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A Comparative Study of FDI in Retail in India vis-à-vis Malaysia

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Abstract: *The role of foreign investment in driving economic growth and development in an economy has been a major one ever since the development of United Nations in the 1960s and trade reforms that emerged around the same time period. The purpose of this research paper is to do a comparative analysis of FDI in retail in India with respect to the FDI in retail in another developing economy, primarily in the regions of South-East Asia so as to be able to estimate the possible future impacts of the same in India. For this purpose we have considered Malaysia due to the similarities in the economic conditions pertaining in both countries during the introduction of FDI in the respective countries. The paper is the result of secondary research from various sources. This paper includes the comparative analysis of FDI and FDI policies in retail of both countries and impact of it on the economic development of both countries.*

1. INTRODUCTION

Kotlerstates, "Retailing includes all the activities involved in selling goods or services directly to the final consumers for personal, non-business use". Almost all major Indian private corporate groups for example the Tatas, Reliance as well as the Birlas have by now entered the retail sector.Retailing has been an important service industry in India that has been subjected to accelerated growth over the past decade, primarily due to the increase in urbanisation, higher availability of disposable income with the population as well as the overall growth of the economy. In fact, it has been identified as a sunrise industry with enormous future growth potential. According to the article published by Batra Hemant, titled "FDI in the Retailing Sector- Pros and Cons", the retail sector in India consists of the unorganised as well as organised form of retailing. The traditional forms of retailing consist of the local kirana shops, owner operated general stores, convenience stores, handcart and pavement vendors, weekly haats, and bazaars. In contrast, the organised retail sector includes licenced retailers who are registered for sales tax, income tax etc. The privately owned large retail businesses and the corporate-backed retail chains and hypermarkets constitute the organised retail industry in India. Unorganised retailing accounts for more than 90% of all retail trade in India. The evolution of India's retail sector has seen the ushering in of modern formats of retailing, all other formats that can be seen in the earlier stages of this process coexist. In fact, the potential changes in the relative balance of power among these various formats and their direct beneficiaries in the advent of large foreign retailers are at the core of global ongoing debates among the developing countries.

Table 1: Size of the Retail Industry in Terms Value and Employment In India;

	2001	2012
GDP (billions of USD)	450	1958
Estimated merchandise consumption (retail sales in billions of USD)	120	490
• Unorganised retail sector	95.8%	92.9%
• Organised retail sector	4.2%	7.1%
No. of direct employees in the organised retail sector (millions)	18	22
No. of employees in the organised retail sector (millions)	0.1	0.7

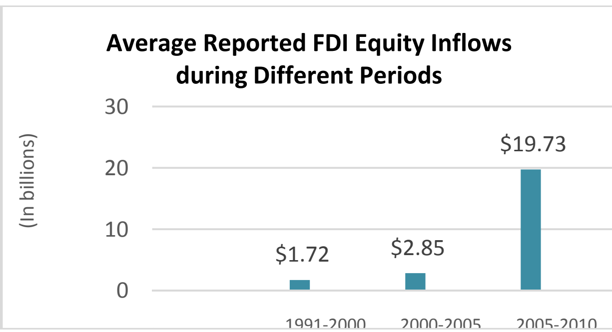
Source: Adapted from Technopak Analysis

2. FDI IN RETAIL SECTOR IN INDIA

Until 2008, India's policies regarding FDI were rigid and limited. FDI in Multi Brand Retail Trading (MBRT) was entirely prohibited. Single Brand Retail Trading (SBRT) was allowed 51% FDI through the Government subject to numerous conditions for example, products to be sold should be of a "single brand" only, products to be sold under the same brand internationally, the foreign investor should be the owner of the brand and "Single Brand" product-retailing would cover only products which are branded during manufacturing processes.

India is a developing nation with the development being largely dependent on its infrastructure. Even today there exists a lack of investment in the logistics infrastructure for retail chain thereby creating inefficiencies in supply chain operations of retailing. The integrated cold chain infrastructure in India, which is the second largest producer of fruits and vegetables (almost 200 million MT) is very limited having a total capacity of 23.6 million MT only. There are several indirect channels, such as franchise agreements, cash and carry wholesale agreements, strategic licensing agreements, manufacturing and wholly owned subsidiaries, through which foreign companies including large retailers have already had access to the Indian market. For example, German retailer Metro AG entered India through cash and carry wholesale trading channel. Wal- Mart has entered India as a joint venture with Indian firm Bharati Enterprises. For now however, the foreign retailers will be allowed only in cities with population of more than one million.

