International Journal of Management and Commerce
www.managementjournal.in
Online ISSN: 2664-6854; Print ISSN: 2664-6846; Impact Factor: RJIF 5.46
Received: 04-10-2020; Accepted: 18-10-2020; Published: 07-11-2020
Volume 2; Issue 2; 2020; Page No. 48-52

# An overview of India's foreign direct investment (FDI) in retail policy and its impact on the growth of retail sector

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**Abstract**
India retail sector has grown by leaps and bounds in the recent years. One of the major reasons for such exponential growth is Foreign Direct Investment (FDI) policy of Government of India. Earlier, FDI in retail sector in India was not allowed. But to speed up the growth of retailing in India, the government of India has opened doors to Foreign Direct Investment (FDI) in retail sector. In 2006, the Government eased retail policy for the first time allowing FDI up to 51% through the single brand retail route. Initially, FDI was allowed in some selected sectors only. However in July 1911, the Government of India has recommended 51% FDI in Multi-Brand Retail and 100% FDI in Single-Brand Retail through approval route. In 2018, 100% FDI permitted in Single Brand-Retail through automatic route. This has changed the whole scenario of Indian retail industry in India. In this paper an attempt has been made to study the recent Foreign Direct Investment (FDI) policy in retail and analyze its impact on the growth of retail sector.

**Keywords:** foreign direct investment (FDI), growth, retail sector, retail policy

## Introduction

Retailing can be said to be the network between the producer and the individual consumer. Retailing is the last link that connects the individual consumer with the manufacturing and distribution chain. It sells the goods to the consumer at a margin profit. To speed up the growth of retailing in India, the government of India has opened doors to Foreign Direct Investment (FDI) in retail sector. Now, Indian retail industry is emerging as one of the most attractive sector for foreign investors.

FDI plays a major role in the development of the country. It contributes in the process of development like transfer of financial resources in various sectors, spreading the technology, improving the managerial skills and progress of growth. Prior to 1991, Government of India was very apprehensions in allowing FDI in retail sector.

From 1991 FDI was limited to only a few sectors like manufacturing, infrastructure etc. However in July 1911, the Government of India has recommended 51% FDI in Multi-Brand Retail and 100% FDI in Single-Brand Retail through approval route. In 2018, 100% FDI permitted in Single Brand-Retail through automatic route.

## Meaning of Retailing

The word 'retail' is derived from the French term 'retaillier', which means to cut a piece of or to break bulk. The term retailing applies not only to the selling of tangible products, but also the selling of different service products. Retailing involves a direct interface with customers and it includes co-ordination of business activities right from the design stage of a product to its delivery as well as post delivery services to the customers.

Retailing facilitates the flow of goods and services from manufacturer to ultimate customers. Retailing includes all the activities involved in selling goods and services to ultimate consumer for personal and non-personal use.

A retailer is a person, agent, agency, company or organization which is instrumental in reaching the goods and services to the ultimate consumers. Retailer is an ultimate link between the producers and consumers and responsible for matching of individual demands of the consumer with the supplies of different manufacturers. Retailer performs specific activities such as anticipating customer's needs, developing assortments of products, acquiring market information, financing etc.

## Evolution of Retail in India

**Table 1**

| | |
|---|---|
| Pre 1990s | ▪ Manufacturers opened their own outlets |
| 1990-2005 | ▪ Pure-play retailers realized the potential of the market.<br>▪ Most of them in apparel segment. |
| 2005-2010 | ▪ Substantial investment commitments by large Indian corporate.<br>▪ Entry in food and general merchandise category.<br>▪ Pan-India expansion to top 100 cities.<br>▪ Repositioning by existing players. |
| 2010 Onwards | ▪ Cumulative FDI inflows from April 2000 to September 2019, in the retail sector reached US$ 1.89 billion.<br>▪ Retail 2020: Retrospect, Reinvent, Rewrite. |

| | |
|---|---|
| | ▪ Movement to smaller cities and rural areas.<br>▪ More than 5-6 players with revenues over US$ 1 trillion by 2020.<br>▪ Large scale entry of international brands.<br>▪ Approval of FDI limit in multi-brand retail up to 51 per cent.<br>▪ Rise in private label brands by retail players.<br>▪ Sourcing and investment rules for supermarkets were relaxed.<br>▪ E-commerce has emerged as one of the major segments.<br>▪ 100 per cent FDI in single brand retail under automatic route. |

