Foreign Direct Investment in the Retail Sector in India

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ABSTRACT

The Government of India was initially very apprehensive of the introduction of the Foreign Direct Investment in the Retail Sector in India. The unorganized retail sector as has been mentioned earlier occupies 98% of the retail sector and the rest 2% is contributed by the organized sector. Hence one reason why the government feared the surge of the Foreign Direct Investments in India was the displacement of labour.

The unorganized retail sector contributes about 14% to the GDP and absorbs about 7% of our labour force. Hence the issue of displacement of labour consequent to FDI is of primal importance. There are different viewpoints on the impact of FDI in the retail sector in India, According to one viewpoint, the US evidence is empirical proof to the fact that FDI in the retail sector does not lead to any collapse in the existing employment opportunities. There are divergent views as well. According to the UK Competition Commission, there was mass scale job loss with entry of the hypermarkets brought about by FDI in the UK retail market.

Even though organized retail sector in India is at the infant stage, India has today become a budding target for FDI. India today offers the most persuasive investment opportunity for mass merchants and food retailers looking to expand overseas as Indian economy is growing at a raid pace with consumers having high purchasing power. With a robust economy experiencing unrelenting growth, India has exerted a pull and an irresistible enticement to companies looking to expand their scope of operations. FDI is a sturdy source for the intensification of retailing and will create enormous opportunities for innovation in retail sector in India but at the same time it is quite likely that a section of the domestic retailing industry will be severely hurt due to the entry of foreign retailers. In this study it has been tried to accentuate both the thoughts in detail and concluded the most constructive view on FDI in Indian retailing.

Introduction

India being a signatory to World Trade Organization's General Agreement on Trade in Services, which include wholesale and retailing services, had to open up the retail trade sector to foreign investment. There were initial reservations towards opening up of retail sector arising from fear of job losses, procurement from international market, competition and loss of entrepreneurial opportunities. However, the government in a series of moves has opened up the retail sector slowly to Foreign Direct Investment (FDI). In 1997, FDI in cash and carry (wholesale) with 100 percent ownership was allowed under the Government approval route. It was brought under the automatic route in 2006. 51 percent investment in a single brand retail outlet was also permitted in 2006. FDI in Multi-Brand retailing is prohibited in India.

The union Cabinet takes a decision to allow 51% FDI in multi-brand retail sector. Though it is an executive decision, as the parliament is in session, naturally it is taken up by all the political parties. The allies of the government take a firm stand. Opposition is united across the ideological boundaries. The government has to bow down. The decision is suspended pending consultation to create broad consensus among the stakeholders. But though the decision is in suspension the issue is

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far from dead and buried. It is better to discuss it logically in the comparative calm rather than racking up unrelated issues in the political haste.

This study aims at discussing the real issues involved in the Policy of inviting FDI in general and in its implications in retail sector in particular. It is an observation that the present debate has byepassed these real issues and is focused on the side issues. This will be an attempt to discuss the wide implications of the mind set that not only invites and welcomes FDI but projects it as the only panacea for all the economic problems of the great country of 120 crores.

FDI Policy in India: FDI as defined in Dictionary of Economics (Graham Bannock et.al) is investment in a foreign country through the acquisition of a local company or the establishment there of an operation on a new (Greenfield) site. To put in simple words, FDI refers to capital inflows from abroad that is invested in or to enhance the production capacity of the economy.

Foreign Investment in India is governed by the FDI policy announced by the Government of India and the provision of the Foreign Exchange Management Act (FEMA) 1999. The Reserve Bank of India („RBI) in this regard had issued a notification, which contains the Foreign Exchange Management (Transfer or issue of security by a person resident outside India) Regulations, 2000. This notification has been amended from time to time.

The Ministry of Commerce and Industry, Government of India is the nodal agency for motoring and reviewing the FDI policy on continued basis and changes in sectoral policy/sectoral equity cap. The FDI policy is notified through Press Notes by the Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion (DIPP).

The foreign investors are free to invest in India, except few sectors/activities, where prior approval from the RBI or Foreign Investment Promotion Board („FIPB) would be required.

In the current investment regime, no foreign investment is allowed in domestic retail trading. This is based on the perception that opening up retail trading for FDI investment could impact local Venders and lead to job losses. However, manufacturing companies are allowed to carry out wholesale trading of high value items purely to institutional customers or wholesale distributors on a cash and carry basis.

Indian retail trade is of enormous size ($180 billion), nearly 10 per cent of GDP, employing 21 million persons, which is about 7 per cent of the labour force. It is six times bigger than Thailand and five times larger than South Korea and Taiwan. China's retail trade is 8 per cent of GDP and 6 per cent of employment. But the trade in India is fragmented, unorganized, un-networked, and individually small.

The 12 million kirana shops are mostly family or 'ma-pa' owned, with little capital for expansion or credit to receive or to extend to consumers. About 96 per cent of these shops have 500 sq ft or less of space with limited stock or choice to offer. During all these years, instead of shedding tears for indigenous trade and resisting FDI, had the government declared it an industry, it would done the trade a world of good

Modern retailing is designed not only to provide consumers with a wide variety of products under one roof, but also of assured home delivery and information feedback between consumers and producers. A modem retail outlet will also make it easy to buy on credit and provide for servicing and repair of products sold. With IT application, the modem retail store can cut transaction costs such as due to inventory, delivery and handling. That is precisely how the US based Wal-Mart grew to be a giant because it reduced its distribution costs to 3 per cent of sales compared to 4.5 per cent of others.

Wal-Mart had entered the Chinese market a few years ago (in 1996). Now it wants to enter India and bring FDI to set itself up to network. India is today the only major economy that still does not permit FDI in retail trade. In China, 35 of the world's top 70 retailers have already entered and set up business. They have helped in boosting their exports. Wal-Mart alone exported in 2002 about $12 billion worth of goods. These retailers source their goods from inside China.

India is targeting for its GDP to grow by 8 to 10 per cent per year. This requires raising the rate of investment as well as generating demand for the increased goods and services produced. Exports are one way of generating that demand. Encouraging private consumption expenditure is another way. Both these can be facilitated by allowing marketsavvy, market-intelligent and best management practices, through corporations such

as Wal-Mart, Carrefour, Ahold, JC Penny to enter India.

These retail giant houses can bring their better managerial practices and IT-friendly techniques to cut wastage and set up integrated supply chains to gradually replace the presented disorganized and fragmented retail market. As India's urbanization grows, these modem food delivery systems are required. Foreign companies want to come in, and we need their money and techniques to prepare our transition to the inevitable globalised market of the future.

The status of organized retailing in some South East Asian countries that allowed FDI in retailing has been given in below:-

Country	Organized Retailing	Traditional Retailing
Malaysia	50%	50%
Thailand	50%	50%
Philippines	35%	65%
Indonesia	25%	75%
South Korea	15%	85%
China	10%	90%
India	2%	98%

In view of the demands made by industry and the need to boost the retail trade, the Government is actively considering removing the restrictions. A recent note circulated by the Ministry of Commerce has proposed permission for FDI up to 100 per cent in retail trade subject to Government approval on a case-to-case basis.

However, this permission, if it is given, will be with lots of strings attached. Besides following rules on minimum capitalization, the foreign entrants will be expected to neutralize the outflow of foreign exchange (repatriation of dividends) by way of export earnings on a year-to-year basis.

FDI in retail sector has been a key driver of productivity growth in Brazil, Poland and Thailand. This has resulted in lower prices to the consumer, more consumption and higher profit for the producer. FDI in retail trade has forced the wholesalers and food processors to improve, raised exports, and triggered growth by outsourcing supplies domestically. The availability of standardized products has also boosted tourism in these countries.

The biggest opposition to allowing 100% FDI is the feared exit of the small retailers. Currently, moves are on to counter these apprehensions and the players are keenly awaiting the final decision from the Government.

FDI Policy with Regard to Retailing in India: It will be prudent to look into Press Note 4 of 2006 issued by DIPP and consolidated FDI Policy issued in October 2010 which provide the sector specific guidelines for FDI with regard to the conduct of trading activities.

a) FDI up to 100% for cash and carry wholesale trading and export trading allowed under the automatic route.

b) FDI up to 51 % with prior Government approval (i.e. FIPB) for retail trade of „Single Brand products, subject to Press Note 3 (2006 Series)

c) FDI is not permitted in Multi Brand Retailing in India.

