In This Perspective

With positive macro-economic news coming in from most quarters within India and from the large developed economies, the consumer sectors in India are seeing increased activity from Indian firms, international companies, investors, and real estate developers. In this second edition of the Perspective, we present updates and analyses across retail, consumer products, fashion (textile & apparel), healthcare, tourism, and education.

India’s ‘roti, kapda aur makaan’ consumption hierarchy is changing. This has already changed to ‘roti, mobile, gaadi aur necklace’ and may soon further evolve to ‘roti, mobile, personal transport, and jewelry & watches’. In this article, we present the drivers of this change and implications this has for consumer product companies.

Over the last 12-16 months, the Indian media has gone to town over modern retail’s failure to take-off, grow and attain profitability. However, the reality is very different. In A Financial Deep Dive into India’s Retail Sector, we present an analysis of how the modern retail landscape is likely to shape up by 2014. We also present opportunities for modern retailers to increase margins and returns. Continuing with retail, in a piece titled Retail Real Estate Trends, we provide a snapshot of key trends and imperatives for the industry. These include the importance of collaboration between retailers and developers, and the need for transparency in occupancy charges.

The upcoming introduction of GST in India presents retailers and manufacturers an opportunity to optimise their supply chains. We provide details on how they can capitalise on this opportunity in GST: An Opportunity to Enhance the Supply-chain.

In FDI: A Catalyst for Growth of the Textile & Apparel Industry, we explore how FDI can push the textile and apparel industry towards a new growth path, and the factors that make investment in this industry an attractive option.

Building Operational Efficiency in Healthcare Delivery presents how hospitals can reduce costs and improve efficiencies, the importance of customer relationship management, best practices in hospital revenue management cycle, and the role of facility planning in improving performance.

We trace the journey of tourism and its growth in India, the factors which gave it a growth push, and the distinct forms of tourism that have now taken shape. This is covered under Indian Tourism – Managing Growth by Breaking Barriers.

Forecasting the Financial Potential in Education examines the investment scenario for creation of additional capacity in the education sector and the relevant regulatory developments. It also presents some investment thumb rules for entrepreneurs and investors.

Lastly, in Social Media: An Emerging Medium for Business Growth, we present the emergence and significance of social media networks and how companies across the world are leveraging their power for diverse business and social purposes.

We hope you enjoy reading this Perspective, as much as we did putting it together.

Raghav Gupta, President | raghav.gupta@technopak.com
Roti, Mobile, Gaadi aur Necklace
Arvind Singhal
The consumer spending priorities have shifted much beyond the basic survival needs of ‘roti, kapda aur makaan’ and may soon reflect a new set—‘roti, mobile, personal transport, and jewellery & watches’.

A Financial Deep Dive into India’s Retail Sector
Raghav Gupta, Purnendu Kumar, Rohit Bhatiani
An analysis of how the modern retail landscape would shape up in 2014 and the opportunities for modern retailers to increase margins and returns.

Retail Real-estate Trends
Anil Rajpal, Rohit Bhatiani, Preeti Gupta
A snapshot of key trends and imperatives for the industry that is currently in a state of renewal and covers its journey from being owner or developer driven to being retailer driven.

GST : Impact on the Supply Chain
Anil Rajpal, Sachin Jagtap
Post the introduction of new GST system in India, it is time for the manufacturers, retailers and service providers to align their supply chains by basing their logistics and warehousing decisions purely on efficiency optimisation as opposed to tax optimisation.

FDI : A Catalyst for Growth of the Textile & Apparel Industry
Prashant Agarwal, Luv Jasuja, Rohit Nasa
Exploring how FDI could catapult the Indian textile and apparel industry into a different growth trajectory and how well positioned is this industry to attract the foreign investment.

Building Operational Efficiency in Healthcare Delivery
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Corporates in healthcare are continuously evolving and adopting best practices including ‘Kaizen’, CRM, revenue cycle management, facility re-design, and electronic medical records to rationalise costs and bring in efficiencies.
Reconnecting with Consumers
Arvind Singhal
The Indian consumer has changed fundamentally over the past a few months. He now looks for lower-priced, acceptable-quality options and has turned more ‘fickle’, ‘greener’ and socially connected. What does this mean for manufacturers and marketers of consumer goods and services?

Indian Tourism: Managing Growth by Breaking Barriers
Lokesh Kumar, Rahul Alex Daniel, Nikhil Saigal, Barbara Cebula
A quick look at India’s travel and tourism industry, which backed by strong economic growth and a major thrust from the government, has shown healthy growth and added a bouquet of niche products like wellness, caravan and helipad tourism.

Forecasting the Financial Potential in Education
Raghav Gupta, Stuti Mody, Kiran Walia
Examining the investment scenario for creation of additional capacity in the education sector, some regulatory developments and key thumb rules for interested entrepreneur/investors.

Social Media: An Emerging Medium for Business Growth
Raghav Gupta, Veenu Sharma, Ashima Anand
Understanding why and how companies across the world are leveraging the power of social media, a new and growing medium that has revolutionised the way people communicate with others.

About Technopak
Roti, Mobile, Gaadi Aur Necklace

This article appeared in Business Standard on August 13, 2009

Notwithstanding the current concerns regarding the impact on consumer spending on account of a truant monsoon, India will see a spending of almost US$ 437 Bn in 2009 (assuming a GDP growth rate of 6%). Further, factoring in a 5% inflation and assuming that GDP will further grow at 6%, the consumer spending is likely to cross about US$ 479 Bn in 2010.

However, a deeper analysis of this gross data on consumer spending throws up some very interesting insights. For as long as we remember, roti, kapda aur makaan have been the primary needs and drivers of private consumption. Indeed, it seems that the impact of the sustained economic growth of the last 18 to 20 years is that for a very large part of the population, consumption has moved beyond the basic survival needs. While food & grocery continue to account for the largest quantum of spending - about US$ 260 Bn in 2009, followed by healthcare - about US$ 34 Bn and textiles & clothing the third largest - about US$ 31.25 Bn, the surprise numbers 4, 5, and 6 items on the consumer spending list in 2009 are spending on mobile phones and talk-time - about US$ 25 Bn, jewellery & watches - about US$ 24.58 Bn, and personal transport comprising two/four-wheelers including spending on fuel and repairs/maintenance - about US$ 23.95 Bn.

This data, of course, is at some variation with the official data since this spending includes some through the parallel economy, but is more reliable since it has been arrived at ‘bottom-up’ sector by sector. More interestingly, the growth rates in spending on non-basic needs are much faster now and therefore, it is likely that by 2012, spending on textiles and clothing could be relegated to the sixth spot and the hierarchy (excluding healthcare) will be roti, mobile, personal transport, and jewellery & watches.

The shift in consumer spending priorities does not stop here. The total outlay of the government on higher education is about US$ 2 Bn. The estimated revenue of the higher education coaching market (including preparation for entrance examinations like JEE, CAT, GRE and GMAT) is about US$ 2.08 Bn. If tutoring and other self-learning is included, the guesstimated private spending in 2009 is almost US$ 10 Bn! Spending on domestic leisure (and religious) travel and tourism is expected to cross US$ 12.50 Bn in 2009, while the spending on consumer durables and consumer electronics is just about US$ 11.45 Bn. Spending on leisure and entertainment in 2009 is about US$ 11.45 Bn, nearly equaling the entire size of the personal and home care FMCG industry! Other very fast-growing categories of consumer spending include personal computing (including internet) where consumers will spend almost US$ 2.08 Bn in 2009, and personal grooming services where the spending is over US$0.83 Bn already and growing in strong double digits.

There are several implications of these mega-shifts in consumer spending patterns. For the manufacturers and marketers, some of the imperatives include giving a fresh, much-deeper look into consumer and shopper behaviour using new age tools that go beyond traditional consumer/market research and then work the appropriate value proposition and delivery channels for their basket of goods and services. For entrepreneurs as well as businesses seeking to diversify, the implications are that there are incredibly large new business opportunities though, perhaps, these opportunities will require new business models (product, channel, consumer connect, delivery). Students planning their careers now would be well advised to study these new emerging sectors and plan accordingly. As is clear from the above, the sectors that are likely to create the most jobs (besides retail since most of this consumption will be facilitated through modern brick & mortar retail channels) are healthcare, telecom, travel & leisure, education & training, media & entertainment, personal grooming and fitness etc. The government itself has to get a much better understanding of these shifts since the implications are not only on its own revenue generation opportunities through direct and indirect taxation, but also in many other dimensions including vocational and higher education, and infrastructure (such as retail).

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A Financial Deep Dive into India’s Retail Sector

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Introduction

Like any new greenfield industry in the country, modern retail has also seen a flurry of activities with entrepreneurs and corporates across geographies setting-up their ventures across various categories and formats in the last 4-5 years. While most of them are still testing waters and figuring out the right retail model/s, some have taken the early lead based on understanding of the local consumers and investment in the back-end.

The industry is still in its early stage and has been in the media for wrong reasons in the recent months, with media writing off the modern retail evolution as a non-starter. While its true that there have been few instances of store closures due to sub-optimal location or poor execution, we feel that the market is still open and a significant business opportunity lies ahead for the retailers. The overall market continues to grow at 5+% and consumer aspiration for a better service environment still remains intact. In this article we have tried to understand the changes that are happening and the forecast on the retail landscape by 2014.

While retailers are working on multiple formats across categories trying to identify the right retail model for themselves, the performance across formats will vary as each retail format has its own unique financial as well as operating performance metrics such as gross margin, operating cost, space productivity etc. This article also analyses the retailer inventory levels vis-a-vis those of the international peers, and identifies potential opportunities for retailers to increase the return on capital.

Modern Retail Growth across Product Categories

The modern retail in India has been primarily driven by the apparel & footwear category, with players like Raymond, Madura Garments, Arvind Brands etc. setting up their outlets in 80s and 90s. While the margin offered by this category was high, the back-end too was fairly organized i.e. strong supplier base. The consumers especially the men at that time were also graduating from ready-to-stitch to ready-to-wear segment, which helped these retailers in creating significant differentiation from the local mom & pop textile stores.

Now with the entry of large corporates, other categories have also started to make their presence felt and the momentum in modern retail is building across categories, with food & grocery expected to see a lot of action in the coming years. This growth is due to entry of large Indian corporates like Reliance, Aditya Birla, TATA, Bharti, regional entrepreneurs and global retailers like Wal-Mart, Tesco, Carrefour, SPAR and others establishing their presence in the country.

The 2nd category which will have a significant impact is consumer electronics and mobile phones, where modernization has gained momentum not only due to retailers like Croma, Reliance Digital, Next and e-zone, but also due to major investments made by giants in consumer products like Sony, Samsung and LG. Most of these brands have established their own exclusive stores for their expansion strategy as
it helps them in showcasing their latest and high value products in a very high service environment. As the current MBOs in the market are too small and cluttered, they do not provide a great experience to the consumers. Going forward, the big-box formats like hypermarkets and cash & carry will also contribute significantly in the growth of modern retail in this category.

Apparel, which currently accounts for a major part of modern retail industry, will continue to modernize further with major growth coming from the entry of international retailers like Zara, Marks & Spencers, Top Shop and others. The hypermarkets, which currently get almost 30% to 40% of their revenues from apparel, will also help the category to modernize across various tiers of towns. We also see the emergence of large EBO’s of 4,000 - 5,000 sq. ft. targeted at the family audience in the coming days.

Other interesting categories to have a higher contribution in modern retail include footwear (with contribution from major sportswear brands, domestic footwear brands and hypermarkets), watches (brands as well as department stores) and impulse driven categories like books & music.

The growth in modern retail will get accelerated with the entry of global players and brands while Indian players continue to grow and create their own niche in the market on their own or in partnership with major global players.

Financial Returns in Various Categories

A study by Technopak on the financial returns across product categories and retail formats shows that in some of the categories like apparel, watches etc., the margins as well as the return on capital employed is on the higher side. Hence, these categories saw the entry of early modern retailers in the country. Other categories like food & grocery and consumer electronics rate lower on these parameters, and hence need higher space productivity and large business scale to create a viable long term business proposition.

In a category like consumer electronics, although the returns are lower, the retailers need to focus on additional services like extended warrantees, financing, etc. which helps them in improving their bottom-line (See GOME example later in the article). They also focus heavily on private labels which helps them earn the valuable extra margins. Internationally, this category has seen dominance of large players like Best Buy who have performed better than their industry peers and generated above average returns.

We understand that the financial performance is an important criteria for any player interested in entering this sector; however, the final decision must be made after taking into account elements like scalability, ability to differentiate, consumer need gaps and organization’s own strengths. For example, categories like apparel/ fashion seem financially attractive but their downside is the threat of high markdowns. The challenge is to keep the brand relevant and fresh year after year. Also, with value retailers like Wal-Mart and Target focusing on the fashion aspect of their apparel brands in recent times, the apparel retailers across the globe are coming under pressure.
Margin Concentration Across Product Categories

Technopak undertook a thorough analysis of the supply chain for various retail categories to understand the spread of margin concentration across various stakeholders like manufacturers and retailers. The study shows that the categories involving high degree of R&D and marketing acumen tend to have a high margin concentration towards the manufacturers/brands while retailers enjoy higher margins on others. As shown in Exhibit 3, in categories like consumer electronics, FMCG, pharma etc., most of the product development happens at the manufacturer/brand level, hence the margins passed on to the retailers are on the lower side. In case of food & grocery, since most of the products in India are still consumed in raw form and very little value addition happens on the product from the farm till it reaches the consumer, the overall margin in the chain is low and more or less equally distributed between the retailer and the supplier.

It is very important for a retailer to focus on increasing sales productivity, tighter inventory control, introduction of private labels and providing value added services in order to improve its financials. A classic example of the same is consumer electronics category wherein retailers work on private labels, extended warrantee etc. to increase their bottom-line.

International Case Study in Margin Enhancement

GOME is the leader in China’s CDIT retail market with product sales equivalent to US$ 6.6 Bn, presence in almost every Chinese province and more than 850 stores. GOME has a strong adherence to ‘Every Day Low Prices’ (EDLP) as well as ‘All Under One Roof’ strategies.

CDIT is one of the most difficult categories in terms of managing higher gross margins. On top of that, the adoption of EDLP strategy makes business very difficult for retailers like GOME. Despite that the company has been able to maintain strong profitability. Although GOME has not been able to
increase its gross margin from its product sales greatly, it has been able to increase its profitability by increasing the share of revenue from other income streams like income from supplier/brands, rental and display income and services like air conditioner installation. As shown in Exhibit 4, GOME has been able to increase its gross income significantly which has resulted in gross margin improvement. Typically, most of the other income elements involve very little expense for the retailer and hence, contribute directly to the bottom line. Indian retailers would also need to focus on extracting maximum value from their existing assets in order to grow profitably.

Inventory Management:
The Key to Profitability

Indian modern retail is still in a very nascent stage with most of the retailers in the early stage of growth. It is very important for the retail CEOs to invest in robust dashboards to monitor the performance of the company. Till now, most of the retailers in India were focusing on the top-line growth and product margin improvement; however, the recent slowdown has forced many of them to rethink on the way key operational parameters in the business are monitored. While top-line growth, sales per square feet, gross margin, rentals etc. are important, it is equally important to focus on the inventory. An analysis carried out by Technopak on inventory management in apparel category (see Exhibit 5) shows that Indian retailers are way behind their international counterparts on inventory management while almost being at par with them on gross margin. A higher inventory not only leads to greater risk of markdowns but also results in an increasing need for working capital further leading to lower ROCE. Further analysis shows that just 1% increase in sales and gross margin would increase the ROCE by 5% and 7% respectively whereas a reduction of 1 month inventory would lead to a 10% increase in ROCE. Given the current inventory levels of Indian retailers, an improvement in inventory through better forecasting, replenishment and lesser wastage can easily decrease inventory levels thus freeing up important capital which can be utilized for expansion plans.
Focus on Same Store Sales Growth

Till 2008 Indian retailers were rapidly increasing their same store sales due to increasing consumption, product price inflation and relatively low maturity of the stores. We saw a lot of pressure on same store sales growth in the recent months which can be attributed to slowdown in consumption and cannibalization from the new stores. Since the growth can’t always be in double digits, it becomes important for the retailer to keep improving its value proposition and continuously work on increasing the same store sales growth as the operating costs are bound to increase year after year. Also, as most of the retailers are in expansion mode, lower growth in same store sales may lead to increase in debt requirement to support expansion plans.

An analysis of the same store sales growth in some of the other markets shows that in food & grocery, the same store sales growth mirrors ‘Consumer Price Inflation’ in food. In other categories like apparel, the same store sales growth is more dependent on how various retailers differentiate on merchandise, design and product development.

As the retail sector in India matures, the high same stores sales growth is expected to come down and retailers would need to devise strategies to increase consumer ticket value and entice more consumers to the stores. Technopak expects that the ability to achieve high same store sales growth would be the key driver for success in future.

Conclusion

The modern retail in India is a bit unique since in most of the categories players see competition coming not from the other modern retailer but from the unorganized sector that works on low price, very high service standards and convenience proposition.

Retailers in India experienced high growth during the period 2004-07. However, as the slowdown hit the Indian economy in 2008, modern retail in India too felt its impact to a large extent. Slowdown in consumer spending and difficulty in finance availability created tremendous difficulties for Indian retailers. At the same time, the slowdown also made retailers realize the importance of profitable growth rather than top-line growth. Modern retail will experience significant growth in all categories in the next few years but retailers would need to focus on improving operations to achieve sustainable growth. With worries on external factors like low consumer spending and high occupancy cost subsiding to a certain extent, retailers would need to focus on international issues. While better inventory management is expected to improve the working capital management, other initiatives like private label development, merchandise improvement are expected to encourage customers to spend more and increase top-line revenues.

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Retail Real-estate Trends

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Introduction

Indian retail and real-estate sector underwent numerous changes in 2008. Lower consumer spending, high real-estate cost and lack of quality real-estate development prompted Indian retailers to revamp their current operations by closing stores at unprofitable locations, renegotiate rentals with developers, curb spending and reposition themselves to ride through the tough times. All this has resulted in altered relationships between real-estate developers and retailers.

Currently, the Indian retail industry is experiencing a steep learning curve. The industry is witnessing expansion, consolidation, acquisition; and retailers are restructuring and re-planning toward robust & efficient business models for long-term sustainability. The market is taking a ‘U’ turn from being a landlord/developer driven market to being retailer driven. The current turbulence has been a reality check for retailers to take stock of their strategy and operations and leaves the industry in a stronger position to take advantage of the rebound.

The mall space in top-nine cities (Delhi, Mumbai, Kolkata, Chennai, Bangalore, Pune, Hyderabad, Ahmedabad and Ludhiana) is estimated to be around 37 Mn sq.ft. On a pan-India level, based on the mall supply estimates for 37 cities spread across the four geographical zones of India, 2009 is expected to see an addition of around 44 Mn sq.ft. of mall space. According to Cushman & Wakefield(C&W), however, just about 41% of the supply is likely to get delivered by the year-end.

Top cities in India such as NCR, Mumbai, Kolkata, Pune, Bangalore, Chennai and Hyderabad witnessed on an average 10% vacancy rates in 1Q 2009 for available space in operational malls. NCR recorded the highest level of vacancy rate of 25% in 1Q 2009 owing to sluggish retail sales and despite the shortfall in mall supply-rate.

We expect that the modern retail would be back on its growth trajectory in the next two to three quarters. The demand for quality real-estate is expected to grow exponentially over the next 4 to 5 years fuelled by demand from the organized retailers. The success of retail real-estate business depends on the developer’s ability to recognize and respond to the changing consumer and market trends.

As per Technopak and C&W, it is estimated that an additional 65 Mn sq.ft. of mall space would be required in these top 9 cities by 2013-14.

