Challenges of Retailing in India (A Short Note)

Mohammad Amin

Available at: https://works.bepress.com/mohammad_amin/23/
Challenges of Retailing in India

Using Enterprise Surveys data on 1,948 retail stores in India, this note highlights the key problems and challenges faced by retailers in 41 large cities of India. Inadequate power supply, access to finance, corruption, tax rates and land related problems are the most important obstacles to further growth. Competition in the sector also appears to be low, reducing labor productivity. Differences in the severity of these problems across regions and retail stores of various sizes are discussed.

The retail and wholesale sector in India is one of the largest sectors contributing 14 percent to the national GDP and 10 percent to formal employment. The sector has also shown strong growth in recent years, with a compounded annual growth rate of over 8 percent during 2000-2006 (at constant prices) compared with 7 percent for the national gross domestic product. Despite the large size, the retail and wholesale sector has received very little attention in India and elsewhere - largely due to data limitations. This note uses Enterprise Surveys’ data on 1,948 retail stores in 41 large cities of India to highlight the key problems and policy issues.

The sample consists of traditional or grocery stores (64 percent of the sample), consumer durable stores (26 percent) and modern format stores (10 percent). The median floor area of the shop equals 150 square feet with annual sales of Rs 500,000 (USD 10,309) and growing at a rate of 6.6 percent per annum. The number of employees (excluding the manager) per store average 4.7 – a figure highly inflated by a handful of large stores: about 43 percent of the stores are run by the owner/manager with no additional employees; 35 percent have between 1-3 employees and the rest 22 percent have between 4 and 500 employees. Over 93 percent of the stores have a single owner and roughly half the stores use rented or leased land (as opposed to own land).

Using these data, this note highlights the key obstacles and problems faced by Indian retailers and how the severity of the obstacles varies across rich and poor states and small and large stores. Inadequate power supply, poor access to finance and high corruption are the three most pressing problems. The note also sheds light on the low level of competition in the sector and its consequences for the efficiency of retail stores.

Inadequate power supply is the most important obstacle to retailing

From a list of twenty obstacles, stores were asked to identify the one most important for their business (figure 1). Most stores (33 percent) identified electricity as the most important obstacle followed by access to finance (16.7 percent), corruption (11.5 percent), land related problems (9.8 percent) and high taxes (9.1 percent). These top five obstacles are consistent across small and large stores as measured by the floor area of the shop. However, large stores are less concerned about finance and more about taxes.

The data also show an interesting pattern across high-income (leading) and low-income (lagging) states. Compared with the lagging states, fewer stores report access to finance as the single most important obstacle in the leading states (22.9 vs. 9.7 percent). This is also true of electricity (40.6 vs. 28.7 percent). The opposite holds for corruption (8 vs. 15.4 percent), tax rates (3.2 vs. 12.6 percent) and land related problems (7.3 versus 11.1 percent). We note that these comparisons do not imply that leading states perform worse in absolute terms than the lagging states in governance related issues (corruption,
taxes). Rather, with economic development, governance related issues (corruption, taxes) become greater binding constraints for stores’ operations than finance and infrastructure.

Figure 1: Obstacles to doing business faced by retailers in India

Source: Enterprise Surveys.

Less developed states face more power outages

Table 1: Power outages

<table>
<thead>
<tr>
<th>Stores facing outages (%)</th>
<th>Outage incidents per month</th>
<th>Hours of outage per month</th>
<th>Losses from outages (% of annual sales)</th>
</tr>
</thead>
<tbody>
<tr>
<td>All stores</td>
<td>82.9</td>
<td>26.9</td>
<td>65.1</td>
</tr>
<tr>
<td>Leading states</td>
<td>77.4</td>
<td>23</td>
<td>47.6</td>
</tr>
<tr>
<td>Lagging states</td>
<td>90.6</td>
<td>42.8</td>
<td>126.3</td>
</tr>
<tr>
<td>Ahmedabad</td>
<td>22.5</td>
<td>1.2</td>
<td>1.5</td>
</tr>
<tr>
<td>(city with best power supply)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gurgaon</td>
<td>100</td>
<td>91.6</td>
<td>339</td>
</tr>
</tbody>
</table>

Retailers in ECA and Manufacturing firms in India
Table 1 confirms much better supply of electricity in leading vs. lagging states. However, we must be careful in rushing to a conclusion from this. Figure 2 shows that losses to Indian retailers per hour of power outage are much higher at initial hours of power outage. Consistent with the figure and the fact that leading states have fewer hours of power outages, an hour’s reduction in power outage in the leading states implies cost saving to retailers (in absolute terms) that is about 1.93 times the same in the lagging states. Hence, on pure efficiency grounds, increasing power supply in the leading states seems more beneficial than in the lagging states.