Foreign Investor's Concern Regarding FDI Policy in India

For those brands which adopt the franchising route as a matter of policy, the current FDI Policy will not make any difference. They would have preferred that the Government liberalize rules for maximizing their royalty and franchise fees. They must still rely on innovative structuring of franchise arrangements to maximize their returns. Consumer durable majors such as LG and Samsung, which have exclusive franchisee owned stores, are unlikely to shift from the preferred route right away.

For those companies which choose to adopt the route of 51% partnership, they must tie up with a local partner. The key is finding a partner which is reliable and who can also teach a trick or two about the domestic market and the Indian consumer. Currently, the organized retail sector is dominated by the likes of large business groups which decided to diversify into retail to cash in on the boom in the sector – corporate such as Tata through its brand Westside, RPG Group through Food world, Pantaloon of the Raheja Group and Shopper s Stop. Do foreign investors look to tie up with an existing retailer or look to others not necessarily in the business but looking to diversify, as many business groups are doing?

An arrangement in the short to medium term may work wonders but what happens if the Government decides to further liberalize the regulations as it is currently contemplating? Will the foreign investor terminate the agreement with Indian partner and trade in market without him? Either way, the foreign investor must negotiate its joint venture agreements carefully, with an option for a buy-out of the Indian partner s share if and when regulations so permit. They must also be aware of the regulation which states that once a foreign company enters into a technical or financial collaboration with an Indian partner, it cannot enter into another joint venture with another Indian company or set up its own subsidiary in the 'same field' without the first partner's consent if the joint venture agreement does not provide for a 'conflict of interest' clause. In effect, it means that foreign brand owners must be extremely careful whom they choose as partners and the brand they introduce in India. The first brand could also be their last if they do not negotiate the strategic arrangement diligently.

FDI in Single Brand Retail

The Government has not categorically defined the meaning of "Single Brand" anywhere neither in any of its circulars or nor any notifications.

In single-brand retail, FDI up to 51 per cent is allowed, subject to Foreign Investment Promotion Board (FIPB) approval and subject to the conditions mentioned in following

(a) Only single brand products would be sold (i.e., retail of goods of multi-brand even if produced by the same manufacturer would not be allowed)

(b) Products should be sold under the same brand internationally,

(c) Single-brand product retail would only cover products which are branded during manufacturing and

(d) Any addition to product categories to be sold under "single-brand" would require fresh approval from the government.

FDI in Multi Brand Retail

The government has also not defined the term Multi Brand. FDI in Multi Brand retail implies that a retail store with a foreign investment can sell multiple brands under one roof.

In July 2010, Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce circulated a discussion paper on allowing FDI in multi-brand retail. The paper doesn t suggest any upper limit on FDI in multi-brand retail. If implemented, it would open the doors for global retail giants to enter and establish their footprints on the retail landscape of India. Opening up FDI in multi-brand retail will mean that global retailers including Wal-Mart, Carrefour and Tesco can open stores offering a range of household items and grocery directly to consumers in the same way as the ubiquitous *kirana'* store.

Need of the Study

Foreign direct investment is that investment, which is made to serve the business interests of the investor in a company, which is in a different nation distinct from the investor's country of origin. A parent business enterprise and its foreign affiliate are the two sides of the FDI relationship. Together they comprise an MNC.

The parent enterprise through its foreign direct investment effort seeks to exercise substantial control over the foreign affiliate company. 'Control' as defined by the UN, is ownership of greater than or equal to 10% of ordinary shares or access to voting rights in an incorporated firm. For an unincorporated firm one needs to consider an equivalent criterion. Ownership share amounting to less than that stated above is termed as portfolio investment and is not categorized as FDI.

FDI stands for Foreign Direct Investment, a component of a country's national financial accounts. Foreign direct investment is investment of foreign assets into domestic structures, equipment, and organizations. It does not include foreign investment into the stock markets. Foreign direct investment is thought to be more useful to a country than investments in the equity of its companies because equity investments are potentially "hot money" which can leave at the first sign of trouble, whereas FDI is durable and generally useful whether things go well or badly.

FDI or Foreign Direct Investment is any form of investment that earns interest in enterprises which function outside of the domestic territory of the investor. FDIs require a business relationship between a parent company and its foreign subsidiary. Foreign direct business relationships give rise to multinational corporations. For an investment to be regarded as an FDI, the parent firm needs to

have at least 10% of the ordinary shares of its foreign affiliates. The investing firm may also qualify for an FDI if it owns voting power in a business enterprise operating in a foreign country.

The issue of FDI in multi-brand retail sector is much deeper than what meets the eye. It is not just an issue of wrong timing or lack of political consensus. The political parties may support or oppose any issue on popular considerations. One can not blame them for that. The manner of opposition, claims for and against the issue is also sometimes aimed at the gallery rather than being serious matters of policy considerations. We are witnessing all kinds of claims and counter claims on the issue of FDI in retail sector. Thus I am taking up this study.

Objective of the study

- To study the factors that make India an attractive destination for retailers
- To analyze benefits and problems of allowing FDI in India in the multi brand segment
- To make recommendations on how and under what conditions can FDI be allowed in the Indian Retail Sector so as to reduce the risk of lifting restrictions
- on the multi brand segment
- To analyse the Indian Retail Industry vis-à-vis global industry and identify the advantages and disadvantages of FDI.
- To review the FDI Trends in India and the need for FDI in Retail in context of: Stakeholders and End Consumers.
- To identify the key implications on the unorganized retail in India in case the FDI of 51% in multibrand is allowed by the government.

Scope of the Study

The study was limited to the analysis of FDI in Retail Sector in India based on already available literature.

Literature Review

- Hymer (1960), Caves (1996), Dunning (1993) found that MNEs have both tangible and intangible resources, or explicit and tacit knowledge, in the form of technologies, managerial skill, international networks, capital, and brand names and goodwill (Hymer 1960, Caves 1996, Dunning 1993).
- Teece (19770 stated that the MNEs can supply these resources to local firms in equity joint ventures (intra-firm), in non-equity strategic alliances, or in arm s-length transactions through the external market. The transfer mechanism through the market or intra-firm depends on transaction costs (Teece 1977).
- Lucas (1990) has also analyzed the issue by examining the question of why capital does not flow from rich to poor countries and critically explored some candidate answers that are based on human capital and capital market imperfections. With regard to human capital, he shows that the rich country s optimal policy is to retard capital flows so as to maintain real wages at artificially low levels in the poor country. As far as capital market imperfections are concerned, Lucas s paper analyzes a borrowing contract between poor and rich countries. In this paper, the focus is on linkages and on the rational behavior of different foreign investors in the face of reform uncertainty.
- Cheng, (1993) noted the growing importance of cross-border R & D activities and suggested that additional research on FDI should be done on why firms internationalize their R & D
- Anand and Delios (1996) documented that the relatively slow growth of FDI from Japanese MNCs in India as compared to China is attributed to the desire to gain only market access in India.
- Garg, et al. (1996) documented that along with the regulation of product prices, since 1986 the Indian government has limited the profits pharmaceutical companies can earn to approximately 6 percent of sales turnover. From 1970 through the early 1990s, industry pre-tax profitability as a percent of sales declined consistently, one reason for which was the rate of return constraint. Indeed, in 1977- 1978 industry profitability 11.7 percent. In 1982-1983 this dropped to 7.5 percent, further declining to 3.5 percent in 1987-1988. Since 1992, industry profitability has been rising, and by 1996 it had reached approximately 10 percent of sales (Garg, et al., 1996).