This current slowdown in mall construction, however, is expected to keep the supply low over 2009-11. It may help in maintaining a healthier demand-supply equation in the retail-real-estate sector.

India is getting into an interesting phase as far as retail and real-estate is concerned and we will be witnessing many world-class shopping centers being created by developers. Builders backed by the global funds and skill-sets are now well equipped to create center which can be benchmarked against the very best in the world and take Indian real-estate sector into the next orbit.

Our estimates predict positive signs of growth coming through an increased demand for all segments of the retail real-estate sector. The challenge for the sector is to create properties though proper planning and differentiation so that operations can be extended over a period of time.
Lower or negative revenue growth over last year on same store basis and high rental cost of the stores added in 2007-08 have forced brands/retailers to take a re-look at their real-estate portfolio. In the second half of 2008, malls across the country saw a drop of 25% to 30% in footfalls and 10% to 15% dip in sales. Retailers are delaying their expansion plans, resizing their existing stores or are closing down stores at unviable locations.

Corrections of rentals in the range of 25% to 40% across major cities and markets have been witnessed over the last 2 to 3 quarters. Retailers have become more cautious in their approach and are undertaking detailed feasibility studies before signing any new deal for taking up space in the malls. They are also negotiating with developers before closing the deal. Developers are experiencing low occupancy rates and have low negotiation power for charging high rental rates due to sluggish demand from retailers for new space booking. Mall operators and builders are looking at various options to increase profits.

Big retail companies are forging revenue share arrangements and minimum-guarantee opportunities with mall owners and developers. This is expected to be the model of business relationships between organized retail and property owners in the future. The use of the revenue-share model is expected to gain momentum in the future as more and more Indian developers become corporatized. Retailers are looking at building long-term and success based relationships with mall developers.

Developers are also offering greater incentives in the form of longer rent-free period, reducing fixed occupancy cost, sharing capex with retailers, concessions in rentals to prevent exit of existing tenants. Furthermore, innovative marketing initiatives such as free gift vouchers to customers with every purchase and free parking are being adopted to draw customers in the malls.

Retailers are also helping developers with their operational expertise to devise strategies best fitted with the overall mall positioning and concept such as devising good tenant mix and assistance in overall mall management. It is expected that such initiatives and tie-ups would be key to success in the future with the growing realization between retailers and developers to devise models that are best suited to their financial interests.

### Prominent Tie-ups

<table>
<thead>
<tr>
<th>Prominent Tie-ups</th>
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<tbody>
<tr>
<td>Phoenix tie-up with Entertainment World Developers Pvt. Ltd. and Big Apple Real Estate Pvt. Ltd.</td>
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<td>Entry of Kshitij Retail Destinations in mall management space</td>
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<tr>
<td>Provogue’s tie-up with Liberty International</td>
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Increasing Role of Entertainment Formats in Mall Development

Entertainment is an increasingly vital component in the development of new malls. One of the key developments that has happened over the past few years is the addition of entertainment element as part of the shopping center.

In a bid to offer a complete shopping-and-entertainment experience for the entire family, mall developers in India are also placing an enhanced emphasis on entertainment-oriented components such as multi-plexes, video-game arcades, playing area for children etc.

New age shopping centers have started including elements such as sports facilities, theatres, children’s activities, gardens and restaurants to provide customers with multiple options on where to shop, what to do. It makes the entire mall environment much more vibrant as well as provides an element of differentiation.

There is a growing need for more such developments in the future to create differentiation between various malls. Developers need to realize that their shopping centers need to be entertaining, and that shoppers want their malls and town centers to blend with and reflect on their own communities. This shopping and entertainment concept that includes interactive retailing, state-of-the-art movie theatre complexes, mini-motor speedways, natural rock climbing walls, cycling, ice rinks, lakes etc. has done very well globally and gained popularity as a mall format. A large number of major malls in the US & other countries have repositioned themselves over the years and included entertainment as a key element to attract higher and wider footfalls. Much of that adaptation has been centered on becoming a one-stop entertainment, dining and shopping destination with broader appeal than that offered by simple food courts.

<table>
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<th>Exhibit 2</th>
<th>Key Developments with Entertainment Element - India</th>
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<tr>
<td>Entertainment Examples - India</td>
<td>Planned Components</td>
</tr>
<tr>
<td>DB Realty Orchid Ozone mall spread over 2.5 Mn sq.ft. expected to open by 2009 end.</td>
<td>A mystifying water themed atrium, a 20-screen mega-plex, a kids ‘play &amp; care’ zone and food courts offering world cuisine overlooking the water themed atriums.</td>
</tr>
<tr>
<td>Ambuja Housing Development in Kolkata.</td>
<td>A 1,000 sq.ft. butterfly park on the second level housing 40 species of butterflies.</td>
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In the Indian context, multiplexes have already emerged as the most significant entertainment option in the malls. The need of the hour is to look at more innovative entertainment elements as a key to differentiate malls.

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<th>Exhibit 3</th>
<th>Key Developments with Entertainment Element - International</th>
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<tbody>
<tr>
<td>Entertainment Examples</td>
<td>Planned Components</td>
</tr>
<tr>
<td>The Dubai Mall</td>
<td>World's largest aquariums featuring 33,000 living animals; an olympic-size ice rink; an entertainment section including the region’s first SEGA indoor theme park; and KidZania® - a children's ‘edu-tainment’ center.</td>
</tr>
<tr>
<td>Mills Corporation, an American mall developer (mails ranging from 1.2 Mn sq. ft. to 1.9 Mn sq.ft.</td>
<td>With an average occupancy rate of 96%, offers ‘Shopper-tainment’ – interactive retailing, state-of-the-art movie theater complexes, mini motor speedways, natural rock climbing walls, ice rinks, laser tags and more.</td>
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The retail center of the future — whether it is enclosed or open-air, big or small, theme-based or general - will also be designed to resemble a community, not just a place to shop. This implies an environment that forges links with the communities by opening wellness centers, libraries, city halls and play area for children.
Rising Importance for Brand Building in Malls

Established developers are trying to move towards a national footprint of malls. This is based on the belief that a multi-city presence gives better access to funds and global expertise. Also, it helps in attracting the retailers by leveraging the brand value gained in one city.

The developers are using the power of an existing brand name to support company expansion plans same as well as new cities.

Exhibit 5

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<th>Examples of Brand Building in Malls</th>
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<tr>
<td><strong>Major Developers</strong></td>
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<tr>
<td>K Raheja Group promoted Inorbit Mall</td>
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<tr>
<td>Prestige Group</td>
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<tr>
<td>JP Infrastructure Pvt. Ltd.</td>
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<td>Phoenix Mills</td>
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Strong brand equity and early mover advantage can lead to quick returns and early break-even. Strong planning and operational capabilities expand the developers’ experience and ability to launch successful retail spaces across different locations. Brand image and identity spreads across various locations, thus leading to negligible advertisement and marketing costs for future projects. Consumers are more willing to try the new mall as they perceive it to have the same quality and service level and other attributes as in their original favorite.

A chain of malls brings an image of consistency and attracts brand loyalty. However, it is very important for the developer to maintain the same quality and service standards of the brand across different cities. This strategy of leveraging on the brand can be extremely successful and profitable if it is correctly implemented and can create the right image for the new mall even before it starts functioning in the city.
Mall developers in India joined their peers across the globe in developing large malls and launched many ambitious projects with size greater than 1 Mn sq.ft. Size gradually became important for Indian mall developers. Many developers got in the race to build the biggest mall in a city/town more as an ego fulfilment exercise overlooking the importance of catchment needs, demand-supply scenario and sustainability aspects. This trend was not restricted to just mega malls in metropolitan cities and was soon seen in other cities like Ahmedabad, Nagpur etc. too. In some cases, the sheer size of these projects along with the supply of other upcoming retail real-estate developments didn’t fit very well with the catchment’s retail appetite resulting in an oversupply scenario. Also, with the change in economic scenario, low consumer sentiment and lack of footfalls, many retailers became cautious about their expansion plans. Retailers are either walking out of malls or rightsizing their portfolios to overcome their challenges.

In face of the oversupply of retail space and resulting difficulties in getting tenants on board even during the construction phase of such large projects, the developers are now making necessary changes by tweaking the size of the mall to suit the demand-supply scenario. Mall developers now are becoming increasingly aware of the importance of getting the size of the mall right. The perception of what the right size of a retail real-estate development should be, is undergoing a significant shift.

There have been different views on mall sizes. A large mall would bring all the required components under one roof however, it would be difficult to lease a very large mall and get multiple anchor tenants. On the other hand, a small mall may not be able to have the right retail anchors and entertainment mix. We feel the right strategy is to base the size of the mall on the size of its catchment area, its purchasing capacity, need gaps and existing and potential supply of retail space in the catchment.

Right sizing would start from the planning stage involving a thorough study of the needs of the catchment, existing supply and potential competition. This would also benefit the developers with regards to completion on time, lower spend on attracting retailers and lower capital requirement. In addition to right sizing the mall, developers also need to differentiate their malls through elements like entertainment, handicrafts etc.
Renovation and Re-invention of High-streets

High-streets which till sometime back were the key customer interaction point for most of the product brands, are undergoing changes to compete with the onslaught of malls. Most of the new brands in recent times have preferred opening their stores in malls rather than high-streets as it guaranteed higher footfalls and better marketing & promotional activities for retailers and hassle free shopping environment for shoppers.

High-street locations in India lack appropriate planning and are fraught with problems such as lack of maintenance of common areas, encumbrances on property, absence of single ownership and management, parking hassles etc. Despite these issues, retailers are now favoring high-streets as they feel locating the outlet in a high-street can act as a quasi-advertising medium and help them reduce their ad budgets. New brands tend to look at a high-street location to boost visibility. The trend of locating stores on the high-streets has picked up in the last one year as retailers experienced higher space productivity in stores on a high-street compared to those in a regular mall. Another reason for this could be the completion of fewer malls on time or lack of availability of quality retail real-estate space. Also, due to space limitation inside the city, most of the shopping malls are being developed outside the city limits, and the preference for shopping locations near home or within the city is driving consumers more towards the high-streets.

In order to meet the expectations of consumers and retailers, high-streets are undergoing re-invention and renovation through up-gradation in overall appearance, facilities, tenant-mix and infrastructure. Local municipalities along with market associations are also playing active role in upgrading the high-streets. Key initiatives include up-gradation of Khan Market, Connaught Place and promotional events and festivals.

We also expect these initiatives to spread to other high-streets in coming years. To make high-streets a sustainable business proposition for retailers, there is a need to focus on proper planning and regulations that can make high-streets more attractive and competitive in terms of tenant-mix, shopping environment and rentals especially in the wake of rising competition from new age malls.

We also expect that with increasing focus on up-gradation of high-streets, professional high-street management companies in line with mall management companies would emerge. These companies would be responsible for entire upkeep, marketing and leasing of the high-street markets.
Opportunity for Professional Mall Management Operators on the Rise

Professional mall management is emerging as a critical factor for the success of malls and the retail industry across the world owing to increasing competitiveness in the industry and the need to achieve greater differentiation among malls in order to lure more retailers and consumers. Mall management basically takes care of issues such as positioning, zoning, tenant-mix, promotions/marketing, facility & finance management (infrastructure, footfalls and ambience) etc.

Mall management in India is expected to gain significance now. With a growing demand-supply mismatch in retail real-estate in most cities, there would be greater need for mall developers to plan and run their malls more professionally.

Lack of mall management along with inappropriate tenant-mix would lead to poor mall traffic and closure of individual stores in malls. Professional third-party mall management service providers are hence likely to come to the fore. These third-party players not only understand the business challenges, but also have the ability to help the retailers deal with them effectively. Professional operators help the developers in conducting rigorous feasibility studies or market research, defining mall positioning, tenant-mix, layout of components in the mall, managing all operational, financial and administrative aspects and providing leasing assistance. Thus, managing all the stages of mall development including mall planning, construction and even post-development mall activities, an aspect that is considered very crucial for continued mall viability.

In developed markets, mall management is an established and independent service line with more focus on professional mall management. With increasing competition, customer and retailer’s needs would become even more important. All this will require continuous effort and professional approach. We feel that mall management companies are expected to fill this need-gap in the near future.

Currently, India has few end-to-end mall management companies and we expect that initially, the mall management efforts will happen through a consortium of firms from various backgrounds such as management consulting, real-estate and marketing & advertising.
Convergence of Leisure, Hospitality, Office and Retail Space

Consumer’s expectations in terms of product and services have undergone a sea change. Today, value for the consumers comprises quality, comfort, and convenience on one side and product price, effort and shopping hassle on the other. This has led to an actual “reduction” of distance that consumers are willing to travel from their homes for a non-work related activity.

A number of malls are being developed as a part of a large residential development, driven by the concept of providing a total quality lifestyle with residential, retail, entertainment, office & hospitality space - all part of an integrated development center. Developers of hybrid center are essentially creating streetscape-type shopping experiences with the convenience of everything at the doorstep.

Internationally, retail led mixed usage model has been quite successfully adopted by most of the popular malls including the River Center Mall on the River Walk in downtown San Antonio, Texas, and the incredibly successful mall at Caesar’s Palace in Las Vegas and Dubai Mall.

In India, developers are trying to replicate this model and have planned their future projects as integrated townships. Malls are now shedding their status as single-use development and have started to incorporate space for office, hotel, entertainment, civic and cultural activities. The above measures have helped in transforming shopping centers into “community” centers with events and experiences that the entire family can enjoy.

The growing popularity of mixed-usage developments over time is expected to upkeep the trend in the future with a lot of developments slated to come up on the similar lines. However, developers need to ensure with proper planning that the individual components planned are as per the catchment area, city profiling and correct execution of the same.

<table>
<thead>
<tr>
<th>Exhibit 6</th>
<th>Integrated Development Initiatives</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>India</th>
<th>International</th>
</tr>
</thead>
<tbody>
<tr>
<td>Phoenix Mills Ltd. – 8 to 10 market cities</td>
<td>Dubai Mall in Dubai</td>
</tr>
<tr>
<td>Nirmal Lifestyle Mall – 20 lifestyle cities varying from 4 Mn to 44 Mn sq.ft. by 2020</td>
<td>River Center Mall on the River Walk in Texas</td>
</tr>
<tr>
<td>City Center in Kolkata</td>
<td>Caesar’s Palace in Las Vegas</td>
</tr>
<tr>
<td>Ambience Mall in Gurgaon</td>
<td></td>
</tr>
</tbody>
</table>
Increasing Prominence of Community Markets

Today’s consumer needs a place where he can relax and meet friends apart from a just a shopping environment. This need is met by a community center that creates an environment that forges links to their communities by opening wellness centers, libraries, city halls and children’s play areas along with some services such as supermarket, pharmacy, bakery, sweet-shops, gift-shops, dry-cleaners etc. to cater to the nearby residential areas apart from regular shoppers.

Sponsors or marketing events on a regular basis.

Organizing fashion shows to draw more crowd.

Quiz competitions or craft fairs.

Shoppers look for places where they can interact comfortably and spend time with their friends and colleagues in an environment that is neither work nor home. The malls & community markets have a great opportunity to fill this gap. It brings in more customers, helps in keeping higher footfalls even on weekdays and it keeps them at the mall for longer periods of time.

Creating a sense of place and a feeling of community is a multi-dimensional task that requires a deeper understanding of human behavior, needs, and expectations. Shopping center developers need to respond to consumer interest in places that differentiate themselves, feel ‘authentic’ and provide not just a shopping experience but also one that reflects their lifestyles. They need to create a feeling wherein shoppers recognize that they can do a lot more than merely shopping.
Need for Greater Transparency in Occupancy Charges

In addition to the high occupancy cost, retailers are also facing issues related to high loading (super to carpet area ratio) and high Common Area Maintenance (CAM) charges. The key concerns of most of the retailers include lack of standardization of CAM and loading charges leading to wide variation across malls even in same cities. Retailers feel there is a lack of clarity and transparency on establishing CAM and loading charges and on what constitutes the same.

In some of the cases, retailer CAM charges as high as 30%-40% of the rental charges thus impacting overall store financials. Mall developers often have the tendency to make CAM charges as a profit centre however, in order to create a win-win situation it is very important for mall developers to understand that CAM should be cost-neutral. Mall developers can levy a small service charge for managing the maintenance and upkeep of mall.

Transparency in CAM charges would go a long way in establishing better trust amongst the retailers and mall developers. Internationally, a number of mall developers have shifted to fixed CAM charges which are negotiated with the retailer. The developers are also providing complete transparency on the charges incurred as a part of CAM through independent audits from retailers.

Loading is another contentious issue between mall developers and retailers. As in case of CAM, loading also varies from 40%-50% across various malls. It is not only the high amount of loading but also what constitutes additional area, is also not very clear to retailers. It is very important for mall developers to create a standardized definition for loading. Retailers and mall developers should collaborate and arrive at a consensus on the constituents of loading factor in a mall.

A greater transparency in CAM and loading would help create a sustainable long-term relationship between the mall developers and the retailers.
Various opportunities are emerging in retail real-estate sector which could be tapped for fuelling the growth in this sector. Certain concepts that have been tried and tested in international markets and are doing wonderful business, can be introduced in India to create elements of differentiation for a mall.

Some of key emerging opportunities include:

**Outlet Center**
An outlet center offers discounted merchandise for slow-moving items and non-seasonal merchandise for various categories. Dominating categories include apparel & footwear, consumer durables, furniture, furnishings and electronics. It basically appeals to brand-conscious and bargain-oriented customer who also wants to be a fashion leader. Outlet centers have progressed quickly from no-frills warehouses to well designated buildings with landscaping, gardens and food courts and are competing with other mall formats internationally. This sort of a concept, leveraging first-mover advantage, does not exist in India. Customers typically tend to spend more time in such centers as compared to other malls. This is mainly due to the availability of deep assortment of brands at economical prices. There can also be a scope and need for introducing better elements of entertainment and a food court to ensure a wholesome shopping experience.

**Lifestyle Center**
A lifestyle center is essentially a premium shopping destination designed for the entire family. It combines the traditional retail functions of a shopping mall with leisure amenities for upscale consumers. Typically, a lifestyle center has an open-air and up-scale design. The elements of architecture and landscaping are carefully combined to attract wider footfalls converting shopping from a chore to a fun activity for shoppers. It combines the carefully selected tenant-mix to ensure long-term sustainability and unique food and entertainment options.

Lifestyle centers have emerged as the most successful way to differentiate and create space in the already established retail malls in the US. There is a scope to introduce this unique concept in India to provide an all-in-one shopping and entertainment experience to shoppers.
Conclusion

Indian retail and retail real-estate industries are currently going through a difficult phase due to sluggish demand from the consumers. Since these industries are in their nascent stage currently, the formats and business practices are still evolving and the standards are yet to evolve. With greater learning, increasing consolidation and entry of international players, we expect that the Indian retail real-estate space would be benchmarked against the very best in the world.

The outlook for Indian retail looks quite promising in the near future and the current turmoil should be over in 2 to 3 quarters. Mall developers would be required to undertake greater planning and restructuring at the right time and differentiate their projects from others in the market to keep pace with the market demand expected from the retail & other segments. Future strategies for mall developers would entail the development of market-specific solutions for different demographics, psychographics, regions and locations. Extensive market research and professional services for each aspect of mall operation is likely to gain more importance to ensure project sustainability.

The market is witnessing consolidation on both sides - developers and retailers. The market would witness some developments of international scale and quality. The retail center of the future- whether it is enclosed or open-air, big or small, themed or general-would also be designed to resemble a community, not just a place to shop and entertainment would emerge as a vital component in the development of new malls.

The present crisis may be taken up in a positive spirit - a learning experience for the sector to grow stronger, more disciplined and organized at the end of the day. The real-estate industry needs to gear up well to respond to the changing demands and growing competition.

