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Foreign Direct Investment in Retail – A Study to Analyze What Works Best for India

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ABSTRACT *Over the past few years, the growth of the Indian economy was enormous, mainly due to the increasing availability of resources. Today, India stands as the 5th largest retail market in the world. This growth of the retail industry has attracted a number of foreign countries to India. They have started looking at India as a profitable investment avenue. Foreign Direct Investment (FDI) opens up the economy for international players, thereby boosting the growth of developing nations. This paper is a study undertaken to analyze how FDI has impacted various countries and what would be its impact on Indian retail market. The study evaluates the pros and cons of FDI in retail in Indian market and relates it to other developing economies. From the results of analysis, the study concludes whether India should go for FDI in retail market.*

INTRODUCTION

Foreign Direct Investment (FDI) is the direct investment in business by individuals or companies from another country. Like companies, countries also need capital to fund their development projects. FDI helps the host nation develop capital and increase its tax revenues from investments done through FDI. The capital raised helps in funding infrastructure and numerous other development projects. Increase in FDI has generally fueled an improvement in economic growth of a country.

The retail industry is mainly divided into (1) Organized and (2) Unorganized Retailing. In an organized retailing, business activities are undertaken by retailers with license. This group is pays sales tax and income tax to the government. Examples to this group are the hypermarkets and retail chains. On the other hand, in unorganized retailing, business activities are carried out by small vendors who are not licensed. For example, vendors selling items in the pavement comes under this category.

In India, the retail sector is dominated by unorganized retailers. The organized retail however is at a very budding stage. The retail sector provides the largest source of employment after agriculture.

LITERATURE REVIEW

(Khare, 2013) opines that FDI in retail segment would be beneficial for India. However, the government should protect the interests of millions whose livelihood is dependent on small and medium retail market. The author contents that FDI in retail would contain inflation by better connecting famers and customers.

(Bhattacharyya, 2012) suggests that since Indian Government recommends retail firms to source a percentage of manufactured products from small and medium domestic enterprises, Foreign Direct Investment will provide a boost to these small and medium enterprises. The author argues that FDI in retail sector will generate significant employment opportunity for rural and semi-urban youth thereby helping Indian economy.

(Sikri, S & Wadhwa, D, 2012) indicates that India lacks an efficient supply chain management. This could be attributed to the dominance of unorganized retail market. Improvement of supply chain management will bring down inventory cost which will eventually benefit the consumer.

OBJECTIVES OF THE STUDY

The objective of the study is to understand the following aspects regarding FDI in retail sector in India.

1) To understand whether FDI is beneficial to the retail industry.
2) To analyze the arguments against and in favor of FDI in retail.
3) To understand whether FDI in retail will benefit Indian economy.

Government Policy on the types of retailing in India

The types of retailing in India can be divided into (1) Single brand retailing and (2) Multi brand retailing. In single brand retailing, foreign companies will be allowed to sell goods sold internationally under a single brand (Sikri, S & Wadhwa, D, 2012) Examples to single brand retailing are Nike, Reebok, Nokia etc. FDI in Multi Brand retail refers to a retail store with a foreign investment can sell multiple brands under one roof. Examples to multi brand retailing are Wal-mart, Tesco, Carrefour etc. By opening up FDI in retail for multi brand retailing, retail giants like Wal-Mart can open stores offering a range of goods directly to consumers.

Government of India has allowed 100% FDI in single brand retailing and 51% FDI in multi brand retailing. However, in both sector government has imposed a 30% domestic sourcing requirement. This implies that retailers in both these segments have to rely on medium and small enterprises in India to carry out their business activities. Most international retailers have objected to this clause citing difficulty to comply with this regulation citing difficulty to source high end luxury goods. Currently, government is considering removing the 30% sourcing norm for single brand retailers. This will make it possible for single brand retailers like Apple to open their own stores in India.

Pros and Cons of FDI in Retail in India

FDI will promote economic growth and improves forex position of the country. It also helps in generating employ-

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ment opportunities by increasing production and bringing in more capital. Competition within the local market will increase making the market more efficient with new technologies and management skills. FDI also helps in increasing exports thereby bringing in more tax revenues.

People opposed to FDI in retail however argue that domestic companies will eventually end up being acquired by foreign multinational corporations (MNC). Small enterprises will not be able to compete with large MNC's which would ultimately lead to monopoly. Another argument against FDI is that Government will have less control over the functioning of such companies.

CASE STUDIES

Case Study of FDI in Retail Market in China

China opened up its economy for FDI in 1979. It was in 1992 that FDI in retail was allowed with a cap of 26%. By 2004 China allowed 100% FDI in retail. Clearly, the Chinese manufacturing sector has grown tremendously after its policy of 100% FDI in retail. Proof to this are $60 billion annual export to United States and 95% of products sold in Walmart China are sourced locally.

Case Study of Retail Market in UAE

UAE has always welcomed foreign investments and many MNC retailers consider it as an attractive investment location. Despite allowing FDI in retail, the local market was in fact able to outclass international brands like Carrefour. The local retailer Lulu is an example that if good quality products are provided by local retailers, international brands will not be able to create a monopoly of its own. Hence, it counters the argument that FDI in retail will hinder the growth of small and medium enterprises.

CONCLUSIONS

FDI in the retail sector is not only promising to the foreign companies, but will also be very beneficial to the Indian economy. By looking into the case studies of countries like China, UAE and by also analyzing the pros and cons of FDI in retail, it appears quite clear that FDI will promote manufacturing sector, create growth opportunities, increases exports, brings in more capital, increases forex reserve, brings in advanced technologies and management skills, and above all fuel the economic growth of India.

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