- Lee and Mansfield (1996) found that the developing country technology polices have often favored the objective of national selfdetermination at the expense of foreign technology transfer. In particular, host country policies of weak intellectual property protection and forced licensing of technology, although intended to facilitate technology spillovers, are more likely to discourage FDI and the transfer of leading edge technologies by MNCs (Lee and Mansfield, 1996).
- Dijkstra (2000), Tybout (2000) and Vachani (1997) found that investment policy liberalisations have major impacts on firms in less developed countries (LDCs) where the pre-liberalisation level of protection was high. Not all firms are affected equally; some will be losers while others will be winners, depending on their characteristics
- Feinberg & Majumdar (2001) found that Liberalisation of FDI policies offers opportunities for firms as well as threats. If FDI (and trade) liberalisation results in faster growing national economies, then firms face larger, faster-growing markets domestically.
- The studies of FDI in the US, Japan and Europe have been prevalent, similar research on FDI in India is however limited. Restricted policy environment towards FDI and weak property protection rights have been described to cause significant R&D spillovers in Indian pharmaceutical sector [Feinberg and Majumdar 2001].
- Aditya K.R. Bajaj and Swastik Nigam (2007) in this work made an attempt to analyze and study the impact of globalization in the pharmaceutical industry and FDI spillovers in various forms to the domestic pharmaceutical industry in terms of domestic productivity and competitiveness etc. The analysis of the study reveals that the spillover effects have had a manifold impact on the Indian pharmaceutical industry, with the new WTO patent regime introduced in 2005, the foreign players have found greater security in operating in India and due to the spillover effects of a competitive environment, the domestic players have substantially increased their productivity, probability and hence compete on stranger footing with the incoming pharma firms.
- Jaya Gupta(2007) in his paper made an attempt to review the change in sectoral trends in India due to FDI Inflows since liberalization. This paper also examines the changed policy implications on sectoral growth and economic development of India as a whole.
- Jayashree Bose(2007) in his book studied the sectoral experiences faced by India and China in connection with FDI inflows. This book provides information on FDI in India and China, emerging issues, globalization, foreign factors, trends and issues in FDI inflows, FDI inflows in selected sectors. A comparative study has also been conducted on FDI outflows from India and China. This book also revealed the potential and opportunities in various sectors in India that would surpass FDI inflows in India as compared to China.
- Sudershan K (2007) in his thesis made an attempt to examine the impact of FDI inflows on financial performance and export performance of select pharmaceutical companies and the financing pattern of FDI and Non-FDI based select pharmaceutical companies. The study is conducted for a period of 15 years i.e. from 1991 to 2005 and the data analysis is done using both traditional methodologies, such as common size statements, trend analysis and ratio analysis and econometric modeling such as pooled cross section time series analysis or panel data analysis. Based on the results, the study reveals that higher proportion of FDI will result into better performance of companies. As far as export performance is concerned, the performance of FDI based pharmaceutical companies in India.
- Tanay Kumar Nandi and Ritankar Saher (2007) in their work made an attempt to study the Foreign Direct Investment In India with a special focus on Retail Trade. This paper stresses the need of FDI in India in retail sector and uses the augment that FDI is allowed in multiple sectors and the effects have been quite good without harming the domestic economy. The study also suggests that FDI in retail sector must be allowed.
- The review of literature reveals that on a particular sector FDI has a direct impact and

on a particular sector it has an indirect impact. A study on the impact of FDI on manufacturing sector reveals that FDI inflows in chemicals, electrical and electronics shows direct impact and FDI inflow in drugs and pharmaceutical sectors shows indirect impact (spillover effects). (Rajit Kumar Sahoo, 2005)

- Dr. Kent H. David and Dr. Shomali Hamid (2007) in their report COMPARATIVE ANALYSIS OF FDI IN CHINA AND INDIA analysed the FDI from Chinese perspective and makes a passing reference to India, they also discusses the role of overseas Chinese investment, and the ASEAN economies. They also found that the size of Chinese economy, its annual growth rate, and political stability have also played a role in attracting Foreign Direct Investment over last twenty-eight years. They analyzed the impact of the human capital on FDI inflow into India during the reform period of 1992-2005 and found statistical evidence for the same.
- Sinha S Swapna in their report on COMPARATIVE ANALYSIS OF FDI IN CHINA AND INDIA- can laggards learn from leaders? Analyse the gap in the literature on FDI from Indian perspective. She also explores and analyse the determinants FDI in India and China at micro state level and also makes attempt to compare India and China. She philosophize the lessmerging market laggards need to learn from leaders in transforming their economy in global scenario.
- Wei Wenhui in his report China and India: Any difference in their FDI performances..? Explore the determinants of inward FDI in China and India and the causes for their huge difference. He used random-effect models to analyze separately the determinants of FDI from OECD countries in China and India, and then applied the Oaxaca-Blinder decomposition to examine the causes of the differences. It was found that China's much higher FDI from OECD countries was mainly due to its larger domestic market and higher international trade ties with OECD countries. India, however, had advantage in its cheaper labor cost, lower country risk, geographic closeness to OECD countries, and cultural similarity.
- Dr. Keshava R. S. in his report on The effect of FDI on India and Chinese Economy; A comparative analysis analysed that India is still far behind China in becoming the attractive FDI destination, for the obvious reason such as power shortage, poor infrastructure, security consideration, absence of an exit policy etc. If India has to reach its target of attractive more FDI for its development, The Indian Policy makers should understand that the good intentions and mere plan layouts alone are not sufficient condition, but a bold aggressive third generation reforms is the need of the hour. Only then one can expect India to attract FDI to its potential and can become a popular investment destination as China.
- Zheng Zing in his report on A Comparison of FDI Determinants in China and India explores foreign direct investment (FDI) determinants in China and India and fills the gap in the literature by providing a comprehensive empirical comparison analysis. Two panel data sets and two statistical models are employed to identify the determinants of FDI inflows from home countries worldwide to the two host countries by considering both home and host countries' characteristics. The empirical results show some interesting similarities and differences between the two countries. Market growth, imports, labor costs, and country political risk/policy liberalization are the determinants for both countries.
- Dexin Yang (2003) in his study, "Foreign Direct Investment from Developing Countries: A case study of China s Outward Investment" presents an interpretation of FDI by Chinese firms. The research is motivated by the phenomenon that compared with foreign investment in China; direct investment from China has so far attracted relatively little attention from researchers. Given the difficulties in providing a convincing explanation of the patterns of China s outward FDI by using mainstream theories, this thesis develops a network model of FDI by formalizing network ideas from business analysis for application to economic analysis, and interprets China s outward FDI in terms of network model. This thesis holds that Chinese firms were

engaged in FDI for various network benefits. Accordingly, the geographic distribution of China s outward FDI reflected the distribution of network benefits required by Chinese firms and the relevant cost saving effects for containing such benefits. As the functioning of networks relies on elements of market economies, the development of China s outward FDI was affected by the progress of marketisation in China.

- Minquan liu, Luodan Xu, Liu Liu (2004) in their study, "Wage related Labour standards and FDI in China: Some survey findings from Guangdong Province" presents findings from a Survey of Foreign Invested Enterprises (FIEs) in Guangdong China, on the relationship between Foreign Direct Investment and wage – related labour standards (regular wages, and compliance with official overtime and minimum wage) which show that wage – related standards are statistically high in FIEs whose home countries standards are higher, after controlling for other influences. However, a cost – reduction FIE is more likely to be associated with inferior standards.
- D.N Ghosh (2005) in his paper „FDI and Reform: Significance and Relevance of Chinese Experience" finds that if India shed its inhibitions about FDI and follow in the footsteps of China, than India would be in a position to realize its full potential. China s FDI saga has been a textbook replay of what institutional economics would call "adaptive efficiency" on the part of its political regime. The country made courageous but careful choices in difficult circumstances, signaling radical departure from the belief system it as been accustomed to for decades. The study concluded that both china and India have demonstrated that for a late industrializing country the Washington consensus is not necessarily a good model to follow. It might be appropriate for countries with a good institutional infrastructure and efficient private sector, but for others it can be a recipe for disaster. China seems to have discovered its own reform model with "Chinese Characteristics". A western observer calls it the "Beijing Consensus". India is currently fumbling to validate a different kind of model – call it the "India Consensus"- for democrating country in a globally interdependent world.

It is concluded from the analysis of the above studies that political environment, debt burden, exchange rate, FDUI spillovers significantly influence FDI flow to the developing countries. It is also observed that countries pursuing export led growth strategy and firms in clusters gain more benefits from FDI. It is also found that improve infrastructure, higher growth rate, higher degree of openness of the host economy and higher levels of human capital attract FDI to the developed as well as developing nations. It augments domestic savings and enhances efficiency of human capital (through transfer of new technology, marketing and managerial skills, innovation and best practices)

Research Methodology

Secondary sources primarily comprises of qualitative data. These included articles and news reported in the print and electronic media about the rationale and efficacy of the FDI in India with specific reference to Retail sector. Such reports cover a variety of states and were help to understand issues that were common across the spectrum.

Conceptual Framework

Foreign Direct Investment

These three letters stand for foreign direct investment. The simplest explanation of FDI would be a direct investment by a corporation in a commercial venture in another country. A key to separating this action from involvement in other ventures in a foreign country is that the business enterprise operates completely outside the economy of the corporation s home country. The investing corporation must control 10 percent or more of the voting power of the new venture.

According to history the United States was the leader in the FDI activity dating back as far as the end of World War II. Businesses from other nations have taken up the flag of FDI, including many who were not in a financial position to do so just a few years ago.

