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# Impact of FDI Retail Policy on Domestic Organized Retailers – A Comparative Analysis with China, Germany and Chile

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ABSTRACT

The Indian Retail sector has tremendous growth potential. It is already one of the largest contributors to GDP and employs more than 8% of the work force in India. However, the current Indian FDI policy in retail has earned more flack from within the country than from foreign retailers due to its potential threat to the unorganized and existing organized retail in India. Several emerging economies have gone through the same phase much before and today are reaping the benefits of a modern retail sector. India is still lagging behind in reforms in this sector. This paper aims to examine the threats of FDI in retail to the existing organized retail in India as against its benefits by drawing comparisons with the experiences of other economies like China, Germany and Chile.

**KEYWORDS** Foreign Direct Investment (FDI), Retail, Multi Brand Retail, Single Brand Retail, Organized retail

**Introduction**

In 2004, The High Court of Delhi defined the term 'retail' as a sale for final consumption in contrast to sale for further sale (Wholesale) or processing. The retail sector is classified as organized and unorganized. The two coexist in different proportions in countries across the world. Organized retailing refers to trading done under license. Typical features of organized retail are professional management and high levels of centralization in merchandise and organized supply chain management

Unorganized retail refers to businesses run by owners or trusted employees/relatives. This includes local kirana stores, convenience stores, road side vendors and hand carts.

**Single and Multi-Brand Retail**

'Single brand' implies that foreign companies would be allowed to sell goods sold internationally under a 'single brand'. However, the retailers would be able to sell multiple products under the same brand.

Multi Branding in Retail –It refers to selling multiple brands under one roof.

**The Retail Sector in India**

The retail sector was said to be at USD $5 billion in 2012 and is expected to grow at

| Table 1 - Quantum of retail trade | | |
|---|---|---|
| Country | Organized | Unorganized |
| India | 6 | 94 |
| China | 20 | 80 |
| Indonesia | 30 | 70 |
| Thailand | 40 | 60 |
| Malaysia | 55 | 45 |
| Taiwan | 81 | 19 |
| **Source: Booz & Company analysis, FICCI, 2012** | | |

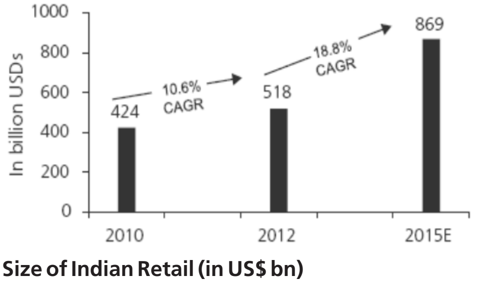


**Fig-1: Size of Indian Retail (in US$ bn)**
**Sources: Source:Economist Intelligence Unit, Euro Monitor, Aranca Research**

CAGR of 18.8% to touch USD$ 869 billion by 2015. By 2020 it is expected to touch US$1.3 trillion. According to research from CRISIL, organized retail is also expected to grow at CAGR of 24% to touch 10.2% by and to 20% by 2021 of total share of the retail market in India.

The uniqueness of the Indian Market lies in the high proportion of the unorganized sector. This is a typical characteristic of a market in its nascent stage of development. The share of organized retail has gone up from 3% in 2007 to almost 14% in 2014. India has over 14 million stores; 11 stores per 1000 persons, the highest density of stores in the world.

**Objectives of the study**

1) To examine the impact of reforms in Retail FDI Policy in countries like China, Germany and Chile on existing Indian organized retailers
2) To draw comparisons based on experiences of retail reforms in above countries and India on existing Indian organized retailers

**Methodology**

This research is based on secondary sources of data. Books, journals, newspapers, survey reports & websites have been extensively used. The conclusions and recommendations of this study are based on analytical, descriptive and comparative analysis of secondary sources.

**Comparative Analysis**

Countries like China, Germany and Chile have undergone retail transformation much ahead of India. The positive impact on organized retail in these countries can throw some light on what to expect from the arrival of foreign retailers in India.

**Case 1- China**

China too opened up FDI in retail in a phased out manner starting with FDI cap of 26 percent in 1992 which was increased to 49 percent in 2002 along with restrictions such as location where foreign retailers could open their store. China took 12 yrs to liberalize its FDI regime with occasional reversals in policy as well. Finally in 2004, 100 percent FDI was allowed. In the last 20 yrs, China has made tremendous progress in the retail sector. Both the existing and foreign retailers have achieved tremendous growth. However, China's biggest retail firms are Chinese. From 1996 to 2001 over 600 Hypermarkets opened and the no of small outlets increased from 1.9 million to 2.5 million, a 60% growth.

Source: DIPP - Effect of FDI on Traditional Market in China

| Type | No. of stores in 1996 | No. of stores in 2001 |
|---|---|---|
| Traditional | 1,920,604 | 2,565,028 |
| Supermarkets | 13,079 | 152,194 |

| | | |
|---|---|---|
| Convenience | | 18,091 |
| Hypermarkets | | 593 |

After 20yrs, the domestic retail chains like the Shanghai Bailian group, Suning Home Appliances, Gome Home Appliances and Dashang Group, all have higher sales than Walmart in China. The share of unorganized retail is still 80% in China. Employment in the retail and wholesale sectors increased from 28 million people to 54 million people from 1992 to 2000.