In India, there is still a significant gap between the demand and supply of quality real-estate space. Therefore, projects with good mall management practices in place will command a premium in the future. There is no shortage of customers if the developer has the right product-mix, location and track record.

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Preeti Gupta, Consultant | preeti.gupta@technopak.com
GST: Impact on the Supply Chain

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Impact of GST 24
Detailed Impact of Removed Tax Barriers on Cross-border Sales 25
Network Re-engineering for GST 26
Our Approach 28
Introduction to GST

GST is the biggest indirect tax reform undertaken in India since independence. Indirect taxes in India can be classified into 3 categories based on the entities that collect it - Central Taxes, State Taxes & Local Taxes. Some of the examples include:

- Central Indirect Taxes: Customs Duty, Central Excise Duty, Central Service Tax etc.
- State Indirect Taxes: Sales Tax (Sales VAT), State Entry Tax, Central Sales Tax, etc.
- Local Indirect Taxes: Octroi, Entertainment Tax etc.

It is important to note that while Central State Tax (CST) falls under the purview of the central government, the tax goes into the kitty of the state government where the sale originates. In the pre-reforms era of taxation, indirect taxes were largely charged at different stages of the goods and services value chain with no regard to taxes paid earlier or later in the chain. Thus, the taxes were cascading in nature resulting in several disadvantages which were addressed by the introduction of a Value Added Taxation (VAT) system.

Thus, the fundamental indirect tax reform that we have seen in the past 23 years is the shift to VAT. It means that the tax is levied at each stage only on the value added in that stage. In other words, Value Added = Market Price of Outputs – Market Price of Inputs Therefore, VAT = % Tax Rate * Value Added

<table>
<thead>
<tr>
<th>Exhibit 1</th>
<th>Key Reforms in Indirect Taxation through VAT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disadvantages of Pre-reforms System</td>
<td>VAT Reforms</td>
</tr>
<tr>
<td>Different tax rates for different products within a category and at different stages of the supply chain created complexity in manufacturing and trading decisions.</td>
<td>Aim at applying as few rates as possible across products and across the supply chain of a product making supply chain decisions simpler.</td>
</tr>
<tr>
<td>Due to the high rates charged in a cascading manner, evasion of taxes was encouraged. There was a lack of a tax chain where the subsequent stages in the supply chain were not inter-linked from a tax perspective. This meant that creation of an audit trail and policing of tax compliance was difficult.</td>
<td>The self policing mechanism of VAT ensures higher compliance as VAT is inter-linked throughout the supply chain or sections of the supply chain. In such a scenario it is difficult to evade taxes as that would require collusion from multiple parties.</td>
</tr>
<tr>
<td>Overall taxes in the entire system were high due to extensive evasion and a relatively smaller tax net.</td>
<td>VAT has resulted in higher compliance and a wider tax net. Hence, the tax authorities are amenable to lower rates.</td>
</tr>
<tr>
<td>As tracking the tax paid in the supply chain is not easy, it was difficult to extend tax benefits or fully extend tax benefits based on end use. The Government might want to give end-use tax breaks such as on exports, disaster relief supplies etc.</td>
<td>Due to the series of input credits in the supply chain, VAT is implemented as consumption based tax. This means that the ultimate burden is borne by &amp; at the point of final consumption. Thus, it is easier to provide end-use benefits.</td>
</tr>
<tr>
<td>Discouraged anciliarisation as there is no tax if inputs are manufactured within the company. Anything bought from outside was taxed with a cascading effect.</td>
<td>As tax is only on value addition, the impact is the same whether value is added within or outside the organisation</td>
</tr>
<tr>
<td>CST became the additional tax burden that companies had to bear on inter-state sales besides the sales tax paid on intra-state sales. As a result, organisations either incurred the tax incidence or used stock-transfer to avoid cross-border sales and tax. This often meant having stocking points in destination states and hence, networks designed on tax considerations rather than supply chain considerations.</td>
<td>CST is being removed to allow organisations to design networks, purely on supply chain considerations.</td>
</tr>
</tbody>
</table>

We could regard the evolution of GST as a gradual transformation of a disbursed, complex and cascading structure into a largely unified value added system of taxation. Exhibit 2 depicts this in more detail.

The country was first introduced to the VAT system through the introduction of MODVAT in lieu of central excise duties in 1986. MODVAT was further reformed into the CENVAT regime in 2000. VAT in lieu of Sales Tax, was introduced in 2005 and CST was reduced from 4% to 2% during 2007-08. Finally, GST is slated to be introduced in 2010 which will encompass Sales VAT, CENVAT and possibly subsume some of the local taxes such as Octroi.
Impact of GST on the Supply Chain

We have all seen and are aware of the impact that VAT has had on the supply chain so far. There are 4 key characteristics of the GST regime that will impact the supply chain further:

- It is expected that we will have a dual GST structure - State GST and Central GST. Central GST chain may extend right up to the last transaction at the retail level.
  - State GST would comprise of VAT/Sales tax, State cesses and surcharges on goods and services, Octroi, Entry tax, taxes on lotteries, betting, gambling and purchase tax as the main components.
  - Central GST would incorporate Central excise duties, additional customs duty (Countervailing Duty - CVD), surcharges, allied levies and service tax as the key taxes.
- Octroi and Entry tax are expected to be disbanded but the likelihood of the contrary cannot be ruled out.
- Inventory during transition will be impacted as post GST, inventory will carry Central GST and new GST rates credit.
- The tax disincentive of cross-border sales and supplies which is currently there because of CST will hopefully go.

### Exhibit 3

#### Impact of GST on the Supply Chain

<table>
<thead>
<tr>
<th>GST Characteristic</th>
<th>Impact on Supply Chain</th>
<th>Implication</th>
</tr>
</thead>
</table>
| Extended Central GST Chain                | • At present, service tax on logistics services consumed during distribution and retail are not off-settable against CENVAT  
• Extended Central GST chain will allow the offset in post manufacturing networks  
• This will lower the cost of logistics outsourcing as the 10.3% service tax charged by logistics companies can be largely offset against the Central GST liability | This will boost outsourcing in supply chains and provide greater impetus to 3PL's                                                                                               |
| Affected Inventory                         | • Post GST, inventory will also carry Central GST & inter-state GST input credit, the tax rates may also get changed for many products  
• Unless the GST rates go up for its products, the firms would be encouraged to minimise pre-GST inventory which has less input credits  
• As the GST implementation date approaches closer, one could expect uncertainty and panic regarding pre-GST inventory as was seen during VAT introduction | Organisations need to study GST’s final mechanisms and plan inventory transition very carefully for themselves, suppliers and customers                                                                 |
| Subsuming Octroi & Entry Tax              | • Octroi and entry tax are not in line with the spirit of GST although in some cases entry taxes are VATable  
• Once these taxes are paid reverse flow of goods becomes difficult, hence companies prefer postponed and uni-directional flow of goods across entry tax and Octroi borders | Organisations will be encouraged to locate warehouses and hubs in entry tax and Octroi zones and stock more inventory there                                                                 |
| Organisations will be encouraged to locate warehouses and hubs in entry tax and Octroi zones and stock more inventory there | • There are two possible scenarios through which tax barriers would be removed:  
  - Scenario 1: CST rates would reduce to zero with no carry-over of input credit across states  
  - Scenario 2: Stock-transfers are disallowed/taxed and inter-state sales are taxed with carry-over allowed  
  • In both cases, companies would no longer be required to have a warehouse in every state just to facilitate stock transfers and avoid CST | Organisations can and should design their networks purely on supply chain considerations and not tax considerations                                                                   |
While the implication of the first three characteristics is straightforward, the impact of removed tax barriers on network design needs to be understood in much greater detail.

Detailed Impact of Removed Tax Barriers on Cross-border Sales

Previously we mentioned that whether CST is reduced to zero or cross-border sales are taxed with offset allowed, the implication remains the same. Exhibit 4 shows an illustrative example that proves this point. For the sake of simplicity, we are ignoring logistics costs in the landed-cost component and also ignoring any input credit available at the ‘source’ location.

Exhibit 4

### Commercial Impact of GST

<table>
<thead>
<tr>
<th>Stock Transfer Sale</th>
<th>Landed Cost</th>
<th>Margin</th>
<th>Input VAT Credit</th>
<th>Price Before Tax</th>
<th>VAT</th>
<th>CST</th>
<th>Tax</th>
<th>Net Tax</th>
<th>Final Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>100.0</td>
<td>24.2</td>
<td>-</td>
<td>124.2</td>
<td>0%</td>
<td>0%</td>
<td>-</td>
<td>-</td>
<td>12.4</td>
</tr>
<tr>
<td>Depot</td>
<td>124.2</td>
<td>-</td>
<td>-</td>
<td>124.2</td>
<td>12%</td>
<td>4%</td>
<td>5.0</td>
<td>5.0</td>
<td>129.2</td>
</tr>
<tr>
<td>Distributor</td>
<td>129.2</td>
<td>6.5</td>
<td>5.0</td>
<td>130.6</td>
<td>12%</td>
<td>4%</td>
<td>5.2</td>
<td>0.3</td>
<td>135.9</td>
</tr>
<tr>
<td>Retail</td>
<td>135.9</td>
<td>13.6</td>
<td>5.2</td>
<td>144.2</td>
<td>12%</td>
<td>4%</td>
<td>5.8</td>
<td>0.5</td>
<td>150.0</td>
</tr>
</tbody>
</table>

### Table1: Current - Stock Transfer Sale

<table>
<thead>
<tr>
<th>Stock Transfer Sale</th>
<th>Landed Cost</th>
<th>Margin</th>
<th>Input VAT Credit</th>
<th>Price Before Tax</th>
<th>VAT</th>
<th>CST</th>
<th>Tax</th>
<th>Net Tax</th>
<th>Final Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>100.0</td>
<td>21.8</td>
<td>-</td>
<td>121.8</td>
<td>0%</td>
<td>2%</td>
<td>2.4</td>
<td>2.4</td>
<td>12.4</td>
</tr>
<tr>
<td>Depot</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Distributor</td>
<td>124.2</td>
<td>-</td>
<td>-</td>
<td>124.2</td>
<td>4%</td>
<td>0%</td>
<td>5.0</td>
<td>5.0</td>
<td>129.2</td>
</tr>
<tr>
<td>Retail</td>
<td>129.2</td>
<td>6.5</td>
<td>5.0</td>
<td>130.6</td>
<td>4%</td>
<td>0%</td>
<td>5.2</td>
<td>0.3</td>
<td>135.9</td>
</tr>
</tbody>
</table>

### Table2: Current - 2% CST Sale

<table>
<thead>
<tr>
<th>Stock Transfer Sale</th>
<th>Landed Cost</th>
<th>Margin</th>
<th>Input VAT Credit</th>
<th>Price Before Tax</th>
<th>VAT</th>
<th>CST</th>
<th>Tax</th>
<th>Net Tax</th>
<th>Final Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>100.0</td>
<td>24.2</td>
<td>-</td>
<td>124.2</td>
<td>0%</td>
<td>0%</td>
<td>-</td>
<td>-</td>
<td>124.2</td>
</tr>
<tr>
<td>Depot</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Distributor</td>
<td>124.2</td>
<td>6.5</td>
<td>5.0</td>
<td>130.6</td>
<td>4%</td>
<td>0%</td>
<td>5.2</td>
<td>0.3</td>
<td>135.9</td>
</tr>
<tr>
<td>Retail</td>
<td>135.9</td>
<td>13.6</td>
<td>5.2</td>
<td>144.2</td>
<td>4%</td>
<td>0%</td>
<td>5.8</td>
<td>0.5</td>
<td>150.0</td>
</tr>
</tbody>
</table>

### Table3: GST-Zero CST Sale

<table>
<thead>
<tr>
<th>Stock Transfer Sale</th>
<th>Landed Cost</th>
<th>Margin</th>
<th>Input VAT Credit</th>
<th>Price Before Tax</th>
<th>VAT</th>
<th>CST</th>
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<th>Net Tax</th>
<th>Final Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>100.0</td>
<td>24.2</td>
<td>-</td>
<td>124.2</td>
<td>4%</td>
<td>-</td>
<td>-</td>
<td>5.0</td>
<td>129.2</td>
</tr>
<tr>
<td>Depot</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Distributor</td>
<td>129.2</td>
<td>6.5</td>
<td>5.0</td>
<td>130.6</td>
<td>4%</td>
<td>-</td>
<td>5.2</td>
<td>0.3</td>
<td>135.9</td>
</tr>
<tr>
<td>Retail</td>
<td>135.9</td>
<td>13.6</td>
<td>5.2</td>
<td>144.2</td>
<td>4%</td>
<td>-</td>
<td>5.8</td>
<td>0.5</td>
<td>150.0</td>
</tr>
</tbody>
</table>

### Table4: GST - Inter State Sale Taxed with Offset Allowed

<table>
<thead>
<tr>
<th>Stock Transfer Sale</th>
<th>Landed Cost</th>
<th>Margin</th>
<th>Input VAT Credit</th>
<th>Price Before Tax</th>
<th>VAT</th>
<th>CST</th>
<th>Tax</th>
<th>Net Tax</th>
<th>Final Price</th>
</tr>
</thead>
<tbody>
<tr>
<td>Source</td>
<td>100.0</td>
<td>24.2</td>
<td>-</td>
<td>124.2</td>
<td>4%</td>
<td>-</td>
<td>-</td>
<td>5.0</td>
<td>129.2</td>
</tr>
<tr>
<td>Depot</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Distributor</td>
<td>129.2</td>
<td>6.5</td>
<td>5.0</td>
<td>130.6</td>
<td>4%</td>
<td>-</td>
<td>5.2</td>
<td>0.3</td>
<td>135.9</td>
</tr>
<tr>
<td>Retail</td>
<td>135.9</td>
<td>13.6</td>
<td>5.2</td>
<td>144.2</td>
<td>4%</td>
<td>-</td>
<td>5.8</td>
<td>0.5</td>
<td>150.0</td>
</tr>
</tbody>
</table>

Source: Technopak analysis
• **Table 1:** Suppose a firm currently does a stock transfer from State A to State B, before selling in State B to avoid paying CST. It thus gets a margin of US$ 0.50 per unit and incurs local VAT only when it sells in State B to its distributor through its depot. The distributor charges a margin of US$ 0.14 per unit and charges the final price by adjusting the input credit (which is available since the sale from depot was intra-state). In this case,

\[
\text{Price to Retailer} = (\text{Distributor Landed Cost} + \text{Distributor Margin} - \text{Distributor Input Credit}) \times (1 + \text{VAT Rate}).
\]

Similarly the MRP comes out to US$ 3.13/unit after accounting for input credit at retail level as well as retailers’ US$ 0.28/unit margin.

• **Table 2:** In today’s 2% CST scenario, the firm incurs US$ 0.08/unit loss in margin if it were to do a cross-border sale to the distributor, without going through a stock transfer at the depot. The calculations are based on the premise that the US$/unit retailer margin, distributor margin and MRP are maintained at the same level.

• **Table 3:** If CST rates were to become zero then the firm can do cross-border sale (at 0% rate) directly to the distributor without any loss of margin to itself, the distributor or the retailer and yet charge the same MRP to the consumer.

• **Table 4:** If CST is abolished and inter-state sales or stock transfers are taxed with input credit allowed at the destination, then also the margins and MRP remain intact for everyone.

Thus, we see that when tax barriers on cross-border sales are removed whether through the route shown in Table 3 or 4, it becomes unnecessary to have a depot in the destination state. The supply chain can then be designed not on tax considerations but purely on logistics cost and customer service considerations.

Hence, a key feature of post GST supply chain networks would be fewer warehouses or distribution centres than before. This means simpler and leaner networks which could incur lower costs of operation as explained below. Exhibit 5 provides an approximate guide on the number of warehouses for a distribution company dealing in fast moving goods can have in a GST scenario. The specific business realities of the company will also have a great bearing on the actual number of warehouses required.

### Network Re-engineering for GST

We have already established that an optimum network design post GST would be different from an optimum network design in today’s taxation scenario. The re-organised network will in fact be significantly different.

- The move towards fewer warehouses would require many warehouses to combine, close and re-locate.
- Required capacity of many warehouses will undergo changes. With fewer warehouses, the average size of the warehouse will go up.
- Hubs are not directly impacted by CST considerations. However, fewer & larger warehouses may make it feasible to route plant production directly to warehouses rather than through hubs, due to larger throughputs. Thus, the size and number of hubs could get affected.
- The linkages between factories-hubs-warehouses-customers for various products will get re-aligned.
Exhibit 6 lists all the pros and cons of doing a network re-engineering exercise for GST. Clearly, the benefits outweigh the disadvantages. Besides providing a simpler and more manageable network, Technopak estimates between 5% to 10% net savings in logistics + inventory carrying costs of an organisation through this exercise. Fewer warehouses would mean a straight saving on warehousing costs. The inverse root law states that:-

**Safety Inventory** \( \alpha \frac{1}{\sqrt{\text{Number of Stocking Points}}} \)

This means that the safety stock requirement would also go down. Prima-facie, it would appear that some of these savings would be offset by the increased cost of freight. With fewer intermediate stocking points (warehouses) between sources and customers, the average freight legs should get longer. However, this might not necessarily always be true as the network linkages of source-warehouse-customer could actually get shorter by removal of inter-state sale barriers. Exhibit 7 explains this in greater detail.

In Case 1, the source is in State A (left) and the customer is in State B (right). Due to CST barriers, the customer can only be served from a warehouse in State B but by back-tracking in the direction of the source. In Case 2, after the introduction of GST, the network linkage is re-defined and the back-tracking is saved substantially by serving the customer directly from the factory, or a warehouse “on the way” in State A itself. The freight distance saving translates directly into freight cost saving.

---

**Exhibit 6**

**Pros & Cons of Network Re-engineering for GST**

<table>
<thead>
<tr>
<th>Pros</th>
<th>Cons</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduced fixed warehousing costs</td>
<td>Higher lead times to customers</td>
</tr>
<tr>
<td>Reduced inventory (inverse square root law)</td>
<td>Possibly higher freight cost especially secondary freight</td>
</tr>
<tr>
<td>Simplified planning and reduced warehouse and C&amp;FA management</td>
<td></td>
</tr>
</tbody>
</table>

**Exhibit 7**

**Freight Savings Due to GST**

**Case 1: CST at 2%**

- Plant
- State Boarder
- 1000 kms
- Old Warehouse
- Customer 1
- Customer 2

**Illustrative freight distance (and hence cost) saving of 400 kms for customers 1**

**Case 2: GST**

- Plant
- State Boarder
- 1000 kms
- Old Warehouse
- New Warehouse
- Customer 1
- Customer 1

- 500 kms
- 200 kms
Impact on Warehousing

New or enlarged warehouses will have to be designed/re-designed. Technopak estimates that for most organisations, 6-8 locations will have mega warehouses with complex operations in the near future. Thus, modernisation of key warehouses is strongly recommended on account of:

- Large sizes, high throughputs and more complex operations
- Increasing level and variety of service required by customers, especially organised retailers
- Increasing scarcity of skilled labour and real estate requiring vertical and mechanised warehouses

Impact on Service Level

The key fallout of GST aligned networks is fewer warehouses but this also has two implications on customer service:

- **Longer Lead-times to Customers:** This would not be an issue as long as the network redesign exercise puts a minimum lead time/distance constraint while serving customers in the new network.
- **Improved Assortment:** Often SKUs needed by customers are not available at the warehouse meant to serve them although they may be idling at another warehouse. This is especially true for slow moving items. With stock aggregated at fewer warehouses, the planning and assortment availability improves for slow moving SKUs.

Thus, service to customers could be maintained or even improved in a network re-engineering exercise. The key here is to undertake a professional scientific exercise as opposed to manual experience based methods that many firms have used for designing their legacy networks.

