

White Paper on RETAIL SECTOR

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Breaking Business Barriers
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SECTION 1 - INTRODUCTION

1.1 Introduction to Ease of Doing Business

The “Ease of doing business” is a World Bank index which is widely used to rank 189 countries for their present business laws and regulation environment every year. The index, however, does not take into account general conditions like macroeconomic indicators, market proximity, infrastructure etc. Further, the “Ease of doing Business” ranking is characterised by the average of 11 sub-indices like starting a business, getting credit, electricity, registering property so on and so forth. A higher ranking indicates efficient and simpler regulations for business and strong protection of property rights. This index not only identifies the source of the obstacle for doing business in a country, but also serves as the basis for policymakers to compare the regulatory environment for business across countries and design more compelling regulatory reforms for future.

India is one of the fastest growing economies in the world and has become one of the most attractive investment destination in the world. On analysing “Ease of doing business” index for 2016, we observe that India has moved up its ranking to 130, up by 4 units as compared to the previous year. The improvement in ranking is mainly because of the ongoing reforms and the 2 major drivers are, “Distance to frontier” sub index where India outperformed all the South Asia countries since 2004. The biggest improvement came from “Getting Electricity” sub index where the ranking jumped to 70 in 2016 from 137 in 2015. In order to complement its economic growth, India has to set major reforms to improve “Ease of doing business” ranking and attract more investors.

While Government of India (GOI) is constantly encouraging investments, the Department of Industrial Policy and Promotion (DIPP) is commending the government's initiative by taking several initiatives to ease doing business in India. The future reforms taken by GOI must ensure that India is on equal footing amongst other countries in terms of flexible, favourable, efficient and transparent business environment.

With this in view, the British High Commission (BHC) has initiated a study called “Breaking Business Barriers” for various sectors in India which focuses on stakeholder engagement and arriving at insights around business barriers. Specific recommendations have been identified for each of these sectors. The main objective of this report is to emphasize on the retail sector and the various barriers faced by businesses. We hope that the findings of this report would help bring the issues of retail sectors to the forefront and also serve as a reference point for the imminent need to pursue reforms in business policies and processes.

1.2 Introduction to Breaking Business Barriers

Centre for Public Policy Research (CPPR) in association with the *British High Commission (BHC)* has taken up an initiative '**Breaking Business Barriers**' aiming to curtail the regulatory barriers in

setting up, operating and exiting a business in the state of Karnataka, Kerala and Tamil Nadu. The initiative focuses on easing the business climate in seven sectors: Drugs and Pharmaceuticals, Education, Energy, Information Technology (Hardware & Software), Infrastructure, Retail and Manufacturing.

The initiative intends to enhance the development of a business-friendly environment in these states, by removing the regulatory barriers in doing business. The collaboration with the stakeholders has helped to identify the issues and challenges faced by them in operating the business and work towards finding a solution. In this regard, CPPR organized round table meetings with the Government representatives and business community in order to understand all relevant information regarding policies, taxation regimes, rules and other general information for doing business.

The website *EasyBiz* (easybizindia.com) India is created for the purpose of giving insights into the policy framework in the three states and measure state competitiveness. The website offers an interactive portal for the entrepreneurs to flag the issue faced by them in operating the business and work with one another to resolve the issue. The portal also has a clear process flowchart of the steps involved in starting a business (licenses, NOC, certificates) in the three states.

SECTION 2- SECTOR OVERVIEW

2.1 Definition of the sector

Organization for Economic Co-operation and Development (OECD) defines retail trade in the International Standard Industrial Classification (ISIC) as the re-sale (sale without transformation) of new and used goods to the general public, for personal or household consumption or utilisation (OECD,2008). In 2004, The High Court of Delhi defined the term 'retail' as a sale for final consumption in contrast to a sale for further sale or processing (i.e. wholesale) (Legal India,2011).

