• BRIEFING PAPER •

The Pitfalls of FDI in Multi-Brand Retailing in India

There is a growing pressure on policymakers from foreign governments and big retailers to permit foreign direct investment (FDI) in multi-brand retail in India. At present, India allows 51 percent FDI in single-brand stores (e.g., Apple) and 100 percent FDI in cash & carry and wholesale trading. The retail trading by foreign multi-brand retailers (e.g., Wal-Mart Stores) is prohibited under the current regulatory regime.

The Committee of Secretaries has recently recommended that the sector be opened, with some riders that are easy to meet. Understandably, big domestic players in the retail business would welcome such a step, as they will be direct beneficiaries of investments into the sector. The government is yet to issue its formal notification, presumably evaluating the implications.

It is imperative that policy making with respect to FDI in multi-brand retail must take into account the unique situation of India, and not blindly follow Western practices. No other country (except China) faces the challenge of meeting the needs of 1.2 billion people. No other country has close to 400 million people below the poverty level, to be given some basic livelihood. No other country has the social complexity coupled with a fractious polity, which can erupt into social unrest with ease, when inherent balance is disturbed. In such a scenario, policymakers must serve the needs of

the broadest base of the population, not just those at the top of the economic pyramid.

To begin with, one should assess the pros and cons of FDI in multi-brand retail over the next 10 to 20 years, not in immediate terms. In the short term, there is no denying that foreign capital will flow into the country and the government can claim that its economic reform agenda is intact. However, the adverse implications will be felt over long time in terms of job loss and the displacement of small retailers and traditional supply chains.

A large number of countries (rich and poor) have experienced negative impacts of multinational retail chains. Therefore, it is important for Indian policymakers to learn lessons from such experiences and adopt a cautious approach towards opening up the multi-brand retail sector.

The Indian Scenario

The oft-repeated argument that “As China has done, so India should do” is flawed, and does not take into account the key differences between the two economies. Unlike India, China enjoys a huge trade surplus with US and other major trading partners. China’s manufacturing base is very strong. Because of its globally competitive manufacturing sector, China can afford to open its retail sector to foreign investment. In contrast, Indian economy is services-led, with services outpacing industry and agriculture. The services sector accounts for 55 percent of India’s GDP.

According to the A.T. Kearney Global Retail Development Index (2011), Indian retail sector accounts for 22 percent of the country’s GDP and contributes to 8 per cent of the total employment. India’s retail sector is highly fragmented, with self-organized retailing accounting for as much as 96 percent of the total retail trade.

India’s low-cost retail trade exists in various forms (small stores to pavement vendors) and acts as a social security valve. Millions of small retailers make a living by serving small communities and neighbourhoods.

The Big Players

Once the multi-brand retail sector is opened up, multinational retail giants with turnovers of tens of billions of dollars will be lining up for a share in the Indian market. Some of the prominent big players keen to enter into India include Walmart from US (sales last year of over $400 billion (bn) from 9,000 stores), Carrefour from France (sales $130 bn from 9,500 stores), Tesco from UK (sales $100 bn from 5,400 stores), and Metro from Germany (sales $96 bn from 2,100 stores).

The predatory practices adopted by several multinational retail chains are well documented. Given their financial strength, big multinational players have the capacity to invest and sustain losses for years in order to wipe out competition. In the process, however, a large number of small and local retailers could be wiped out. For instance, take the case of Thailand where three foreign retailers took over 38 percent of the market within 13 years, thereby throwing thousands of local retailers out of business. Thailand is now struggling to contain the expansion of big retailers, and prevent monopolistic practices.

The big multinational retailers will not be content with setting up a few stores in India. Rather they will collectively set up thousands of shops all over the country over a period of time. Their business model demands that they build large volumes, which they would use to buy at lower prices, and this will help them to build larger volumes (leading to more concentration) till it becomes very difficult for small and local retailers to compete with them.

Good for Consumers and Farmers?

Is it good for the consumer then, if prices are lowered initially? Up to a point, the consumer will

Table 1: Grocery Retail: Market Share by Country (2010) (in percent)

Country	Top Retailers	Market Share	Combined Market Share of Top Retailers
Sweden[a]	ICA Stores	50	
	COOP	20	
	Axfood AB	16	**86**
Belgium[b]	Carrefour	29	
	Delhaize	25	
	Colruyt	25	**79**
Australia[b]	Woolworth	46	
	Coles	32	**78**
Germany[b]	Metro, Edeka, Rewe, Schwarz, Tegelmann		**75**
Mexico[a]	Walmart	47	
	Soriana	14	
	Commercial Mexicana	9	**70**
UK[b]	Tesco	30	
	Asda	17	
	Sainsbury	16	**63**
France[b]	Carrefour	25	
	Le Clerc	17	
	Mosquetaries	13	**55**
Brazil[b]	Carrefour	14	
	Cia. Brasileira de Distribuicao	13	
	Walmart	10	**38**
Thailand[a]	CP-All (part of 7-Eleven)	11	
	Tesco Lotus	9	
	SHV Makro	5	
	Big C-Casino Group	5	
	Central Retail	2	**32**

[a] 2010.