The practice has grown significantly in the last couple of decades, to the point that FDI has generated quite a bit of opposition from groups such as labor unions. These organizations have expressed concern that investing at such a level in another country eliminates jobs. Legislation was

introduced in the early 1970s that would have put an end to the tax incentives of FDI. But members of the Nixon administration, Congress and business interests rallied to make sure that this attack on their expansion plans was not successful. One key to understanding FDI is to get a mental picture of the global scale of corporations able to make such investment. A carefully planned FDI can provide a huge new market for the company, perhaps introducing products and services to an area where they have never been available. Not only that, but such an investment may also be more profitable if construction costs and labor costs are less in the host country.

The definition of FDI originally meant that the investing corporation gained a significant number of shares (10 percent or more) of the new venture. In recent years, however, companies have been able to make a foreign direct investment that is actually long-term management control as opposed to direct investment in buildings and equipment.

FDI growth has been a key factor in the "international" nature of business that many are familiar with in the 21st century. This growth has been facilitated by changes in regulations both in the originating country and in the country where the new installation is to be built. Corporations from some of the countries that lead the world s economy have found fertile soil for FDI in nations where commercial development was limited, if it existed at all. The dollars invested in such developing-country projects increased 40 times over in less than 30 years. The financial strength of the investing corporations has sometimes meant failure for smaller competitors in the target country. One of the reasons is that foreign direct investment in buildings and equipment still accounts for a vast majority of FDI activity. Corporations from the originating country gain a significant financial foothold in the host country. Even with this factor, host countries may welcome FDI because of the positive impact it has on the smaller economy.

Foreign direct investment (FDI) is a measure of foreign ownership of productive assets, such as factories, mines and land. Increasing foreign investment can be used as one measure of growing economic globalization. Figure below shows net inflows of foreign direct investment as a percentage of gross domestic product (GDP). The largest flows of foreign investment occur between the industrialized countries (North America, Western Europe and Japan).But flows to non-industrialized countries are increasing sharply. Foreign direct investment (FDI) refers to long term participation by country A into country B.

It usually involves participation in management, joint-venture, transfer of technology and expertise. There are two types of FDI: inward foreign direct investment and outward foreign direct investment, resulting in a net FDI inflow (positive or negative). Foreign direct investment reflects the objective of obtaining a lasting interest by a resident entity in one economy ("direct investor") in an entity resident in an economy other than that of the investor ("direct investment enterprise"). The lasting interest implies the existence of a long-term relationship between the direct investor and the enterprise and a significant degree of influence on the management of the enterprise. Direct investment involves both the initial transaction between the two entities and all subsequent capital transactions between them and among affiliated enterprises, both incorporated and unincorporated.

- **Foreign Direct Investment** – when a firm invests directly in production or other facilities, over which it has effective control, in a foreign country.
- **Manufacturing FDI** requires the establishment of production facilities.
- **Service FDI** requires building service facilities or an investment foothold via capital contributions or building office facilities.
- **Foreign subsidiaries** – overseas units or entities.
- **Host country** – the country in which a foreign subsidiary operates.
- **Flow of FDI** – the amount of FDI undertaken over a given time.
- **Stock of FDI** – total accumulated value of foreign-owned assets.
- **Outflows/Inflows of FDI** – the flow of FDI out of or into a country.
- **Foreign Portfolio Investment** – the investment by individuals, firms, or public bodies in foreign financial instruments.
- Stocks, bonds, other forms of debt.
- Differs from FDI, which is the investment in physical assets.

Portfolio theory – the behavior of individuals or firms administering large amounts of financial assets.

Product Life-Cycle Theory

- Ray Vernon asserted that product moves to lower income countries as products move through their product life cycle.
- The FDI impact is similar: FDI flows to developed countries for innovation, and from developed countries as products evolve from being innovative to being mass-produced.

The Eclectic Paradigm

- Distinguishes between:
  - **Structural market failure** – external condition that gives rise to monopoly advantages as a result of entry barriers
- **Transactional market failure** – failure of intermediate product markets to transact goods and services at a lower cost than internationalization

The Dynamic Capability Perspective

- A firm s ability to diffuse, deploy, utilize and rebuild firm-specific resources for a competitive advantage.
- Ownership specific resources or knowledge are necessary but not sufficient for international investment or production success.
- It is necessary to effectively use and build dynamic capabilities for quantity and/or quality based deployment that is transferable to the multinational environment.
- Firms develop centers of excellence to concentrate core competencies to the host environment.

Monopolistic Advantage Theory

- An MNE has and/or creates monopolistic advantages that enable it to operate subsidiaries abroad more profitably than local competitors.
- Monopolistic Advantage comes from:
  - *Superior knowledge* – production technologies, managerial skills, industrial organization, knowledge of product.
  - *Economies of scale* – through horizontal or vertical FDI

Internationalization Theory

- When external markets for supplies, production, or distribution fails to provide efficiency, companies can invest FDI to create their own supply, production, or distribution streams.
- Advantages
  - Avoid search and negotiating costs
  - Avoid costs of moral hazard (hidden detrimental action by external partners)
  - Avoid cost of violated contracts and litigation
  - Capture economies of interdependent activities
  - Avoid government intervention
  - Control supplies
  - Control market outlets
  - Better apply cross-subsidization, predatory pricing and transfer pricing

Definition

Foreign direct investment is that investment, which is made to serve the business interests of the investor in a company, which is in a different nation distinct from the investor's country of origin. A parent business enterprise and its foreign affiliate are the two sides of the FDI relationship. Together they comprise an MNC.

The parent enterprise through its foreign direct investment effort seeks to exercise substantial control over the foreign affiliate company. 'Control' as defined by the UN, is ownership of greater than or equal to 10% of ordinary shares or access to voting rights in an incorporated firm. For an unincorporated firm one needs to consider an equivalent criterion. Ownership share amounting to less than that stated above is termed as portfolio investment and is not categorized as FDI.

FDI stands for Foreign Direct Investment, a component of a country's national financial accounts. Foreign direct investment is investment of foreign assets into domestic structures, equipment, and organizations. It does not include foreign investment into the stock markets. Foreign

direct investment is thought to be more useful to a country than investments in the equity of its companies because equity investments are potentially "hot money" which can leave at the first sign of trouble, whereas FDI is durable and generally useful whether things go well or badly.

FDI or Foreign Direct Investment is any form of investment that earns interest in enterprises which function outside of the domestic territory of the investor. FDIs require a business relationship between a parent company and its foreign subsidiary. Foreign direct business relationships give rise to multinational corporations. For an investment to be regarded as an FDI, the parent firm needs to have at least 10% of the ordinary shares of its foreign affiliates. The investing firm may also qualify for an FDI if it owns voting power in a business enterprise operating in a foreign country.

History

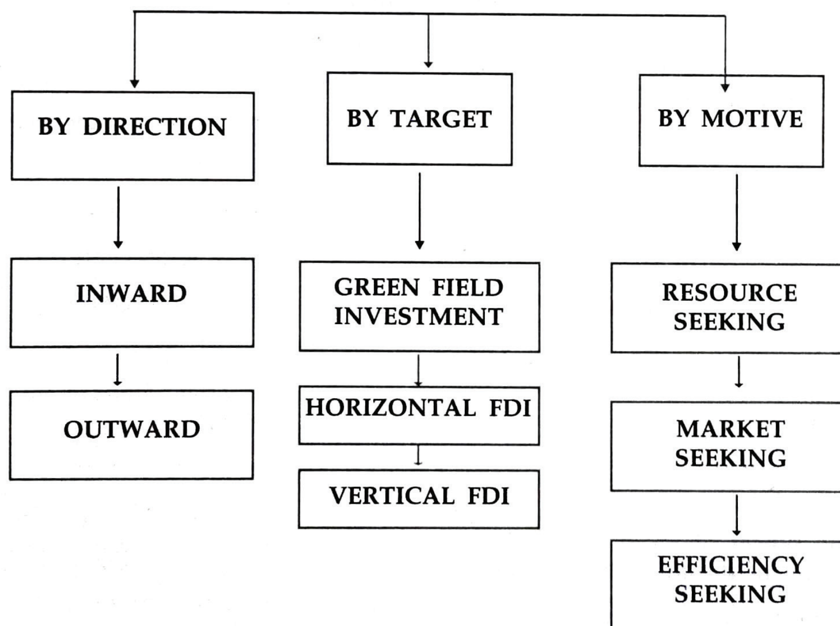
In the years after the Second World War global FDI was dominated by the United States, as much of the world recovered from the destruction brought by the conflict. The US accounted for around three-quarters of new FDI (including reinvested profits) between 1945 and 1960. Since that time FDI has spread to become a truly global phenomenon, no longer the exclusive preserve of OECD countries.