Our Approach

A scientific tool-based redesigning of the distribution network would be helpful in delivering optimal logistics and inventory carrying costs without compromising on service levels to customers. Exhibit 8 illustrates this scientific tool-based approach in greater detail.

Exhibit 8

<table>
<thead>
<tr>
<th>Network Re-engineering Approach</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Inputs</strong></td>
</tr>
<tr>
<td>• Collate demand pattern and existing supply chain costs of manufacturing, freight, handling, fixed warehousing, variable warehousing and taxes (VAT / CST / Excise)</td>
</tr>
<tr>
<td>• Understand existing service levels and logistics constraints</td>
</tr>
<tr>
<td>• List the external business environment factors affecting network design and performance</td>
</tr>
<tr>
<td>• Identify candidate locations for warehouses &amp; hubs based on Technopak’s understanding of the Indian logistics sector</td>
</tr>
<tr>
<td><strong>Model Design &amp; Creation</strong></td>
</tr>
<tr>
<td>• Design a Mixed Integer Linear Program (MILP) model based on a firm’s internal and external business environment translating into appropriate variables, constraints &amp; assumptions</td>
</tr>
<tr>
<td>• Pre-processing of input data to improve model performance and ensure accuracy of results</td>
</tr>
<tr>
<td>• Scenario building &amp; sensitivity analysis</td>
</tr>
<tr>
<td><strong>Output</strong></td>
</tr>
<tr>
<td>• Number, size &amp; location of hubs &amp; warehouses</td>
</tr>
<tr>
<td>• Network linkages between various supply chain entities</td>
</tr>
<tr>
<td>• Optimal transport modes and mix</td>
</tr>
</tbody>
</table>
Exhibit 9 depicts our methodology that helps organisations meet the GST deadline in the most optimal state. We deliver an end-to-end solution which includes the first four design stages as well as implementation hand-holding.

Benefits Beyond Zero GST

A network re-engineering exercise with us has many more benefits than just the ones arising from the GST opportunity. Some of the other benefits are:

- Robust design to support growth over next 3-5 years
- Optimal realisation of back-haulage and direct despatch opportunities
- Savings from optimisation of legacy network
- Transport mode optimisation in the re-designed networks
- Evaluation and factoring of opportunities arising from GST and entry tax rationalisations
- Improved service levels to all or key customers
- Optimal network flow paths for goods, hub-spoke connections and feeder depot concepts

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FDI: A Catalyst for Growth of the Textile & Apparel Industry

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Growth Prospects 32
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An Attractive Destination for Investment 35
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Background

The Indian textile and apparel industry is one of the oldest and most significant industries in the country and one of the largest in the world. Apart from China, no other country can match the size, spread, depth, and competitiveness of the Indian textile and apparel industry. Moreover, the global elimination of quotas at the end of 2004 has greatly enhanced the opportunities for India to showcase its inherent strength and become a top sourcing and investment destination.

Today the industry contributes around 14% to industrial production in the country, 4% to the GDP is estimated to directly employ approximately 35 Mn people apart from the indirect employment in allied sectors, thus making it the second largest employer after agriculture. It accounts for about 15% to the country’s exports, and is, in sum, an important economic engine for the nation.

In part, the very diversity, scale and spread of the industry which has been its strength, has also been its weakness. However, in the past 10 years, the industry’s actions, government policies as well as market events have begun to converge, providing several growth opportunities for the sector domestically as well as in the global market.

Indian Textile and Apparel Industry: Current Size

The present size of Indian textile and apparel market is US$ 62 Bn of which US$ 22 Bn is exports while the rest US$ 40 Bn is the domestic market.

Exhibit 1

Current Size : Indian Textile and Apparel Market

The Indian domestic textiles and apparel market is one of the fastest growing market in the world. It is expected to become one of the major consumption bases in near future. Out of the total market size of US$ 40 Bn, clothing contributes US$ 30 Bn, while the remaining US$10 Bn is contributed by textiles (home textiles, technical textiles and other textiles end-uses).

The domestic market has shown a significant growth in past few years registering a CAGR of ~18%. Though men’s wear is the largest category with a value of US$ 10.3 Bn, kid’s wear and women’s wear are the fastest growing categories.

The textile industry plays a significant role in getting the foreign exchange reserves into the country as it contributes to approximately 15% of the total exports from the country. Exports in textiles and apparel have registered a strong growth in last few years – 11% CAGR from 2004-05 to 2007-08.
The single largest category is woven apparel followed by knitted apparel, made-ups and cotton based textiles.

**Growth Prospects**

India’s current domestic consumption of US$ 40 Bn is expected to grow to ~US$ 200 Bn over the next 25 years (growing at over 7% per year). India’s exports are expected to grow to ~US$ 125 Bn from the current level of US$ 22 Bn by 2035.

However, the visible bottleneck to the above growth is the shortfall in the supply to meet the aforementioned demand. The current manufacturing capacities cannot meet the unprecedented growth in the demand and therefore, we would need mega investments to the tune of US$ 130 - 135 Bn over next 25 years in textile and apparel manufacturing.

If the required demand is not met by indigenous manufacturing then it would be met by imports from Asian countries like China, Bangladesh, Vietnam, Korea etc.; Eastern European countries like Romania, Bulgaria, Tunisia etc.; and African countries like Kenya, Nigeria, Egypt etc.

One of the biggest questions to be answered here is - who will invest? We firmly believe that FDI can act as a catalyst to trigger this investment. One of the most commonly known benefits of FDI is the “Crowding-in” effect. With entry of foreign firms in the sector, the confidence level of investing in the sector increases and it has been usually seen that more and more domestic manufacturers follow suite.

Considering the above logic, we believe that approximately 75% to 80% of the investment would still be done by the domestic business houses, but the balance 20% to 25% investment required as FDI will give the required confidence to invest in the sector.

A prime example of the same would be what US auto sector underwent in the 1980s.

- Companies invest in the US because it is single largest economy in the world and its labor pool is one of the best educated, most productive and innovative, and it provides world class infrastructure.
- The US auto sector in the 1980s had several features that made it an attractive setting for FDI. Both the end-product automobile sector, where there were only ‘The Big Three’ US assemblers (General Motors, Ford, and Chrysler), and the large number of firms in the auto component supply sector provided such an opportunity.
- There was substantial inward FDI that originated predominantly from a single country, Japan. This investment likely increased the competition that then led to productivity changes. In addition, the Japanese entrants possessed superior production techniques and management practices, which created the potential for technology transfer.
- They began to produce vehicles in North America and began to purchase inputs from US auto-component manufacturers.
- The results suggest that increased competitive pressure in the auto sector was the main cause of overall productivity improvement, at least during the initial stages of foreign direct investment of the 1980s.

<table>
<thead>
<tr>
<th>Sector</th>
<th>Investment Required (US$ Mn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Spinning</td>
<td>55,000</td>
</tr>
<tr>
<td>2. Weaving</td>
<td>25,000</td>
</tr>
<tr>
<td>3. Knitting</td>
<td>10,000</td>
</tr>
<tr>
<td>4. Fabric Processing</td>
<td>40,000</td>
</tr>
<tr>
<td>5. Home textiles</td>
<td>4,200</td>
</tr>
</tbody>
</table>
Importance of FDI

FDI is becoming one of the most discussed topics in the drive for economic globalization. On one hand, multi-national companies consider FDI as an important means to reorganize their production facilities globally while on the other it is regarded as an important vehicle for economic development particularly for developing economies.

FDI plays a pivotal role in the development of an economy. The key advantages that FDI and foreign corporations bring with it are listed as under:

- FDI provides capital which is usually missing in the target country
- FDI brings new technologies that are usually not available in the target country
- Foreign investors are able to finance their investments projects better and often cheaper
- Foreign corporations create new workplaces
- Foreign corporations bring new know-how and managerial skills into the target country
- Foreign corporations provide better access to foreign markets
- Foreign corporations can help to change the economic structure of the target country
- "Crowding in" effect: The foreign corporations often bring additional investors into the target country (example, their usual subcontractors)
- Foreign corporations improve the business environment of the target country
- Foreign corporations bring new “clean” technologies that help to improve the environmental conditions
- Foreign corporations usually help increase the level of wages in the target economy
- Foreign corporations usually have a positive effects on the trade balance

One of the biggest challenges in Indian textile and apparel industry is that 95% of the industry is unorganized – small fragmented units. The advent of FDI will bring in latest technology and marketing techniques that will add fuel to the organized growth of this sector. Investing companies will bring over the latest know-how and manufacturing techniques, resulting in higher efficiencies and low cost of manufacturing. These advantages can be passed on to the consumer creating higher consumption; consumption at the right price will increase.

Multinationals and transnational companies conduct extensive due diligence and risk analysis before investing in a country. At the same time, they are investing for the long term. This is a confidence booster for other companies – both international and domestic.

FDI is favored for two main reasons – growth of the organization by tapping into new markets, and/or reducing costs by accessing low cost production countries. Leading examples of these two scenarios are China and Bangladesh.

China Offers Both-Domestic Market and Low Cost Production

- China has been the most favored FDI destination in recent years; cumulative FDI from 1991 to 2008 amounts to ~US$ 840 Bn
- In 2007, China attracted ~US$ 92 Bn FDI; 2% of global FDI
- More than 50% of FDI is in the manufacturing sector (including textile & apparel)
- China has a complete ‘Open Door Policy’ and has developed state-of-the-art infrastructure
Bangladesh Offers Low Cost Production.

- The cumulative FDI in Bangladesh from 1998 to 2008 amounts to US$ 6.5 Bn
- 16% of FDI is in the textile sector, amounting to ~US$ 1 Bn
- 75% of the country’s export earnings come from textiles and apparel
- Readymade garment exports increased from US$ 643 Mn in 1990, to US$ 12 Bn in 2008
- This has been possible due to the proactive role of the government and trade associations

India’s case is similar to that of China. India is in a unique position to offer both a substantial and fast growing domestic market and a country rich of resources required for low cost production. In sum, investing companies have been motivated to enter into collaborations with host country firms due to increasing gains that can be made by producing brands in the host country and selling them into the host country market. Host country companies have been motivated by the scope for gaining technical and marketing expertise from foreign partners.

FDI in India: Current Scenario

Due to India’s recent liberalization of its foreign investment regulations, the country has become one of the fastest growing destinations for FDI inflows. India offers many advantages for foreign investors like strong economic growth leading to increased buying power by the middle class, low wages, and an educated work force. India’s Special Economic Zones (SEZs) attract foreign investment by providing tax incentives, assistance with bureaucratic and administrative problems, and access to reliable infrastructure.

Indian economy is growing at the rate of in excess of 6% per annum since last 10 years. Even in times of recession / slowdown in most of the developed economies, India is expected to maintain this level of growth. From 1990 to 2007, India’s GDP has grown at an annualized rate of 8% which is second only to China among present trillion dollar economies.

From August 1991 to March 2009, India has attracted a total FDI of US$ 106 Bn, of which approximately US$ 90 Bn was invested during Apr ‘00 to Mar ‘09.

Extending its liberalization policies to other industries, India also raised the level of foreign equity ownership permitted in civil aviation, refineries, some mineral mining, construction, industrial parks and commodity exchanges in January 2008.

In the textile and apparel sector, 100% FDI is allowed under the automatic route. FDI in sectors to the extent permitted under automatic route does not require any prior approval either by the Government of India
or Reserve Bank of India (RBI). FDI inflows for this sector account for about 1% of the total FDI inflows to the country.

Though the textile and apparel sector is considered as the sunshine sector of India, till date only 1% of total FDI inflow has come in this sector.

However, given the advantages that India offers as an FDI destination, specific to textile and apparel sector, it is a matter of time that major Textile and Apparel Transnational Corporations (TNCs) recognize the real potential of India in this sector and significant investment follows. After China, India is the second most attractive destination for FDI in textile and apparel sector, other than South Asian countries of Bangladesh and Vietnam. These are the countries where the FDI and textile and apparel exports have seen a major growth. The primary reason for major investment in other countries has been duty free access to major markets, a parameter on which India ranks way behind. In order to achieve the projected growth of textile and apparel sector, it becomes still more important to make efforts to educate the international investing community about the merits of investment in India.

An Attractive Destination for Investment

There are many factors that make India an attractive destination for foreign investment in textile and apparel industry. These are listed below.

- **Vertically Integrated:** To begin with, the Indian industry is amongst the very few in the world that is truly vertically integrated from raw material to finished products (from fiber to retail).

- **Broad Range of Products:** Although cotton has the largest share (around 58% of mill consumption), Indian industry has over the years steadily diversified its raw material base to include man-made fibers such as polyester, viscose, acrylic, polypropylene etc. (accounting for around 39% of raw material consumed), as well as other natural fibers (including silk, wool, linen etc.).

- **Production Capacity:** India has one of the largest textile production capacities in the world which continues to grow and modernize. The capacity in spindles in the mill sector increased from 35.9 Mn in 2007 to 38.4 Mn in 2008. The number of shuttle-less looms rose to ~20,000 in 2008 from 16,600 in 2007.

- **Fabrics:** The Indian weaving and knitting base today includes products as diverse as fine dress fabrics, shirting, worsted suiting, denim, fleece, jersey, flat / woolen knits, technical fabrics etc. Much of this diversification of fabric product base has occurred in the last 10 to 20 years as domestic consumption patterns have changed as well.

- **Value Addition:** In apparel, far beyond the embroidered, beaded or sequined dresses in women’s wear and bleeding madras shirts in menswear that so typified India’s image in the past, India produces active
sportswear, weather-proof outerwear, foundation garments, suits, socks, infant wear and a whole host of other products for all ages. Production of made-ups includes a wide variety of bed, bath and table linen, kitchen accessories, etc.

- **Flexibility:** In addition to this, the industry has consistently remained flexible in terms of production quantity and lead time. While typical production runs are governed by fabric color minimums, India presents the possibility of producing quantities as low as a few hundred pieces. This capability is especially critical in an unpredictable market where retailers and brands are looking to source ever-smaller quantities of product, increasingly closer to the season.

- **Cost Advantage:** Certainly, an abundant low cost base of labor has been one of the Indian industry’s advantages. Research works by organizations like Kurt Salmon Associates, Werner among others have highlighted India’s cost advantage, as well as the long-term sustainability of this advantage.

What is more important is that, among this abundant workforce, the fabric or garment-making skill is very high as entire communities have participated in the trade and sustained and refined workmanship. It is this existing base of needlecraft that has enabled the Indian industry to retain its position as one of the key suppliers of apparel and textiles, and also add new products to its portfolio by rapidly learning the techniques.

- **Specialists:** Also, building on top of the textile engineering base which began in the 1950s, the 1990s have seen growth of “fashion management” studies, including marketing and merchandising, garment manufacturing technology, design management, fashion communications management etc. Simultaneous growth of the organized branded market within India, as well as the entry of larger companies sourcing from India, has given these fashion management graduates the playing field on which to further hone their skills, and provide a pool of management talent to Indian as well as global companies like Gap, Target, JC Penney, Nike, Reebok, Tesco, Next, Asda, Wal-Mart etc.

In addition to the advantages offered by the Indian textile and apparel sector, the government has been very proactive in developing investor friendly policies and several other initiatives:

- **Foreign Investment Policy:** Foreign investment is permitted in virtually every sector, except those of strategic concern such as defense and transport. Foreign companies are permitted to set up 100% subsidiaries in India. No prior approval from exchange control authorities RBI is required, except for certain specified activities. Under current policy, FDI can come into India in two ways:

  » **Automatic Route:** FDI in sectors/activities to the extent permitted under the automatic route does not require any prior approval either by the Government or RBI. The investors are only required to notify the proper regional office of the RBI within 30 days of the receipt of inward remittances and file the required documents with that office within 30 days of the issue of shares to foreign investors.
Prior Government Approval Route (for both foreign investment and foreign technical collaboration): In the limited category of sectors requiring prior government approval, proposals are considered in a time-bound and transparent manner by the Foreign Investment Promotion Board (FIPB).

FDI in Special Economic Zones (SEZ)/Export Oriented Units (EOU)/Industrial Parks: FDI up to 100% is permitted under the automatic route for the establishment of SEZ. Proposals not covered under the automatic route require approval by FIPB. FDI up to 100% is permitted under the automatic route for setting up 100% EOU, subject to sectoral policies. FDI up to 100% is permitted under the automatic route for the establishment of industrial parks.

Repatriation of Investment Capital and Profits: All foreign investments are freely repatriable except for cases where NRIs choose to invest specifically under non-repatriable schemes.

Important Labor Rules/Regulations Applicable in India: Under the Constitution of India, labor is a subject in the “concurrent list”, under which both the central and state governments are competent to enact legislation subject to certain matters being reserved for the centre. There are several important Labor Acts since 1952, which are highly protective of labor.

Policy on Intellectual Property Rights: India is a signatory to the agreement concluding the Uruguay Round of GATT negotiations and establishing the World Trade Organization.

Taxation Policy in India and Tax Incentives: India is moving towards a reform of its tax policies and systems to facilitate the globalization of economic activities. Tax holidays are available in SEZs set up to make industry globally competitive. Infrastructure sector projects enjoy special tax treatment and holidays. Since 31st March, 2004, a user-friendly tax administration has been introduced with round-the-clock electronic filing of customs documents. Foreign nationals working in India are generally taxed only on their Indian income. Income received from sources outside India is not taxable unless it is received in India. Further, foreign nationals have the option of being taxed under the tax treaties that India may have signed with their country of residence. India has entered into Double Taxation Avoidance Agreements with 65 countries including the U.S., U.K., Japan, Germany, and Mauritius. Though the Indian government gives different kinds of investment incentives, major incentives are given in the form of tax exemptions on profit from the development and operation of infrastructure projects including power.

Overall, FDI in India is allowed in all sectors except the following four: retail trading (except for single brand product retailing), atomic energy, lotteries, gambling and betting. In all other sectors, it is allowed with different equity limits ranging from 26% to 100%. The FDI environment in India has undergone a sea change since the inception of economic reforms in 1991. India’s strengths as an investment destination rest on strong fundamentals, including a large and growing market; world-class scientific, technical and managerial manpower, cost-effective and highly skilled labor, an abundance of natural resources, a large English-speaking population and an independent judiciary.

Key Imperatives for Future

India is well placed in the global map, right behind China which undoubtedly is the best destination for FDI as of today. However, there are still a lot of measures which can be undertaken by the Government of India to improve its’ position even further. Some of these measures are:

• Improved Marketing: India needs to approach investors with better marketing plans in terms of projecting India as a major hub for investment. Road shows/conferences should be held in various countries to highlight India’s strengths and investment attractiveness. Emphasis on the fast growing and evolving domestic market, industrial growth and key benefits for textile and apparel industry in India need to be communicated clearly as part of marketing efforts. Considering that the western markets are maturing, India is still one of the very few countries with untapped potential for entry and expansion of leading global brands and retailers.
• **Increased Scale**: India should develop large scale industrial zones (area > 100-200 sq. kms.) with all the facilities and business friendly environment in place. Although many SEZ’s and Integrated Textile Parks (ITPs) have been planned on similar line, there needs to be faster development on these areas and scale needs to be increased for these zones so as to establish entire supply chain for various textile activities.

• **Ready Made Infrastructure**: Industrial zones in India should approach foreign investors only after establishment of all support infrastructures and with proper homework in terms of incentives / benefits, well laid out and definite plans and offerings to the investors.

• **Single Window Clearance**: At the implementation level, the government needs to devise a mechanism to have single window clearance and single approval for all aspects of starting a business. This would go a long way in reducing the time taken for starting business in India and encourage investors to look at India as a favorable investment destination.

• **Clearance of Applications**: Application clearance under the Incentive schemes like Technology Upgradation Fund Scheme and speeding up the process of establishing Free Trade Agreements with European Union would also help in attracting European investors to invest in India.