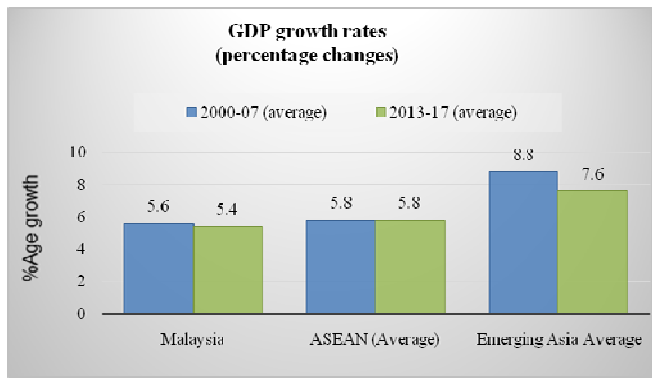
Opening up of door policies adopted by the Government of India through its new economic policies has attracted more investments in to the country that also brings with it funds for the development of infrastructure, in India. Indian Industries have thus gone global and in the same direction the inflow of FDI in to the country has increased at a faster rate.



The funds procured through FDI can be utilised for numerous purposes, the primary being the development of infrastructure. At present India lacks basic infrastructure in terms of roads, warehouses, production of electricity, multi brand international products, etc. Sectors where FDI is expected to have a positive impact are employment, remunerative prices for farmers, food inflation and supply chain operations. BBC News had reported that UK supermarket giant Tesco had plans to invest an initial £60m ($115m) in the form of FDI, to open a wholesale cash-and-carry business in Mumbai, India. Tesco had also signed a deal to help the retail performance of India's Tata group, Trent and develop its hypermarket business (although for a fee). The Chief executive of Tesco, Sir Terry Leahy had said that this move would give the group "access to one of the most important economies in the world". "Our wholesale cash-and-carry format will bring improved value, range and service to thousands of Indian businesses," he said. There are, however, certain legal limits for Tesco’s FDI plans in India. Large overseas retailers are currently barred by law at the retail level in India, and are limited to either wholesale, licence or franchise arrangements only. As per the deal with Tata retail arm Trent, the Indian firm hopes to increase the number of Star Bazaar hypermarkets it runs from four to more than 50 in the next five years. Tesco's new wholesale operation is also expected to supply the Star Bazaar stores. Tesco currently operates 3,729 stores employing more than 440,000 people in 13 countries across the globe, including Hungary, Slovakia, Malaysia and Thailand.Similar moves were also initiated previously by US-based rival Wal-Mart alongside India's Bharti Enterprises.

3. MALAYSIAN ECONOMY

For the purpose of comparative analysis of the impact of FDI in retail in India we will compare the same with the FDI in retail in Malaysia. Malaysia like India is a developing economy having high potential for growth and development. The Malaysian economy has demonstrated strong resilience in the face of external uncertainties. It had been expected to remain strong despite the slowdown of global economy during 2005. Economic growth in Malaysia continues to be consistent with all sectors registering high output. It is driven by service and manufacturing sector and by global economic growth prospects. India also is an economy driven by service and manufacturing sectors.



Source: OECD Development Centre, MPF-2013

4. FDI IN MALAYSIA

In spite of the global uncertainties and greater competition for foreign direct investment (FDI) in the emerging economies, FDI inflows into Malaysia have stabilised over the years. This is primarily due to the improving investor confidence amid strong global growth and a lively domestic business environment. According to a survey by A.T.Kearney’s FDI Confidence Index for 2004, Malaysia had demonstrated the strongest improvement in investor confidence among all the countries, rising for 23rd in 2003 to 15th in 2004.

In the wholesale and retail trade, hotels and sub-sectors of the Malaysian economy, foreign investments have been largely aimed for the set up and expansion of hypermarkets and new hotels in lieu of the growing affluence of tourism **industry** in Malaysia. Also, Malaysia has taken up numerous liberalisation initiatives to encourage FDI in Malaysia’s Exchange Control Act. It is believed that liberalisation measures will not only foster FDI by Malaysia but would also allow foreign investors to expand their businesses in Malaysia.