**Source:** Technopack Advisors Pvt Ltd, BCG

## Classification of Retail Sector

The retail is mainly classified into two sectors namely:

1. Organized Sector
2. Unorganized Sector

Organized retailing is one in which the trading or merchandising is carried out by licensed or authorized retailers who are registered for goods and service tax and other taxes. The companies owned super markets, hyper markets, retail chains and other privately owned retail store comes under this organized retailing. The revenue generated by these enterprises is accounted for by the government. Unorganized retailing, on the other hand, refers to the traditional formats of low-cost retailing. Regarding the unorganized retailing, it stands for 95% of the Indian retailing and is occupied by the sole-owner managed general provision stores, pan shops, convenient stores, Handcart and pavement vendors.

## Review of Literature

Verma at al. (2012) discussed various marketing strategies which must be adopted by big giant retailers to capitalize the Indian market. The researcher suggested that adoption of local culture, targeting youth, high volume low margin business mode, e-tailing, owner feel to sales person, adoption of franchise and direct business model can help business community to understand Indian consumer well. The researcher pointed out that retail market in India is dominated by unorganized retailers. India being an attractive destination for foreign players will definitely be affected in terms of growth.

Nizamuddin (2013) in his paper tried to explore the impact of FDI on employment generation. With the help of ordinary least square method, time series analysis and by applying t-test the researcher concluded that the FDI has a negative impact on employment generation in India. The researcher suggested that FDI policy must be liberalized in a phased manner.

Mundra *et al*. (2013) examined the expansion of FDI in retail in global scenario. The study pointed that in China, Thailand, Chile, Indonesia and Brazil, FDI is permitted in retail sector. The retail sector in India is accompanied by challenges like geographically dispersed population, small ticket sizes, a complex distribution system, less usage of IT, mass media limitations and existence of replica goods. The study discussed the impact of FDI on various stakeholders and concluded that restrictions on FDI policy must be reduced to make the industry more productive and competitive. The doubts attached to opposition of FDI policy must be analyzed in proper perspective.

Fulzele & Zodage (2013) tried to find out the positive impacts of FDI in Indian retail sector. India possesses a number of opportunities to attract foreign players to invest. The study concluded that FDI in necessary for the growth and development of farmers, generating new employment opportunities, benefits to consumers, development of SSIs, capital inflow, infrastructure development, inflation control, improvement in retailing services, technical know-how infusion, growth of GDP, decline in cost of production of goods and services.

Sharma & Bansal (2015) examined the trends of FDI in retail in Indian retail sector. The study highlighted the perceived opportunities of opening FDI on one hand like capital infusion, benefits to farmers and consumers, improvement in supply chain, logistic and technology and potential threats such as dominance of organized retail, increased unemployment due to removal of middlemen, increase in real estate cost because of increase in demand to set up new big outlets and negative impact on Indian culture. FDI in retail should be allowed in a phased manner. Formulation of national commission is suggested to tackles the problems of retail sector in a well-defined manner.

Chawla at al. (2016) tried to review the FDI in Indian retail sector. The researchers concluded that gone are the days, when customers were dependents on nearby store for fulfilling their needs. With the new concepts like e-tailing, customized products a big shift has been seen in the response of customers. Positive as well as negative points are attached to the liberalized FDI policy in retail sector. FDI in no doubt is likely to bring improvement in state of Indian economy, but the stake of small retailers must be taken care of while formulating and implementing the policy.