• **Investor Friendly Environment**: There needs to be a major drive undertaken to reduce red-tape and bureaucracy in the system. A more investor friendly environment needs to be built to add to all the existing inherent strengths of the Indian textile industry. On the annual Corruption Perception Index, India’s score has remained the same for two consecutive years at 2.7. In the same period Pakistan improved from 2.3 to 2.6 and China from 3.1 to 3.5. The higher the score, the less corrupt is the country.

**Conclusion**

India is poised to become an even bigger participant on the global front, both as a consumer and as a producer. The large domestic market is very attractive and as a base for the low cost production is a combination not offered by many nations at this point of time. However, in order to become a leading FDI destination in the textile and apparel sector, a lot needs to be done. The Government needs to work on a focused ‘Pull Strategy’. The way ahead is to identify and highlight the key strengths, the available resources and the large growing domestic market through focused marketing efforts.

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Building Operational Efficiency in Healthcare Delivery

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Overview

With the turn of the century, the dynamics of work, health and life have undergone a sea change. Every sphere has seen growth and opportunities in leaps and bounds with newer and better ways of doing things and also doing altogether newer things. The emphasis is shifting towards improving efficiency, precision and reducing time and cost.

Although this wave of change has swept across every industry, such dynamism and corporatization has completely changed the face of the healthcare industry. While there are an increasing number of patients, there is also an ever-increasing disease profile and burden. The disease pathway has become much more complex and not just limited to diagnosis and treatment. On the other hand, the implementation of information management systems has made the operation and administration of a hospital more professional and business-like.

Over the last decade input costs have gradually increased, however due to increased competition Healthcare Providers are unable to pass this burden onto patients in the same proportion. This presents Hospital Administrators with a complex task of not only streamlining existing operations but also providing flexibility for future changes in the business model. Hence, now more than ever, with rising demand and unprecedented growth of the sector, there is a growing need to come up with newer models to improve operational efficiency and make processes, infrastructure and our outlook to management more lean and specific.

From the softer skills of Customer Relationship Management (CRM) to the core activities of Revenue Cycle Management (RCM), hospitals are undergoing a complete overhaul of how they do business and more importantly focussing on ‘who they do business for’.
Changing Healthcare: ‘The Toyota Way’

Changing market dynamics and consumer attitudes are forcing companies to redefine their business models. With growing competitive pressures and rising input costs, they recognize the need to restructure, redefine, redevelop and constantly improvise.

While there is no standard formula to do the same, hospitals have improvised and developed their own USP models. However, over the years the challenge that still remains is to reduce the cost of care or keep it constant for the patient while progressively increasing the parameters of quality, accessibility and affordability.

Some innovative practices adopted by hospitals to reduce the costs and improve on the throughput:

- A popular ‘for-masses’ Indian hospital charges different fees for diagnostic services at different times of the day. They have been able to increase patient volumes by differential pricing. Therefore, while an MRI/CT scan may cost up to US$ 100 (~INR 5000) for a person choosing to get it done in the day, a poor person can get the same for US$ 10 (~INR 500) at 2 a.m. in the night. More and more hospitals are making an attempt to bridge the socio-economic gap in healthcare delivery through such practices.

- To streamline operations, use of ‘Case Process Maps’, wherein the activities of all the staff involved in a procedure are mapped and time plotted allowing the variations to be studied and corrected. This helps to cut out redundancy and errors while improving accuracy and efficiency.

Many hospitals are adopting the classic Japanese Process Improvement Triad as shown. Activities such as re-organization, value mapping and best practices are designed to help implement these principles.
Another example is the innovative restructuring and transformation brought about on these very principles by the Virginia Mason Medical Center (VM) in Seattle.

Virginia Mason, a 336 bed hospital present in 9 locations and employing over 400 physicians and 5000 employees in 2000, was undergoing a period of organizational lethargy. In a bid to bring greater efficiency and vitality to their institution’s operations, the senior administration designed a hospital-wide program called the Virginia Mason Production System and successfully ‘leaned’ various arms of the hospital. At the heart of the system were Rapid Process Improvement Workshops (RPIWs) with VM having inculcated over 500 of them. These workshops essentially redesigned the job descriptions of physicians and front-line staff as described below:

The system aims to go to the root cause of a problem involving all the levels of hierarchy concerned. Each task is graphically represented through boxes showing the process flow and time allocated. A copy of this is displayed on the wall and observed from time to time to identify the missing links and areas requiring improvement through Rapid Process Improvement Workshops (RPIWs).

These workshops are conducted over five working days and change is implemented the following Monday.

Also there are monthly, bi-monthly and 90-day audits to further improve and regulate work-flow. This approach helps in identifying and correcting problems in real-time.

Exhibit 4

An example of a RPIW Chart tracing movement or footsteps of staff while on duty. The colored lines represent different nursing and paramedical staff movements.

Exhibit 5

Results Achieved

<table>
<thead>
<tr>
<th>Results:</th>
<th>In two years ('02-'04)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Savings in budgeted capital</td>
<td>US$ 12 Mn to US$ 15 Mn</td>
</tr>
<tr>
<td>Reduction in staff walking distance</td>
<td>38%</td>
</tr>
<tr>
<td>Reduction in travel distance of supplies</td>
<td>77%</td>
</tr>
<tr>
<td>Saving in inventory</td>
<td>50%</td>
</tr>
<tr>
<td>Reduction in lead time</td>
<td>53%</td>
</tr>
<tr>
<td>Gain in productivity</td>
<td>44%</td>
</tr>
</tbody>
</table>

The system also promotes the concept of ‘kaizen’ which is continuous incremental improvement.

By going the Toyota Way, Virginia Mason Hospital showed how work-flow optimization techniques were appropriate for universal application. Some of the improvements they observed in just two years are illustrated in the Exhibit 5.

Most of these radical overhaul methods do not require huge investments or manpower. These learnings can be replicated in Indian hospitals to result in significant savings and quality healthcare for all.
Customer Relationship Management (CRM) is a method for an organization to track, maintain and organize a database of its current and prospective customers. In the healthcare sector, there is a wide difference between the customer and the consumer. While an ill patient is the consumer, a doctor prescribing medicines is an essential customer. Hence, there is a series of relationships that need to be nurtured and managed to enhance patient retention.

CRM is increasingly being applied in the healthcare industry in the following ways:

• The consumer or patient in healthcare is not one, essentially by choice. Apart from the illness, the consumer finds himself dealing with financial burdens, anguish of medical procedures along with the ongoing mental agony. Here the intervention of an active CRM goes a long way in building patient confidence and goodwill. It eventually becomes a deciding factor for the patient while choosing a hospital again. Customer satisfaction is one of the major drivers of repeat business.

• Another important consideration is that in a hospital, the patient comes in contact with the entire series of touch points, right from the receptionists, doctors, nurses, paramedics, to the administrative personnel. So in an active CRM programme it is necessary to train every member of the hospital in providing quality care and service to the patient. It also plays an important role in retaining a patient.

• The adage that the cost of efforts undertaken to retain a customer is ten times lesser than that of acquiring a new one, still holds true. The mathematical parameter of Customer Lifetime Value (CLV), where financial
• gains are defined in terms of customer relationship, is of great significance here with service being the key differentiator.

• Medical Tourism: Today healthcare has become global. India has a growing number of international patients and more and more hospitals are rushing to upgrade their services, infrastructure and most of all their technologies. The service they provide and the follow-up, all contribute to a growing number of patients returning for new treatments.

As depicted in Exhibit 7, even if CRM fills 50% of its cancelled appointments i.e. 30 appointments, it is equal to US$ 93,750 in savings. CRM program also promotes optimal utilization of the deployed resources.

A new method making use of database marketing is proving to be very profitable and insightful wherein a specific customer is targeted for advertising on the basis of previous consumption and usage trends. A comprehensive database of all present customers, possible suspects and prospects is maintained. This method gives direction, flow and individualism to marketing which in turn results in huge cost savings and increased footfalls as the mode and message of advertising for women in child bearing age group is drastically different from, say, a sixty- year- old retired man.

Some Industry Illustrations

Perhaps the most important application of CRM is in disease prevention. It has been estimated that if patients are recommended preventive health check-ups on the basis of their past medical history, 90% of them are likely to come in for a check-up.

<table>
<thead>
<tr>
<th>Exhibit 7</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of appointments / day</td>
</tr>
<tr>
<td>Total number of working days</td>
</tr>
<tr>
<td>Average consultation charge</td>
</tr>
<tr>
<td>No-shows</td>
</tr>
<tr>
<td>Revenue lost</td>
</tr>
</tbody>
</table>

* For a 200 bedded Specialty hospital

Tenet Healthcare Corporation (hospital chain in the United States) analyzed their US$ 60 Mn marketing expenditure for a particular division and realized that they were spending 75% of it on non-directional media advertising.

Customer Potential Management Corp. (CPM), a healthcare marketing firm, uses Neural Network Technology (an artificial intelligence tool) to sort prospects by service line, e.g. cardiology, oncology. They also use several insightful indices such as Consumer Healthcare Utilization Index (CHUI) and Patient Disease Index (PDI) which help them to identify which customer is most likely to need which service and when.

Although CRM has been adopted by numerous industries across India to yield dramatic results, the Healthcare sector is yet to realise its full potential and use it as a powerful tool to aid patient retention.
Hospital Revenue Cycle Management

Less than 10% of the Indians are estimated to be covered under some sort of health insurance. Most patients pay for their hospital expenses directly. Today, in most hospitals in metro cities, over 50% of patients have some form of third-party reimbursement plan. Failure to realise this could seriously affect the working capital of a hospital.

For this purpose hospitals worldwide are looking at options to optimize as well as maximize the amount and speed of patient revenue collection.

The hospital revenue cycle has 3 major components:

- **Front-end**: From the time the patient comes in first contact with the hospital to registration
- **Core**: Provision of actual healthcare services
- **Back-end**: Billing and discharge of the patient

Improvement in Hospital Revenue Cycle Management cannot be achieved instantly by merely installing new technology. It involves a careful blend, integration and organization of the necessary people, processes and technologies.

Some of the drivers of an efficient and effective revenue cycle include:

- Strict accountability
- Standardization
- Monitoring & measurement
- IT implementation
- Integration of processes

Exhibit 8

**Standard Revenue Cycle with Activity Analysis**

- **Front-end**
  - Collection and recording of cash received
  - Contractual allowances
  - Appointments Scheduling
    - Registration
    - Patient information collection
    - Information verification
    - Insurance validation
  - Registration
    - Computing the deductibles and co-payments
    - Public health insurance program counselling
  - Clinical documentation (used in the billing process and communicated to third-party payer)

- **Back-end**
  - Follow up for outstanding payments/accounts receivable
  - Denial management

- **Core**
  - Billing and collection
    - Claims review, approval and denial along with insurance company
  - Charge capture into Hospital Information System (HIS)
  - Diagnosis and procedure coding
While managing a hospital revenue cycle, the following ought to be kept in mind:

- **Payment collection**: Hospitals can optimize revenues by putting in place a defined process for collecting payments from patients either at registration or at day end.
- **Third-party payers**: Absence of standard protocols leads to ambiguity which causes complexity in the matter and delays.
- **Follow-up**: Hospitals need to have an agile follow-up system to ensure timely payments.
- **Denial management**: This involves sorting out circumstances which led to claim denial. They can vary from failure on part of patient to adhere to standard procedures or clinician confusion with respect to treatment.
- **Healthcare is witnessing a transition from Out-of-pocket spending towards Corporate and Third-party Payments. As a result, Hospital Revenue Cycle Management will become a critical factor in determining the financial health of the providers.**

### Exhibits

**Exhibit 9**

**What to look out for:**

- Outstanding revenues that exceed the industry average
- Receivables in excess of 30% of revenue
- Increase in bad debts as % of revenue
- Lack of Working Capital

**Exhibit 10**

**Some of the Best Practices**

**Registration**

- Collection of all necessary demographic data for scheduled patients
- Defined prerequisites
- On-line alert indicators
- Regular tracking and monitoring

**Payment collections**

- Standardized policies, procedures and employee training
- Optimal utilization of IT
- Electronic claims-submission

**Denial Management**

- Denial tracking
- Case reviews
- Documentation of all interactions

---

Average collection period = \( \frac{\text{Net amount receivable} \times 365}{\text{Net patient revenues}} \) (Measured as days in net accounts receivable)

A shorter average collection period implies that the hospital receives faster payments from the insurer.
In India, barring a few private hospitals, all records are maintained in physical form. Each patient has a unique clinical history and their own sets of tests and records which are necessary to be recorded and filed for future reference. Such a scenario poses a daunting challenge for every member of the healthcare delivery team. Even if storage is possible, the crux of the problem is fast retrieval of patient’s medical data at vital times.

Also if a patient’s records are filed in one hospital, for a cross referral check or an opinion at a second hospital, the patient has to go through the entire process of documentation and testing again adding to his financial distress.

Electronic Medical Records (EMRs) eliminate the burden of tedious paperwork occupying much of the physician’s quality time. They serve as a comprehensive database of the patient’s entire history, but they are also very user-friendly as they help to locate relevant data instantly when needed across multiple locations and point of times. Providing instant portability they also prove useful in other supplementary fields such as liaisoning with the insurer, tracking public health as well as administrative roles of auditing.

**Exhibit 11**

<table>
<thead>
<tr>
<th>Advantages of EMR</th>
</tr>
</thead>
<tbody>
<tr>
<td>Continuity in treatment</td>
</tr>
<tr>
<td>Safe with authorised viewership</td>
</tr>
<tr>
<td>Vital information at vital times</td>
</tr>
</tbody>
</table>

**National Health Service (NHS)**

UK’s public healthcare system is a pioneer in implementing electronic records. Apart from the obvious benefits, confidentiality is maintained at every level by providing Smart Cards to physicians limiting their access to only relevant areas of the record.

In the United States, the Department of Veterans Affairs (VA) has the largest enterprise-wide HIS that includes an EMR system, known as the Veterans Health Information Systems and Technology Architecture (VistA). VistA imbibes an Imaging System which provides comprehensive database including specialties such as cardiology, radiology and orthopedics. A graphical user interface known as the Computerized Patient Record System (CPRS) allows physicians to review and update a patient’s EMR at any of the VA’s facilities. CPRS allows the providers to place orders, indent medications, special procedures, x-rays, patient care nursing orders, diets, and laboratory tests.
While on first glance the benefits and ease make the system of digital records seem like a complete winning proposition there are however some roadblocks to its implementation such as:

- Heavy initial investment
- Low acceptability
- Confidentiality & privacy concerns
- Lack of global uniformity
- Low adoption rate: It is estimated that less than 30% of U.S hospitals have adopted electronic records

EMRs, though requiring significant investment, represent the way forward to create a much needed centralised database. While most corporate hospitals in India have started implementing EMR, the smaller hospitals would require significant assistance and financial support.

Many companies like Google, have innovated and taken technology a step further by coming up with a whole range of medical technological applications such as predicting epidemic trends and also making healthcare advice available on cell phones.
Facility Planning: Role in Performance Enhancement

In recent times, patient expectations and demand for quality healthcare facilities in India have undergone a transformational shift. However, hospitals of yesteryears were neither planned to accommodate future growth nor to provide the care and service standards that are expected today.

Over time as demand grew, so did hospitals. However, this growth was accretive in nature and the ad hoc additions or extensions resulted in various trade-offs, leading to operational inefficiencies and compromised functionality.

In today’s changing environment, as hospitals look to improve their performance, they should take into account various design parameters that can result in direct or indirect economic benefits. Some of the parameters that can lead to operational efficiencies and thereby, cost savings are:

- Patient monitoring
- Patient flow
- Nurse travel distances
- Standardization

A large part of a patient’s ‘length of stay’ is spent under critical or post surgical care, where constant patient observation and monitoring is essential. In this stage, patients are extremely vulnerable and response times become very important. For smooth recovery of patients, it is essential that staff be able to respond to the clinical need of the hour. For this, patients should be under direct nurse observation at all times.

This can be achieved in many ways, one of them through an appropriate layout that allows staff to observe, manage and attend to patients constantly. A C-shaped patient care unit with 8 to 10 bed management unit size is considered good.

A large percentage of patients follow a well established and clear patient pathway during a hospital visit.

Good alignment of a patient’s physical journey with his or her clinical journey can lead to better and quicker delivery of care. Patient flows should
therefore be streamlined to avoid constant backtracking and cross-overs. These not only lead to confusion and chaos, but also issues of infection. At the same time, high volume traffic, restricted traffic and after hours departmental needs should be kept in mind.

Given the complexity of healthcare environments, overlaps in patient movement cannot be completely avoided. However, all efforts should be made to minimize them.

Nursing care forms one of the most important components of patient care during hospital stay. Nurses spend an unbelievably large part of their time walking from room to room, attending to patients. Long corridors and inefficient planning contribute to making travel time for nurses significant.

Good travel distance planning leads to better operational efficiency as nurses are able to respond to patient’s clinical needs and any emergency calls in a timely manner. In addition, it results in less staff fatigue and more staff satisfaction.

One of the design strategies to address the issue of travel time is decentralized nursing stations. However, it is important to strike the right balance between centralization versus decentralization. To what extent should nurses’ work area be decentralized? What should be the overall patient unit layout in order to optimize resources as well as minimize travel distances for staff?

While there is no universal answer as different organizations have different models of care, the thumb rule of an 8 to 10 patient bed management unit is a good starting point.

New construction for healthcare is increasingly looking at standardization as a means to achieve operational efficiency.

Standardization helps in optimizing use. If various rooms are equipped to handle multiple types of procedures, the overall utilization is more efficient. In case demand outweighs planned capacity for different procedures, standardized rooms can help in accommodating the additional patient/case volumes.
In addition, standardization also helps in reducing medical errors. For instance, in same handed patient rooms, familiarity with layout and location of equipment and drugs allows staff to respond faster and better and work more efficiently.

A little intervention and thought at the planning stage can lead to long-term tangible and intangible benefits for an institution. With better planning, more efficiency can be achieved with the same doctors, the same service and the same staff.

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Re-connecting with the Consumer

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Financial results for the most recent quarter seem to confirm that the worst is behind for most companies including those that are engaged in consumer interfacing businesses. The recovery in consumer spending is visible across almost all the sectors including automobiles, consumer electronics and durables, information technology and communication, apparel and footwear, and leisure and entertainment. Major organised retailers too, even though collectively modern retail still accounts for no more than 5% of total consumer spending in India, are reporting a rise in same-store sales data. There are laggards and poor performers in each of these sectors, of course, but that is always to be expected in good times as well as not so good times.

With the scare of deficient monsoons somewhat mitigated in recent weeks, and with an early festive season this year, the prospects for growth in consumer spending look promising for the coming quarters. Does this imply that it would be back to the heady days of the recent past when the Indian consumers’ optimism about spending was at an all-time high and just about every manufacturer and marketer could expand their capacity very aggressively? The answer is no.

While India’s own gross economic data may not reflect a serious impact of the recent global economic meltdown on India, the ripples have affected India and Indian consumers very perceptibly and it is quite likely that the Indian consumers’ behaviour would have undergone a subtle but fundamental change in just these few quarters. There are several global consumer trends that seem to be applicable to the Indian consumers too, notwithstanding their very different demographic profile compared to the rest of the world. The first key trend is the ‘shift to thrift’ and a redefinition of what constitutes “value” in the mind of the consumers. While consumption in terms of volume is still steadily increasing, consumers want to save money everywhere and hence, are seeking lower-priced, acceptable-quality options all around, be it apparel and footwear, travel & leisure, food & grocery, or eating out. This trend is applicable to all income strata barring the minuscule one at the very top.

