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# Foreign Direct Investment in Indian Retail: Myths and Reality

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**ABSTRACT**

India is the second largest country in the world in terms of its population. In terms of purchasing power, it is considered one of the biggest economies in the world. Indian economy has certain noticeable elements like vast consumer market, big retail sector, inadequate domestic supply, weak infrastructure, lack in technological background, low GDP, poor management skill, inadequate finance, unemployment etc. Recently, the Indian government has decided to allow 100% FDI in multi-brand retailing; but the question is: does our nation really require FDI? This paper is an attempt to visualize the consequences of FDI in multi-brand retailing. The paper also contains suggestions to improve the domestic market and precautions to be taken for FDI in India.

**KEYWORDS** FDI, Indian Retail industry, Challenges and Opportunities of FDI

## 1. INTRODUCTION

### 1.1 Foreign Direct Investment (FDI)

FDI in general refers to the net inflows of investment to acquire a lasting management interest in an enterprise operating in an economy other than that of the investor. It usually involves participation in management, joint ventures, transfer of technology and expertise.

Following drastic economic crisis in 1991, India made a new economic policy in July 1991. This new policy removed all unnecessary rules and gave liberal environment to foreign investors for FDI inflows under automatic route. As a result, FDI increased from 1 $ billion in 1990 to more than 24.2 $ billion in 2010. The segments fetching higher inflows were service sector, telecommunication industry, construction business and computer software and hardware industry. FDI flow was higher from the countries like Mauritius, Singapore, Japan, U.S.A, Netherlands, U.K, Germany, France, Switzerland and South Korea. There are more than 63 zones in India where FDI is involved. However, some sectors are prohibited from FDI; the Indian government reserves some zones as public sector.

**Figure 1.1 shows the FDI inflows in India since 2000**

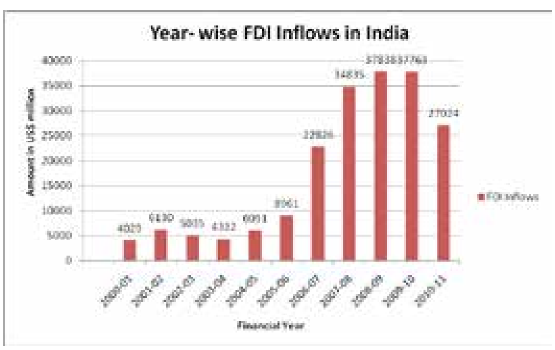


**Figure 1.1: FDI inflows in India since 2000 (In US $)**

## 2. CHALLENGES AND OPPORTUNITIES OF FDI IN RETAILING.

### 1. Indian Economy as a whole

According to Government of India (GOI) report, the organized retail sector will grow at the rate of 25% with the opening of retail sector for foreign investors. Retailing in India is the single largest component of the services sector in terms of contribution to Gross Domestic Product (GDP). In 2009-10 service sector contributed 55.2% to India's GDP, out of which the contribution made by the trade amounted to 14.9%. It is to be noted that unorganized retailing forms 96% of trade. As per economic survey 2010-11, the retail sector was expected to record healthy sales in 2010-11 and grows by 10.2%. Thus, even without FDI driving it, the retail sector is expanding at a furious rate. Then, what is the need for FDI?

### 2. Customers

According to GOI, Foreign Direct Investment in retail sector will benefit customers the most as they can buy a variety of appropriately packaged goods of standard quality at reasonable price.

This argument of government does not hold true. The alleged benefits of consumer choice are being inflated. Indeed the availability of excessively wide choice makes it so complex and time consuming for the consumer to decide that it leads to stronger loyalty to particular brands. Moreover, in the name of variety, the suppliers only offer line extensions and not more.

The consumer loses the power to bargain. He has to buy goods at the rate offered by the Multinational stores. He is offered goods which might not be useful to him. Such stores will sell processed and semi processed food instead of traditional cuisine. Traditional food and fruits will be replaced by the foreign items which will change the culture, life style and tradition of the consumer. The balance will be tilted in favor of the seller instead of the consumer.

### 3. Employment

The GOI claims that FDI in retailing will create the jobs. Good inflow of FDI creates new employment opportunities in industries and in the markets. Government claims that multi-brand retailing will produce employment for 1 crore people by 2020. But ultimate evidence behind this claim is still lacking.

Mohan Guruswamy et.al in their article FDI in India's Retail Sector: More bad than good? stated that organized retail roughly employs 5 lakh people while the unorganized retail trade employs 3.95 crores. On the other hand, each Wal-Mart worker replaces approximately 1.4 retail workers representing a 2.7% reduction in average retail employment (Neumark, Zhang and Ciccarella, 2008). India's total retail industry worth 20 lakh crore and is employed with 4.40 crore people. This shows India's retail sector is much promising employment provider and it shows that the entry of retailer like Wal-Mart will definitely take of the employment of many.

