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10th August, 2010

Honorable Shri Anand Sharma

Commerce & Industry Minister

Government of India,

Room No. 45,

Udyog Bhawan,

New Delhi – 110011,

India

Subject: Response to DIPP Discussion Paper – "FDI in Multi Brand Retail Trading"

Honorable Sir,

The department of Industrial Policy and Promotion (DIPP) released the discussion paper on "FDI in Multi-Brand Retail Trading". DIPP has circulated the paper and has requested for views and suggestions specifically on section7.

We would like to congratulate DIPP for this initiation and a very comprehensive paper outlining various studies and facts from around the world.

We not only affirmatively agree that there is a evaluating opening FDI in retail sector but the government will have to facilitate the flow to village & district level as this will fuel to the socio-economic upliftment of the citizens at the lowest strata of our society.

An affirmative step in this direction has to be taken considering the positive outcomes of allowing FDI to participate in various stages / areas of multi-brand retail trading both front end and backend.

We are happy to participate with your views and have structured our response along the lines of questions.

ISSUES FOR RESOLUTION

7.0 Should FDI in multi brand retail be permitted? If so, should a cap on investment be imposed? If so, what should this cap be?

Yes, FDI should be permitted in multi-branded retail.

- Large international players have advanced knowledge of management, particularly in inventory management and merchandising. This diffusion of knowledge to the domestic players is likely to enhance their productivity and efficiency through utilization of new technologies. Domestic players will learn through experience.
- Foreign players would ease the capital constraints faced by most of the domestic players and there is a possibility of reduction in overall cost of capital.
- International players will adopt an integrated supply chain management system. This is going to improve the efficiency of the current environment and definitely will bring down product prices. The prevailing distortions in the present supply chain system, particularly in food articles (vegetables and grains), need to be addressed immediately. An efficient system would eradicate the leakages and hoarding practices.
- FDI will bring in expansion of stores and operations which would ultimately lead to employment generation in front end stores, the supply chain management system and the related back end sectors.
- FDI will be a boost to Indian Shopping Centres Industry which is at present burdened with high debt and operational cost. One average size mall creates 1000 direct jobs and upwards of 5000 indirect jobs. Hence, investments in shopping centres are vital for the economy and cannot be ignored.
- FDI will ensure greater transparency with more disclosure of data which will help new entrants to take viable investment decisions besides enabling Government to design and implement policies based on information and knowledge.

In order to generate sufficient and tangible interest from quality international players it may be necessary to ensure that there should be no cap of investment.

7.1 To develop the retail trade in food grains, other essential commodities and multi-brand retail in general; should FDI be leveraged for creating back-end infrastructure? To ensure that foreign investment makes a genuine contribution to the development of infrastructure and logistics, should it be stipulated that a percentage of the FDI coming in (say 50%) should be spent towards building up of back end infrastructure, logistics or agro processing?.

It is not necessary to enforce FDI in retail to have a restrictive clause for investing in the backend infrastructure creation as it will be imperative for any sizeable and noteworthy player to be doing so on their own accord without which it will be difficult for the player to timely merchandise the stores on daily basis in case of perishables and weekly or fortnightly basis in case of non-perishables.

Further, modern and traditional retailer very often works in the form of 'hub and spoke model' i.e. , one distribution and warehousing facility to support a particular region having 10-20 front end outlets. In continuance, the Government may have to provide subsidies and loans at viable interest rate to support the equity capital in setting up these backend facilities.

It will also help to bring down the prices of perishable goods like milk & milk products, fruits and vegetables over medium to long term.

While one can expect the modern retailers will encourage outsourcing a major part of their back end, they will be in the process to augment the local intellectual knowledge/systems/processes and elevate the local environment to suit their need raising the bar of the entire eco system.

Reducing commission of trade intermediaries will improve realisations to farmers and increase operating margins of large retailers. Further, the quality of goods will not deteriorate with reduction in intermediaries as the more hands the goods change, quality of product available to consumers deteriorate.

7.2 It is necessary to encourage only genuine players in this sector and avoid a situation where retail outlets are run through working capital support from financial institutions. Should a minimum threshold limit for investment in backend infrastructure logistics be fixed? If so, what should this financial threshold be?