Year	Number of FDI Projects	Capital Investment (US$)
2007	35	$632.81 bn
2006	123	$1.44 bn
2005	94	$1.46 bn
2004	125	$1.72 bn
2003	186	$3.82 bn

5. POLICIES FOR FDI IN RETAIL IN MALAYSIA

The wholesale and retail sector falls under the supervision of the Ministry of Domestic Trade and Consumer Affairs through the committee on Wholesale and Retail Trade. It regulates and supervises the retail industry, including the foreign participants. Foreign companies who want to set up retail operations in Malaysia have to take prior approval from the Committee. Malaysian government has continuously focussed to attracting FDI in retail and has opted for a positive business environment policy for the same, it has amended the Foreign Investment. It has also introduced further liberalisation in Malaysia's Exchange Control Act as an initiative to boost FDI inflows. Some of the policy measures proposed and undertaken for FDI in retail in Malaysia are as follows:-

- Minimum capital requirements has increased from MYR10 million to MYR50 million.
- New hypermarkets cannot be built within a 3.5 km radius of a housing area or a city centre.
- Hypermarkets application will only be considered for locations with a population of 350,000 or higher.
- Floor space should not be less than 8000sq m and a counter must be set up every 1,000sq m.
- Five year freeze on the developments and construction any new hypermarkets in Petaling Jaya, Kuala Lumpur, Shah Alam, Johor Bahru and Penang.
- Restrict foreign involvement in certain retail formats i.e., mini-market,supermarket, provision shop/general vendor, 24-hour convenience store, medical hall, petrol kiosk, permanent wet market and permanent pavement store.
- A socio –economic impact study has to be conducted before the opening of hypermarkets, department stores, speciality stores and superstores.

6. FDI POLICIESFOR RETAIL IN INDIA

- FDI in Multi Brand Retail Trade (MBRT) may be permitted up to 51%, with Government approval;
- Fresh agricultural produce, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products, may be unbranded.
- Minimum amount to be brought in, as FDI, by the foreign investor, would be US $ 100 million.
- At least 50% of total FDI brought in shall be invested in 'backend infrastructure', where 'back-end infrastructure' will include capital expenditure on all activities, excluding that on front-end units.
- At least 30% of the procurement of manufactured/ processed products shall be sourced from 'small industries' which have a total investment in plant & machinery not exceeding US $ 1.00 million.
- Self-certification by the company, to ensure compliance of the conditions as above.
- Retail sales locations may be set up only in cities with a population of more than 10 lakh as per 2011 Census only 53 cities qualify for FDI in multi-brand retail out of nearly 8000 townsand cities and may also cover an area of 10 kmsaround the municipal/urban agglomeration limits of such cities.
- The FDI in multi-brand retail is being opened in 53 cities only with population of 1 million and for the rest of the country, current policy regime will apply.
- Government will have the first right to procurement of agricultural products;
- FDI in single brand retail trading may be permitted up to 100% with Government approval;
- Products should be sold under the same brand internationally i.e. products should be sold under the same brand in one or more countries other than India.
- 'Single Brand' product-retailing would cover only products which are branded during manufacturing.
- The foreign investor should be the owner of the brand.
- In respect of proposals involving FDI beyond 51%, 30% sourcing would mandatorily have to be done from SMEs/ village and cottage industries artisans and craftsmen.

7. EXPECTED IMPACT OF FDI IN INDIA

FDI in retail in Malaysia showcased a massive improvement in its economic conditions. The amount generated was invested in the development of infrastructure and improving the standard of living of the people in Malaysia. The policies set by the MalaysianGovernment ensured that the MNCs that intend on making FDI in retail in Malaysia got ample time to provide details of their operational plans, whether or not it would hamper or benefit the local surroundings and the existing local mom and pop retailers, etc. Two year notice period also gave the Malaysian Government time to evaluate the company and its impacts fully so as to be able to take accurate action for Malaysia's overall economic development. Introducing FDI in the retail sector in India can have either positive or negative impacts depending upon thetype of policy framework and the implementation of FDI rules and regulations by the Indian Government. This, however, requires the Government of India to primarily analyse the areas that require immediate improvement, the problems that may arise due to FDI in the country and alternate solutions for the same. According to the United Nations Conference on Trade and Development (UNCTAD), there are several avenues which FDI affectsfor the development of a country. Some of these are employment and incomes, capital formation, market access, structure of markets, technology and skills, fiscal revenues, and political cultural and social issues.

