries and middlemen in India have dominated the value chain. The 60%+ margins for middlemen and traditional retail shops have limited growth and prevented innovation in Indian retail industry. Until 2010, intermediaries and middlemen in India have dominated the value chain. The 60%+ margins for middlemen and traditional retail shops have limited growth and prevented innovation in Indian retail industry.

A 2007 report noted that an increasing number of people in India are turning to the services sector for employment due to the relative low compensation offered by the traditional agriculture and manufacturing sectors. The organized retail market is growing at 35 percent annually while growth of unorganized retail sector is pegged at 6 percent. As of 2008, Organized retail is expected to garner about 16-18 percent of the total retail market (US \$ 65-75 billion) in the next 5 years. India has topped the A.T. Kearney's annual Global Retail Development Index (GRDI) for the third consecutive year, maintaining its position as the most attractive market for retail investment. The Indian economy has registered a growth of 8% for 2007. The predictions for 2008 is 7.9%. The enormous growth of the retail industry has created a huge demand for real estate. Property developers are creating retail real estate at an aggressive pace and by 2010, 300 malls are estimated to be operational in the country.

Growth after 2011: -

Before 2011, India had prevented innovation and organized competition in its consumer retail industry. One report estimates that in the year 2011 Indian retail market will be generating sales of about \$470 billion a year, of which \$27 billion comes from organized

retail such as supermarkets, chain stores with centralized operations and shops in malls. The opening of retail industry to free market competition will enable rapid growth in retail sector of Indian economy. The Economist forecasts that Indian retail will nearly double in economic value, expanding by about \$400 billion by 2020. The projected increase alone is equivalent to the current retail market size of France.

In 2011, A.T. Kearney estimates India's organized retail had a 31% share in clothing and apparel, the home supplies retail was growing between 20% to 30% per year and food accounted for 70% of Indian retail. It means tThe Indian market offers endless possibilities for investors.

As of 2013, India's retail and logistics industry employs about 40 million Indians (3.3% of Indian population).

Until 2011, Indian central government denied foreign direct investment (FDI) in multi-brand retail. In November 2011 Central Government announced retail reforms for both multi brand stores and single brand stores such as Walmart, Carrefour and Tesco, as well single brand majors such as IKEA, Nike, and Apple.

In January 2012, India approved reforms for single-brand stores welcoming anyone in the world to innovate in Indian retail market with 100% ownership, but imposed the requirement that the single brand retailer source 30 percent of its goods from India. Indian government continues the hold on retail reforms for multi-brand stores. In June 2012, IKEA announced it had applied for permission to invest \$1.9 billion in India and set up 25 retail stores. On 20 September 2012, the Government of India formally notified the FDI reforms for single and multi brand retail, thereby making it effective under Indian law. On 7 December 2012, the Federal Government of India allowed 51% FDI in multi-brand retail in India. The government managed to get the approval of multi-brand retail in the parliament despite heavy uproar from the opposition. Some states will allow foreign supermarkets like Wal-Mart, Tesco and Carrefour to open while other states will not.

The Indian retail market: -

Indian market has high complexities in terms of a wide geographic spread and distinct consumer preferences varying by each region necessitating a need for localization even within the geographic zones. India has highest number of outlets per person (7 per thousand) Indian retail space per capita at 2 sq ft (0.19 m²)/ person is lowest in the world Indian retail density of 6 percent is highest in the world. While India presents a large market opportunity given the number and increasing purchasing power of consumers, there are significant challenges such as Geographically dispersed population, , complex distribution network, little use of IT systems, limitations of mass media and existence of counterfeit goods.

Advantages of FDI:-

- a) Indian retail sector is highly fragmented with around 97% of its business being run by the unorganized retailers. The organized retail is in its infancy. With the entry of FDI the retail sector will become organized.
- b) Foreign investment in food-based retailing would ensure adequate flow of capital into the country and its productive use, multiplying the same. It will promote the welfare of farmers by agriculture growth, and thereby increasing their income level.
- c) Due to the presence of Intermediaries, prices lack transparency and due share of farmer is not paid to him. Indian farmers at present realize only 1/3rd of the final price paid by the consumer as against the 2/3rd price realized by the farmers in the countries with a greater share of organized retail. FDI will assist in reducing the dominance of value chain by intermediaries.
- d) In the absence of intermediaries, the consumer will end up paying less for a better product. FDI in retail will make the consumer happy as well.
- e) It will serve as an antidote to inflation. The producer will get direct payment from the retailer and the same will be higher than what he was getting earlier due to the foul play by the intermediaries.
- f) In accordance to the provisions made, any company going for 51% partnership in retail, will have to tie-up with a local partner. This will improve the income levels of all concerned and will make economy flourish with quality branded products at a lower price.
- g) FDI will improve the investment in logistics of the retail chain leading to an efficient market mechanism. FDI will become catalyst in avoiding erosion & wastage in quality and quantity of the produce
- h) FDI in the retail sector will spur competition as the current scenario is of low competition and poor productivity. India will flourish in terms of quality standards and consumer expectations.
- i) FDI will ensure better operations in production cycle and distribution. Due to economies of operation, production facilities will be available at a cheaper rate thereby resulting in availability of variety products to the ultimate consumers at a reasonable and lesser price.
- j) FDI enables transfer of skills and technology from overseas and develops the infrastructure of the domestic country. Greater managerial talent inflow from other countries is made possible. Domestic consumers will benefit getting great variety and quality products at all price.

- k) FDI will provide necessary capital for setting up organized retail chain stores. It is a long term investment because unlike equity capital, the physical capital invested in the domestic company is not easily liquidated

Limitations of FDI:-

- a) The unorganized retail sector is the largest source of employment after agriculture and has deep penetration in rural India. It generates more than 10% GDP of India. There is all probability that there will be a great job loss in this sector. The worst affected would be the rural youth.
- b) The foreign big players like Wal-Mart coming with huge investment may not procure material from the domestic producers and might import the same from international market.
- c) The present Distribution System on which a large urban and rural population depends will also receive a setback and it will be difficult to procure and redistribute the material, once the dependence on FDI increases.
- d) The fear is on the existence of micro, small and medium enterprises with the introduction of FDI in India. They will lose their existence.
- e) Foreign capital will penetrate in the country and will seek ways to multiply itself with unthinkable application for profit. In the long run, given the socio-economic structure, it may widen the gap between the rich and the poor.
- f) FDI will lead to job losses. Small retailers and other small 'Kirana store owners' will suffer a large loss. Giant retailers and Supermarkets like Walmart, Carrefour, etc. will displace small retailers.
- g) Supermarkets will establish their monopoly in the Indian market. Because of supermarket's fine tuning, they will get goods on low price and they will sell it on low price than small retailers, it will decrease the sell of small retailers.
- h) Jobs in the manufacturing sector will be lost because foreign giants will purchase their goods from the international market and not from domestic sources. This has been the experience of most countries which have allowed FDI in retail.
- i) Local producers will suffer or go vanished completely due to competition with foreign brands.

A number of merger and acquisitions have begun in Indian retail market. PWC estimates the multi-brand retail market to grow to \$220 billion by 2020.

"Consumer is king and if that is the philosophy working behind the policy then what is wrong in it."

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