The retail growth rate in China in 2014 was 11.6%. By 2018, China's retail market is expected to surpass USA as world's largest retail market. According to a report by AT Kearney's 2015 Global Retail Expansion –An Unstoppable Force, global fast fashion retailers like Uniqlo Stores, H&M, Zara and others opened a total of 264 stores in China in 2014. The domestic conglomerate Sanpower acquired 89 percent stake in House of Fraser, a UK based Departmental store which plans to open 50 stores in China. Chinese consumer electronics giant Suning plans to enter the grocery segment by opening 1000 supermarket stores across China by 2020.

The phenomenal growth of Chinese retailers despite the presence of foreign giants is a proof that domestic organized retail and foreign retailers can grow alongside in a highly competitive but growing market. Thus it may be too early to predict the negative impact of foreign retailers on existing organized retail in India.

**Case 2 – Germany**

The rapid growth of organized retail in Germany happened more than two decades ago. This led to major consolidation of retail stores. Many unorganized and small retailers could not adapt to the sweeping changes and were wiped out. For those that survived, evolved by modernizing and improving their efficiency. In turn, the manufacturers too had to work on cost reductions and higher efficiencies which were passed on at least in part to the buyers through the retailers. An interesting retail format that not only survived but thrived despite severe competition was Aldi, a German retailer. Aldi efficiently continued with the small-store format because they found it was what consumers wanted. There are other examples in Germany of innovative strategies like cooperative buying through central organizations, have one brand name to gain from marketing and have one set of processes to benefit from large-scale, technology-led process development.

Thus innovation is the key to survival in a competitive environment. New formats, technological up gradation leading to efficiency, cooperative buying are the hallmark of success of small formats in Germany. Faced with competition, Indian entrepreneurs will definitely learn to innovate to survive as can be already observed.

Top retailers in Chile

| Rank | Company | Sales 2010 ($M) | Increase over 2009 | Profits 2010 ($M) |
|---|---|---|---|---|
| 1 | Cencosud | 13,226 | 26% | 633 |
| 2 | Falabella | 8,923 | 28% | 883 |
| 3 | D&S (Walmart) | 4,861 | 7% | 89 |
| 4 | Mall Plaza | 3,653 | 68% | n.a. |
| 5 | Hipermercados Lider | 3,320 | 19% | n.a. |

Source: AméricaEconomia

**Case 3 – Chile**

The Chilean retail sector took off in 1990's. Carrefour and Ahold, the number two and number three global retail chain entered the Chilean retail sector and by 2002, together held 13 percent of the total sales of the top eight retail chains in Chile amounting to US$4.6 billion. In a drastic turn of events, by 2006 the share of these two global giants had gone down to zero percent of the total sales of US$12.6 billion of the top eight retail chains despite similar growth rate in retail sector in Chile as that of China in the same period. The Chilean subsidiaries of two foreign chains had been bought by the top-two Chilean chains, D&S (Later taken over by Wal-Mart) & Cencosud. Similarly JC Penny, US top departmental store too sold its share to local competitor Almacenes Paris after running losses for 5 yrs.

At present the department store sector is dominated by Falabella, Almacenes Paris (Now part of the Cencosud group) and Ripley – all domestic retailers. The failure of foreign companies to enter the Chilean market is attributed to strong competition posed by existing national chains. Their strong brand recognition, excellent market and consumer know-how and location advantage proved to be fatal for the foreign giants.

Currently, Chile's many strong local retailers continue to grow organically alongside foreign giants like WalMart. Falabella announced plans to open 215 new stores and 16 new shopping centres across Latin America in 2015 with an investment of invest $3.51 billion. By the end of 2011, the supermarket industry foresaw 10,000 new jobs being created due to growing demand, a 9% increase over 2010.

**Conclusion**

The dominance of domestic organized retail in China is the result of slow and cautious policy liberalization which so far the Indian Government too has followed. The factors that contribute to the massive growth of the likes of Wal-Mart in their home country, like infrastructure support and cost efficiency in supply chain and logistics were absent in China then as they are in India now. Hence it is unlikely that foreign retailers will be able to achieve the scale at the cost of existing domestic retailers.

The Indian retail market is huge, complex and diverse and these features are most likely to favor the mom and pop/ kirana stores as the new entrants will find it difficult to serve this market and reach the desired and sustainable scale of operation. One of the major weaknesses of kirana stores in India is the lack of scale of operations which can be overcome with cooperative buying.

Organized retailing does take off layers of intermediaries driving down the prices which benefits the consumers and expands the market and reach of products which benefits the producers. Encouraging organized retailing will give much needed boost to manufacturing sector by increased foreign investment and will also generate employment.

The multinationals that invest in retail business in India would also source Indian goods for their international outlets in a big way and thus provide a boost to Indian exports.

Many sectors including agriculture, food processing, manufacturing, packaging and logistics have reaped benefits of FDI in other countries. There is no reason why it cannot be emulated in India.

Simplification, removal of unnecessary restrictions and proper implementation of the Retail FDI policy will help India generate employment and enhance quality of life of consumers.

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