The recent economic crisis (and the fear it has invoked in India) has brought to the fore the importance of family ties. Hence, Indian consumers are already spending more time on family and home-oriented activities and thus, there are more opportunities for products and services that can be offered to the whole family such as value-priced travel and vacation packages, home entertainment, and home décor and furnishing.

In times of stress, consumers are increasingly looking for ‘small wonders’ - essentially small (low ticket size) products to perk themselves up more frequently. These need not only be related to small packs of juices and chocolates and other food products but also a host of other items including skin and body care, gifts for self, apparel, books and music etc.

Indian consumers were never really brand-loyal to begin with. They are becoming even more fickle and this trend will be one of the more enduring ones for years to come, as they seek more options both for the products and for the retail channel they buy from.

Indian consumers, like their counterparts in more advanced societies, are also exhibiting light shades of ‘green’. The trend towards becoming more conscious to the ecology and environment is going to gather momentum.

And finally, while Indian consumers were already highly socially networked, technology (mobile and internet) is making this social networking even more pervasive and powerful.
What does this mean for manufacturers and marketers of consumer goods and services? The most important message is that they must ‘re-connect’ with their consumers even if such marketers have been in business for decades. This implies investing more in understanding the consumer, accelerating product innovation and speeding up new product launches, re-engineering product attributes and the retail channel to offer more value to each consumer segment, creating better interactivity with the consumers extending beyond traditional advertising and point-of-purchase touch points, and reaching out to them/listening to them through their social networks.

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Indian Tourism: Managing Growth by Breaking Barriers

- Tourism - Growth Drivers
- Government Recognizing Tourism as a Top Priority
- Opportunities for Investment
- Looking Forward Together
Background

Travel and Tourism is an inseparable part of the world in which we live making a significant contribution to the country’s economy, as well as to the quality of life of its citizen’s.

Globally, travel and tourism, accounts for 10% of the GDP, 8% of jobs and 12% of investment annually. It also has the highest potential for growth with the industry, currently growing at more than 4% per annum with an average of 3% in developed economies and more than 7% in emerging markets. In India, travel & tourism is currently contributing 2.2% directly to the GDP and is expected to grow at 6.6% as compared to the retail industry, which despite its high contribution of 35% to the GDP, is expected to witness a growth, which is marginally higher than the hospitality sector, at 8%.

Travel makes a positive contribution to the planet and its people, assuring human contact, providing pleasure, expanding business opportunities, easing diplomatic relations and opening eyes to new horizons and perspectives. The resilience of tourism – with demand repeatedly bouncing back despite successive high profile challenges ranging from terrorism to disease – shows how keenly and widely it is appreciated by its customers. Tourism is appreciated by all – so much so that they compete for the benefits it can bring, economically, socially, and environmentally. It is helping build economies emerging from poverty, conflict and confusion. It stimulates infrastructure development, secondary economic activity and gives value to natural and built heritage that would otherwise be under threat.

Tourism – Growth Drivers

Tourism acts as a unifying force as people travelling can witness the dynamism of their own country at work and learn about their own nation. This experience helps in fostering goodwill and understanding between various linguistic, religious and communal groups living in different parts of the country.

Development of the tourism industry provides employment for many and has helped build stronger economic structures which in turn have helped in attracting international tourists and the foreign exchange they bring in. Tourism also contributes to the development of the local handicrafts and cottage industries. It is said that with every 40 Km drive from a state premise, one witnesses vast changes in the topography, the dialect, the food habit and the attire in a united and diverse India, which presents a multi-faceted tourism product ranging from 27 world heritage sites, mountains, beaches and deserts intermingled with an opportunity to experience diverse cultures and religions.

With both Indians and foreign nationals travelling within the country, the tourism industry is estimated to be worth US$ 43 Bn in 2008 with close to 612 Mn tourist visits during the year. Currently, the industry experiences a healthy growth of 17% in value terms and 14% in volume terms. Approximately 75% of the tourism spend in the country is fuelled by domestic travelers (shown in Exhibit 1).

Traditionally, mankind has been extremely inquisitive and very travel friendly, the quest for knowledge and to walk the unknown has encouraged travelers from far and wide to experience the wonderful and diverse nature of the country. Although the industry and the government have taken strong measures to boost the inflow of foreign travelers in India by effective marketing strategies, it is the domestic traveler who has contributed to the overall growth of tourism as a sector in India. The growth rates in both international and domestic travel are extremely encouraging.
The number of domestic tourists has almost doubled from 309 Mn in 2003 to 612 Mn in 2008. Similarly, the number of foreign tourist visits has doubled between 2003 and 2008.

Close to 90% of the above visits are fuelled by domestic travelers and the dependence on the foreign travelers is miniscule (only 2%) as shown in Exhibit 2.

The most important growth driver is the robust economic growth that has been witnessed in the country. India’s GDP has been growing at a rate of 6% since the liberalization of economy in 1991 and has grown over 8% in the past a few years. At 8% CAGR, India’s GDP would almost triple from US$ 1200 Bn to US$ 3500 Bn by 2023.

Currently, India is the 12th largest economy in the world in absolute terms and is expected to overtake most of the European nations in the next 15 to 20 years. It will eventually become the world’s 3rd or 4th largest economy by 2050. Despite the recent economic downturn, various industry sources still peg the economic growth at over 6%.

India’s strong economic growth has caused the GDP per capita to increase rapidly over the past 5 to 10 years. At the current rate, the GDP per capita in 2013 would be double of what it was in 2003.

More and more families are expected to leave the deprived or aspirers category (annual household income less than US$ 4200) and join India’s burgeoning middle class. By 2025, the Indian middle class is expected to constitute 46% of the Indian population. Subsequently, discretionary spends would be going up and this bodes well for the tourism sector.

In 2005, the Indian middle class was approximately 6% of the population, but is expected to constitute 46% of the population by 2025.
The tourism industry has been supported by the advent of Low-Cost Carriers (LCC) in the airline space. These low-cost carriers have brought down the cost of travel and boosted the growth of domestic air travel immensely. The advent of low-cost airlines which cut down on expensive customary in-flight passenger services has opened-up air travel for the middle class.

Exhibit 6 clearly indicates the increasing share of LCC from 33% to 47% between 2006 and 2008.

The advent of LCC has spurred domestic air travel to grow from 11 Mn travelers to close to 36 Mn travelers in the last decade. Operational airports in the country have gone up from close to 40 airports in 2004 to 81 airports at present. The airports of several metros are undergoing renovation and re-positioning.

Airline tickets, tour packages are all set to go cheaper with the 2% reduction in service tax.

State-run oil companies have slashed Aviation Turbine Fuel (ATF) prices by 7%, the 11th reduction since Sep last year.

The government is drawing up a whopping bailout package - to the tune of US$ 1 Bn for Air India. The salient features of this package would be to cut airport charges for a limited period by 50 %, to remove the 8% excise duty on ATF and to reduce the charges which the airport operator charges from the oil companies, leading to enhanced performance.

With the Airports Authority of India (AAI) installing systems like Standard Instrument Departure (SID) and Star Terminal Arrival Routes (STAR) for the first time in India at the Mumbai airport, air travel within the country is likely to become faster and more convenient. In addition, the new installation is expected to help airlines save on fuel.

**Government Recognizing Tourism as a Top Priority**

Till 2002, Indian tourism was promoted through delegates at the Indian tourist offices located globally. These promotional campaigns were not very effective as their approach was unorganized, varied, and limited by the skills and capabilities of the delegates. Realizing the need for a consistent approach, the Tourism Department of India appointed Ogilvy & Mather (O&M), Delhi, to develop a print campaign and
Enterprise Nexus, Mumbai, to create a television commercial.
In September 2002, the tourism department unveiled a new campaign called ‘Incredible India’ to promote Indian tourism globally. The first phase of the campaign, for a period of three months, was jointly funded by the Government of India and Experience India Society, an association of travel agents in India. The campaign that focused on the Himalayas, wildlife, yoga, and Ayurveda, was widely promoted in the print media, television, and the internet. The television campaign was telecasted on CNN, BBC, and other popular channels across the world.

The government has identified 37 destinations for tourism development and over the last two years, over 600 projects in 300 tourist destinations have been developed with an investment of US$ 20 Mn. Central financial assistance of US$ 1 Mn and US$ 2 Mn has been raised to US$ 5 Mn and US$ 10 Mn respectively for major destinations depending on tourist traffic.

Through many innovative branding exercises, the government has been trying to promote tourism and build awareness about India as a tourist destination – both in the domestic market and abroad. International events such as Commonwealth Games in 2010 are also expected to increase arrivals in India. It is expected that the inbound traffic is set to double to 10 Mn visitors in the wake of the Commonwealth Games in 2010.

To motivate travel agents to promote India and to familiarize them with new tourism products, the Ministry of Tourism would provide financial assistance for participation in travel marts or annual conventions. Through the India Tourism Initiative, the government plans to lease out heritage monuments which would attract tourists from all across the globe.

The government has introduced a Capital Subsidy Program for budget hotels, a 5 year income tax holiday for 2 to 4 star hotels and an exemption of fringe benefit tax for guest house facilities. Development of the ‘Home Stay’ concept and small capital subsidy for the development of budget hotels to encourage travel stay options are being made popular.

In the 9th Five Year Plan, assistance has been provided for the construction of budget accommodation, tourist complexes, wayside amenities, tourist reception centers, adventure & sports facilities, sound & light shows, illumination and refurbishment of monuments. These schemes have been merged into two schemes in the 10th Five Year Plan– integrated development of tourist circuits and product/infrastructure and destination development.

The central government has introduced a scheme for assisting large revenue generating projects: Projects like tourist trains, cruise vessels, cruise terminals, convention centers, golf courses etc. would qualify for assistance. While considering projects for grant-in-aid under this scheme, priority will be given to projects promoted by private sector and the projects with public private partnership (PPP).

A scheme of capacity building for service providers has been introduced and under this scheme the institutions are conducting training at the Institutes of Hotel Management (IHMs) for the faculty and students.

Uttarakhand State Government has announced 100% tax exemption for a period of 3 years to multiplex projects in the state and for 5 years to all new amusement parks and ropeways. Similarly, Rajasthan Government has reduced luxury tax from 10% to 8% for all hotels. Other states like Kerala, Gujarat, Madhya Pradesh and Orissa are promoting themselves through the introduction of destination promotion coupled with PPP.

The government is investing heavily on the infrastructure in the country. In the 11th Five Year Plan, investment towards modernization of highways, development of civil aviation, irrigation systems, ports, railways, telecom and power will be to the tune of US$ 472 Bn. In addition to the above, investments to the tune of US$ 91 Bn have been planned in other infrastructure sectors like tourism infrastructure, urban
infrastructure, rural infrastructure, SEZs, and water sanitation infrastructure, thus making a total of US$ 563 Bn worth of infrastructure investments in the 11th Five Year Plan period. This investment in infrastructure will boost tourism potential over the next decade.

Technopak conducted a survey to understand and identify the key recommendations to the government and the industry, where the key priority areas for domestic and international tourists were identified. The findings of the survey over the random sample are quite in line with some of the government initiatives being taken.

As per the survey, the following were the responses towards the most important motivator for visiting a tourist destination:

- For 59% of the respondents, it is the infrastructure (roads, public utilities, bus stand, taxi services, railway stations and airports)
- For 40% of the respondents, it is the overall hygiene conditions at a location
- For 31% of the respondents, it is the availability of information, booking and services (guides, tourist information)
- For 29% of the respondents, it is the easy connectivity to the city (frequency of flights/trains/buses)
- For 28% of the respondents, it is the hotel stay (room availability, budget category hotels and quality)

When interviewed, most Indian travelers mentioned the infrastructure within the city and overall hygiene as the biggest need gaps for tourism within India.

**Niche Tourism Products**

The growing concern worldwide over global warming and climate change combined with rising oil prices, the energy crisis and the economic slowdown has led to dramatic changes in consumer attitudes, travel seasonality and other travel patterns and trends. It is influencing individual choices regarding travel destinations, the length of trips and other factors such as the availability of environment-friendly modes of transport and environmentally-responsible service providers.

World travellers are also increasingly looking for quality products and experiences that offer value for money, especially environment-friendly travel and tourism related products and services as well as those that enable them to take part in local community activities.

The Ministry of Tourism recognizes the significance of these shifts in lifestyle preferences and travel trends. By keeping pace with the latest trends in global travel, this strengthens India’s global image as a dynamic and relevant ‘brand.’

**Initiatives at State-level with Involvement of Locals:**

States are taking initiatives in teaming with locals to provide a flavor of their culture and traditions. Some of the key initiatives are mentioned below:

**Himachal Pradesh:** The Himachal Government has introduced a scheme - ‘Himachal Pradesh Home Stay Scheme 2008’ under which tourists are given the opportunity see the rural areas of Himachal and enjoy their stay in comfortable home-stay accommodations.

**Gujarat:** Through the ‘Vibrant Gujarat’ programme, the Gujarat Government plans to actively market the tourism sector. With a 1,650-km coastline, the state has plans of developing beaches in regions like Kutch and Mandvi.

**Madhya Pradesh:** The Government of Madhya Pradesh is keen to initiate the development of an artificial beach in the state. The concept is based on ‘Ocean Dome’ artificial beach in Japan. The total investment for the project is estimated around US$ 440 Mn.
Kerala: Kerala has introduced innovative tourism initiatives. Two of its villages, Aranmula and Kumbalangi, are being promoted as tourist destinations in a big way as part of the ‘Endogenous Tourism Project’ of the United Nations Development Programme and Government of India. Another concept called ‘Home Stays’, plans to promote rural tourism. The ‘Dream Season’, is another scheme wherein the Kerala Tourism Development Corporation has coordinated with most hotels to offer economical packages. Besides this, the Kerala Travel Mart which is a bi-annual event showcasing the best of Kerala is the only tourism mart in the subcontinent that brings together the business fraternity and entrepreneurs behind the tourism products and services of the state.

Rajasthan: Rajasthan has a developed tourism infrastructure, with close to 6,000 hotel rooms spread over more than 150 hotels. Of these, over 1,400 rooms (54 hotels) belong to the heritage category. Tourism Department has estimated that investment of over US$ 600 Mn is required in the tourism industry in Rajasthan over the next 10 years. It is estimated that the private sector’s share of investment can be up to US$ 200 Mn.

Andhra Pradesh: Andhra Pradesh has about 18 projects lined up under various categories such as temple circuit development, eco-tourism projects, adventure tourism and rural tourism projects with a significant investment by the central and state government. The tourism department is developing the temple circuit of Tirupati and surrounding regions with an investment of US$ 9.5 Mn.

The Ministry of Tourism is also officially promoting the following tourism circuits and looking forward to develop more with the private sector. Exhibit 8 represents key tourist circuits in India.

Exhibit 8

<table>
<thead>
<tr>
<th>Tourist Circuits in India</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>The Golden Triangle</strong></td>
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<tr>
<td>Delhi, Agra &amp; Jaipur</td>
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<tr>
<td><strong>The Desert Adventure</strong></td>
</tr>
<tr>
<td>Jodhpur, Jaisalmer, Bikaner &amp; Barmer</td>
</tr>
<tr>
<td><strong>The Heart of Heritage</strong></td>
</tr>
<tr>
<td>Gwalior, Orchha, Khajuraho</td>
</tr>
<tr>
<td><strong>The Buddhist Circuit</strong></td>
</tr>
<tr>
<td>Sarnath, Kushinagar, Bodhgaya, Nalanda, Rajgir, Vaishali, Sanchi, Amaravati &amp; Nagarjunakonda</td>
</tr>
<tr>
<td><strong>The Great Pilgrimage</strong></td>
</tr>
<tr>
<td>Prayag, Varanasi, Puri &amp; Konark</td>
</tr>
<tr>
<td><strong>The Beaches of India</strong></td>
</tr>
<tr>
<td>Goa, Dha, Mormugao, Mamallapuram &amp; Gopalpur-on-Sea</td>
</tr>
<tr>
<td><strong>Adventure Sports</strong></td>
</tr>
<tr>
<td>Srinagar, Manali, Kulu, Thar Desert, Satiska, Mount Abu, Fateh Sagar, Dal Lake, Shivalik &amp; Ooty</td>
</tr>
<tr>
<td><strong>The Temple Trail</strong></td>
</tr>
<tr>
<td>Kanchipuram, Madurai, Trichurpalli, Kanyakumari, Bhadra Swami, Puri &amp; Konark</td>
</tr>
<tr>
<td><strong>Religion in Stone</strong></td>
</tr>
<tr>
<td>Belur, Halebid, Mysore &amp; Hassan</td>
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<tr>
<td><strong>Backwater of Kerala</strong></td>
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<tr>
<td>Alappuzha &amp; Kumarakom</td>
</tr>
<tr>
<td><strong>Island Holidays</strong></td>
</tr>
<tr>
<td>Andaman, Nicobar &amp; Lakshadweep</td>
</tr>
<tr>
<td><strong>The Lure of the Jungle</strong></td>
</tr>
<tr>
<td>Corbett, Jim Corbett, Bandhavgarh, Sariska, Rathnambhore, Bharatpur, Pench, Bandipur, Sasan Gir, Kaziranga &amp; Manas</td>
</tr>
<tr>
<td><strong>The North East</strong></td>
</tr>
<tr>
<td>Gangtok, Guwahati, Shillong &amp; Kohima</td>
</tr>
</tbody>
</table>

All forms of tourism coupled with their respective circuits are divided into the following niche products of tourism.

**Culture, Heritage and Ethno-Tourism**

Chhattisgarh, amongst other states has identified and is developing ethnic villages. The private sector is also being encouraged for proper maintenance and professional site management of important heritage sites/monuments.

Traditional festivals like Dusshera at Bastar, Madai at Dantewada and Narainpur are to be marketed for domestic and global exposure.

The number of domestic tourists visiting heritage sites has increased from 19 Mn in 2005 to 21 Mn in 2007 representing a growth of 5%.
**Adventure Tourism**
Adventure sports such as water sports, trekking, rock-climbing, para-sailing and bungee-jumping are popular with the younger travelers and working executives. The development of adventure tourism is a part of the policy for the diversification of tourism products in India.

The government is providing incentives in states like Himachal Pradesh and Goa to invest in adventure gear to promote this form of tourism.

**Eco-Tourism**
India’s forests, national parks and wildlife sanctuaries are a major attraction for a whole lot of tourists from around the world. Each state today is taking several steps for their preservation. Natural attractions are being promoted with increased local participation. The mystique of aboriginal tribal ethno-medicine which can be found in Ayurveda is marketed in order to attract tourists.

The cultural initiative titled ‘Utsavam’ won an award at Pacific Asia Travel Association 2008 for being instrumental in reviving the cultural heritage of Kerala as well as for the enrichment of the local community. Envisaged as an annual event, the objective of this initiative is to revitalize the unsung artistes who have dedicated themselves to perfecting their vocation.

**Avian Tourism**
Adding another dimension to the Kerala’s backwater and health tourism is the avian tourism to attract birdwatchers from all over the world.

**Medical Tourism & Spas**
India has originated as one of the most important hubs for medical tourism. Many people from the developed countries come to India for the rejuvenation promised by yoga and ayurvedic massage therapy as well as for high-end surgeries like cardiac bypass surgery or knee/hip replacement. Residents are equally patronizing alternative medicine therapies and undertaking travel to specialist facilities across the country.

**Highway Tourism**
Besides catalyzing diversification of tourist traffic and revenue from the urban centres, planned development of highway tourism opens opportunities for enhancing local employment and uplifting rural economy through local feeder enterprises, which will find scope to grow in the vicinity of such highway tourist complexes. Haryana serves as a great example for highway tourism.

The National Highway Development Program envisaged 4-6 laning of the existing high-density highway corridors linking the four mega-cities of Delhi, Mumbai, Chennai and Calcutta. It also aimed at the creation of north-south and east-west corridors.