If the intent is to encourage genuine players, a minimum threshold limit is not imperative.

Besides, in our view if capital or institutional financial support would have been available with the local or international source then the "blood bath" that the retailers have seen in the last 3 years would have been subdued and many smaller traditional and modern retailers would have survived in this situation.

In this given global business environment, the investible surpluses with retailers are few and far between. Only those retailers which have survived this economic juggernaut will either have their own proprietary capital or will be able to attract investors to set up operations in newer markets. An investor generally faces substantial risk, like country , political, economic, sovereign, currency, etc. Hence, the volatility increases significantly leading to high opportunity cost and low risk appetite from the investor's perspective

In these circumstances, any form of restriction will only result into less inflow of funds.

As already mentioned in point 7.2, to have a sustainable business model a retailer with large investment will have to invest in back end logistics to bring down the opportunity cost of capital.

7.3 To develop our rural sector, should conditionalities be put on the FDI funded chains relating to employment? For example, should we stipulate that at least 50% of the jobs in the retail outlets should be reserved for the rural youth?

FDI funded retailers in rural sector will have no choice but to source manpower locally, especially at lower level to be cost competitive. As there will be very few urban citizens will be keen to relocate to rural environments.

7.4 Similarly, to develop our SME sector through local sourcing, should we stipulate that a minimum percentage of manufactured products be sourced from the SME sector in India?

The biggest beneficiary of FDI in retail is SME sector because they are the one to produce the majority of the SKUs (Stock Keeping Units) which typically are merchandised through modern retail formats

A case in point is being, various exporters from different parts of the world who run small & medium enterprises are supplying to the largest modern retailers. Very similar to auto ancillary, the small & medium enterprise sector supplying to modern retail will become even more vibrant demonstrating the multiplier effect. Thus it is not necessary to put any restrictions on sourcing.

The Indian SME exporters will find markets locally to be delivering value to these modern local retail formats and will become larger organizations supplying to traditional and modern retailers. SMEs will also enhance their design skills to meet specific standards of their delivery.

Very often, vendors cluster around the 'hubs' to build optimization and efficiency.

Invariably, retailers will continue sourcing from SME sector even after the marginalized ports for transport of FMCG products, brown & white goods improve.

7.5 How best can small retailers be integrated into the upgraded value chain? Can they be provided access to the logistics/ supply chain set up by the FDI funded retailers? Should it be stipulated that a minimum percentage of the latter's sales should be made to retailers through special wholesale windows?

It would not be advisable to set these limitations. Local retailers are currently able to shop from Cash-and-carry players.

We do not feel there should be stipulation of access to logistics/supply chain set up by FDI funded retailers, however many of these operators outsource these function to third party operators and Indian retailers can leverage on these operators.

7.6 As a part of a calibrated reform process, should foreign investment for such stores be initially allowed only in cities with population of more than 10 lakhs (2001 census)? As there may be difficulties faced with regard to availability of real-estate in such cities for setting up such ventures, should an *area of 10 kms around the municipal/urban agglomeration limits of such cities be included within the definition of the city?*

If we want to build rural retail infrastructure and to generate rural employment opportunities, then this is a counterproductive question.

FDI in smaller cities will be more helpful where diffusion of knowledge to the domestic players is likely to enhance their productivity and efficiency through utilization of new technologies.

Besides, within a particular city there should be no restriction on where they can set up their stores.

7.7 Will any of the conditionalities mentioned above be inconsistent with our commitments under the agreement on TRIM at WTO? If not, to ensure national treatment, can such conditionalities be extended to all retail chains in India above a certain size? Will such extended conditionalities be consistent with Article 301 of the Constitution?

It would be glad to understand whether retail – as a service – comes under the aegis of TRIM.

7.8 What additional steps should be taken to protect small retailers? Should an exclusive legal and regulatory framework be established to protect their interests? Is a Shopping Mall Regulation Act required? Does this require intervention at national level or should this be left to the States?

Indian retailers themselves have to take a large number of licences from various government bodies to establish shop. The same can work efficiently for the FDI based retailers as well.