Figure 2: States with better power supply are likely to gain more than the rest from further improvement in power supply

Retained earnings is the most common source of finance
The bulk of investment in working capital is financed by the retained earnings of the stores (78 percent). Similarly, among the firms that invested in fixed capital, 82 percent of their investment was financed by the retained earnings. Is the use of external finance low because Indian retailers are credit constrained? Consider a store as “credit constrained” if it wanted to borrow but did not because it thought the loan would not be approved, collateral requirements were unattainable or the application procedures were complex. About 14 percent of the stores in the full sample are credit constrained with a
high of 52 percent in the state of Bihar and a low of 6.4 percent in Maharashtra. Small stores are more likely to be credit constrained than the rest. The same holds for lagging compared with leading states although this is largely restricted to stores of intermediate size (figure 3).

Figure 3: Small-sized stores are more credit constrained than large-sized stores

![Bar chart showing credit constraints by store size and state]

For a comparison, credit constrained stores equal 7.6 percent in the ECA countries. Even countries in ECA, such as Uzbekistan and Moldova, that have roughly similar per capita GDP as India, show fewer credit constrained firms (6.6 and 4.7 percent, respectively).

Large stores suffer more from corruption
Inspections by government officials can culminate into a bribe payment or a request for one. About 40 percent of the stores in the sample were inspected during the survey year. Roughly, 44 percent of these inspections culminated in a bribe payment or a request for one with the figure rising to over 90 percent in the state of Punjab and 87 percent in Bihar. In other words, 17.4 percent of all stores surveyed either made a bribe payment to government officials or were asked for one (henceforth, incidence of bribe). While there is substantial variation across states in the incidence of bribe (with or without conditioning for visits by government officials), the variation has little to do with per capita income of states or other available measures of overall development. The same
holds for the frequency of inspections. Relative to small stores, the incidence of bribe is higher for large stores but this is entirely so because large stores are more frequently inspected (figure 4). Somewhat surprisingly, bribe incidence is roughly same in leading vs. lagging states.

Figure 4: Large-sized stores are more likely to pay bribes than the small-sized stores

![Incidence of bribery and store-size](image)

Source: Enterprise Surveys. Higher values along the horizontal axis imply larger floor area.

Non-availability of land is not the only land-related problem
Among the stores that reported access to land as a moderate or bigger obstacle to doing business (32 percent), non-availability of land was identified as a contributory factor by 81 percent, unclear ownership titles by 29 percent, problematic and costly registration process by 63 percent and difficulty in obtaining permits to use the land by 47 percent. In some states such as Haryana, Madhya Pradesh and Maharashtra, costly registration process is identified as a bigger problem than the non-availability of land by a majority of stores. In short, a comprehensive approach towards land reforms is necessary.

Retailing in smaller cities
The metropolitan cities of Bangalore, Chennai, Delhi, Hyderabad, Kolkata and Mumbai have traditionally been the retailing hub of India and also the main contributors to the ongoing retailing boom. Arguably, a similar expansion of retailing activity in the relatively small non-metropolitan cities would be required if the retail sector is to make a significant impact at the macro level. There is much talk about expansion of retailing activity in the relatively smaller non-metropolitan cities of India. For the business environment, the key difference between the metropolitan and the rest of the cities lies in power supply. In the non-metropolitan cities, losses due to power outages average 5.5
percent of annual sales of the stores and hours of power outage in a typical month average 78.9. Corresponding figures for the metropolitan cities are much lower at 2.6 percent and 32.5 hours, respectively.

**Competition in Indian retailing is low**

Less than 40 percent of the stores reported the competitive pressure as fairly important or very important for the prices of the store’s main products. Corresponding figure in ECA equals 71 percent. In short, competition in Indian retailing seems low by international standards. Amin (2007) finds that pro-competitive reforms could increase labor productivity in Indian retailing by as much as 87 percent.

The note attempts to highlight the main problems confronting the retail sector in 41 large cities of India. Inadequate power supply, access to finance and corruption are some of the most severe problems faced by Indian retailers. Competition in the sector seems low and pro-competitive reforms could improve retailing efficiency significantly.

**References**


---

1 These estimates are based on National Accounts Statistics and taken from Gordon and Gupta (2004).

2 Cities in the sample include (in alphabetical order): Ahmedabad, Bangalore, Bhopal, Bhubaneswar, Chandigarh, Chennai, Coimbatore, Cuttack, Delhi, Dhanbad, Faridabad, Ghaziabad, Greater Mumbai, Guntur, Gurgaon, Gwalior, Hubli-Dharwad, Hyderabad, Indore, Jaipur, Jamshedpur, Kanpur, Kochi, Kolkata, Kota, Kozhikode, Lucknow, Ludhiana, Madurai, Mangalore, Mysore, Nagpur, Nashik, Noida, Patna, Pune, Surat, Vadodara, Vishakhapatnam.

3 States are grouped into leading, middle and lagging states based on their level of development. The grouping is taken from Kochar et al (2006). Leading states include Delhi, Gujarat, Karnataka, Kerala, Maharashtra and Punjab. Lagging states are Bihar, Jharkhand, Madhya Pradesh, Orissa and Uttar Pradesh. The remaining states are classified as the middle (income) states.

4 This is a conservative definition of credit constrained stores because it assumes that stores who borrowed externally did not face any constraint on the amount borrowed.

5 The metropolitan cities include Bangalore, Chennai, Delhi, Hyderabad, Kolkata and Mumbai.