FDI has grown in importance in the global economy with FDI stocks now constituting over 20 percent of global GDP. Foreign direct investment (FDI) is a measure of foreign ownership of productive assets, such as factories, mines and land. Increasing foreign investment can be used as one measure of growing economic globalization. Figure below shows net inflows of foreign direct investment as a percentage of gross domestic product (GDP). The largest flows of foreign investment occur between the industrialized countries (North America, Western Europe and Japan). But flows to non-industrialized countries are increasing sharply.

Foreign Direct investor

A foreign direct investor is an individual, an incorporated or unincorporated public or privateenterprise, a government, a group of related individuals, or a group of related incorporated and/ or unincorporated enterprises which has a direct investment enterprise – that is, a subsidiary, associate or branch – operating in a country other than the country or countries of residence of the foreign direct investor or investors.

Types of FDI



Types of Foreign Direct Investment: An Overview

FDIs can be broadly classified into two types:

1. Outward FDIs
2. Inward FDIs

This classification is based on the types of restrictions imposed, and the various prerequisites required for these investments.

Outward FDI: An outward-bound FDI is backed by the government against all types of associated risks. This form of FDI is subject to tax incentives as well as disincentives of various forms. Risk coverage provided to the domestic industries and subsidies granted to the local firms stand in the way of outward FDIs, which are also known as 'direct investments abroad.'

Inward FDIs: Different economic factors encourage inward FDIs. These include interest loans, tax breaks, grants, subsidies, and the removal of restrictions and limitations. Factors detrimental to the growth of FDIs include necessities of differential performance and limitations related with ownership patterns.

Other Categorizations of FDI

Other categorizations of FDI exist as well. Vertical Foreign Direct Investment takes place when a multinational corporation owns some shares of a foreign enterprise, which supplies input for it or uses the output produced by the MNC.

Horizontal foreign direct investments happen when a multinational company carries out a similar business operation in different nations.

- Horizontal FDI – the MNE enters a foreign country to produce the same products product at home.
- Conglomerate FDI – the MNE produces products not manufactured at home.
- Vertical FDI – the MNE produces intermediate goods either forward or backward in the supply stream.
- Liability of foreignness – the costs of doing business abroad resulting in a competitive disadvantage.

Methods of Foreign Direct Investments

The foreign direct investor may acquire 10% or more of the voting power of an enterprise in an economy through any of the following methods:

- by incorporating a wholly owned subsidiary or company
- by acquiring shares in an associated enterprise
- through a merger or an acquisition of an unrelated enterprise
- participating in an equity joint venture with another investor or enterprise

Foreign direct investment incentives may take the following forms:

Low corporate tax and income tax rates

- tax holidays
- other types of tax concessions
- preferential tariffs
- special economic zones
- investment financial subsidies
- soft loan or loan guarantees
- free land or land subsidies
- relocation & expatriation subsidies
- job training & employment subsidies
- infrastructure subsidies
- R&D support
- derogation from regulations (usually for very large projects)

Entry Mode

- The manner in which a firm chooses to enter a foreign market through FDI.
  - International franchising
  - Branches
  - Contractual alliances
  - Equity joint ventures
  - Wholly foreign-owned subsidiaries
- Investment approaches:
  - Greenfield investment (building a new facility)
  - Cross-border mergers
  - Cross-border acquisitions
  - Sharing existing facilities

Why is FDI Important for any Consideration of Going Global?

The simple answer is that making a direct foreign investment allows companies to accomplish several tasks:

1. Avoiding foreign government pressure for local production.
2. Circumventing trade barriers, hidden and otherwise.
3. Making the move from domestic export sales to a locally-based national sales office.
4. Capability to increase total production capacity.
5. Opportunities for co-production, joint ventures with local partners, joint marketing arrangements, licensing, etc;

A more complete response might address the issue of global business partnering in very general terms. While it is nice that many business writers like the expression, "think globally, act locally", this often used cliché does not really mean very much to the average business executive in a small and medium sized company. The phrase does have significant connotations for multinational corporations. But for executives in SME s, it is still just another buzzword. The simple explanation for this is the difference in perspective between executives of multinational corporations and small and medium sized companies. Multinational corporations are almost always concerned with worldwide manufacturing capacity and proximity to major markets. Small and medium sized companies tend to be more concerned with selling their products in overseas markets. The advent of the Internet has ushered in a new and very different mindset that tends to focus more on access issues. SME s in particular are now focusing on access to markets, access to expertise and most of all access to technology.

The Strategic Logic Behind FDI

- **Resources seeking** – looking for resources at a lower real cost.
- **Market seeking** – secure market share and sales growth in target foreign market.
- **Efficiency seeking** – seeks to establish efficient structure through useful factors, cultures, policies, or markets.
- **Strategic asset seeking** – seeks to acquire assets in foreign firms that promote corporate long term objectives.

Enhancing Efficiency from Location Advantages

- **Location advantages** - defined as the benefits arising from a host country's comparative advantages.- Better access to resources
  - Lower real cost from operating in a host country
  - Labor cost differentials
  - Transportation costs, tariff and non-tariff barriers
  - Governmental policies

Improving Performance from Structural Discrepancies

- **Structural discrepancies** are the differences in industry structure attributes between home and host countries. Examples include areas where:
  - Competition is less intense
  - Products are in different stages of their life cycle
  - Market demand is unsaturated
  - There are differences in market sophistication

Increasing Return from Ownership Advantages

- **Ownership Advantages** come from the application of proprietary tangible and intangible assets in the host country.
  - Reputation, brand image, distribution channels
  - Technological expertise, organizational skills, experience
- **Core competence** – skills within the firm that competitors cannot easily imitate or match.

Ensuring Growth from Organizational Learning

- MNEs exposed to multiple stimuli, developing:
  - Diversity capabilities
  - Broader learning opportunities
- Exposed to:
  - New markets
  - New practices
  - New ideas
  - New cultures
  - New competition

The Impact of FDI on the Host Country

Employment

- Firms attempt to capitalize on abundant and inexpensive labor.
- Host countries seek to have firms develop labor skills and sophistication.
- Host countries often feel like "least desirable" jobs are transplanted from home countries.
- Home countries often face the loss of employment as jobs move.

Fdi Impact on Domestic Enterprises

- Foreign invested companies are likely more productive than local competitors.
- The result is uneven competition in the short run, and competency building efforts in the longer term.
- It is likely that FDI developed enterprises will gradually develop local supporting industries, supplier relationships in the host country.

Highlights of FDI in Multi-brand Retail

- Union cabinet clears 51% for multi-brand supermarkets.
- Minimum investment from foreign retailer is $100 mn.
- At least 50% of the total FDI must be invested in „back-end infrastructure.
- Minimum 30% of the local sourcing requirements from small industries.
- Retail outlets to come up in cities with more than 1 million population
- The govt will have the first right to procure agricultural produce.

The investment needed for entering the sector has been fixed at $100 million in towns with population of more than 10 lakh as earmarked by 2011 census; half of which they need to allocate towards building back-end infrastructure and better logistical support for the exploding Indian retail sector led by burgeoning middle class population and growing consumer spending.

Furthermore, the new guidelines may commit supermarkets run by foreign retailers to strict local sourcing requirements to the extent of 30% of manufactured or processed goods from small industries. Going by the 10 lakh population threshold to open supermarkets, 53 cities that accounts for over 42% of total urban population will be eligible to have internationally renowned retail outlets.

Lastly, the cent percent opening up of single-brand retail segment will foster growth in India s infrastructure for luxury retail markets such as jewellery, fine dining, luxurious real-estate, global branded apparels, yachts, and swanky hotels amongst other niche segment offerings.

FDI in multi-brand retail will give a boost to the organised retail sector, which positively impacts several stakeholders, including producers, workers, employees, consumers, the government, and, hence, the overall economy.

In a true potential scenario, opening up of FDI can increase organized retail market size to $260 billion by 2020.

Best case scenario: Opening up of FDI in retail can increase organised retail market size to $260 billion by 2020.

This would result in an aggregate increase in income of $35-45 billion per year for all producers combined; about 3-4 million new direct jobs and around 4-6 million new indirect jobs in the logistics sector, contract labour in the distribution and repackaging centres, housekeeping and security staff in the stores.

The government too stands to gain by this move by transparent and accountable monitoring of goods and supply chain management systems. The government can be expected to receive an additional income of $25-30 billion by way of a variety of taxes.

SMEs

FDI can help SMEs supply in: large volumes, increase quality and become a vendor to international players and increase the quality of products and become cost competitive in global arena.