8. POSITIVE IMPACTS OF FDI IN RETAIL IN INDIA

- Currently there is a complex chain for procurement of goods due to several middlemen. FDI in retail will create an environment where direct procurement from the farmers would be made for horticulture products so as to enable them with secure remunerative prices, which would in turn reduce the cost of goods at the retail outlets.
- FDI in retail in India would bring together the best management practices from all over the world. It would bring with itself the skills and knowledge in the ways of conductthat would help Indian employees to learn and implement in other industries as well.
- Having exposure to the ways of conduct, products being supplied by FDI retailers, etc. would inform the domestic retailers of what and how the global retail scenario is like and the upcoming trends in the industry.
- Another major advantage of FDI in retail is that it would bring the trade balance to a near balanced scenario. FDI would also increase the liquidity of capital in an economy by the way of accumulation of foreign exchange reserves within the economy.
- Since the status of the human resources in a country is also instrumental in attracting FDI from overseas developed countries, India would take an active interest in increasing the quality of their workers and having every citizen to receive at least nine years of education.
- Several developing countries like China, Indonesia, Thailand, Malaysia, Russia, and Chile have a booming small-scale retail sector, and they had opened FDI to 100 percent several years earlier. Then Indian Commerce and Industry Minister Anand Sharma had told reporters in an interview in 2011 that if one visits Beijing, Kuala Lumpur or Jakarta, one can find that markets are full of small retail players as well as large scale foreign players without compromise in the employment levels.
- If a particular country has plenty of natural resources it always finds investors willing to put their money in them. Since India is rich in minerals and natural resources, attracting FDI and having efficient utilisation of the same is evident.

Infrastructure is very important for FDI. So if a country keens to have overseas investors they have to focus on developing their infrastructure. This way a country indirectly ends up pioneering towards growth and development itself.

9. EGATIVE IMPACTS OF FDI IN RETAIL IN INDIA

- Replacement of established national brands by the brands of the retail gains. For example, Wal-Mart is committed to buying the best goods at the cheapest prices so as to give its customers the best value for money. That is the reason as to why it sources so heavily from China. 70% of merchandise in Wal-Mart contains components made in China.
- Acceptance towards foreign brands can create a direct threat on Indian established brands providing best quality products with reasonable prices that may lead to disruptions in price of domestic commodities.
- While the levels of FDI tend to be resilient during periods of economic uncertainty, it has the potential of adversely affecting the net capital flow of a developing economy especially if the country does not have a healthy and sustainable FDI schedule.
- A large part of Indian retailers unorganised and employs unskilled labour. However the foreign retailers would be employing skilled labour only. This may cause an increase in the unemployment of the unskilled labour at large.

10. INWARD FOREIGN DIRECT INVESTMENT AND ECONOMIC DEVELOPMENT

Impact Area	Potential dynamic benefits of FDI	Potential dynamic costs of FDI	Indicators
Employment and Income	Provides employment and incomes directly.	May indirectly crowd-out other employment by replacing existing employment or pushing up factor prices; may lead to increased wage inequality.	Long-run employment generation inside firm and in suppliers and buyers. Long-run wage development in foreign firms and spillover effects on wage levels in other firms inside or outside sector
Physical capital	Stable source of external finance, improving the balance of payments, and potentially raising fixed capital formation.	May pre-empt investment and opportunities of domestic firms.	Long-run relationship between FDI and Domestic capital formation
Technology, skills and management techniques	Provides up to date techniques, skilled personnel and advanced management techniques, raising the return to skills offering additional incentives for education. Positive spillover effects on domestic firms through backward and forward linkages, demonstration effects and human resource development.	Spillovers are not automatic or free. Reliance on foreign technology and skills may inhibit development of local capabilities. Increased linkages raise dependency of domestic firms on TNCs.	Intra and Extra-Sectoralspillover effects on productivity in other firms. Share of inputs sourced locally Supplier development. Upgrading and long-run development of technology, training and skill levels in foreign firms