Saran & Singh (2018) focused on inflow of FDI in Indian retail industry. The researchers pointed out that there is a need of initial and desirable action by the industry as well as Government of India to utilize the full potential productivity of retail sector in India. Apart from it, Indian retail sector need a national policy for retail to complement growth of various channels that not only promote the growth of domestic but also foreign investments in this sector. A conducive regulatory environment for retailers will help to build 'New India', benefiting consumers, industry and consumers and economy at large. India has more favourable conditions for FDI in retail than any other countries of the world because of growth in discretionary income, changing lifestyle, tax reforms like implementation of GST etc.

## Objectives of the study

- To study the present Foreign Direct Investment (FDI) in Retail Policy of India.
- To study the advantages and disadvantages of FDI in Retail Sector.
- To analyze the impact of FDI on the growth of Indian retail sector.

## Research Methodology

Research Methodology is the systematic and theoretical analysis of the methods applied to a field of study. It includes the process used to collect information and data for the purpose of making decisions. In the present paper, the secondary source of information has been used. The data has been collected from journals, books, annual reports and websites.

**Foreign Direct Investment (FDI)**

Foreign direct investment (FDI) can be defined as an investment made by a company or entity based in one country, into a company or entity based in another country. Foreign Direct Investment differs substantially from indirect investment such as portfolio flows, wherein overseas institutions invest in equity listed on a nation's stock exchange. Entities making direct investment typically have a significant degree of influence and control over the company into which investment is made.

The investing company may make its overseas investment in number of ways-either by setting up a subsidiary or associate company in the foreign country, by acquiring shares of an overseas company or through a merger or joint venture. The accepted threshold for a foreign direct investment relationship, as defined by the OPCD, is 10%. That is the foreign investor must own at least 10% or more of voting stock or ordinary share of the investee company. The foreign direct investment in any country is the net inflow of investment (capital or other), in order to acquire management control and profit sharing or the whole ownership of the company operating in the receiving country. The foreign direct investment generally encompasses the transfer of technology and expertise and participation in joint venture or management.

The foreign direct investment is profitable both to the country receiving investment and the investor. For the investor company FDI offers an exclusive opportunity to enter into the international or global business, new markets and marketing channel, elusive access to new technology and expertise, expansion of company with new or more products or services and cheaper production facilities. While the host country receives the foreign funds for development, transfer of new profitable technology, wealth of expertise and experience and increased job opportunity.

**FDI Policy in Retail Sector in India**

Foreign Direct Investment in the retail sector in India enlists varying rules for different areas in this sector. Earlier, foreign players could own up to 49% in a local single-brand retail trading chain but had to approach the Department of Industrial Policy and Promotion for permission to acquire the remaining 51%. Under the new policy, up to 100% FDI in allowed in local single-brand retail trading without getting approval from the Department of Industrial Policy and Promotion. However this is subject to certain conditions. At least 30% of the raw materials needs to sourced from India, especially from rural cottage industries and other micro, small and medium enterprises or even artisans and craftsman. The product should be branded during manufacturing and items should be sold under a single brand name, internationally. In case of multi brand retail entities, up to 51% of FDI is allowed subject to prior government approval and some other conditions. The FDI Policy also allows for investment without any additional requirement of approval from the government in case of units which are part of market place model of e-commerce, wherein the role of e-commerce unit is to merely provide a platform for connecting buyers and sellers. On the other hand, FDI is not permitted in the inventory based model wherein the e-commerce entity owns and controls the inventory of goods sold on its portal.

**Arguments of Opposition on FDI in Retail Policy**

- FDI in retail sector would lead to massive job losses. The international retail giant would replace the small retailers, leading to losses of income worth crores for Indian.
- In India, there is very high shopping density and where most of the small shop owners are self-employed; their displacement would adversely affect economy on the whole.
- The Global retailers could also resort to predatory pricing, which would lead to the formation of an oligopoly or monopoly. The market for essentials could end up being controlled by foreign organizations, knocking out the local stores from the market.
- Foreign investment would lead to consolidated markets, making the consumer captive with limited choices, unlike fragmented markets which provide more options.
- It would not create more markets but just displace the existing ones.
- It would also lead to loss in manufacturing sector as well, since most structured international entities make their purchase internationally.
- India doesn't need foreign retailers, since home grown companies and traditional markets may be able to do the job.
- Work will be done by Indians, profits will go to foreigners.