[b] 2009.

Source: Compiled by author from various official and business publications. The complete list of publications is available with the author.

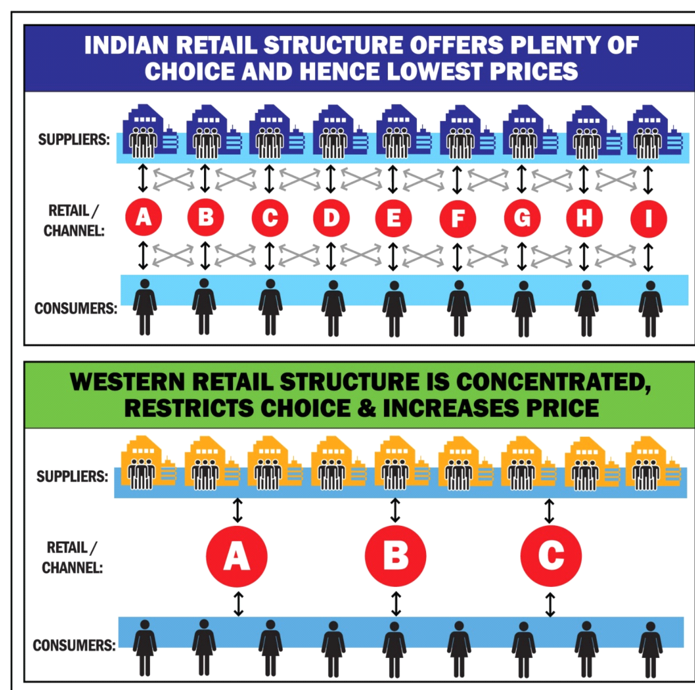
benefit. But once big multinational players establish domination, the consumer becomes captive to them. That is when their mark ups will go up, and the consumer will have no choice but to pay the higher price. In essence, big retail business is a game of concentration and domination. In almost every market in the world, big multinational chains have edged out other players, leading to unfair concentration. In the grocery business, for instance, market shares range from 20 percent to as high as 80 percent. In Table 1, the market share of top retailers in several developed and developing countries is given. What is alarming to note is that market share in Brazil (38 percent) and Thailand (32 percent) has been achieved in just over a decade.

The usual business model of big multinational retailers is "buy lowest, sell highest." They aim for size and scale to gain the power to dictate terms in the retail markets. There are several reasons to believe that they will not give Indian farmers a better price. In the US, for instance, farmers received over 40 cents for every food dollar spent at supermarkets in 1950s. Presently, they merely receive just 19 cents.

Since foods and vegetables are highly perishable items and refrigeration infrastructure is poor in India, producers will have no option but to sell their products at the price demanded by big retailers. No big foreign or domestic private retailer is going to invest huge amount of money in building rural infrastructure. This major problem can only be solved by undertaking massive public investments in the rural infrastructure such as roads, power supply and cold storages. It requires a different set of policy measures by both central and state governments.

Employment Creation or Displacement?

Presently, retail market structure in India is just the opposite of West, with no single player dominating any segment of the market. This structure tends to benefit both consumers and suppliers. The multinational players can superimpose their retail model on the Indian markets due to strong financial muscle and global sourcing. In the process, millions of jobs will be displaced not merely in the self-organized sector but also in the corporate retail sector as they will find it difficult to survive the onslaught of big retailers such as Walmart.



Unlike developed countries, 51 percent of the India's total workforce are self-employed. One of the biggest avenues of self employment is in retail trade due to very little entry barriers. For a vast majority of unskilled and poor people, retailing offers an excellent safety valve. Given the lack of alternative employment opportunities available, it is highly unlikely that the displaced unemployed (post foreign investment in the retail sector) will be absorbed in agriculture or manufacturing sector. Therefore, the resultant social pressure and strife cannot be overlooked.