Fiscal revenues	TNCs can raise fiscal revenues for the domestic government through the payment of taxes in case of new economic activities with more value added.	If TNCs crowd-out domestic firms, fiscal revenues may actually be lower through the use of special tax concessions, eventually leading to an erosion of the tax base. Special tax concessions are an implicit subsidy and in case of lack of transparency can lead to rent-seeking behaviour.	Long-run fiscal payments through foreign firms and through a change in economic activity more generally.
Poverty	If the effects in this column are important, this provides an enabling environment thereby directly and indirectly alleviating poverty.	If the effects in this column are important, this provides a disabling environment thereby directly and indirectly worsening poverty.	Combination of the above indicators. Long-run effect of social investment. Lon-run effect of core health, environmental and infrastructure programmes.

Source: TeVelde (2004) building on table in UNCTAD (1999)

11. CONCLUSION

The intense competition posed by foreign retailers has provided additional motivation for local retailers to leverage on retail technology so as to better understand consumer purchasing behaviour, optimise operational procedures in terms of cost minimisation and output maximisation and to enhance the overall efficiency of retailing in developing countries. The rapid expansion of foreign owned retailers such as Giant, Tesco, Ikea and Carrefour was initially expected to dominate the retail landscape in Malaysia by 2010. However, it has been seen that even with the existence of such multinational retailers the local retailers still continue to flourish in the economy of Malaysia. As a part of the effort to promote goods made by local retailers, the government has imposed a quota on goods displayed on foreign retail shop shelves to ensure that reasonable shelf space is given to Malaysian manufacturers and retailers. Employment has risen steadily over time due to such foreign retailers. Also the investment brought into Malaysia through retail sector has contributed largely to the development of its infrastructure.

In India, the retail sector has played a phenomenal role throughout the world in increasing productivity of the consumer goods and services. It is currently one of the largest industries in in various countries in terms of employment and establishments. India is one of the most dynamic and fast paced economies that is considered a hub for FDI opportunities. Today, FDI which used to be viewed as unhelpful, negative and bringing inappropriate technology to developing countries, has a radically different view. FDI is now seen as beneficial and nearly all countries try to provide a welcoming climate for investment. Countries increasingly recognise that they can affect the attraction of FDI using both general economic policies and appropriate specific FDI policies. The impact of FDI on economic growth however depends on the type of FDI, firm characteristics, economic conditions and policies. The type and sequencing of general and specific policiesin areas covering investment, trade, innovation and human resources are now seen as crucial in affecting the link between FDI and development. Appropriate policies to benefit from FDI include building up local human resource and technological capabilities to raise the absorptive capacity. Besides this, the rising income and convergence of consumer's tastes and preferences, greater knowledge and demand for foreign brands and emergence of retail credit facility will act as locomotives for the growth in demand for FDI in retail. This would not only lead to the development of infrastructure in India, but would also help in improving employment, purchasing power, credit facilities, etc. It would help debt ridden domestic companies such as Pantaloons, Provogue, etc. Hence, we conclude that FDI in retail in India has both pros as well as cons and the success of the same, thus depends on the policy structure developed by the government of India. The new policy given by the government of India would provide a significant boost to the $28 Bn Indian retail market which is expected to reach $260 Bn by 2020.

With sluggish growth in the developed markets across the globe and Indian retailers being bogged down by high debt and high cost of expansion, the new policy presents a win-win situation for both foreign and Indian retailers. The stock markets also reflected the positive outlook for the sector, by pushing up some retail stocks by up to 30% within 2 days of the announcement of such policy in 2011. The policies implemented would positively impact a wide section of the Indian population. Consumers are expected to save 5-10% on their regular household expenditure and get a wider choice of products. Farmers will get 10-30% higher remuneration for their produce as back end infrastructure investment will eliminate the middlemen. The infusion of capital and setting up of new stores will also provide a boost to real estate as well as create 3-4 million new jobs in retail and a further 4-6 million jobs in logistics, contract labour, security, etc. It would thus lead to an overall increase in the efficiency of Indian economy.

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