2.2 Retail Sector in India

In the past two decades retail industry in India has undergone remarkable transformation. This sector is expected to reach \$1 trillion in 2020 from \$600 billion in 2015 (A.T Kearney, 2015). While the average CAGR for the retail store is expected to be 12 per cent till 2020, modern trade which includes supermarkets, hyper markets and all other organized retail outlet is expected to grow at 20 per cent CAGR. The traditional retail trade which includes small grocery stores is expected to grow at 10 per cent per annum for the next five years. India is ranked 15 on the Global Retail Development Index, which measures the retail investment. The retail market accounts for 22 per cent of country's GDP and also contributes 8 per cent of the total employment. It is also the second largest sector in terms of employment after agriculture, employing over 40 million people (DNA, 2015)

Rural retailing in India is poised to grow rapidly in the coming years mainly due to increasing organized retailing. Rural market in India provides sea of an opportunity for the retail sector. According to National Council of Applied Economic Research (NCAER) reports, rural India is home to 720 million consumers across 627,000 villages

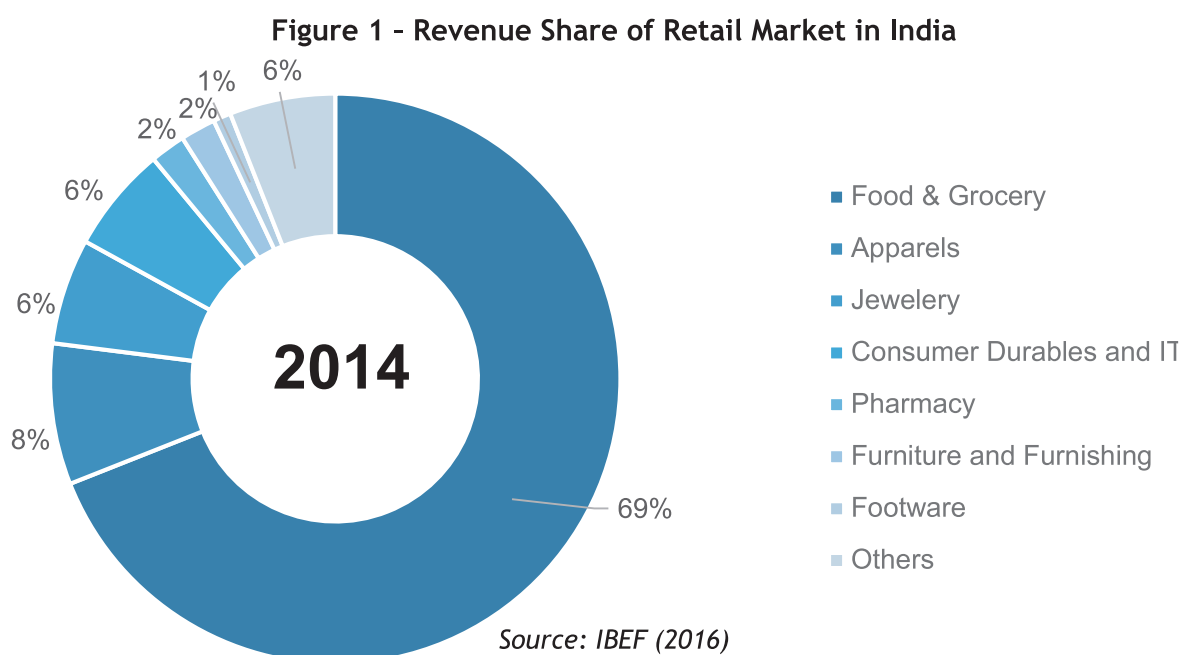
While consumption still is the leading factor for retail growth, other dominant factors that determine future growth of this sector include:

- Rising incomes which is expected to increase 3 times from \$6,393 in 2010 to \$18,448 by 2020 (Live Mint, 2016)
- Urbanization: 40 per cent of the population is expected to live in urban cities by 2020 from 30 per cent in 2010 (Mc Kinsey & Company, 2010)
- Higher brand consciousness and easier access to credit (KPMG, 2014)
- E-commerce market is going to increase 4 times and expected to reach \$80 billion over the next 5 years (Emarketer, 2014)

