Insights into the Growth of New Retail Formats in India

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Introduction

Retailing in India is receiving global recognition and attention. It is not just such global players as Wal-Mart, Carrefour, Tesco, and the METRO Group that have plans to expand in this market; even domestic corporate behemoths such as Reliance, TATA, KK Modi, the Aditya Birla group, and the Bharti group are now forging ahead in the development of retail businesses. On 27 June 2007, Reliance announced that it would invest US $ 5.6 billion in retail ventures to become India’s largest modern retailer. The industry is buoyant in terms of growth, and the early entrants are opening new stores at a rapid pace. Considering both the organized and unorganized sectors, retailing in India is currently estimated to be a US $ 350 billion industry, with organized retailing making up only about 3% of it. By 2010, organized retail is projected to reach US $ 23 billion (KSA Technopak 2005 report) and make up 20-25% of retailing sector sales (KPMG, 2005). The KPMG report also predicts that retailing will grow faster than GDP in the next 5 years. However, it should be noted that while there is excitement in the organized sector, the traditional format that includes small independent, largely mom-and-pop stores is also expanding rapidly, with almost 1.0 million stores being added every year.

Indian consumer tastes and preferences are changing rapidly, leading to radical alterations in lifestyles and spending patterns, which in turn are giving rise to new business opportunities. Shopping malls are becoming increasingly common in large cities, and at least 150 new shopping malls are expected by the end of 2008. The number of department stores is growing at a healthy rate of 24% per annum. Supermarkets have come in to garner an increasing share of the general food and grocery trade. Such changes are being witnessed even in rural areas. Many corporations, such as ITC, DCM, TATA, and Godrej, are experimenting with new store formats.
The Larger Picture

The Indian economy has shown impressive growth of over 6% per annum over the last 5 years. According to the Reserve Bank of India, the GDP growth rate in 2003-04 was a 15-year high, at 8.5%. Subsequently, real GDP growth accelerated from 7.5% during 2004-05 to 8.4% during 2005-06, on the back of buoyant manufacturing and services activity supported by a recovery in the agricultural sector. A similar growth rate is expected in 2007-08. With strong economic growth, consumerism has been increasing, and India has become the fourth largest economy after USA, Japan, and China, when compared on the basis of purchasing power parity.

A sizable proportion of disposable income in India is concentrated in the urban areas, but rural markets are not very far behind. In fact, the 20 million middle-class homes in rural India house a population equal in number to the population in urban India and thus with the same purchasing power (Marketing Whitebook, 2006). Therefore, there is significant and considerable opportunity for organized retailers in the rural areas. Given the increasing urban exposure of rural India, the urban and the rural upper-income groups can form an interesting continuum market comprised of 23 million households or 115 million consumers. In 2006-07, the consuming class was made up of about 60 million households, or 300 million consumers (Bijapurkar, 2003).

Data recorded by India’s National Council of Applied Economic Research (NCAER) shows that in 1998-99, a total of over Rs 91,500 crore (≈ US $ 22 billion) was spent by consumers on a basket of 22 fast-moving consumer goods (FMCG) products tracked by NCAER. Of this sum, 37% was spent by the two lowest-income groups in rural India, and only about 20% by the top two income groups in urban areas. There are nearly 42,000 rural haats [periodic markets], with an average of 300 sales outlets per haat, and the average sales at each outlet account for $18. Each of these haats attracts about 4,500 customers. In rural India there are 50 million Kisan [Farmer] Credit Card (KCC) holders. Life Insurance Corporation, the state-owned undertaking that has a more than 90% share of insurance nationally, sold 50% of its policies in rural India in 2006 (Marketing Whitebook, 2006).

Thus, the rural market holds immense promise for organized retailers, but companies need to find business models to serve it profitably. Unlike the urban market, it is less developed in terms of infrastructure and facilities. Although the cost of doing business in the rural market would be lower than that in the urban market, reaching out to the rural populace is a concern. A suitable business model and retail format to fit local tastes and preferences need to be developed. For example, Wal-Mart originally started in the rural market in the USA, while its competition started in the urban market. It illustrated how, with the right business model, an organized retailer can succeed in the rural and small town market.