Presentation
on
Regulatory Mechanism on FDI Retail in India

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“The views expressed herein are that of the author of the presentation and may not represent the views of the organization to which he is affiliated.”

FOREIGN DIRECT INVESTMENT (FDI) IN INDIA

FDI Defined by OECD : Foreign direct investment reflects the objective of establishing a lasting interest by a resident enterprise in one economy (direct investor) in an enterprise (direct investment enterprise) that is resident in an economy other than that of the direct investor… The direct or indirect ownership of 10% or more of the voting power of an enterprise resident in one economy by an investor resident in another economy is evidence of such a relationship.

Foreign Direct Investment (FDI) is permitted as under the following forms of investments-

- Through financial collaborations.
- Through joint ventures and technical collaborations.
- Through capital markets via Euro issues.
- Through private placements or preferential allotments.

WHY FDI ?

- Gain a foothold in a new geographic market.
- Increase a firm's global competitiveness and positioning.
- Fill gaps in a company's product lines in a global industry.
- Reduce costs in areas such as R&D, production, and distribution.

FACTORS REQUIRED TO ATTRACT FDI

- Low cost BUT Qualified, Educated/Skilled Labor Pool.
- Long-term Market Potential OR Yields greater than can be achieved Domestically.
- Access to Natural Resources.
- Geography
- Stability of the economic and Political Environment

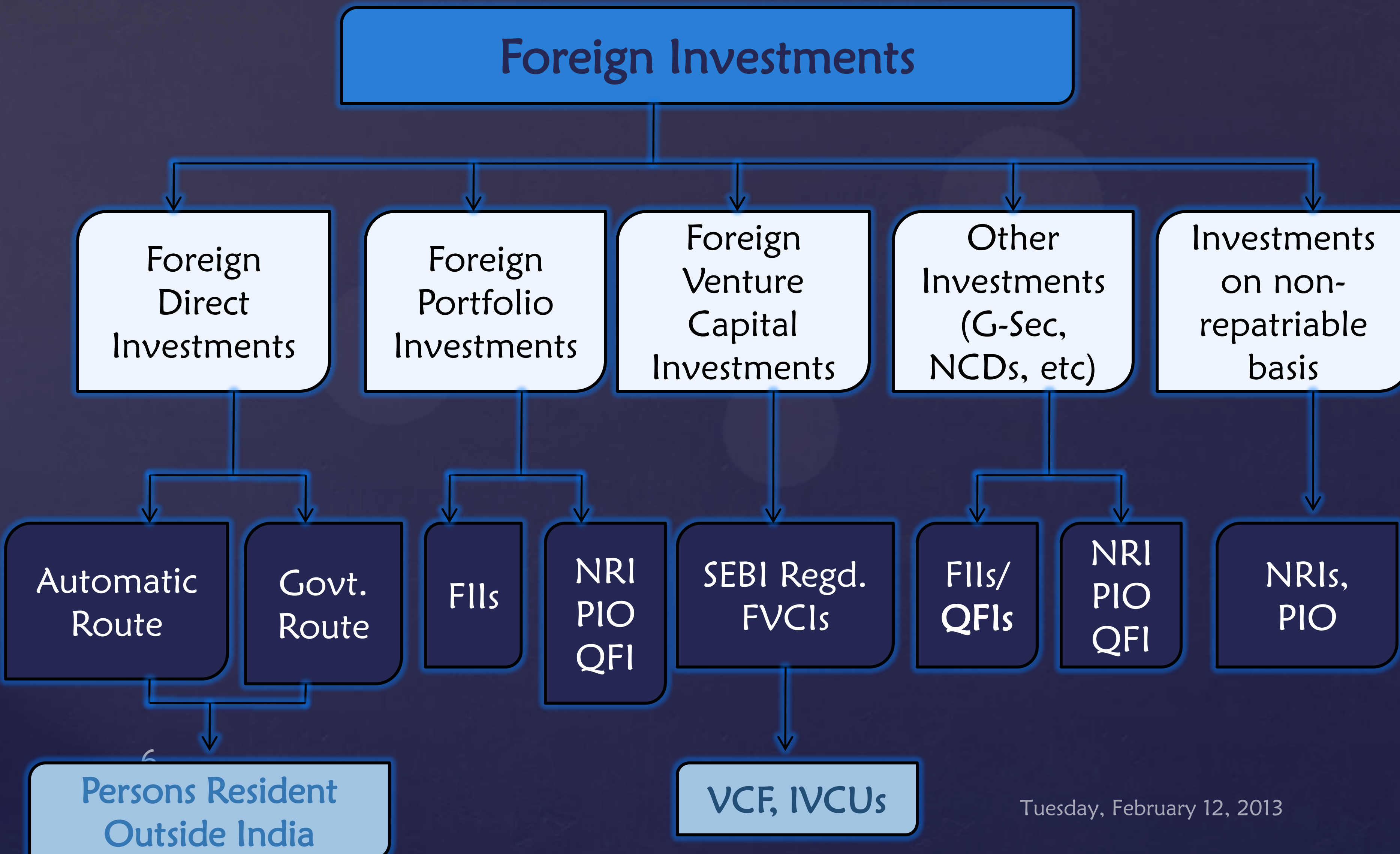
‘Foreign Investment '