In addition, bonds floated by the National Highways Authority of India, which is charged with the execution of the project, have been exempted from capital gains.

**Rail Tourism**
The Indian Railways has introduced several new services to promote rail tourism - luxury tourist trains, exclusive steam & hill charters, tour packages, ‘Bharat Darshan’ – special tourist trains for the budget travel segment, budget hotels – near important railway stations all over India, car rentals and a special package for Buddhist passengers.

The Indian Railway Catering and Tourism Corporation Limited, a public sector enterprise under the Government of India, introduces a range of new tourism products from luxury tourist trains to exclusive steam and hill charters, ‘Bharat Darshan’ trains and budget hotels near railway stations.

The ‘Kalka Shimla Toy Train’ has about 7 coaches that can accommodate around 200 passengers in a single trip. The train acquires a moderate average speed of 25-30 km throughout its journey enabling its travelers to soak in the beauty of the picturesque valley.
The Buddhist special package in its eight day trip covers Delhi, Gaya, Rajgir, Nalanda, Varanasi, Gorakhpur, Lumbini and Gonda.

**Caravan Tourism**
A new policy guideline to promote ‘Caravan Tourism’ in India and facilitate the infrastructure required for the same would be announced. Private players will be able to ply their vehicles on selected routes, and tourists can stay on board. There would be no need for hotels.

**Wellness Tourism**
A new policy guideline for promoting ‘Wellness Tourism’ in India would be announced. The policy would aim to leverage India’s potential in traditional systems of wellness and medicines like Ayurveda, Siddha and Yoga and to project India as a unique destination for spiritual healing. Wellness Tourism Road Shows would also be organized in overseas markets starting with Scandinavian countries in the first phase.

**Heliport Tourism**
With a view to promote tourism in hilly and remote areas, guidelines would be framed to provide central financial assistance to States and Union Territories for construction of helipads/heliports at selected destinations which have tourism potential but lack good connectivity.

## Opportunities for Investment

### Hotels
India currently has around 115,000 hotel rooms spread across all the categories and is facing a shortfall of 155,000 rooms. The hospitality sector is expected to see an estimated investment of US$ 12 Bn in the next 2 years, and various new international hotel brands will break ground.

Given the current growth, demand-supply gap and investment norms (100% FDI allowed), the country provides opportunities for International brands to enter India with a long term commitment.

For the Commonwealth Games in 2010, the government is expected to provide 10,000 budget rooms as compared to the requirement for 40,000 to 50,000 of such rooms.

A five-star hotel room requires and investment of US$ 125,000 to US$ 210,000 compared with only US$ 62,000 – US$ 83,000 for a 3 or 4-star hotel room. The further down budget hotels can have the hotel up and running on limited services platform with an investment of US$ 31,000 for a room. The gestation period for a 5-star property is 3 years or more, whereas a budget hotel can be up and running in well under 2 years. The land cost should ideally by 20% to 30% of the project cost, but the trend has seen this figure touching the new heights of 50% to 60% as well.

### Tour Operators
The inbound MICE (meetings, incentives, conventions and events) segment is growing at 15% to 20% annually.

The government is taking active measures to create world class convention facilities to attract large- scale meetings in India. Currently, India has only 0.3 % of the world’s MICE business and there is great potential in showcasing India as a business as well as a leisure locale. Tour operators with an increase in the number of tourists and destinations have more opportunities to promote places of interests within country.
Education and Employment

The industry with current employment at the level of 140,000 and 53,000 graduates, will generate 235,000 positions in the next 5 years. However, there would still remain a gap of 42,000 graduates and qualified personnel.

There are only 25 IHM’s and there are approximately 180 institutions (150 colleges in the private sector) granting certificate/diploma/degree courses in specialized areas like Food & Beverage (F&B) Production, Food & Beverage (F&B) Service, Housekeeping etc.

Opportunities for Foreign Tourism Bodies

The number of Indians travelling abroad has increased sharply in the past 10 years and in 2008 reached a level of 11 Mn outbound travelers. This number is expected to grow to 29 Mn by 2018.

From the above chart, we can see that the number of outbound tourists from India has been seeing a steady growth and has almost tripled from 4 Mn travelers in 1998 to 11 Mn travelers in 2008. This number is expected to further increase to 18 Mn in 2013 and 29 Mn in 2018.

West Asia and South East Asia are the most popular destinations for Indians travelling abroad. Together these 2 regions constitute almost 48% of the total outbound traffic from India.

The phenomenally high number of Indians travelling to places in the West and South East Asian countries opens up a host of opportunities for the other countries in this vicinity to attract travelers and tourists.

Some key takeaways for foreign tourism boards include the following:

• Extensive destination marketing and promotions in conjunction with the Ministry of Tourism
• Showcase destination to focus groups and participate in domestic travel fairs
• Conduct a familiarization visit for the top outbound travel companies
Offer incentives like visa on arrival or free transit visa
Organize culinary fairs in collaboration with the top 5-star hotels in the country in order to showcase culinary styles across cultures

Looking Forward Together

Each day, the tourism industry meets the aspirations of millions of people who want to travel to share experiences, to encounter different cultures. It has grown in response to increasing demand and it has been at the forefront of innovation, adapting its services and harnessing the best new technologies to deliver consistent quality and value for money.

The results are evident in more jobs and greater prosperity, enhanced customer choice and experience, and widened understanding around the world. The tourism industry is uniquely well placed to play a crucial role in how the world meets new challenges of this century.

The prospect of solutions to today’s and tomorrow’s world problems is brought closer when enlightened governments and engaged local communities choose to work together with the industry. The common determination to co-operate more closely has raised the possibilities for ensuring that growth is managed to stimulate economic activity around the world, that communities are respected, that the world’s resources are protected and the barriers of distance, inequality of opportunity or lack of imagination are overcome.

The tourism industry is eager to harness its imagination and energy to this open ended challenge and it looks forward to sharing the common task with government and industry.

Challenges Before the Industry

The tourism industry in India is faced with certain challenges of regulatory as well as external nature. These are highlighted below.

Regulatory Challenges

- Complex Tax Structure: The hospitality industry faces multiple tax structures at the central and state level. This makes payment of taxes quite cumbersome.
- High Taxes: The taxes charged are compounded by the luxury taxes which push up the average room cost.

External Challenges

- Economic Slowdown: The hospitality industry has been hit by the global economic meltdown. Foreign tourist arrivals have been badly hit and occupancy levels across the country have fallen.
- Impact of Terrorism: The recent terrorist attacks in Mumbai have shaken the confidence of MNCs and business travelers. Many have been forced to re-consider their travel plans and subsequently, the winter season which implies brisk business for the hospitality industry has seen far lower occupancies.
- Cost of Land: When compared to other markets across the globe, in India, the cost of the land constitutes a very large chunk, especially in case of large infrastructure projects. This delays the break-even of these projects and discourages further investments.
- Cost of Debt: The cost of debt in India is higher than the cost of debt in other countries. This again discourages further investments.
- Skilled Manpower Shortage: The industry is facing a manpower shortage which pushes up the cost of acquiring quality talent.
Our Recommendations

Recommendations for the Government

• Take a close look at ways and means of improving the existing infrastructure and hygiene conditions at places of tourist interest and public places

• Conduct a joint promotional campaign for various states in India and allocate budgets for marketing at international travel fairs to boost tourist inflow in the country

• Play a significant role in rationalizing the cost of land auctioned for hotel development. This would assist the industry in creating value by adding substantial inventory of hotel rooms required to diminish the demand-supply gap

• Assist in building and developing educational institutions to fulfill the emerging demand for skilled manpower in the tourism sector

• Grant ‘Infrastructure’ status to the hotel industry under SEC 80-IA of IT Act and increase depreciation on hotels from 10% to 20%

• Rationalise Floor Space Index (FSI) /Floor Area Regulation (FAR). This would allow hotels to build more rooms on the same property eventually leading to more affordable room rates. Subsequently, the government can reduce development charges for adding more rooms in existing hotels

• Further incentives will boost investments in the sector such as offering a tax holiday to the industry

• Abolition of 12.5% service tax on tour packages

• Implement uniform luxury tax code

• Extend the 5 year tax holiday scheme which currently covers only 2, 3 and 4-star hotels and convention centers with a capacity greater than 3,000 to include 5-star hotels too

Recommendations for the Industry

• Promote Public Private Participation

• Deliver on scheduled timelines and share accountability with the government on public private partnership projects to reduce the cost involved in development

• Develop an academic think-tank to trigger off the right kind of training in hotel management institutes in India

• Establish commendable Master’s and PhD programs in hospitality

• Undertake measures towards employee retention

• Coaching, development and training of employees for their long-term carrier development and retention process

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Forecasting the Financial Potential in Education

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Unique Dynamics and Growth Drivers of the Indian Education Sector

Education is the key to unlocking and building lasting value in a robust economy. For any country to grow and prosper, a well positioned educated young population is the fundamental requirement to meet the demands of an increasingly global economy and productive value creation. Over 50% of India’s Education sector is private (in the US, the private sector’s share is 32% and in China it is 25%) and in 2008 this stood at US$ 40 Bn. This is projected to grow to US$ 70 Bn by 2013 and US$ 115 Bn by 2018 (from a demand growth perspective, if supply keeps pace). We have a large demand-supply gap, and on average poor to middling quality. There is clearly an opportunity for more private players to enter the education space.

Few unique drivers of the education sector in India are interesting to examine. Historically, education has been delivered in the country by the government or through “Non-profit” charitable trusts. The number of quality institutes imparting higher education are limited, inducing tremendous competition for the limited number of seats available in the IITs, IIMs and other quality institutions. Higher education in the private sector is not generally perceived as a quality alternative. The Indian mindset is culturally geared towards choosing limited study streams such as engineering, medicine and management. There is a need to link the employment needs in India to the enrollments in higher education, in order to create a pool of productive employable workforce.

Sizeable Investment Needed to Create Additional Capacity

The financial potential in all segments of education in India is huge. The demand-supply scenario as per the current and projected enrollment ratios at the K-12, higher education and vocational education segments indicate the need for huge capacity creation. The investments required to build this capacity have been estimated below at very conservative assumptions.

<table>
<thead>
<tr>
<th>Demographic Advantage</th>
<th>More than 55% of the Indian population will be under the age of 25 by 2010. This would lead to increased demand for quality higher education and a skilled workforce.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increasing Affordability</td>
<td>High income households (income more than US$ 10,410) expected to increase from 5 Mn to 14 Mn by 2018 resulting in higher affordability. This will propel awareness towards consumption of education as a priority and an essential tool for career growth.</td>
</tr>
<tr>
<td>Knowledge Led Economy</td>
<td>India, once considered an agrarian economy is now dominated by the services sector. The share of services has increased from 31% in 1991 to 55% in 2007. This increase in the services sector has led to a steady increase in the demand for an educated skilled workforce.</td>
</tr>
<tr>
<td>Increased Participation of Women in the Workforce</td>
<td>A large young working population with a median age of 24 years, nuclear families in urban areas, along with emerging job opportunities in the services sector driven economy has led to increase in working women in India. The population of working women is estimated to touch more than 25% by 2015.</td>
</tr>
<tr>
<td>Technology Aided Delivery</td>
<td>Increasing penetration of technology will aid virtual learning and education delivery.</td>
</tr>
<tr>
<td>New Employment Avenues</td>
<td>Globalization has led to the increase of newer employment avenues. Industries such as outsourcing (KPO, LPO), legal, retail, aviation, animation, healthcare, supply chain &amp; logistics, have increased employment opportunities, and the demand for highly skilled manpower</td>
</tr>
</tbody>
</table>

Source: Technopak analysis & industry reports
Currently, the total number of students enrolled in K-12 schools in the country is ~317 Mn, which comprises of 147 Mn in the age bracket of 6 -11 years, 72 Mn in the age bracket of 11-14 years and 97 Mn in the age bracket of 14-18 years. The number of students eligible for enrollment is expected to grow to 328 Mn by 2013 and further to 351 Mn by year 2018. Clearly, India will need to add at least 34 Mn additional seats in K-12 segment in the next ten years to cater to the education needs of its continuously growing population, as shown in Exhibit 2.

The cost per additional seat, at a conservative estimate is— US$ 2400 (cost of land included at ~US$ 1 Mn per acre). This translates into a minimum investment requirement of US$ 80 Bn of investment over the next 10 years to establish these 34 Mn seats.

The enrollment in higher education is currently at 17 Mn at a Gross Enrollment Ratio (GER) of 13%. Enrollments are projected to grow at a CAGR of 5.6%, reaching 22 Mn by the year 2013 and 29 Mn by the year 2018. As per these estimates, 12 Mn additional seats in the higher education would need to be created by the year 2018 as shown in Exhibit 3. The cost per seat in a regular higher education institution is ~US$ 8300. Therefore, the total investment that India needs for creating the projected additional capacity in higher education alone would require an investment of ~US$ 100 Bn.

The vocational education and training landscape of India is extremely underdeveloped. India currently has 5,500 industrial training institutes and 1,745 polytechnics as compared to 500,000 similar institutes in China. This infrastructure caters to only ~2.5 Mn people annually. There are 175 trade training programs in India compared to 1,500 in the USA. Clearly there is a pronounced skill gap in terms of both quality and quantity in the country.

As estimated 85-90 Mn people with vocational skills would be required in various sectors between 2008-2013. According to industry sources, the split of people intake sector-wise over the next 5 years will be 44.8% from the services sector, 31.2% from agriculture and 12.6% from manufacturing.

Cost per seat will vary significantly in this segment depending on the location, scale, positioning of training service and investment by private players vs. the government. Indicative costs per seat in the private sector are outlined for a few representative short term vocational streams as shown in Exhibit 4.
Cost per Seat Estimations in the Private Higher Education Segment

Cost per seat estimations in higher education would vary depending on the scale of the project and the cost of land. Enclosed are few parameters on which we have calculated that a medical seat would cost ~ US$ 104,166 and a non-medical seat would cost ~US$ 14,580 to be created by a private player. The assumptions backing these estimates are outlined below. In these calculations we have assumed that 100% students would be residing in the hostel and the cost per acre of land is ~ US$ 520,800.

Thumb Rules for Investments in Private Education

It has become evident in the last decade or so that government alone cannot bear the cost of the education sector and this sector particularly lacks proper investments, which is a constraint in coping with growing market demand and global competition. To bridge the gap, the private sector has stepped in. Education as an investment sector is often viewed as safe by the investors. With the attractive rates of return and the growth potential, it is one of the hot favorite sectors for the private players and private equity funds in India.

A few thumb rules for entrepreneurs and companies wanting to invest in education are listed below.

'Market' Assessment

A pragmatic assessment of the “catchment” in each segment of education is important, from the standpoint of achieving required student enrollment, before planning an investment. The catchment (travel time from institute) for a pre-school would be 30 minutes, for a K-12 day school would be 60 minutes, and for a residential school this would be 5 hours. Demand for a vocational training institute originates from within its city premises, with few students travelling across cities for enrollment. A university or a higher education institute would attract students from all parts of India (as well as South Asia, the Middle East and Africa), the catchment being dictated by the quality of education on offer and the reputation of the institute.

Key Financials

A regular day K-12 school, built over 2 acres of land with a capacity of 2,100 students, would require an investment of ~US$ 3.1 Mn, and so would an MBA Institute with a capacity of 240 students enrolled in a 2 year course spread over 1.5 acres of land. An engineering college with a capacity of 1,600 students spread over 10 acres of land would require an investment of ~US$ 21 Mn. The project cost for setting up a private

<table>
<thead>
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<th>Exhibit 6</th>
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<tbody>
<tr>
<td><strong>Cost Per Seat Estimations in Different Streams of Higher Education</strong></td>
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<td></td>
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<tr>
<td>Max No of Students Enrolled</td>
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<tr>
<td>Course Duration</td>
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<tr>
<td>Capex (US$ Mn)</td>
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<tr>
<td>Cost per Seat (US$)</td>
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<tr>
<td>Cost Per Seat Excluding Land (US$)</td>
</tr>
<tr>
<td>Area of Land</td>
</tr>
<tr>
<td>Hostel Development Cost (US$)</td>
</tr>
</tbody>
</table>

Source: Technopak analysis
university over 300 acres of land, with a capacity of 40,000 students is estimated at ~US$ 312 Mn. For the MBA and engineering institutes, the land value is assumed at ~US$ 520 Bn per acre and for the university at US$ ~291 Bn per acre. In these ventures, financial returns are attractive, with EBITDA levels of 30% plus and project IRRs ranging from 25% to 35% levels.

**Regulation**  
Shortage of quality education institutions is a product of India’s tightly controlled regulatory structure. Education is regulated at both the central and state government levels. Higher education has several regulatory bodies, including AICTE and UGC, but there is no umbrella regulation for K-12 schools, nor a uniform law for schools. There are considerable entry barriers and regulations that need to be met, and a thorough understanding of these is advised.

### New Developments in Regulation in Indian Education

#### Right to Education Bill Adopted by Parliament

The Indian Parliament has adopted ‘The Right of Children to Free and Compulsory Education Bill, on 4th August 2009,’ which envisages free and compulsory education to children in the 6-14 years age group. As per this bill, every school will have to earmark at least 25% seats in class-1 for free and compulsory elementary education. The bill seeks to do away with the practice of schools taking capitation fees before admission and subjecting the child or parents to any screening procedure. The bill also seeks to ban private tuition by teachers and ensure that no child is subjected to physical punishment or mental harassment. It shall be the duty of every parent or guardian to admit the child to a neighbourhood school for elementary education and no child should be denied admission for lack of age proof. Seeking to carry out radical changes in the primary education pattern, the bill states that no child shall be required to pass any board examination till completion of elementary education.

Stressing the need for a big boost to children’s education, HRD Minister Mr. Kapil Sibal said that out of every 100 children attending elementary school only 12 reached the graduation level; in Europe it was 50 to 70 (students reaching college from the elementary level) and the global average is 27. The Centre wanted to increase India’s average to 15 by 2012 and to 30-35 by 2020, he said.

#### Proposed Reforms in Higher Education

The three-fold objective of expansion, inclusion and excellence has been adopted by the 11th Five Year Plan, to deal with multiple problems related to access, quality, curriculum and faculty shortage in higher education. The 11th Plan expects to deal with the problem of access to higher education through expansion. However, since access is only a part of the problem, simultaneous efforts have to be undertaken not only to improve the quality of all elements in higher education, but also to address the obvious demand-supply differences and establish national & international quality standards in all Higher Education Institutions(HEI).

The proposed liberalization in higher education and allowing FDI in the sector, makes the issue of a single window regulatory body for HEIs even more imperative to facilitate quality expansion.

Mr. Kapil Sibal has stated that the Ministry would reform the current regulatory structure and would push for a SEBI like regulatory body for the education sector, as well as campaign for FDI to be invested in education sector. In his words, “We need to create an authority like SEBI in the education sector, which actually deals with regulation and we need to have an independent credit rating agency that accredits at the entry point by giving a provisional certificate and when the institution is built, to give a final certificate so that the intake can take place and we need to get the government out of this and give it to an independent
regulator. But all this needs a lot of work and a lot of consensus across the board and I think that once we do that, then anybody should be able to enter. I will give you an example. Except for the central government or the state government, nobody can set up a university and then you have the whole deemed university concept. Why should this happen? Anybody should be able to set up a university and he should be able to compete in a market for the quality of that degree and as long as you put a system in place it is very easy to work it out. Once you talk about expansion and inclusiveness, it means opening up the sector, bringing equity into the sector and not diluting quality.”

