FOREIGN DIRECT INVESTMENT (FDI) IN INDIA: CHANGING DYNAMICS POST 1991 IN RETAIL SECTOR

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ABSTRACT

Many experts believe that despite FDI being an important tool in economic development, extensive research on FDI evolution is not available to lay emphasis on the importance it has on Indian economy. FDI in retailing has been extensively debated in India and this research paper will examine the socio-political effect it has on India. The Indian retail sector is chosen to explore how FDI has become relevant to accomplish the goal of becoming a global economy. This research paper mainly explores the evolution of FDI post 1991 economic reforms and therefore studies historical implications of FDI in India. The research paper utilizes a descriptive approach in data collection so as to interpret and analyze market sentiments towards FDI. Secondary research sources such as press releases, government reports, circulars by government departments and other internet sources are referred in conducting this research. The advantages and disadvantages of FDI in retailing are also explored through this research paper.

Keywords: Foreign Direct Investment, Retail Sector, Indian Economy, Global Economy, Socio-Political Effect.

INTRODUCTION

Ever since India got its independence, foreign investment has held the attention of the government policy makers. However, the foreign policies were restrictive and selective. In 1973, Foreign Exchange Regulation Act (FERA) was passed to regulate foreign capital inflows. With limited access to foreign capital and insufficient private capital the government could not meet the rising debt that continued to deteriorate Indian economy until the end of 1980s. This serious Balance of Payment crisis affected in an increased inflation rate of 12 per cent. Along with World Bank and International Monetary Fund (IMF) economic reforms were introduced and consequently India opened its doors to Foreign Direct Investment (FDI). New economic policies were introduced to rebuild the confidence of foreign investors and allowed investments in equity. This move towards a liberalized policy coincided with a growing interest in emerging markets through the world. The foreign equity capital limit was raised to 51 percent for several sectors and to 100 per cent in few others. Many foreign investors retailers entered Indian market through franchising and private domestic firms too started invested heavily in the service sector. In the later part of 1990's India's Gross Domestic Product (GDP) increased by 7 per cent. The inflation gradually decreased to 5 per cent towards the beginning of 2000.

Table1: Economic Indicators India (2010-2013)

Indicators	2010	2011	2012	2013
GDP growth rate (annual %)	10.2	6.6	4.7	4.3
Inflation (%)	10.5	9.5	10.2	9.4

Source: Planning Commission

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RESEARCH PAPER JUSTIFICATION

This research paper aims to examine the economic reforms undertaken after 1991 are crucial to study the evolution of foreign investment in India. As FDI policies affect the stance of global players towards host country, this research paper explores where India stands as one of the preferred nations to do business. Thus the research paper is important in examining the steps taken to implement progressive economic regulations. The study is also pertinent in considering the limitations that has led to a slow growth of FDI, especially in Indian retail sector.

RESEARCH METHODOLOGY

Primary research in the form of a survey has been used to collect data. Most of the views are individual's opinions which are gathered through one-to-one discussion. A wide range of secondary research materials such as government reports, industry reports, corporate literature, academic reports, newspaper articles, and online media reports have been used.

FOREIGN DIRECT INVESTMENT IN INDIA

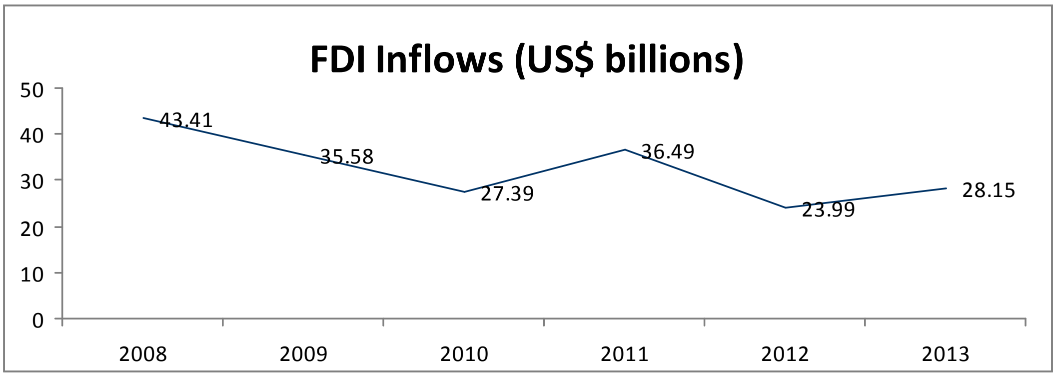
FDI helps is gaining long term capital required for sustainable economic development of India. It helps in financing big projects, opens opportunities to improve trade relations with foreign nations, and boosts economic growth through joint ventures and collaborations. Through FDI jobs can be generated by foreign corporations who invest in India.

Table 1: Top 5 Sectors that are Attracting FDI Inflows

Rank	Sector	Percentage of Total Inflows
1	Service sector	18%
2	Construction Development	10%
3	Telecommunications	7%
4	Computer Software & Hardware	6%
5	Drugs & Pharmaceuticals	5%

Source: Department of Industrial Policy & Promotion (DIPP)

Figure 1 represents the amount of FDI inflows between 2008 and 2013.



Source: World Bank

Figure 1: FDI Inflows between 2008 and 2013

RETAILING IN INDIA

The Indian retail sector is regarded as one of the most attractive retail destinations worldwide. Retailing in India currently occupies 20th position among the top 30 developing countries. There are more than 12 million retail outlets in India selling products within food & grocery, apparel, electronics, and lifestyle segments. Some of the key factors driving the current retail sector in India are emergence of nuclear families, improved standard of living, double income families, high discretionary income and hence greater buying power, and rising demand for luxury items. The retail market in India is expected to grow at 15 per cent and reach Rs.46 trillion by 2016.