Flows of capital from one nation to another in exchange for significant ownership stakes in domestic companies or other domestic assets.

Types of Foreign Investment

1. Foreign Direct Investments
2. Foreign Portfolio Investments
3. Foreign Venture Capital Investments
4. Other Investments (G Sec, NCD etc.)
5. Investments on Non repatriable basis

Foreign Investment in India- Schematic Representation



MAJOR BODIES CONSTITUTED FOR FDI

1991- Foreign Investment Promotion Board (FIPB)

1996- Foreign Investment Promotion Council (FIPC)

1999- Foreign Investment Implementation Authority (FIIA)

2004- Investment Commission

Secretariat for Industrial Assistance (SIA)

Investing in India – Entry Routes

Investing in India

Automatic Route

Inform RBI within 30 days of inflow/issue of shares

Pricing: FEMA Regulations

- Unlisted – CCI
- Listed – SEBI

Approval Route

Foreign Investment promotion Board

CCFI

F D I - APPROVAL

Foreign direct investments in India are approved through three routes:

- Automatic approval by RBI.
- The FIPB Route.
- CCFI Route

AUTOMATIC ROUTE

No need of Prior Approval From FIPB,RBI,GOI.

BUT

The investors are only required to notify the Regional Office concerned of the Reserve Bank of India within 30 days of receipt of inward remittance

AND

File the required documents along with form FC-GPR with that Office within 30 days of issue of shares to the non-resident investors.

The RBI accords automatic approval within a period of two weeks (provided certain parameters are met) to all proposals meeting the relevant requirements.

THE FIPB ROUTE

- FDI in activities not covered under the automatic route require prior government approval.

- Approvals of all such proposals including composite proposals involving foreign investment/foreign technical collaboration is granted on the recommendations of FIPB.

- Application for all FDI cases, except NRI investments and 100% EOUs, should be submitted to the FIPB Unit, DEA , Ministry of Finance.

- Application for NRI and 100% EOU cases should be presented to SIA in Department of Industrial Policy and Promotion (DIPP).

- Application can be made in Form FC-IL. Plain paper applications carrying all relevant details are also accepted.

- No fee is payable.

CCFI ROUTE

- Investment proposals falling outside the automatic route.

And

- Having a project cost of Rs. 6,000 million or more would require prior approval of Cabinet Committee of Foreign Investment ("CCFI").

- Decision of CCFI usually conveyed in 8-10 weeks. Thereafter, filings have to be made by the Indian company with the RBI.

FDI policy decisions of India since 1991:

1991- Liberalization, Indian Economy opened FDI upto 51% allowed under the automatic route in selected priority sectors.

1997- FDI upto 100% allowed under the automatic route in cash and carry (wholesale).

2006- FDI upto 51% allowed with prior government approval in Single Brand Retail.

2008- Government mulled over the idea of allowing 100% FDI in Single Brand Retail and 50% in Multi Brand Retail.

2010- Government proposing to allow FDI in Multi Brand Retailing

2012- Government vide press note 5 (2012 SERIES) allowed upto 51% to Multi Brand Retailing

There were changes at different instances made by Government of India. In this case there was RBI circulars and notification which talks about the changes being made. RBI's circular no. RBI 2012/-13/217 A.P. (DIR SERIES) No. 32, specifically, talks about the FDI in Multi Brand Retail (herein after MBRT). Initially it was passed by Department of Industry Policy and Promotion, Ministry of Commerce and industry under press note 5 allowing MBRT upto 51%.

