The FDI Factor

The recent assurance by the Prime Minister that the government will push for FDI in retail after the state polls in February this year is a welcome sign but as we all know from experience that it may not mean much as this government hasn't shown much boldness in this specific case. Anyhow, I certainly believe that now this matter is at the centre stage and chances are that sooner than later we will have some changes in FDI that will be a step forward from the current situation. In this article, I wish to address specifically the fashion industry and talk about what some of the changes will mean to the future of fashion branding and retail segments in India.

Majority of the discussions regarding FDI are generally focused on multi-brand and F&G retailers and its potential implications on farmers, small retailers and intermediaries. Most of the objections too also concern the above. So far there has been very little, if at all, objection to the 100 per cent FDI in single-brand retailing. From the fashion retailers' point of view, this is very encouraging as most of the large fashion retailers generally have single-brand retailing format. For example, even if Inditex has many brands such as Massimo Dutti, Bershka, Pull & Bear other than Zara, it has separate single-brand stores for each of these brands. Similar is the case of GAP Inc. that has many brands such as GAP, Banana Republic and Old Navy in its portfolio but has different stores for each one of them. Hence, all such companies can very well bring in their brands to India under the 100 per cent single-brand retail policy if the policy is accepted as tabled. In case of fashion retail, the only players that will be left out will be the department stores such as Macy's, Saks, Debenhams, et cetera. However, many of these anyway are not very international in nature and even if they go to other markets they prefer a partnership or licensing route. Since their intent is to open few but large stores, they choose to go with a local partner who can invest the capital and also manage the stores with local management that may be shared with the local partners' other retail businesses.

While Zara may have signed with Tata and has launched few stores in India, my belief is that it will get far more aggressive if the 100 per cent FDI in single-brand retail is allowed. There are two reasons for me to expect that. One being their own aggression that may not require a partner's consent and matching investment and secondly, the pressure of other fashion retailers such as H&M and Liz Claiborne coming to India encouraged by the policy change.

The current policy of allowing 51 per cent FDI in single-brand retail is quite restrictive and many brands have chosen to use the franchisee or licensing route rather than investing directly. This defeats the whole idea of FDI and doesn't do much to bring fresh capital into the retail sector. In fact, it takes away the local capital to fund international brands' retail expansion in India as local partners put in all the capital that they may have otherwise invested with some local brands of their own or of local fashion brand companies.

I don't see much issue with the idea of 30 per cent local sourcing from SMEs as proposed in the new policy. In fact, many retailers mentioned above will be quite keen to source much more of their merchandise locally. At least, in case of apparel, this may not be such a big issue as the textile and apparel supply chain is quite well developed in India and most of these brands and retailers have been sourcing from India. The intent of developing local supply chain is well placed and I am sure that Indian textile and apparel manufacturers will gain immensely from this. However, in the initial years of their launch, many retailers may find it difficult to meet this particular condition and the policy may require some tweaking to offer a multi-year period to allow the retailers to meet this condition of local sourcing. In the long run, I reckon that there will be much more sourcing happening from India even for the global markets by the same brands and retailers.

If we have to look at the picture comprehensively from the fashion retail point of view, the issue of multi-brand retailing isn't of much consequence and as long as FDI is fully opened for single-brand retail, it will be a major boost for the sector and it will see relatively far more activity than it has seen so far in terms of international brand arrivals in the Indian market. Fashion brands thrive in each other's company and hence it is expected that arrival of more brands will mean faster expansion and up-gradation.

Opening up of FDI through FIIs can offer the much-needed capital to these players and thus support the creation of a significant domestic fashion retail fraternity.

Opening up of FDI to 100 per cent in single brand will also allow FIIs (Foreign Institutional Investors through international private equity funds and venture capitalists) to invest into Indian fashion retail that on one side is capital starved and on the other has the onslaught of international players who cannot bring in their capital and are sucking away the local capital. We have been approached by a lot of garment exporters as well as manufacturers who are interested in entering the domestic fashion retail arena due to the shrinking export business or reducing margins in only manufacturing. Not all of them will be able to fund their plans on their own. Opening up of FDI through FIIs can offer the much-needed capital to these players and thus support the creation of a significant domestic fashion retail fraternity. In the absence of such funding options, India may actually turn out to be more dominated by international brands and will not have any fashion retailers who can withstand the GAPs and Zaras of the world.

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Harminder Sahni analyses the highs and lows of the fashion retail industry. Covering a spectrum of topics, each month he looks at the need of the hour for India.

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