**Advantages of FDI in Retail in India**

- **Growth in the economy:** With the coming of foreign companies as a result of FDI, new infrastructure will be built. Sectors like real estate and banking will grow. MNCs will pay a lot of taxes to the Indian Government, which can be used to develop infrastructure.
- **Employment Generation:** FDI in retail will generate many jobs in organized retail sector. It will create positive impact on other sectors as well.
- **Benefits to Farmers:** FDI in retail will benefits farmers and producers by procuring produce from them directly and bypassing the intermediaries. This will improve the margin of farmers. FDI also help in upgrading the farmer's capabilities by providing know-how and capital.
- **Reduction in Wastages:** In India, there is huge wastage due to poor supply chain and inadequate storage facility. FDI in retail will help to reduce this wastage by investing in supply chain and adequate storage facility.
- **Better technology and learning:** MNCs can bring in better technology, best management practices and more learning for Indian players.
- **Benefits to consumers:** Consumers will get branded products at low prices and more variety of products to choose from. It will also ensure better quality with greater transparency and easier mentoring of adulteration and counterfeit products.
- **Push to productivity:** Indian production agriculture and food is very poor. FDI in retail will give much needed push to infrastructure in agriculture and farming practices.
- **Increase in competition:** It will increase competition in the market, which will benefit both consumers and producers.

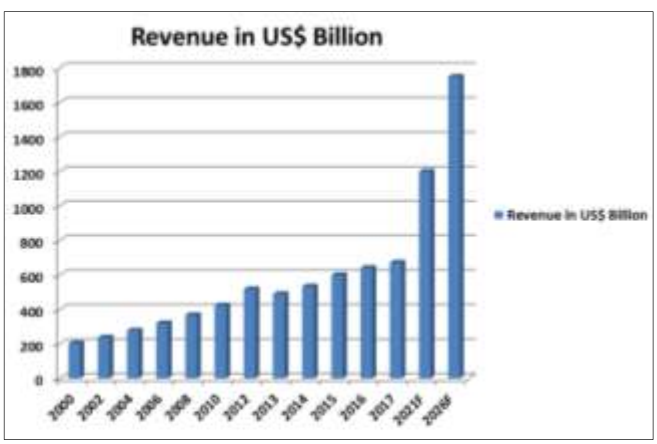
- **Food security:** Investment in needed to be made in agricultural back-end and supply chain. Otherwise, it would be difficult to meet India's growing demands for fruits and vegetables, dairy and poultry products.
- **Encouragement to domestic manufacturing:** According to the Indian Government's condition, foreign companies have to source a minimum of 30% of their goods from Indian micro and small industries. This will encourage the domestic manufacturing resulting into employment generation, technology up gradation and income generation.
- **Cheaper production facilities:** FDI will assure operations in production cycle and distribution. Due to economies of operation, production facilities will be available at a cheaper and thus resulting in availability of variety of products to ultimate consumers at reasonable and cheaper price.
- **Availability of new technology:** FDI allows transfer of skills and technology from abroad and develop the infrastructure of the domestic country. Greater managerial talent will flow from other countries.

**Disadvantages of FDI in Retail in India**
- Retail sector is one of the major employment providers in India. If FDI is permitted in this sector, it can displace the unorganized sector, leading to loss of livelihood to millions of people.
- FDI will drain out the country's share of revenue to foreign countries which may cause negative impact on India's overall economy.
- The domestic organized retail sector might not be competitive enough to tackle international players and might lose its market share.
- Supermarkets and big malls will establish their monopoly in the Indian market. Due to their fine tuning and higher accessibility they will be able to buy goods at lower prices and therefor will be able to sell at lower prices to consumers. This will result in closing of many small retailers and Kirana Stores.
- It is said that FDI will provide employment opportunities, but it is argued that it cannot provide employment to semi-illiterate and un-skilled people who are in large number in India.