Eligibility

Person Resident Outside India *(other than Entity of Pakistan)*	Citizen/ Entity of Bangladesh	NRIs/ Resident and Citizens of Nepal/ Bhutan	Overseas Corporate Bodies (OCBs)

SUBJECT TO

FDI Policy of Government of India	Approval of FIBP	Repatriation Basis subject to inward remittance in free foreign exchange	OCBs derecognized. Erstwhile OCBs – GOI Approval - Government Route. RBI Approval – Automatic Route

Types of Instruments

- Equity Shares, Fully and Mandatorily convertible Debentures/ Preference Shares
- Non Convertible/ Optionally, Partially Convertible Preference Shares
- Fully/ Mandatorily Convertible Debentures into Equity

Subjective Conditions

- Pricing Guidelines/ Valuation Norms/ FEMA
- ECB Guidelines
- FDI Policy

Investing in India

A foreign company to set up business operations in India has the following options:

1. Incorporation of company (governed by the Companies Act, 1956) as a Joint Venture or a Wholly Owned Subsidiary

2. Liaison office/ Representative office / Project office /Branch office of the foreign company which can undertake activities permitted under the Foreign Exchange Management (Establishment in India of Branch Office or Other Place of Business) Regulations, 2000.

FDI Policy …. Prohibited activities

FDI is prohibited in:

(a) Lottery Business, including Government /private lottery, online lotteries, etc.

(b) Gambling and Betting, including casinos etc.

(c) Chit funds

(d) Nidhi company

(e) Trading in Transferable Development Rights (TDRs)

(f) Real Estate Business or Construction of Farm Houses

(g) Manufacturing of Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes

(h) Activities / sectors not open to private sector investment e.g. Atomic Energy and Railway Transport (other than Mass Rapid Transport Systems).

Foreign technology collaboration in any form, including licensing for franchise, trademark, brand name, management contract, is also prohibited for Lottery Business and Gambling and Betting activities.

The core features of the government's foreign investment policies and incentives offered are as below:

- No government approval is required for FDI except for a small negative list.
- "Sector specific guidelines for FDI", covers investments upto specified sectoral caps under the automatic route, with a few exceptions.
- FIPB considers proposals for foreign participation that do not qualify for automatic approval.
- Use of foreign brand names/trademarks is permitted for the sale of goods in India Indian capital markets are open to FIIs.
- "Single window" clearance facilities and "investor escort services" are available in various states to simplify the approval process for new ventures.

FDI in Single Brand Retail

- **FDI up to 51% under Approval Route:**
- 'Single Brand'.
- Sold under the same brand internationally.
- Products which are branded during manufacturing.
- Foreign investor should be the owner of the brand.

- **Additional condition for FDI beyond 51% & up to 100% under Approval Route :**
- Mandatory sourcing of at least 30% of the value of products sold from Indian 'small industries/ village and cottage industries, artisans and craftsmen'.

- 'Compliance ensured through self-certification by the company, to be subsequently checked, by statutory auditors, from the duly certified accounts, which the company will be required to maintain.

FDI in Multi Brand Retail

FDI in multi-brand retail: Key to speed up retail transformation

In an important policy move, the Indian government gave permission for up to 51% FDI in multi-brand retail in September 2012 by Press Note 5 of 2012 issued by DIPP. The objective of this policy is to boost the retail business through adoption of international standards and practices. The entry of international products, practices and technology is expected to enhance the efficiency of domestic retailers. The government has made it mandatory for foreign multi-brand retailers to place at least 50% of their total investment in back-end infrastructure, thus giving a boost to facilities such as logistics and warehousing.

Certain Conditions for FDI in Multi Brand Trading:

- At least 50 per cent of total FDI will be invested in "back-end infrastructure," which will include investment on processing, manufacturing, distribution, design improvement, quality control, packaging, warehouses, storage, logistics and related infrastructure.
- At least 30 per cent procurement of manufactured or processed products shall be sourced from small industries that don't have plant and machinery more than $1 million worth.
- Multi-brand retail outlets can sell unbranded fresh agriculture produce, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products.

Certain Conditions for FDI in Multi Brand Trading:

- Retail sales locations will be set up in cities with a population of more than 10 lakh according to 2011 census and will cover an area of 10 km around the municipal limits of such cities.
- Government will have the first right to procurement of agricultural products.
- Mandatory for investors to source at least 30 per cent of manufactured or processed goods from "small industries“ which is also made mandatory for single-brand retail investors too as part of the move to increase FDI limit to 100 per cent. Compliance with this condition in both cases would be through self-certification of companies, then checked by "statutory auditors".

