

FDI and its effect on the Indian Fashion Apparel industry

The recent resolution on Foreign Direct Investment, or FDI, in the retail sector has been applauded by a large section of both industry professionals and consumers, despite the many voices debating the merits of allowing FDI in the current economic situation and its possible impact on the Indian retail and manufacturing environment. As is quite apparent, the FDI policy is formulated with the objective of bringing in large funds to be invested in improving the supply chain and back-end of the retail sector (especially for the food and groceries segment) and to ensure that the manufacturing sector also gains from large multi-brand retailers being “forced” to source 30% of their products (by value) from Indian Small and Medium Enterprises (SMEs). While it sounds like a great opportunity for India to upgrade its manufacturing and back-end retail setup, there are many loopholes and/or threats which have been elaborately debated in the past few months.

Apparel demand may not be impacted much

From the fashion apparel demand perspective, India has emerged as one of the most attractive destinations for American and European brands in the last 10 years and will continue to hold promise for the next 10 years, irrespective of the policy on FDI. Apparel, being a more brand-driven category than, say, food & groceries, has already seen many international brands enter India over the past 15 years despite the restrictions in the FDI policy in single-brand retail. Modern retail in the apparel segment has a share of ~19% of the total apparel market at present, compared to a mere 3% share of modern retail for the food & groceries segment, which suggests that the apparel market has already seen large brands and retailers operating and expanding.

Thus, with the allowing of 100% FDI in single brand retail there may not be such a large change in the apparel retail landscape excepting probable changes in the operating structure of international brands. Most international brands have forayed into India through either a joint venture or a licensing agreement with an Indian franchise and despite the recent FDI-related policy changes these international brands have not changed their operating structure. Most foreign retailers realize the intricacies involved in the Indian market and therefore generally prefer partnering with a local franchise in entering the Indian market. This aspect will continue in future as well. Again, there are many brands which are operating as fully-owned subsidiaries and will welcome this policy change as it gives them more flexibility and operational control at the front-end.

Industries will benefit-

From the industry’s perspective, allowing up to 100% FDI in single-brand retail and 51% FDI in multi-brand retail seems like a favorable proposition, since a large part of the fashion industry supply consists of SMEs and they will surely benefit if more international brands make a foray into India. Many foreign brands present in India have, over the years, increased their sourcing from India as this gives them the benefit of shorter lead times and lower costs. Many brands have also set up their own back-end manufacturing infrastructure. This trend will continue to widen in the future as, with increasing competition, the pressure on price will increase further, forcing brands to look for ways to cut their costs. Also, with the growing fashion consciousness among Indian consumers, there will be an increased need to shorten lead times which will further force international brands to look at local sourcing options. Thus, with more international brands entering India, the demand in the “domestic apparel market” will increase. Also, large foreign brands and retailers bring with them their best practices in supply chain, manufacturing and product design & quality. This will help Indian small and medium enterprises to upgrade their manufacturing setup and knowhow in terms of products, designs and processes.

A few challenges for small retailers and intermediaries

There will definitely be some impact on the smaller, unorganized apparel retailers and wholesalers / distributors as they might be replaced to a certain extent by the Wal-Marts of the world. In this context, there may be some impact on the large aspirational mid-economy consumer segment which will migrate from unbranded to “branded or private label” apparel. However, the more brand-conscious, mid-premium and super premium consumer segment may not be affected significantly. But then, these challenges exist even in the current scenario of domestic organized retailers expanding their presence within India. Unlike food, there is no requirement for setting up a technologically superior back-end supply chain for apparel; this is likely to be similar to the existing structure with, perhaps, fewer channel intermediaries. There is the IT infrastructure angle that needs to be emphasized to make the supply chain more responsive and efficient; FDI may perhaps reinforce the need for the same.

The manufacturing angle

In terms of manufacturing, 100% FDI has always been an option (for the past 21 years) for the textile and apparel industry. However, the industry has only managed to attract FDI worth USD 1.27 billion thus far in manufacturing, compared to the overall FDI of USD 167 billion. FDI in textile and apparel sector has also declined at a cumulative annual rate of 10% in the past 5 years. These statistics suggest that, while India is an attractive destination for FDI in retail, it is not so much favored for manufacturing. This is partly because, of late, the majority of investments by foreign textile and garment manufacturers have been directed towards lower cost manufacturing locations like Bangladesh, Vietnam, etc. Perhaps the retail FDI policy initiatives may encourage brands with a longer term play in the Indian market to set up their own manufacturing units as well.

Going forward, the FDI policy initiative in retail is a positive move, and is perhaps the right stimulus required to bring the Indian economy back on the fast-growing track. Consumers will be happy as it gives them more options at acceptable and smart prices, even if local brands and retailers will feel more challenged. From the apparel industry’s perspective, it is favorable both from the demand and manufacturing perspective as it will not only provide more opportunities for suppliers but will also improve their manufacturing capabilities. It remains to be seen how the new FDI initiative actually impacts the industry and economy in the years to come.

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