On the supply side, the increased options offered by the producers due to the competition is another important factor for increased demand for the retail products. As of today, the consumer has plenty of options to go with before fixing on what to buy. This increased competition by the players in the market offers a conducive market for the growth of the sector. (Business Today, 2014)

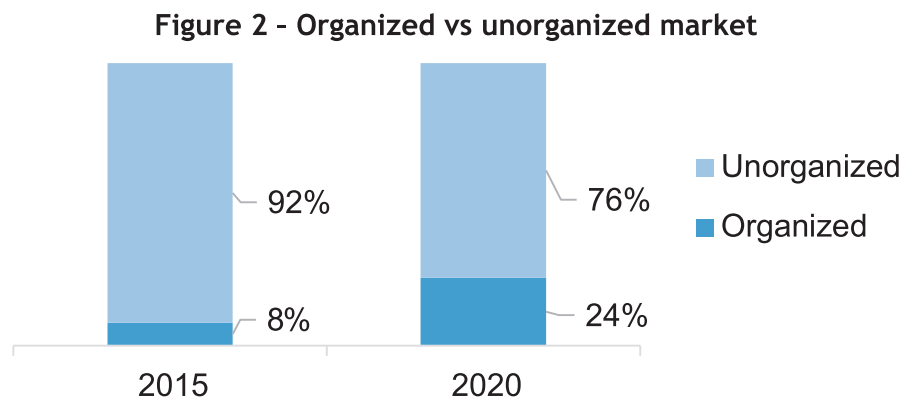
2.3 Main Segments in Retail Sector

Majority of retailers are in the unorganized sector. The share of organized retail has been increasing steadily in the country. Presently it accounts for around 8 per cent of the sector (Kamal, Ashish, 2014)



In 2014, the food and grocery section of the retail sector accounted for 69per cent of the total sales in the retail market followed by the apparel section (8per cent). The jewellery market had a share of 6per cent in the total retail sales (IBEF, 2016).

The organized retail penetration in India is only about 8per cent as compared to 85per cent in the US. The share organized retail market is expected to increase to 22per cent in 2020 (IBEF, 2016).



Source: IBEF (2016)

2.5 E-Commerce in India

E-commerce has defied the traditional structure of businesses trading with consumers bringing to the fore various business models which has empowered consumers. According to the report, *India Logs in @E-commerce*, various factors including favourable demographics, growing internet penetration, wider exposure of online shopping portals in smaller towns and rural areas, proliferation of mobile devices and emerging need for convenience, options and accessibility are driving demand in e-commerce market (Consumer Conexion, 2014).

The report titled, *Impact of e-commerce SMEs in India*, has projected the growth of e-commerce sector to cross USD 80 billion by 2020. E- Commerce has offered significant opportunities to SMEs specifically for exporters, to enter distant markets and communicate globally with all the consumers, distributors and suppliers (KPMG, 2015).

The e-commerce activities come under the purview of different existing laws like Information Technology Act, 2000, Contract Law, Company Act, Foreign Exchange Regulation Act (FERA), Income Tax Act and Sales Tax among others.

2.6 Foreign Direct Investments in retail sector

Foreign Direct Investment (FDI) in India was allowed in retail sector only in 2011 by removing restrictions on foreign investments in supermarkets, hypermarkets and convenience stores. The FDI

policy for retail has been amended several times from then in order to increase the investment cap for multi and single brand retail (The Economic Times, 2015).