Some of the emerging market trends in retailing are the growth in the use of technology and increased purchasing through online retailing. Online retailing is still in its initial stages in India and has a long way to match some of the other developed economies. However, the Indian online retail market is expected to grow at 40-45 per cent in the next four years. Some of the online players currently leading the market are Flipkart, Snapdeal and Amazon India.

Retailing in India is mainly divided into two parts:

Organized: Organized retailing refers to trading activities carried out by licensed retailers. Retailers under such type of retail outlets are registered under sales tax, income tax, etc. Organized outlet can operated more than 2 outlets and is managed by professionals backed by corporations of large privately owned retail businesses. Some of the current formats of organized retailing are department stores, supermarkets, hypermarkets, and shopping malls.

Unorganized: A traditional style of low- cost retailing is known as unorganized retailing. The local kirana shops, general stores, paan/ beedi shops, convenience stores, hand carts and pavement vendors are some of the examples of unorganized retailers. These retail outlets are typically run by the owner and sourcing is done locally to meet local needs. In terms of numbers, unorganized outlets definitely have an upper-hand when compared to organized retailers.

GROWTH IN ORGANIZED RETAILING

The modern supermarket and shopping malls coexist with other traditional retail stores. The unorganized retail segment constitutes close to 92% of the total retail market. Organized retailing is still under-developed in India. Nevertheless modern/organized retailing is growing at a consistent speed, especially in metropolitan cities and big towns. Demands of modern consumers have evolved and most of them insist on affordable prices, high product quality, store ambience and other additional customer services which modern retail outlets offer. In addition, more than 60 per cent of the population comprises of working age group which translates into an attractive consumer base for organized retailers. Some of the modern formats that are gaining popularity are health and beauty, apparel and footwear, lifestyle products, consumer durable products, leisure and personal products.

FDI REGULATORY FRAMEWORK

The FDI regulations are governed by Foreign Exchange Management Act, 1999 (FEMA). Foreign investment in India can be approved via one of the two different routes:

Automatic Approval: Automatic Approval route requires no prior approval by the government or the Reserve Bank of India (RBI). RBI needs to be intimated within 30 days of the inflow of capital. The automatic route is suitable in any sector where there is no 'sector cap'. Some of the examples include housing & real estate, films, advertising and pharmaceuticals.

Government/FIPB Approval: Foreign Investment Promotion Board (FIPB) approval is for proposals where the shareholding is intended to be above a prescribed 'sector cap'. It also may include those activities where FDI is currently not allowed, or where it is obligatory for FIPB to approve.

FOREIGN DIRECT INVESTMENT IN RETAIL

Integrating into global economy through FDI provides India with an opportunity to improve productivity and growth in output. The government is reshaping regulatory policies to meet the new challenges and opportunities in retail sector. By allowing FDI in Indian retail sector, businesses have now integrated with global supply chains to improve technology, quality standards and marketing activities and also create new job opportunities.

FDI POLICY FRAMEWORK

To assist foreign inflows the following framework has been adopted:

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

(b) 100 per cent FDI is allowed, with prior approval from the government for retail trade in 'Single Brand' products.

(c) Upto 51 per cent FDI is allowed in 'Multi-Brand' retailing.

ENTRY ROUTES

As per the current FDI policy, entry routes for foreign investors are:

(a) Franchisee Agreements

(b) Cash & Carry Wholesale Trading

(c) Strategic Licensing Agreements

(d) Manufacturing & wholly owned subsidiaries

CHALLENGES IN IMPLEMENTING FDI IN INDIA

• Lack of large investments in logistics • Availability of retail space • Competition from rural traders such as '*haats*' and village fairs	• Underexploited manpower resource • Inconsistent economic development • Political confrontations at central and state level

ADVANTAGES OF FDI IN RETAILING

Organized retailing in India continues to be one of the least advanced sectors when compared to other emerging markets. Although retail contributes heavily towards GDP the share of organized retailing minor. The industry experts believe that FDI in retail will benefit India due to the following advantages:

(a) Farmers will be benefitted as advanced storage system will be incorporated through backward integration.

(b) The international retail companies possess knowledge on supply chain management, merchandising and operations of new technology.

(c) The concept of one-stop-shop will benefit consumers in providing a wide range of products at affordable prices.

(d) Investors benefit by a transparent regulatory model that negates complex regulatory policies that existed earlier.

(e) FDI in retail ensures retailers follow tax guidelines and thereby increase revenue to the government.

(f) New retail formats ensure all the amenities are provided to the customers including computerized billing system, parking spaces, and return policies.

(g) With the help of mobile applications and increased use of internet, e-tailing (online retailing) helps customers to buy products easily and improve their awareness.

DISADVANTAGES OF FDI RETAILING IN INDIA

Essentially, the modern retailing system consists of disproportionate conditions of trade where large retailers have the power over markets and control small producers and suppliers. When we consider long term sustainability of retailing in India the disadvantages that come along organized retailing should also be studied.

(a) FDI in retail does raise problems concerning displacement of labor as most number of people employed in this sector hail from unorganized retail outlets.

(b) Micro, Small and Medium Enterprises (MSME) may be adversely affected if large corporations import maximum raw materials from other cheaper countries

(c) There are no regulatory restrictions on large Indian organized retailers (unlike foreign investors) and hence have superior power over small players in the market

(d) With retailers expanding stores, there is a rising demand for real estate. This has caused an increase in real estate prices

(e) There have been talks to amend the existing General Agreement on Trade Services (GATS) that may heavily support foreign investors, negating regulations in host country.

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