Setting up of the National Commission for Higher Education

It is been proposed to set up National Commission for Higher Education and Research, a constitutional body like Election Commission. The Prime Minister, Leader of Opposition and Chief Justice of India will select the chairman and the members. Regulatory bodies such as the University Grants Commission, All India Council of Technical Education and Medical Council of India will cease to exist. The thrust is to give full autonomy to universities which will function as self regulatory bodies and will be vested with all academic responsibilities. They will design the function and structure of programmes, including medical and engineering courses. The Commission will oversee the functioning of the universities and act as a facilitator for proper growth of higher education and research.

Objectives of the National Commission for Higher Education and Research would include the following:
- Be responsible for comprehensive, holistic evolution of higher education sector
- Strategize and steer the expansion of higher education
- Ensure autonomy of the universities and shield them from interference by external agencies
- Acts as a catalyst and also as a conduit to encourage joint/cross-disciplinary programs between and amongst universities and institutes
- Spearhead continuous reforms and renovation in the area of higher education
- Establish robust global connectivity and make it globally competitive while creating our own world class standards
- Promote greater engagement and enhance resources to state universities with an aim to bridge the divide between the state and central universities
- Ensure good governance, transparency and quality in higher education
- Connect with industry and other economic sectors to promote innovations
- Devise mechanisms for social audit processes and public feedback on its performance and its achievements
- Devise mechanisms for social audit processes and public feedback on its performance and achievements

Emergence of 14 World Class Universities

The Ministry of Human Resource Development has also announced the setting up of 14 world class universities, of which 9 are expected to be constituted under public private partnership, with an initial budget of US$ 208 Mn. The Government commits to provide funding for all infrastructure and resources including library, laboratory and electronic resources of world class standards on a continuing basis to enable knowledge growth and germination of new ideas. For this initiative, a research endowment fund of an adequate amount not less than US$48 Mn per university shall be provided by the government.

The university shall also have the freedom to source funding from all other non-governmental sources subject to the board limitations such that funding shall not be from unverified or dubious sources or from sources with a biased outlook. These national universities shall be kept out of the purview of the regulatory
oversight of the existing regulatory bodies in higher education in academic matters as well as regulations on maintenance of standards or minimum qualification requirements for appointment to academic posts.

Considering the fact that quality education is the backbone for any robust economy, education is now top priority of the government. Though India currently has over 400 universities and more than 20,000 colleges, it is not sufficient to cater to the education needs of India. It has been proved from the examples of many developed countries that low levels of regulation have been a catalyst in creation of quality education. The stringent regulatory framework governing the Indian education system is limiting its growth. Hence, there is an inevitable and immediate need for the liberalization of the education system to bring in private sector investment and incentives for quality creation.

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Social Media: An Emerging Medium for Business Growth

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Background

Social media or web 2.0 technologies is an evolution in the development of social connectivity and is the new buzzword amongst corporates today. From international friendships to regional conversations, the web is moving from a static collection of pages to a more social communications platform where word of mouth counts. Social media is allowing connections between people in a way that has never happened before. News is spreading faster, trends are gathering pace, and plethora of information is available – to all-on an unprecedented level. The key enablers to this phenomenon are:

- **SPEED**: The ability to connect faster
- **COST**: Ability to participate, create and generate content at very low cost
- **SCALE**: Ability to reach to a large number of people

Social media has become an integral part of the online world. Around 66% of the world’s internet population visits social networks and blogs and 1 out of every 11 minutes spent online is on a social networking site\(^1\). This has significant implications for corporates as the consumers to whom they market their brands and sell their products and services, are evolving with social media and the tools it offers.

Understanding the New Communication Platform

What is social media? It is a combination of channels, platforms, communities, content and tools that powers peer to peer communication or ‘word of mouth’. The social media landscape as shown in Exhibit 1 broadly covers 6 categories depicting various levels of participation in social activities.

A study conducted by ‘Universal McCann\(^2\)’ on a sample of 17,000 internet users across 29 countries in March 2008 measured consumer usage, attitudes and interests in adopting social media platforms. As shown in Exhibit 2, it clearly indicates that a huge chunk of the world’s internet population uses social networking and blogging sites.

### Social Media 2008: Global Universe Estimates

<table>
<thead>
<tr>
<th>Category</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Active internet users in 16-54 years age group</td>
<td>475 Mn</td>
</tr>
<tr>
<td>Watch video clips online</td>
<td>394 Mn</td>
</tr>
<tr>
<td>Read blogs</td>
<td>346 MN</td>
</tr>
<tr>
<td>Joined a social network</td>
<td>270 Mn</td>
</tr>
<tr>
<td>Bloggers</td>
<td>184 Mn</td>
</tr>
<tr>
<td>Subscribe to RSS feed</td>
<td>160 Mn</td>
</tr>
</tbody>
</table>

Source: Universal McCann International

### Increasing Popularity

Social network and blogging sites are now the 4\(^{th}\) most popular activity centres on internet as per one of the studies by Nielson. The increasing popularity of social networks and blogging sites can be understood with the following growth numbers:

1. Nielsen Online
2. This company has been monitoring numbers for the 3 years now
• Twitter and LinkedIn observed a growth of 2,681% and 90% respectively in numbers between May’08- May’09
• YouTube adds 25 Mn visitors a month on an average
• Facebook is growing with an average of 5 Mn users every week

Increase in Time Spent
The rise of social media is not about how people can collaborate on wikis or join in social networks. All of these are just pieces of the story. The bigger point is that it has become a part and parcel of their daily lives. The time spent on social network and blogging sites is growing at over 3 times the rate of overall internet growth which increased by 18% between Dec’07 and Dec’08. In the same period, however, the amount of time spent on ‘Member Community’ sites rose by 63% and on Facebook by a massive 566%.

The numbers indicate the shift from the offline to the digital world; whereby social media has become a global phenomenon. The prevalence of networking sites is increasing with rising numbers of internet users as shown in Exhibit 3.

Exhibit 3

<table>
<thead>
<tr>
<th>A Snapshot of User Levels</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>GLOBAL</strong></td>
</tr>
<tr>
<td>Internet Users</td>
</tr>
<tr>
<td>1.6 Bn users currently to grow to 2.2 Bn by 2013</td>
</tr>
</tbody>
</table>

| Social Media Users        |
| Facebook: 250 Mn          |
| MySpace: 127 Mn           |
| Twitter: 25 Mn            |
| LinkedIn: 45 Mn           |

| **INDIA**                |
| Facebook: 4 Mn           |
| LinkedIn: 2 Mn           |

While the number of internet users is expected to reach 2.2 Bn by 2013, according to a study by Forrestor India is projected to have the 3rd largest internet population growing at an average annual rate of 10% to 20%. This surge in internet population will further push social media to newer heights in the Indian market.

Transforming the Business Landscape

The increase in penetration and usage of internet in developing countries has led to the emergence of a new trend - the growth of social media. Today, people are spending a significant part of their internet time on social networking/ blogging sites. They use social media to communicate with others, express, gather information and share their opinion and even rate products and services. Before buying a refrigerator, one first tends to find information on the product through the internet and understand what others are saying about a particular brand. Peer opinion is considered more ‘genuine’ compared to what the marketer says; and purchases are made based on the testimony of other consumers.

Not only this, the consumers are not mere ‘listeners’ any more. They are now engaging in a two-way communication with the brands, marketers and companies - creating a huge repository of brand related content. The balance of power is shifting towards the consumer with their voice becoming more powerful than marketers. J&J experienced the power of this media when its marketing campaign for the launch of ‘Motrin’ brand (pain relief product) failed miserably; due to the public outrage of mothers on Twitter and Facebook – two very popular social media platforms.

As a result of the ever increasing popularity of the medium, the nature of consumer-business relationship is getting redefined. It offers unparalleled access to unfiltered customer opinion and creates opportunities for businesses to leverage user-generated content in innovative ways. Many companies, especially in the developed economies (where the social media originated and became a phenomenon much before), have recognized the value of consumer generated content and built their presence on social media, where the

3. Global Online Population Forecast
consumer is more active and is spending more and more time. They have progressively adopted multiple platforms to reach their audience, converse with key influencers and target consumers to build brands, market their product and services, generate new leads and much more.

A Shift in Marketing

The ongoing bustle in the social media space has led marketers to re-align their marketing budgets favoring the new medium. According to Aberdeen Group, 63% of the best-in-class companies surveyed across the world plan to increase their social media marketing budgets in 2009, despite the weak economy. As per Forrester Research, in the US alone (where the share of social media spend is merely 3% currently), the social media spend is expected to increase from US$ 716 Mn in 2009 to US$ 3113 Mn in 2013.

Quite in line with other countries like the US, advertising on internet has started gaining momentum in India, as shown in Exhibit 4. Although the current estimated spend in absolute terms is just US$ 146 Mn which is not even 1% of the total internet spend in US (US$ 25 Bn), it is expected to witness an exponential growth year on year due to sudden burst in the internet population 2009 onwards.

According to a survey by Web Chutney, one of the leading digital agencies in India, around 82% of the top 500 marketers in India spend close to 5% of their total advertising budget online. About 26% of this online spend is targeted towards development and maintenance of brand specific web-sites and another 13% goes on newly launched or planned social media initiatives.

The crux lies in the fact that the frenzy of this new phenomenon has pushed companies to explore various tools and techniques offered by social media to reach out to consumers and provide a more connected and meaningful experience. Corporates in India too are slowly waking up to the new media and its potential.

Unleashing the Power of Social Media

The increasing conduciveness of people to social networks has led to fast adoption of the medium by companies. Marketers (e.g. Volkswagen) are getting on board the social media trend with their own networking sites for brand aficionados. These branded web-sites complement the other social media sites. Companies are creating a dialogue and engaging with the right targets, spreading the word around thus, creating a multiplier effect. Many have embraced social technologies to drive business results by making it an integral part of their market intelligence, strategic delivery, development cycle, customer support, marketing and sales. Exhibit 5 highlights key areas where companies have adopted social media.
One remarkable example of a ‘revolutionary’ in social media space is Dell. Social media is the core to the company’s marketing strategy with multiple groups on various social media sites to cater to different customer segments. These include:

- **Dell Forum**: To interact, ask questions, and give suggestions about computer & electronics technology
- **StudioDell**: An interactive helpdesk for consumers, SMEs & IT professionals
- **Direct2Dell**: Dell’s official corporate blog to enable sharing of thoughts
- **Dell@DellOutlet**: A twitter account that tweets out major discounts for Dell computers and products
- **Dell Ideastorm**: A website by the company to post, vote for and see ideas becoming a reality

Dell has used all these platforms not just to reach out to its existing and future customers but also to generate new product ideas and even revenue by achieving sales worth millions.

HP has achieved remarkable success in branding its products by engaging the consumer - enabling people to express themselves in a creative manner. Apart from connecting with consumers, companies like IBM and Best Buy have taken social media to a different level. While IBM uses social media to foster collaboration with stakeholders as well as to connect with its employees across the globe, bridge the geographic boundaries and bring in transparency, Best Buy uses it to bring in a cultural shift in the organization, make staff more customer-oriented and foster innovation. Hyatt Hotels use social media (Twitter – the microblogging platform) to provide customer support through their online concierge service.

Companies across variety of industries such as hospitality, travel and tourism, banking and financial services, life sciences, retail and consumer products, airlines, automobiles, fashion, education and many more are exploring social media to tap opportunities in market research, brand building, product promotion, product development, customer service, collaboration with stakeholders, employee engagement, and recruitment etc. Exhibit 6 highlights some successful cases where social media has been leveraged effectively for business benefits.

### Successful Use of Social Media

<table>
<thead>
<tr>
<th>Area</th>
<th>Company</th>
<th>Activity Undertaken</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increasing Brand Awareness</td>
<td>Adobe</td>
<td>Actively holding consumer interest through engagement ads on social networks – Set up of an Online Game</td>
<td>• The game was played more than 14,000 times during the 1 month campaign&lt;br&gt;• Rise in page view by over 48,000 a week</td>
</tr>
<tr>
<td>Product Promotion</td>
<td>MTV India</td>
<td>Capitalizing on social media to keep the show buzz alive - Creation of an online and highly interactive model of the real game show</td>
<td>• Over 40,000 fans on Facebook</td>
</tr>
<tr>
<td>Product Development</td>
<td>Dell</td>
<td>Partnering with customers to contribute to, and integrated into, Dell’s product development</td>
<td>• 12,511 ideas contributed to community, with 86,255 comments&lt;br&gt;• 366 ideas implemented leading to launch of ‘Lattitude’ Laptop.</td>
</tr>
<tr>
<td>Employee Engagement</td>
<td>IBM</td>
<td>Multiple in-house versions of web 2.0 with the intention of bringing employees, alumni, partners, vendors, and customers together</td>
<td>• 60,000 blog users, 17,000 different blogs, 1 Mn page views per day on internal wikis&lt;br&gt;• Launch of corporate social networking visualisation and analysis tools like Atlas’</td>
</tr>
</tbody>
</table>

### Taking Social Media beyond Business Use

The usage of social media has not been limited to just B2C or B2B areas. Rather, the emerging media has had far reaching effects on a multitude of other sectors like politics, social service, defense services etc.

Many of us are not aware of the role that social media (besides the internet and mobile devices) played in building the brand ‘Obama’ and in turning the tide in Obama’s favor in the recent US presidential elections. An effective strategy was adopted to build the campaign leveraging on the strengths of the social media network. The campaign’s reach across social networking was enormous in scope, with a presence on
every conceivable social network, from Twitter to Facebook, and MySpace to LinkedIn. Even virtual world SecondLife had a concerted effort from the campaign, with news updates piped in from major news sites throughout the campaign. The campaign had realized from the outset that by giving supporters all the tools, they could harness the power of volunteers willing to campaign online, as well as fundraise for their candidate.

The response generated by the campaign was so huge that marketing gurus can use it as a case study while crafting marketing strategies for their own brands.

Exhibit 7

Obama – Success through Social Media

| Twitter 291,000 Followers | MySpace Page 1.26 Mn Friends | Facebook page 32,000 active application users | YouTube 100m+ video view, 164K subscribers |

The campaign helped build a political database of millions of supporters that grew organically and enabled Obama raise over US$ 600 Mn of campaign funds at a relatively low cost. The era of the socio-political campaign has begun!!! Going forward, we will certainly see a much stronger focus on social media from political candidates in other countries too.

Besides politics, social media tools are being profitably used for promotion of social issues and bringing about a social change. These tools can help build awareness and increase the reach of actions towards social causes. WWF created history with its ‘Earth Hour’ campaign on social networking sites such as Facebook etc. The popularity of the campaign created a powerful social movement by reaching out to millions of community users and creating awareness about the importance of collective global action to combat global warming.

One of the other successful social campaign ‘Charity: Water’ has generated funds worth US$ 250,000 for 55 water projects in Ethiopia, Uganda and India, through social media sites all in a matter of just 2 weeks.

The Social Media Wave in India

Having impacted the West, this wave of change has percolated to India as well and is fast gaining edge. Though it all started long back with the advent of corporate blogging, the use of social media is now gaining popularity in India. Leading companies are leapfrogging in the social media space with their own social networking sites and spreading multiple legs across various social media platforms. They are leveraging the medium for multiple purposes - to engage people, pacify customers, strengthen brands and even recruit prospective employees.

Although Infosys, TCS, Rediff, HCL, Cleartrip, FritoLay and Naukri and Indian arms of MNCs like Microsoft, IBM, and Hindustan Unilever are few names that launched their social media presence with corporate blogging, it is the technology sector that has been far ahead in its adoption beyond blogging and is followed by travel companies, financial services firms and consumer product companies. Some of the leading examples of firms using social media are indicated in Exhibit 8.

Planning for Social Media

Looking at the impact of social media on business areas and benefits realised by the ‘revolutionaries’ in this space, many companies tend to just jump to the icing of the cake before having decided what is going to be baked. In other words, they just want to establish presence on social networks without much thought
or planning. They go ahead saying ‘we should start a blog’ or ‘we should create a page on a social network’ or ‘we should create a community’, which actually is the final step in social media planning.

It is essential for a company to adopt a systematic approach towards social media – the mantra is - Listen, Understand and Engage. Even before embarking on a social media journey, it is important for companies to explore the medium and listen to the company or brand specific ‘conversations’ on the web - understand what consumers are thinking and saying about their brand. They should identify and segment the consumers as shown in social media influencer model in Exhibit 9.

The key to success lies in focusing on ‘Influencers’, laying emphasis on identifying the characteristics of the right sort of anchor influencers for the brand and exploring innovative ways to find and engage them. These are the consumers that are most likely to influence others, create the multiplier effect and thus, spread the word about the company or brand.

Companies should consider understanding the medium first, and then plan on its adoption with a social media strategy. A focused approach for companies to adopt social media is centered around the four key elements – the target, the objectives, the plan and the technology and involves the following key steps:

- **Identify the Target Consumer**: Examine the ‘socio-technographic’ profile of target customers.
- **Set Objectives**: Decide what the company wants to accomplish with social media and how the results would be measured.
- **Make a Plan**: Plan for how relationships with customers will change and build a strategy around changing relationship with customers.
- **Adopt Technology**: Pick the appropriate platforms, tools and technologies to implement.

As companies mature in the social media space, the value generated by their social media initiatives also improves. As shown in Exhibit 10, the impact and value generated clearly depends on the objective of the social media initiative and the level of customer involvement.

Companies face many challenges such as technical complexity, management resistance, lack of budget, inability to measure ROI and lack of knowledgeable staff in utilising the social media to its fullest potential. However, the factors that play a great role in determining the success or failure of any social media initiative include the long term vision, focus, initiative and commitment.
The leaders in social media space - Dell, IBM and J&J, all have met these challenges head on and learnt from their mistakes. These firms treat their customers as contributors and stakeholders in their business and reward, promote and empower them. They are far ahead in the social media maturity spectrum.

### Key Success Factors

As ‘complex’ or ‘fickle’ as the social web may appear, there are, in fact, a handful of basic tenets that separate success from failure.

- **Listen, understand and engage with consumers.** Engaging the right people is what makes businesses tick.
- **Success cannot be achieved by merely having a presence on a social media site,** the key lies in constant engagement of customers.
- **Involve top management right from the beginning else with no visibility of serious returns in the initial a few weeks or months,** the initiative would fall flat. Top management would ensure long term focus and commitment.
- **Social media can cause a huge stink,** be prepared to handle the negative conversation and feedback. Companies should have a reputation management strategy in place.
- **Success and benefits will not appear overnight.** Like Dell, companies need to have a long term focus on social media to reap the real benefits. Plan for a comprehensive presence on the web and evolve with social media over a long term.
- **Just being present on one or two social media platforms may not be enough.** The phenomenon is evolving fast and the sites that are very popular today may not remain so in future. Therefore, captivate consumers by having multiple legs across the wide spectrum of social media channels.
- **Integrate the social media strategy with the company’s corporate strategy as well as its marketing strategy.** Non-aligned strategies are bound to fail sooner or later.
- **Do not jump on measuring or quantifying the benefits or impact.** Social media is a ‘journey’, a means/vehicle to reach the desired ‘end’. The success should be measured by the ability to reach, identify and convert influencers as well as the effectiveness of the ‘influencer’ to spread the word to the desired consumers.
- **Social media success is not measured by how broad one’s reach is, but by how deep one’s network is!**

### Conclusion

The social media is a new phenomenon that is often compared with the ‘internet revolution’ seeing its growth and scale. It has already touched our lives in many ways – from connecting with friends and colleagues, providing feedback on products and services, participating in events, to even experiencing the joy of farming on ‘Farmville’ while sitting in our homes and offices. A few years down the lane, we would even be buying products and services through social media.

The medium is growing very fast and holds huge potential but is still in its nascent stage. Therefore, the time is ripe for companies to embrace the media, capitalize on the opportunity presented and become the ‘revolutionaries’ of tomorrow. Those who engage all the stakeholders from employees to consumers to business partners would be the real winners!

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