Present state -

<i>FDI Single Brand</i>	100 per cent
<i>FDI in Multi-brand</i>	<ul style="list-style-type: none"> • 51 per cent • 100 per cent in food processing
<i>FDI in e-commerce</i>	100 FDI – B2B

2.7 Policy

Organized retail in India is managed by both the Ministries of Commerce & Consumer Affairs. While the Ministry of Commerce takes care of the retail related policies, the Ministry of Consumer Affairs regulates retailing in terms of licenses and legislations (FICCI, 2014)

The findings from the study show that retail is yet to be accorded industry status in the country. There is no policy for the retail sector at all India level as of now. Recently, some states have identified the need for creating a separate policy for retail in the wake of emergence of e-Commerce and for facilitating ease of doing business. Andhra Pradesh government recently unveiled the retail policy which is first of its kind policy introduced by any state. The policy has aimed to bring in greater flexibility in terms of open hours, engaging part-time employees, and removal of stock limits for essential commodities, among others. This is considered as a step towards ease of doing business for retail shop owners (Business Standard, 2016).

At present, the sector is guided majorly by the Shops and Commercial Establishments Act which was passed at the Centre, but implemented at the state level. Each state has their own rules to regulate the working conditions and timings to labours employed in the retail shops.

2.8 Overview of retail market in the state

The retail market in Karnataka, Kerala and Tamil Nadu is growing because of the increase in household income and expansion of retail markets. The states have been witnessing growth of retail markets in tier 2 and tier 3 cities (Economic Times, 2015).

Average of 70 per cent and 66 per cent of the population residing in Karnataka and Tamil Nadu respectively fall under the age category of below 40 (DES Karnataka, 2014-2015). This is a promising demography for the retail expansion in the states since age category plays an important role in the market growth (AT Kearney, 2015)

Karnataka and Tamil Nadu have agreed to allow 51 per cent FDI in multi brand retail in the states. However, Kerala has been stringent in allowing FDI in retail sector (Business Standard, 2015).

The Walmart group has signed an agreement with the Karnataka government in February 2016 to open 10 cash and carry stores in Karnataka (Business Today, 2016).

In the fast-growing retail sector, the states have been evolving a model of both large retail stores and the smaller mom-and-pop shops. The State government's take on FDI is based on the decision to ensure that small businesses are not uprooted.

SECTION 3 - WAY FORWARD

The challenges faced by the retailers in the emerging market are discussed in the section. The sector continues to remain unorganized and needs strong attention from the Government. The issues explained below are unanimously agreed by retailers and these issues continue to tamper the sector's growth across the country.

3.1 Entry

Issues:

- **Requirement of Multiple licenses:** The retailer needs to obtain multiple licenses to start the business, like, trade license, APMC license, Signboard license, registration under Shops and Commercial Establishment Act, Weights and measures license, among others. The process of obtaining the licenses/approvals is a time-consuming process and the cost incurred in this process is significantly high. In Kerala, the Dangerous and Offensive trade license needs to be obtained by all the retail outlets irrespective of the type of trade they are involved in
- **Lack of Credit Facility and high real cost:** Retailers continue to borrow money from the multiple suppliers since the banks offer credit to the retailers at a high interest rate and high collateral. The rental for the large spaces are high which has delayed the expansion plans chalked out by the retailers
- **Tax registration:** The retailer needs to register under multiple Tax Acts while setting up the retail shop. Registration for taxes which are levied by the State Government Authorities are not made online in Kerala and Tamil Nadu. A separate registration number for each makes it difficult to remember and file

- **Labour Laws registration:** The Shops and Commercial Establishment Act mandates registration of all the retail outlet or commercial space. The retailer needs to provide documents such as ID proof, rent agreement, building plan for registration under the act. The registration process have not been made online in Kerala and Tamil Nadu

Suggested Reforms:

Administrative reforms:

- The process of registration of the shops/commercial establishments should be made online. Karnataka has adopted an online mechanism to register the shops. The portal provides the list of the documents which needs to be uploaded to register the shop. The websites offer downloadable certificate, ensuring that no visits are done to the department
- The focus group interviews conducted suggested that micro financing for the retailers should be encouraged. The retailers need credit while operating (working capital) which the banks refuse to offer
- The tax registration process should be made online. In Karnataka, the registration of VAT/Profession Tax/ Entertainment Tax has been made online. The online portal provides clear information on procedures