In 2010, Wal-Mart sold $405 billion amount of goods through its 9800 odd outlets located across 28 countries, employing around 2.1 million (21 lakh) persons. This implies that one Wal-Mart supermarket can displace over 1300 Indian small retail stores and thereby render around 3900 persons jobless.

The employment created against this in that supermarket will be 214. Clearly, there will be severe job losses if giant MNC supermarkets are allowed entry into the Indian market.

**4. Supply Chain**

Honorable Commerce Minister pointed out that FDI will eliminate the intermediates between manufactures and farmers. This will increase the profit of agriculturists by 30%. It was found by the researchers that the income of American farmers was reduced to 4% in 2005, which was 70 cent for every one dollar of sales in 20th century. Not only this, multinational retailers' pay less than prevailing market price. Apart from prices, the report states that smaller farmers came under severe pressure from supermarkets due to the latter's requirement for large volumes of each product, pushing farmers to grow single crops rather than the multiple produce they would usually grow to minimize risk.

**5. Farmers & Manufacturers**

According to GoI, the farmers of our country will get better price for their produce with the entry of Multinational stores. This will stop the suicide of thousands of farmers in India. The government also asserts that 50% of the total FDI will be undertaken in the rural areas. However, this argument of the government does not hold true. The Multinational stores demand produce of certain quality and volume. If these standards are not met then they reject the produce. In case of India, it is very difficult for the farmers to maintain consistent quality due to vagaries of weather. Under such circumstances, who will protect the farmers and how will their produce be sold?

**7. Unorganized Sector**

The government asserts that the unorganized retail sector will not be affected and will co- exist with the organized retail sector even after the advent of FDI in retail sector. However, it is a myth that unorganized retail sector in India co-exists with the organized retail sector. The total retail sector was expected to achieve the growth rate of 9% by 2010. When the growth rate of the organized retail is 37% and that of the unorganized retail is that of 5.7%, it is very much clear that the organized sector is growing at the cost of the unorganized sector.

**8. Real Estate**

A report published by Knight Frank India in May 2010, estimates that during 2010-12, around 55 million square feet of retail space will be ready in the major cities like Mumbai, the National Capital Region(NCR), Bangalore, Kolkata, Chennai, Hyderabad and Pune. Furthermore, between 2010 and 2012, the organized retail real estate is expected to grow from the existing 41million square feet to 95million square feet. Arguably, this could drive up real estate prices, with consequent knock-on effects. It is but obvious that Multinational stores will pass on the cost of building infrastructural and logistic facilities to the consumers. This will only make the consumer product all the more expensive.

**9. Regional Imbalance**

It is said that FDI in retail would contribute in pacing up the overall economy of India. But this is not the fact. FDI in retail would be allowed in cities with the population more than 1 million. India's 70% population resides in the rural area but they would not get the benefit of FDI in retail. This would lead to asymmetrical growth in cities causing discontent and social tension elsewhere.

**3. RECOMMENDATIONS**

The metamorphosis of Indian economy from developing to the developed is still not over due to the policy paralysis of the government of India. We feel that the following remedial measures should be considered before resorting to FDI in retail sector.

- A systematic study of unorganized retail sector should be undertaken, their problems should be identified and measures should be taken to develop this sector.
- Basic Infrastructure facilities like power, irrigation, road, warehousing and so on should be strengthened. Training should be imparted to retailers in procuring and maintaining goods.
- The concept of co-operatives should be encouraged in every sphere of agriculture. Such system has already been successful in milk and sugar.
- A mechanism should be established to see that the farmer/ manufacturer gets fair price for his products, without fleecing the consumer.
- The unorganized sector happens to be the second largest generator of employment after agriculture. Therefore, measures like Easy availability of credit facility, Tax benefits, Logistic support a mechanism through which the retailers are able to buy their supply easily and cheaply and so on should be implemented.
- Rural manufacturers/ Farmers/Retailers/Artisans should be given proper direct marketing facilities to sell their products in the urban areas.

**4. CONCLUSION**

India is an agrarian economy. Lack of warehousing facilities, technological expertise, advanced supply and distribution chain coupled with lack of political will to bring about reforms in Power, Irrigation and Agriculture has been responsible for chaotic condition of Indian Economy. The need of the hour is not to invite the FDI in retail sector but to set our home right by ensuring equitable distribution of not just income and wealth but also basic infrastructural facilities.

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