**Growth of Retail Industry in India**

**Table 2**

| Year | Revenue in US$ Billion |
|---|---|
| 2000 | 204 |
| 2002 | 238 |
| 2004 | 278 |
| 2006 | 321 |
| 2008 | 368 |
| 2010 | 424 |
| 2012 | 518 |
| 2013 | 490 |
| 2014 | 534 |
| 2015 | 600 |
| 2016 | 641 |
| 2017 | 672 |
| 2021F | 1200 |
| 2026F | 1750 |




**Source:** indiaretailing.com, BMI Research, Consumer Leads

**Fig 1**

Report by FICCI and Deloitte- October 2018
The retail sector in India is emerging as one of the largest sectors in the economy. It contributes 10% of GDP and 8% of employment. The total market size of Indian retail industry reached US$ 672 billion in 2017. It is forecasted to increase to US$ 1200 billion by 2021 and 1750 billion by 2026. India will become a Favour able market for fashion retailors on the back of a large young adult consumer base, increasing consumer disposable incomes and relaxed FDI norms.

## Growth Drivers for Retail in India

The factors responsible for the growth of retail sector in India are as follows:

**Table 3**

| | |
|---|---|
| Consumer Preferences | ▪ India's per capita GDP increased to ₹143048 (US$1982.65) in FR 19 from ₹129901 (US$ 1800.43) FY18.<br>▪ Indian consumers are now shifting more towards premium brands by paying more for value and service. |
| Brand Consciousness | ▪ Factors like young demographic composition, increasing personal disposable income, more preference towards affordable luxury and rising middle class population are developing preferences for specific brands. |
| Consumer Finance Opportunities | ▪ Consumers have become more comfortable using online services due to demonetization.<br>▪ Online retail segment provides various credit and payment options driven by increasing internet penetration, speed, 24-hour accessibility and convenient and secured transactions. |
| FDI Approvals | ▪ Department for Promotion and Industry and Internal Trade (DPIIT) approved three foreign direct investments (FDI), Mountain Trail Food, Kohler India Corporation, and Merlin Entertainments India in single brand retail sector.<br>▪ The DPIIT has approved two FDI proposals worth more than ₹400 crore (US$ 62.45 million) with in the retail sector. |
| Investments | ▪ India's retail sector investments doubled to reach ₹1300 crore (US$ 188.18 millions) in 2018.<br>▪ As of November 2019 IKEA plans to open three stores in India with an investment of 117.96 billion (US$ 1.69 billion)<br>▪ As of November 2019, Kohler India plans to double retail network in the country in next three years. |

**Source:** News Articles, Ministry of Statistics and Programme Implementation, Anarock Retail

## Conclusion

FDI in retail sector has now become the part of India's economy. Initially, FDI in retail was not allowed. However, with the passage of time, Government of India allowed FDI in retail sector in a phased manner. FDI in retail has many advantages like economy growth, employment generation, benefits to farmers, better technology & learning, reduction in wastage, increase in competition, cheaper production facilities, encouragement to domestic manufacturing etc. However, it also has some disadvantages like displacement of unorganized sector, draining out of country's revenue to foreigners, loss of market share to organized retail sector, monopoly of supermarkets and big malls etc. It can be concluded that advantages of allowing FDI in retail sector has certainly outweighed the disadvantages attached to it, which is evident from the continuous growth of Indian retail sector. The total market size of Indian retail industry reached US$ 672 billion in 2017. It is forecasted to increase to US$ 1200 billion by 2021 and 1750 billion by 2026. FDI is proving a powerful catalyst to spur competition in industries characterized by low competition and poor productivity. The decision of allowing up to 51% FDI in multi-brand retail and 100% FDI in single-brand retail under the automatic route is expected to lead the Indian retail sector to new heights. India is now expected to become the world's fastest growing e-commerce market. The long term outlook for the Indian retail industry is positive, supported by rising incomes, favourable demographics, Entry of foreign players and increasing urbanization

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