It may help to facilitate and reduce the number of clearances or have guidelines and reduce ambiguity in many of the clearances.

It may also help to have a single window system for clearances.

The current laws and regulations are all left to the states. We have to understand how a national intervention will reduce the regulations and streamline it.

As far as "Shopping Mall Regulation Act" is concerned, shopping centres are not retailers, and are only retail infrastructure providers. We actually need less and not more regulation for shopping centres. To enable a more conducive retail infrastructure growth in this country we would urge your ministry in supporting us to for representation to the finance ministry to reduce the threshold of 50,000 square metre FDI in real estate development to a more meaningful 20,000 square metre which will enable better infrastructure development and availability for the modernization of retail in India.

7.9 The present public distribution system provides a valuable safety net to vulnerable sections of society. To ensure that the integrity of the PDS system is not weakened and buffer stock is maintained at the desired level, should Government reserve the right of first procurement for a part of the season or put in place a mechanism to collect a certain amount of levy from private traders in case the level of buffer stock falls below a certain level?

The right to source for PDS is the Governments right and duty. Collecting a levy or fine from private/organized retailer will not be appropriate.

7.10 How should compliance be ensured with the above stipulations? Should a centralised agency, to be nominated by the State Governments concerned, be empowered to grant permissions to every outlet to be opened? The onus of proving compliance with these conditions could rest with the concerned retail chain. The chains could submit an annual statement to such State Government agency providing proof of compliance. Should this agency be empowered to monitor compliance of the present cash and carry outlets too?

We believe that the Government at various levels has enough and more regulations, the execution of which appears to be difficult to handle.

In our humble view it is far more productive to have few regulations and compliances and to pursue them diligently than to have too much compliance which remain unchecked. If given the opportunity we would be happy to communicate more on this issue with your good self moving towards a more self governing and a self compliant and responsible approach.

7.11 The penalty for non compliance could include cancellation of approvals as well as denial of future permissions for such activities. What additional penalties could be levied? Should civil penalties be imposed? Or criminal? Or both?

The Indian legal system is robust to take care of non-compliance issues.

Any non-compliance should be subject to only civil penalties.

Cancellation of approval and denial of future permission is the right of the government and should be retained while this will act as a big deterrent. There should be pre-stipulated remedial measures which can be monitored.

However, DIPP should consider the modalities laid out / rules form time to time to mark to market basis prevalent conditions in the future.

<u>Apart from above issues, following are the obvious reasons – "Why India needs FDI in multi-brand retail"</u>

FDI can act as a catalyst to spur competition in the retail industry, due to the current scenario of low competition and poor productivity. It will bring about:

Supply Chain Improvement enabling large retailers to source perishable products directly from co-operatives, lowering annual wastage amounting to around Rs 63,000 crores. (Source: CRISIL)

i. Investment in Technology

ii. Manpower & Skill Development

iii. Tourism Development

iv. Greater Sourcing From India

v. Upgradation in Agricultural processes

vi. Efficient Small & Medium Scale Industries

vii. Higher economies of scale resulting to low cost goods

viii. Increase in exports of finished products thereby increase in foreign currency reserves

ix. Softening of urban, semi-urban and rural environments

x. Women Empowerment

xi. Better utilization available resources like Manpower, Land, Capital

xii. Use of bank finance efficiently with viable business plans

xiii. Availability of good quality products at right time, right place, to right consumer and at low cost

xiv. Growth in market size

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xv. Benefits to Government through greater GDP

xvi. Higher employment generation at all levels

xvii. It will aligned India's interest in global trade

xviii. Development of quality infrastructure from the perspective that the customer will not go to stores, malls or retail environments which are not connected with excellent physical infrastructure like road, sewerage, water, lighting & sanitation.

xix. FDI in multi-brand retail has the potential to bring down prices of perishable goods like fruits and vegetables over the long term.

Global players should be allowed to enter the multi-brand retail sector in India. FDI will act as a catalyst to this 'low competition' and 'poor productivity' sector.

Yours Sincerely,

sd/-

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COO, Shopping Centres Association of India (SCAI)

Cc. Shri Jyotiraditya Madhavrao Scindia

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