Traditional trade will continue to have its own place and should not decline. Even in the last three years when modern retail has grown 24 per cent, unorganised retail has continued to grow, albeit at a slower rate of 10-12 per cent.

Example of Small-Scale Industries (SSIs): In 1990s when dereservation of small-scale industries (SSIs) was introduced in India, there was speculation around the eventual decline of SSIs.

Since then several studies have shown that the sector continues to demonstrate a healthy growth in the number of units, output and employment.

As an example, the growth for the early period of liberalization (1993-1994 to 1998-1999) which was 16 per cent, fell slightly for the next 5 years (1998-1999 to 2004-2005) to 12 per cent, before accelerating to 19 per cent in the last 5 years (2004-2005 to 2008-2009).

Similarly, the employment generated by registered SSIs grew at 6 per cent in the pre-liberalisation era 1979-1980 and 1989-1990, at 4 per cent in the first decade of the post-liberalisation era (1993-1994 to 2003-2004), and accelerated to 19 per cent in the last 5 years (2003-2004 to 2008-2009).

Better service of small retailers: AnICRIER study, 'Impact of Organized Retailing on the Unorganized Sector, 2008', shows no evidence of a decline in overall employment in the unorganised sector as a result of the entry of organised retailers. Rather small retailers evolve — like adding new product lines and brands, better display, renovation of the store, introduction of self-service, enhanced home delivery, more credit sales, acceptance of credit cards, etc.

Farmers

Farmers in India today receive a small share of the end consumer price.

As an example, for tomatoes, farmers in India earn only 30 per cent of consumer price, while in more developed markets this is in the 50-70 per cent range.

Organised retail has the potential to drive efficiencies in this chain by:

(a) Increasing price realisation for farmers by 10- 30 per cent through sourcing directly or closer to the farm.

(b) Reducing handling and wastage by 25-50 per cent through consolidation as well as investments in technology, either directly or through aggregators.

(c) Upgrading the farmer's capabilities by providing know-how and capital.

(d) Improving farmers' output and yield through better extension services and user friendly processes.

Food Security

In case investments are not made in agricultural back-end and supply chain, it will become difficult to meet India's growing demands for fruits and vegetables, dairy and poultry products.

In fact, any delay in these investments will endanger availability for our future generations.

Consumers

This would result in wider choice for the consumer with better competition

It also would lead to assurance of quality with greater transparency and easier monitoring of adulteration, counterfeit products and traceability.

Furthermore, it would lower prices that can help curb inflation. With its ability to drive efficiencies and leverage scale, modern trade is able to increase affordability for consumers.

For a low income family, organised retail has the ability to lower the cost of the monthly consumption basket as much as 5-10 per cent.

Reacting to widespread fears on how the advent of foreign companies with huge credit for investments affects the small and medium traders in the country, FICCI's secretary general Rajiv Kumar assured, "Allowing FDI will bring development of a robust supply chain, which in turn will help in integrating farmers and small and medium size enterprises."

Ficci members explained that whatever investments foreign retailers want to make in India, a fixed per cent of it will have to be invested on setting the back-end infrastructure right.

An adequate supply chain for procurement of food will have to be established, and since other retailers will have to provide for equal or better quality products, it will straighten the overall infrastructure in this sector.

Currently, the retail sector in India is worth $450 billion, which is most likely to increase to $850 billion in the next ten years.

Approximately 35 per cent of the material is sourced directly from SMEs. In a bid to calm the small traders, who feel most vulnerable, Ficci members argued that as the market of retail grows and

foreign investors come into play, the dependence on SMEs to provide for raw material will also grow.

FDI in multi brand retail will give a boost to the organised retail sector, which positively impacts several stakeholders including - producers, workers, employees and consumers and Government and hence, the overall economy.

Opening up of FDI can increase organised retail market size to $260 billion by 2020. This would result in an aggregate increase in income of $35-45 billion per year for all producers combined; 3–4 million new direct jobs and around 4–6 million new indirect jobs in the logistics sector, contract labour in the distribution and re-packaging centres, housekeeping and security staff in the stores.

FDI will bring about the development of a robust supply chain which in turn will integrate farmers and small and medium size enterprises into the modern trade process, resulting in knowledge and skills transfer, ensuring farmers and SMEs receiving higher prices for their produce/supplies, providing a more transparent mechanism for pricing, helping in planning their supplies.

Findings and Analysis

Permitting FDI in multibrand retail has been one of the most debated issues over the last few years at the policy level. It has been placed on the back burner by successive governments in response to fears about its impact on small retailers, who are large generators of employment.

The main driver for this policy seems to be the recognition that the Indian economy faces serious supply-side constraints, particularly in the food retail chains. Further, there has been lack of investments in the logistics of retail chains creating inefficiencies in the supply chain.

Policy reforms are taking place in India, albeit after a few hurdles. As per estimates, unorganised retail will grow at 13 per cent per annum until 2015, while organised retail will expand at 45-50 per cent. Allowing retail FDI will definitely have an impact on smaller indigenous players and several unorganised peers. The impact can be mid-term to long-term, depending on the strategy adopted by global players.

The proposed FDI approval comes with certain restrictions, for example, retailers will have to invest a minimum of $100 million over five years, and purchase 30 per cent of their goods from small and medium-sized firms (typically local suppliers). Evalueserve believes this will boost the Indian contract logistics industry, especially the warehousing and cold-chain services. At least half of the $100-million investment has to be made to develop Indian rural infrastructure, and to establish a cold-chain system.

The organied retail sector in India has developed across regions of high population density, thus resulting in uneven representation across the country, partly due to state-level policies. In 2011, it accounted for only 7 per cent of the retail segment. Some estimates suggest that the segment will increase its contribution by up to 20 per cent by 2020. Others such as Business Monitor International, which pegged India s retail sector at $396 billion in 2011, have opined that it will grow at an annual average rate of 25 per cent to $785 billion by 2015.

In the organised retail market, we see multi-brand retail (MBRT) and single-brand retail (SBRT) operating mainly through lifestyle and value retailing, with the former focused on categoryspecific lifestyle-focused products and the latter on discounts and value-for-money products.

The Indian retail industry is still at a nascent stage and modernisation of retail trade is long overdue. This policy change by the government will open up strategic investment opportunities for global retailers. This will have a significant positive impact on all the stakeholders and will provide a necessary fillip to the growth of the Indian economy.

With entry of foreign retailers, consumers will experience more variety of products, with improved quality. Foreign 'low-cost' big players will adopt an integrated supply chain management system that, in turn, should help lower prices of products, benefiting consumers at large.

FMCG companies are expected to benefit too. This would be evident through the increased volume of sales due to wider distribution channels. Currently, FMCG companies sell 6% nationally through modern retail outlets and 20% in metros through this channel.

This number is definitely expected to scale up with emergence of foreign retail stores. Modern retailing is likely to play an important role in increasing the consumption of processed food items. It will also aid better understanding of consumer preferences as it is a vital link between the processors and consumers.

New markets for FMCG products could be developed with the growth in foreign retailers, through expansion into new formats, categories, channels, customers, services and geographies. The industry would become more competitive with development of the imported food and beverages market.

In the processed food industry, small and new players will be able to find ways to place their products in modern stores by producing store label brands for them. However, there are a few challenges that the FMCG industry needs to address. Price realisation for the FMCG companies may come down as they need to bargain hard with big retail chains. Also, private labels may pose a threat to established brands.

Currently, lack of adequate storage facilities causes heavy losses to farmers. As per industry estimates, 35-40% of fruit and vegetables and nearly 10% of food grains in India are wasted annually. Though FDI is permitted in cold chains to the extent of 100%, in the absence of FDI in front-end retail, investment flows into this sector have been insignificant. Thus, FDI in retail would help in addressing this issue with compulsory investment of 50% in back-end.

Farmers would also be able to secure remunerative prices. In the present dispensation, there is a complex chain of procurement involving several middlemen. FDI in retail will create the enabling environment and it is expected that progressive states will undertake gradual reform of the APMC Act.

This will ensure direct procurement; however, for this, immediate adoption of a model APMC Act by all states is imperative. Huge investments in the retail sector will see gainful employment opportunities in processing, sorting, marketing, logistic management and the front-end retail business.

According to estimates, there would be employment of one person per 350-400 sq ft of retail space; about 1.5 million jobs will be created in the front-end alone in the next five years.

Assuming that 10% extra people are required for the back-end, the direct employment generated by the organised retail sector in India over the coming five years will be around 1.7 million jobs.

The impact on government would be largely in terms of increase in tax revenues for the exchequer. Also, the government could be aided in regulation of food inflation. With reduced wastage, it is expected that the concern of food inflation would be addressed.