FDI (IN RETAIL) DEBATE

In Favour of FDI:

(1) Advanced management know how in merchandising and inventory management and new technologies.

(2) Lower down the prices.

(3) Assure the quality of product, better shopping experience and customer services.

(4) linkage of local suppliers, farmers and manufacturers, no doubt only those who can meet the quality and safety standards, to global market and this will ensure a reliable and profitable market to these local players.

(5) Regional players are developing their supply chain differentiating their strategies and improving their operations to counter the size of international players.

(6) Joint ventures would ease capital constraints of existing organized retailers.

(7) Development of different retail formats and modernization of the sector.

Contd…….

In Favour of FDI:

(8) Expansion of opposite sell formats as good as modernization of a sector.

(9) Boost to food products, textiles and garments, leather products, etc., to benefit from large-scale procurement by international chains; in turn, creating jobs opportunities at various levels.

(10) Promote India's manufacturing and export sectors, leading to a double bonus for the economy.

(12) Big push to the country's social agenda, too, and has the potential to even positively impact and promote tourism, computerisation, systemisation, government's ability to influence trade when required, address issues such as inflation, reduction of black economy, control over food hygiene, push to real estate etc.

Against FDI in Retail

(1) Indian retailers have yet to consolidate their position to survive with the competition from global players.
(2) After allowing FDI, the domestic retailers were marginalized and this led to unemployment.
(3) FDI in retailing can upset the import balance, as large international retailers may prefer to source majority of their products globally rather than investing in local products.
(4) Global retailers might resort to predatory pricing.
(5) Since lending rates are much higher in India, Indian retailers, especially small retailers, are at a disadvantageous position.
(6) It is said that FDI would provide employment opportunities. But, the fact is that they cannot provide employment opportunities to semi-illiterate people.
(7) If FDI is allowed in retailing then it would result in lowering of prices because FDI will result in good technology, supply chain, etc. If prices were lowered then it would lower the margin of unorganized players. As a result the unorganized market will be affected.
(8) FDI in retail trade would not attract large inflows of foreign investment since very little investment is required to conduct retail business.
(9) Loss of cultural and ethical values due to more influence of the other cultures.

POLICY SUGGESTIONS:

- If FDI in retail is liberalized by considering the following suggestions it is expected bring in more of benefits than threats to the country.
- FDI should be initially allowed in less sensitive sectors and also in the sectors wherein the domestic companies are established strongly.
- Then FDI in retail should be liberalized in a phased manner like the case with China.
- Entry of foreign players must be gradual with social safeguards so that the effects of labor dislocation can be minimized.
- If the manufacturing is strengthened, the displaced employees of the retail industry could be well accommodated there.

POLICY SUGGESTIONS:

- Adequate attention should be paid to procuring, staff recruitment, investments in warehouse, cold storage, infrastructure, competition and retail formats so that not only does the money comes in but also it's a winwin situation for the current national retailer as well as “mom and pop” stores who account for 70% of the retail business even after the arrival of national retailers from the corporate giants like the Tata, Reliance, Future Group and the Birla's.

- A National Commission should be set up to study the problems of the retail sector which should also evolve a clear set of conditionality on foreign retailers on procurement of farm produce, domestically manufactured merchandise and imported goods. This conditionality must state minimum space, size and other details like construction and storage standards

CONCLUSION

- The influence of FDI towards Retailing in India will witness a considerable growth. The share of corporate retail in overall retail sales is projected to jump from around 3% currently to around 9-10% in the next three years.

- A number of large domestic business groups have entered the retail trade sector.

- Several formats of corporate retailing like hypermarkets, supermarkets and discount stores are being set up by big business groups in Tier-2 and Tier-3 cities besides the on-going proliferation of shopping malls in the metros and other large cities. This will have serious implications for the livelihood of millions of small and unorganized retailers across the country.

- If the corporate retail starts spreading in India without any control and if the Government brings in Foreign Direct Investment in the sector, the potential social costs of the growth and consolidation of organized retail, in terms of displacement of unorganized retailers and loss of livelihoods will be enormous.

- Regulation needs to be more stringent and restrictive. Attracting FDI has become an integral part of the economic strategies for India.

- Over the years FDI inflow is increasing and India has tremendous potential for absorbing greater flow of FDI in coming years.

Thank You