Structural reforms:

- The retailers and the traders suggested that trade license should be removed as a mandatory document to operate the shop. The Local Municipality or the Gram Panchayat should provide a list of goods for which trade license should be considered mandatory
- The classification of all the trades under the Dangerous and Offensive list (D&O) is not helping to ease doing business in the states. The license should be made obligatory only to the traders who sell goods which create social or environmental damage
- A single ID for all the taxes makes it easier to file taxes and also enables greater integration of tax payment and filing systems

3.2 Operate

Issues:

- **Monitoring Process:** The retail shops are frequently inspected by various departments at the state level and Municipal Corporations. There is no consistency in the documents which needs to be produced during the time of inspections by the departments. The inspection records are not maintained and is not available to be referred to by the retailer after the inspection

- **Licenses Renewals:** The renewal mechanism for trade license and Shops and Commercial Establishment has not been made online which disrupts the operation of the retail shop
- **Complying with taxes:** On an average a retailer needs to file 2 taxes on a monthly basis and few on a quarterly and annual basis. Complying with taxes is a major issue associated with the complex tax structure, according to the retailers who were interviewed for the study

Suggested Reforms:

Administrative reforms:

- A better inspection mechanism should be developed which offers transparency of inspections held. The Inspection done by the departments should be accessible by the retailer within a stipulated time from the day of inspection. States like Gujarat, Tamil Nadu, and Jharkhand have introduced a mechanism for single inspection by which inspection under 10 Labour Acts could be dealt at once. This has in a way helped the retailers in the states to reduce the compliance cost
- The trade license and the Shops and Establishment license renewal should be made online to ensure faster process and less disruption to business hours. Karnataka Labour Department provides online renewal of Shops and Commercial Establishment.
- Online filing and paying of tax returns are useful in easily and quickly capturing relevant data effectively from the users. This mechanism allows better quality control on the database, by ensuring that it is error-free. The retailers in Karnataka further added that online provision of online filing and payment of taxes has helped to reduce the operational cost of complying with taxes.

3.3 Exit

Issue:

The sector does not have a clear defined exit policy which offers easy closure of retail business. During the study it was found that the retailers take an average of six months to one year to close the shop permanently; this phase involves surrender of license to the labour department and inspections.

Suggested Reform:

The retailers suggested that a single platform must be created through which all the licenses could be surrendered at one go.

SECTION 4- CONCLUSION

An accelerating pace of growth and transformation is expected in the Indian retail industry through the coming years, there are lot of exciting prospects for the future retail marketplace. While the organised retail sector is witnessing difficult phase due to price inflation, decreasing value of rupee, restrictions in FDI policies etc. the long-term outlook for the sector remains positive. The proliferation of demographic trends, positive economic growth, technology adoption and the demand for goods over services will drive new retail environment that will build the strength of the industry. These positives will change the retail landscape and add more excitement to the sector that thrives on customers, innovation and personal appeal, to purchase goods and services.

The consumer's choice is the main driving criteria in retail sector which determines the success of the retailers. Though the retailer needs to obtain multiple licenses from various departments, there is no single regulatory body monitoring the sector. The retailers have been lobbying for industry status and a regulatory body to heed to their demand. The organized retail players - supermarkets, hypermarkets though a new phenomenon has been attracting consumers. An interesting fact is to note that conventional convenience stores continue to exist alongside with the newly established single/multi brand shops. This definitely shows the consumer demand in India and the growing potential for retail stores.

The retail market in India is beginning to grow with the advent of e-commerce and revision of FDI policies. This is indeed a step towards more competition and choices for the consumer.

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The Report on “Breaking Business Barriers (BBB)” has been the culmination of the research conducted by Centre for Public Policy Research on theme of 'Ease of Doing Business' in three southern India states namely; Kerala, Karnataka and Tamil Nadu. The project was executed for a year starting from May, 2015.



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