The policy change will bring about the development of a robust supply chain that, in turn, will integrate small and medium-size enterprises into the modern trade process. This would result in knowledge and skills transfer, ensuring SMEs receive higher prices for their produce/supplies. It would also ensure a more transparent mechanism for pricing, and better access to the intermediate market, in particular at the international level.

FDI in multi-brand and single-brand retail will be a game changer. It will have the same positive disruption effect that telecom liberalisation brought about. It is imperative that we stop 'posturing' and see the matter for what it is: a clear win-win for all stakeholders, and with proper safeguards, this initiative will promote inclusive growth.

Should it have gone into effect, the multi-brand retailing decision would have impacted different stakeholders widely. The scale economies of organized retailing would likely have offered consumers a wider variety of products at lower prices, with safeguards like quality control and checking for counterfeit products, including infringed American goods. Organized retailers would also have to buy products directly from Indian farmers and producers, paving the way for better price realization. The provision of 50% FDI from the United States and elsewhere in back-end infrastructure for storage, logistics, and better extension services would substantially reduce wastage in India s farm produce, which is one of the highest in the world. The provision of 30% sourcing from Indian SMEs (small and medium enterprises) would have helped expand capacity, improve quality, and get exposure to international supply chains, making them internally competitive over time.

Countering these positive aspects, however, the initial impact of multi-brand retailers entering India s market is expected to have a negative impact on the over 12 million unorganized shops and countless kirana (mom-and-pop) stores, as they lack the financial muscle to challenge major retailers in terms of variety, quality, packaging, and other offers.

Conclusion

The government has added an element of social

benefit to its latest plan for calibrated opening of the multi-brand retail sector to foreign direct investment (FDI). Only those foreign retailers who first invest in the back-end supply chain and infrastructure would be allowed to set up multi brand retail outlets in the country. The idea is that the firms must have already created jobs for rural India before they venture into multi-brand retailing. It can be said that the advantages of allowing unrestrained FDI in the retail sector evidently outweigh the disadvantages attached to it and the same can be deduced from the examples of successful experiments in countries like Thailand and China where too the issue of allowing FDI in the retail sector was first met with incessant protests, but later turned out to be one of the most promising political and economical decisions of their governments and led not only to the commendable rise in the level of employment but also led to the enormous development of their country s GDP.

Moreover, in the fierce battle between the advocators and antagonist of unrestrained FDI flows in the Indian retail sector, the interests of the consumers have been blatantly and utterly disregarded. Therefore, one of the arguments which inevitably needs to be considered and addressed while deliberating upon the captioned issue is the interests of consumers at large in relation to the interests of retailers.

It is also pertinent to note here that it can be safely contended that with the possible advent of unrestrained FDI flows in retail market, the interests of the retailers constituting the unorganized retail sector will not be gravely undermined, since nobody can force a consumer to visit a mega shopping complex or a small retailer/sabji mandi. Consumers will shop in accordance with their utmost convenience, where ever they get the lowest price, max variety, and a good consumer experience.

The Industrial policy 1991 had crafted a trajectory of change whereby every sectors of Indian economy at one point of time or the other would be embraced by liberalization, privatization and globalization. FDI in multi-brand retailing and lifting the current cap of 51% on single brand retail is in that sense a steady progression of that trajectory. But the government has by far cushioned the adverse impact of the change that has ensued in the wake of the implementation of Industrial Policy 1991 through safety nets and social safeguards. But the change that the movement of retailing sector into the FDI regime would bring about will require more involved and informed support from the government. One hopes that the government would stand up to its responsibility, because what is at stake is the stability of the vital pillars of the economyretailing, agriculture, and manufacturing. In short, the socio economic equilibrium of the entire country.

Currently

1. FDI upto 51% in single brand retail store with prior govt approval.
2. FDI upto 100% for cash and carry wholesale trading and export under automatic route.
3. FDI is not allowed in multi brand retail sector retail segment. As per the recent developments and reports: The cabinet of Government of Bharat has approved 51% FDI in multi-brand retail. Also FDI ceiling for single brand retail is increased to 100% from current 51%.

State of Retail Business in Bharat today

Organized retail is just 3% of total trade in Bharat today. Whereas organized retail sector in developed economies makes over 70-80% of total trade. Even in the Asian developing economies these figures are around 20-25% of total trade.

There are more than 1.2 Crore retail outlets operating in Bharat and only 4% of them operate in larger than 500 square feet in size. There were retail outlets per 1000 people in 2001 as per the estimates of AC Neilsen and KSA Technopak.

Pros

1. It will lead to closure of tens of thousands of small retail stores.
2. Which may endanger livelihood of 4 crore people.
3. It may tame inflation initially but will fuel the inflation once MNC companies get a stronghold in retail.
4. Farmers may be given lucrative prices initially, but eventually they will be at the mercy of big retailers.
5. SMEs will become victims of predatory pricing policies of big retailers.
6. It will replace ordinary middleman with sophisticated corporate middleman.

7. Create cultural and ecological problems by twisting the food production and availability as per the profit margin.
8. It will promote cartels and creating monopoly.

Cons

1. It will cut the middleman and help farmers get more price and consumers less cost.
2. Prices will be brought down at retail level to tame inflation.
3. Big retail chains will invest in supply chains which will cut wastage, estimated at 40% in case of fruits and vegetables.
4. SMEs will have bigger market, along with better technology.
5. It will bring in much needed foreign technology with global best-practices.
6. It will create more employment than displacing people of small stores.
7. It will induce better competition in the market, benefiting both produces and consumers.
8. Franchising opportunities for local entrepreneurs.

The FDI debate has opened up many issues which deserve proper attention of the policy makers before the retail sector is opened up to foreign investors. The findings and deliberations in this paper reveal that unlike in other sectors, FDI in retail will have a much wider impact on the economy. Essentially, organized global retail chains will break the traditional symbiotic relationship that exists between small producers and small retailers. Also, in the new retailing format, due to unequal terms of trade in a monopoly like situation, small producers and suppliers are likely to suffer most.

Also it is necessary to ensure that no giant pipeline of cheap manufactured goods suddenly disgorges its products to the detriment of the Indian manufacturer thus causing extreme social disruption. Therefore our policy should be to ensure that there is no foreign exchange outgo from the first year. The total value of imports to be retailed and the total value of exports to be retailed should match (not taking capital inflows) every year. We cannot approve of a situation where there are vast imports from the network of thousands of manufacturing sweatshops in China for five years while the Indian suppliers are being developed for later supplies and set off. If FDI in Retail is to be permitted, it should be made foreign exchange neutral for each year, at least for the first ten years.

As in the Thai model where no large markets are permitted within 15 km of the city center – all our metros should have a locational limitation. It will be better to follow the Chinese model of caution and hurrying slowly. China just allowed FDI in retail in 1992 and the cap was at 26%. After 10 years the cap was raised to 49% when local chains had sufficiently entrenched themselves. 100% FDI in retail was permitted only in 2004, after the infant retailing industry had acquired some muscle. Even in as liberal an economy as Japan, large-scale retail location law of 2000 stringently regulates factors such as garbage removal, parking, noise and traffic. Recently Carrefour decided to exit Japan by selling off its eight struggling outlets after four years to the Japanese Aeon Co as the extremely cumbersome Japanese regulations blatantly favor its own homegrown retail firms.

Malaysia s Bumiputra clause insists that 30% of equity is held by indigenous Malayans. Philippines insist that 30% of inventory by value be grown within the country.

With the above said, their research paper also advised that a number of points needed to be kept into consideration when opening up FDI:

1. The opening up of FDI should be phased, over a 5-10 year time frame so as to allow time for domestic retailers to adjust.
2. FDI in multi-brand retailing should be kept restricted in the near future, as Indian retailers would not be able to face this competition immediately.
3. It is not currently desirable for FDI to be above 51%, even in single brand retailing. This will allow checking and control of foreign retailer's business operations, and will help to protect the interests of domestic retailers. However, the sector cap (equity limit) could be increased in due course as it has been in the telecom, banking and insurance markets.
4. Certain products that are sensitive should not be allowed, for example, arms/ ammunition and military equipment. The

excluded products should be expressly stated in policy.

5. There should be restricted zones imposed by the government for the purposes of city planning. E.g. Supermarkets/Hypermarkets should be kept away from the city centers to protect the unorganized and small retailers who operate in these areas.