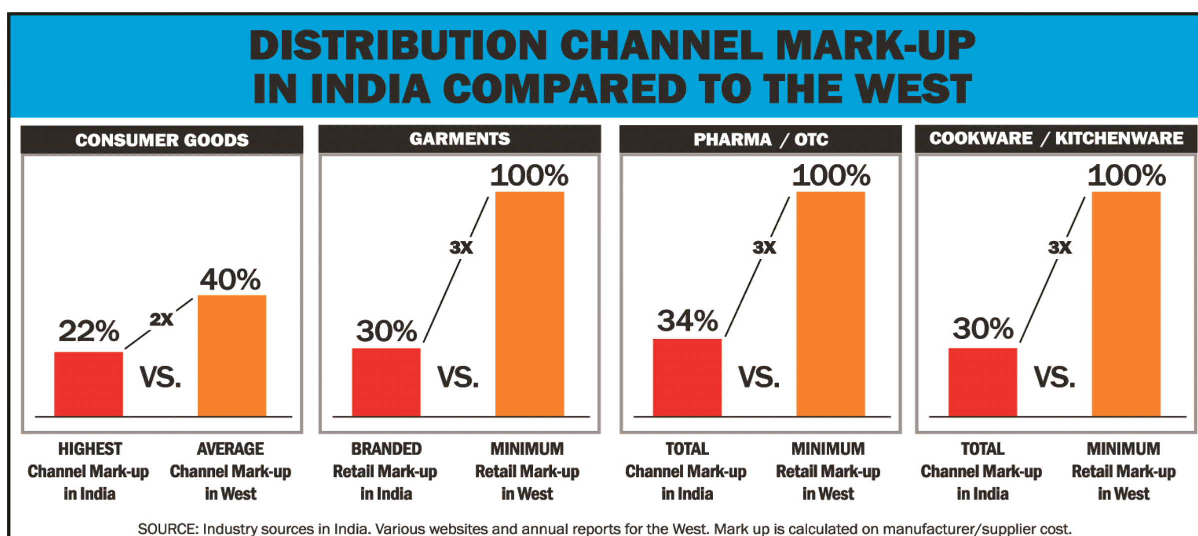
The US provides one of the most poignant examples of reduction in number of stores and employment. The unfettered growth of big retail in the US has put small retailers out of business. Between 1951 and 2011, the population of the US doubled from 155 million (mn) to 312 mn. Yet the number of stores actually declined from 1.77 mn in 1951 to 1.5 mn in 2011. The number of independent stores (with less than ten employees) also declined from 1.6 mn to 1.1 mn during the same period. Imagine if such a process takes place in India, it would pose a serious unemployment problem.

The argument that the entry of big foreign retailers will result in major employment opportunities is misleading. Undeniably, multinational retailers will employ some people to manage stores but, at the same time, they will be knocking off employment in large numbers in the overall economy. It is the net numbers that should be the concern of the policy makers.

If allowed unfettered access to the Indian market, big foreign retailers are likely to source manufactured products from outside (particularly China, Taiwan and other East Asian countries where manufactured goods are much cheaper than India). This would also have negative ramifications on Indian manufacturing. In such a scenario, how can India increase the share of manufacturing from the current 16 percent to 25 percent of GDP by 2025, as outlined under the proposed National Manufacturing Policy (NMP)?

Concerns over Food Security

Another concern relates to the entry of big foreign retailers on nation's food supply chain. Food security is not merely about food but has strong linkages with economic security, national security and sovereignty. The situation should remind us of the times when the British exercised control over the supply of salt to the Indian consumer for more than 180 years. In the recent past, the US has stopped oil companies and port facilities from passing into foreign hands on grounds of national



security. In France, there was a proposal in 2006 by Pepsico to acquire Danone but the French government declared Yogurt as a strategic industry and blocked the bid by Pepsico. The simple policy lesson is that one should not risk overseas entities gaining any sort of control or even influence over the nation's food supply chain. Therefore, the Indian policy makers should assess the implications of opening up food supply chain to overseas corporate bodies and structures.

Taming Inflation

There is no empirical evidence to prove that the entry of big multinational retailers will help control inflation. The claim that they reduce consumer prices may be only applicable on "On Sale" merchandise, which is a part of well-known "loss leader[1]" pricing strategy.

What is important is to look at retail mark-ups (the extent to which selling price is increased vis-à-vis sourcing price). The mark-ups across four categories of products are shown in Graphic (page 5). The retail mark-ups in the West range from 2x more than India to 3x more, and for some categories of goods is as high as 9x. By rapid expansion and market concentration over time, the retailers can easily increase their mark-ups and margin. Thus, it is in the interests of consumers to have a fragmented retail environment where no one retailer can command excessive mark-ups due to abuse of market power.

There is no denying that there are several shortcomings in the Indian retail sector which could be addressed through a slew of policy initiatives by central and state governments.

The arguments supportive of the entry of foreign investment in multi-brand retail in India are highly overstated and backed by little evidence. On the contrary, real world experiences and empirical studies show that the benefits of FDI in retail sector are much fewer in comparison with the economic and social costs. In these circumstances, the opening up of multi-brand retail sector to big foreign players may prove counterproductive and catastrophic.

— Shekar Swamy

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[1] A loss leader is a product sold at a low price (generally below cost) in order to attract new consumers into a shop or online store. The loss leaders are usually popular goods or services. The loss leader pricing strategy is often used by big retailers throughout the world to build a large customer base and secure future recurring revenue.

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