In order to prevent such drawbacks, the government can adopt certain measures to strengthen the domestic unorganized retail sector. Few suggestions are:

1. The retail sector in India is severely constrained by limited availability of bank finance. The Government and RBI need to evolve suitable lending policies that will enable retailers in the unorganised sectors to expand and improve efficiencies.
2. A National Commission must be established to study the problems of the retail sector and to evolve policies that will enable it to cope with FDI – as and when it comes. The proposed National Commission should evolve a clear set of conditionalities on foreign retailers on the procurement of farm produce, domestically manufactured merchandise and imported goods. These conditionalities must be aimed at encouraging the purchase of goods in the domestic market. Conditionalities must also state the minimum space, size and specify details like, construction and storage standards, the ratio of floor space to parking space etc. Giant shopping centres must not add to our existing urban snarl.
3. Entry of foreign players must be gradual and with social safeguards so that the effects of the labour dislocation can be analyzed & policy finetuned. Initially allow them to set up supermarkets of a specified size only in the metros to make the costs of entry high and according to specific norms and regulations, so that the retailer cannot immediately indulge in „predatory pricing.
4. In order to address the dislocation issue, it becomes imperative to develop and improve the manufacturing sector in India. There has been a substantial fall in employment by the manufacturing sector, to the extent of 4.06 lakhs over the period 1998 to 2001, while its contribution to the GDP has grown at an average rate of only 3.7%.23 If this sector is given due attention, and allowed to take wings, then it could be a source of great compensation to the displaced workforce from the retail industry.
5. The government must actively encourage setting up of co-operative stores to procure and stock their consumer goods and commodities from small producers. This will address the dual problem of limited promotion and marketing ability, as well as market penetration for the retailer. The government can also facilitate the setting up of warehousing units and cold chains, thereby lowering the capital costs for the small retailers.
6. According to IndiaInfoline.com, agro products and food processing sector in India is responsible for $69.4 billion out of the total $180 billion retail sector (these are 2001 figures). This is more than just a sizeable portion of the pie and what makes it even more significant is the fact that in this segment, returns are likely to be much higher for any retailer. Prices for perishable goods like vegetables, fruits, etc. are not fixed (as opposed to, say, branded textiles) and therefore, this is where economies of scale are likely to kick in and benefit the consumer in the form of lower prices. But due attention must be given to the producer too. Often the producer loses out, for example, when the goods are procured at Rs.2 and ultimately sold to the consumer at about Rs.15 as in the case of tomatoes now. The Government themselves can tap into the opportunities of this segment, rather than letting it be lost to foreign players. And by doing so, they can more directly ensure the welfare of producers and the interest of the consumers.
7. Set up an Agricultural Perishable Produce Commission (APPC), to ensure that procurement prices for perishable commodities are fair to farmers and that they are not distorted with relation to market prices.

My Views

The above analysis shows that FDI has positive and negative effects on India economy. It can be

concluded that to keep pace with the forecast of Indian GDP, government should encourage foreign investment. To avoid its negative impact on local player's regulatory framework should be redesigned. Government should encourage FDI on gradual basis like currently it is allowed for single brand. Product category wise clauses should be developed to allow FDI like

- The product categories where it can create total threat, FDI should be encouraged in the form of Joint Venture only e. g. India is enjoying strong agriculture base. Encouragement to food–grocery retail would create a threat to Indian agriculture but our poor supply chain demands end to end distribution network to reduce gate prices. For that there is a need of global established giant. So FDI should be allowed but in the form of joint venture to protect our interest part.
- FDI should not be encouraged in the product categories where Indian players are already established and FDI is only detrimental. E.g. Cosmetic products do not need FDI because entry of foreign players would replace Indian established brands with international brands. It would be a direct threat to our big giants HUL, P&G, Johnson & Johnson who are consistently providing qualitative products to consumers in all ranges. But craze of international brand will induce consumers to switch to foreign brands.
- For some categories of products FDI should be permitted for sourcing only not selling in Indian market. E.g. India need support to increase the market share of its Textile products where it has capacity to produce at the lowest rates. Encouragement to textile export can tremendously contribute towards development of our textile sector. Foreigners would get attracted due to lower prices. Thus FDI should be allowed to source or import from India not to sale in India.
- Entry of foreign players should be restricted by the format type and number of stores. E.g. Wal mart store has its different format like Super centers, Discount departmental store etc. with the help of different formats it has successfully covered almost all the locations of the city or country in which it has started its operations. Presence of such giants at all the location can stop the local business. Indian organized retail players are able to develop maximum number of supermarkets not hypermarkets because of heavy investment. So foreign players should be allowed with limited number of stores only.

As per the stats 15% i.e. around $401 bn of the GDP today is generated by 40 million work force. Which means that the wealth is distributed among the larger section. If we look at the Wal-Mart revenue is about $300 bn generated by just 2.1 million workforce.

If we allow big retailers to take over retail segment without proper regulations and fair competition then the larger amount od money will be concentrated with few business houses leading to poverty.

If the problem is rural infrastructure then we should not be dependent on outsiders for our development. We must be self-reliant in the infrastructure related activities.

Government must make sure that commodity pricing, procurement, rural infrastructure, supply chains are in place to promote competition.

Big Retailers have the tendency to get into 'contract farming' for their needs. This will push farmers to produce what they demand in bulk. Certainly, if retail giant asks for particular sort of produce in large quantity then to make more profits more area will be cultivated for that particular crop. Now due to this scenario if food grains production goes down then wouldn t there be a threat to our *food security*? And the farmer himself would be the buyer of the food grains.

Our strength lies in distributed and decentralized development, so in order to improve the life standard of last man of the strata its imperative to take development to every individual by strengthening the small enterprises.

FDI should be allowed there is no need of blanket ban on it, but with appropriate safeguards for strengthening economy to avoid employment and farming crisis like Brazil, Argentina, Thailand etc.

Based on the research carried out, we propose several recommendations for areas that have been highlighted as concerning for FDI in retail. These recommendations are by no means an exhaustive list but should serve as a framework for

consideration of the various ways forward with policy change:-

- The government should revoke the recent Press Notes that relate to permitting cascading subcompanies, as these are only serving to provide a loop-hole for back-door entry by foreign retailers and are not promoting transparency within the policy.
- We recommend that the retail sector is granted 'industry status' as soon as possible so that a legislative framework can be put in place for the control and management of the sector and its day to day operation. Begin recording detailed statistical data of the sector, both foreign, and domestic organised and unorganised so that the impact of FDI when introduced can be closely monitored and policy finetuned accordingly.
- Labour Laws need to be reviewed to be more in line with the requirements of retail sector employment.
- Investment should be made by the government to improve the efficiency of the manufacturing sector so that this sector can grow and provide more employment opportunities going forward.
- City Planning needs to be addressed so that development is in such a way that it protects the traditional trader areas and does not clutter the already densely populated city centers.
- Real Estate Regulations need to be considered for reform so as to facilitate access to land and property for use by the retail sector, and to provide equal access to space for both foreign and domestic players.
- Certain sensitive products should be restricted from foreign retailing, so as to protect the traditional craftsmen and unorganised traders. The products to be restricted needs to be given thought and researched before any decisions are made.
- The government should impose local employment quotas on foreign retailers, firstly to reduce the effects of any potential labour displacement, and secondly to encourage foreign retailers to provide training, skills and development to local people who without it would not be able to transfer to the 'organised' retail sector or back-end services.
- Rules on re-patriation of foreign profits should be revised, to discourage (and restrict) 100% of profits from leaving India. Conditions imposed on requiring foreign retailers to invest a minimum amount in infrastructure and supply chain capabilities would be beneficial.
- Consider providing Tax relief and/or subsidy by way of low rate loans to domestic retailers to provide support.
- Implement a 'phased introduction' of FDI to the retail sector, say over 2-4 years, so as to provide gradual adjustment for the domestic players and to allow fine-tuning and adjustment of policy if issues arise.
- The government should reform price control policies to ensure that foreign retailers cannot sell below a minimum price, rather than the current Maximum Retail Price (MRP).
- Conditions of minimum sourcing from domestic agricultural and manufacturing sectors should be imposed, so as to prevent the creation of a 'China Pipeline'.
- Bureaucracy and formalities should be reduced by updating related legislation, for example, reducing the number of licences required by businesses to open a store. This should assist the domestic players in expanding and will help to streamline the efficiency of the sector.
- Geographical restrictions for foreign investors need to be considered so as to reduce the impact, or prevent the fast expansion of retailers in to rural areas. Special Economic Zones need to be assessed with further research, to review their advantages and disadvantages to both India as a country, and to the foreign players
- Other related regulations such as copyright law, need to be updated and brought in to line with the needs of the future Indian retail sector.

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