Spotlight on India
Understanding the Indian Consumer

The mystique of the great Indian "bazaar" has drawn merchants from around the world for thousands of years. Today, little has changed. India, with more than a billion people, a rapidly expanding middle class, and enormous, unrealized growth potential remains an alluring consumer market for international retailers. Napoleon famously referred to the United Kingdom as "a nation of shopkeepers," a phrase that could just as well describe the erstwhile jewel in the colonial crown – the Indian marketplace of today.

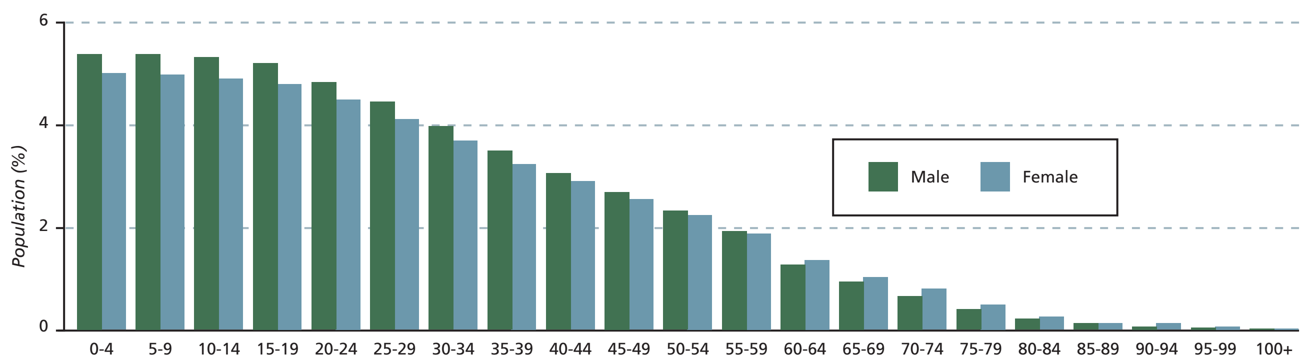
Along with opportunity, this vast country presents equally outsized challenges to foreign investors, including inadequate infrastructure, corruption and complex regulatory hurdles. India's uneven development means that consumers live in different decades concurrently, necessitating careful micro-segmentation. There are 1,500 dialects spoken in India, 780 languages, and multitudes of co-existing faiths, castes, regional differences and culinary traditions; amid such diversity, even adjacent markets can be profoundly different. The rich, educated professionals in neighborhoods around Bangalore, Delhi and Mumbai, for example, are tightly juxtaposed with the poorer, less well-educated inhabitants in slums nearby.

At the heart of the Indian consumer market is a central paradox: this ancient land is now occupied by the youngest citizens in the world, with 450 million inhabitants below the age of 21 (see Figure 1). Young Indians are modern, yet curiously steeped in tradition, and often skeptical of the Westernized pitch of global marketers. Many young, rural Indians are moving into cities and this force of urbanization is expected to fuel future economic growth. The proportion of the urban population is expected to rise to 40% in 2030 from 30% today. Fully 70% of the country's GDP may be concentrated in cities by 2030.

Despite an economic slowdown in recent years primarily due to poor governance, India's economy is projected to grow steadily in the coming years. A January 2014 World Bank forecast suggests growth rates will likely exceed 7% by 2016. While real household disposable income has increased dramatically since economic liberalization in 1991, the inequity between the rich and poor remains vast. Income levels in urban areas are especially disparate—and even the "middle class" has much lower levels of disposable income than in developed economies. Indian companies, not surprisingly, lead the world in delivery of low-cost products such as Tata Motor's $2000 car and mobile telecom provider Bharti's lowest-tariff call plans in the world. A study by India's National Council of Applied Economic Research (NCAER) found that the bottom 60% of households account for 40% of

Figure 1

2010 Population Spread



Source: Businessworld Marketing Whitebook 2012-2013 total household expenditure, indicating that consumption power has trickled down to the bottom of the pyramid. India also has an increasing number of super-rich; in 2013 there were 7,730 individuals in India with a combined net worth of $925 billion.

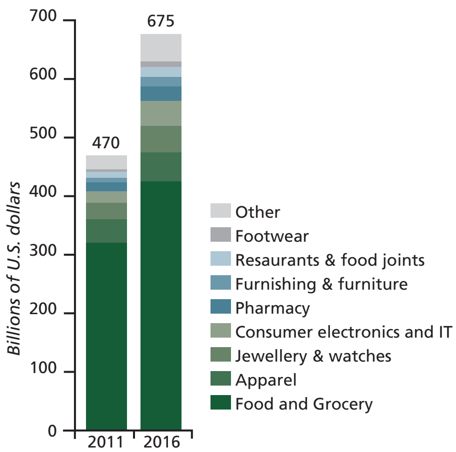
Indian consumers are becoming technologically savvy; cellphone penetration leapfrogged landline penetration in 2004, reaching 875 million subscribers in 2013. Mobile Internet users are spreading quickly as the cost of "smart" mobile phones drops. India's Internet user base is already the third highest in the world after China and the United States and is growing at nearly 40% a year; it will likely include 243 million subscribers by 2014. Online sales, however, currently comprise less than 0.5% of India's retail market. Nonetheless, Western investors remain excited about the sector, with Flipkart, the "Amazon of India," currently serving 10 million customers, and raising $540 million in capital since 2007.

Overall, the size of the Indian retail industry was estimated to be $500 billion in 2013 and is expected to increase to $750-850 billion by 2015. The Indian bazaar remains stubbornly fragmented, with 90% of the trade dominated by small independent retailers. These shopkeepers, or "Kirana" stores, sell all and sundry, from a single egg to slices of bread. "Organized" shops similar to those found in developed markets often struggle. The high population density of most Indian cities means consumers make frequent, small-volume purchases, since homes are relatively small. Larger stores in urban areas rarely attract distant commuters because few Indians own cars and most prefer the convenience of home delivery from a neighborhood store. Poor storage infrastructure favors smaller retailers in both urban and rural settings, since frequent power outages make storing large quantities of perishable food products a risky proposition.

Retailers, wholesalers, distributors and consumer-goods companies face significant supply-chain risks. Cold storage remains highly unreliable. India is the second largest producer of fruits and vegetables in the world, with a yield of approximately 180 million tons in 2011. Yet it has only 23.6 million tons of cold storage space, 80% of which is used just for potatoes. Around 25-30% of fruits and vegetables perish, as warehousing infrastructure is also substandard. A 2010 study found that nearly 18 million tons of wheat and rice were stored under tarpaulin in India, with tens of thousands of tons rotting due to heavy monsoon rains. Overall, logistics costs represent around 14% of GDP in India; in the U.S., by contrast, the proportion is just 8%. Currently, around 80% of India's goods are transported by the rickety road system, with road-transportation companies also being highly fragmented and sub-scale.

Figure 2

Consumer Spending in India



Source: Businessworld Marketing Whitebook 2012-2013

Fueled by the hopes of a retail boom, India saw a massive growth in shopping malls in the first half of the 2000s and subsequent overcapacity in the industry. A recent report found that the number of malls in India had grown from 50 in 2005 to 470 in 2013 and could touch 720 by 2016. This growth is partly a reflection of the bullishness in the Indian economy and a consuming middle class. Many malls now stand silent.

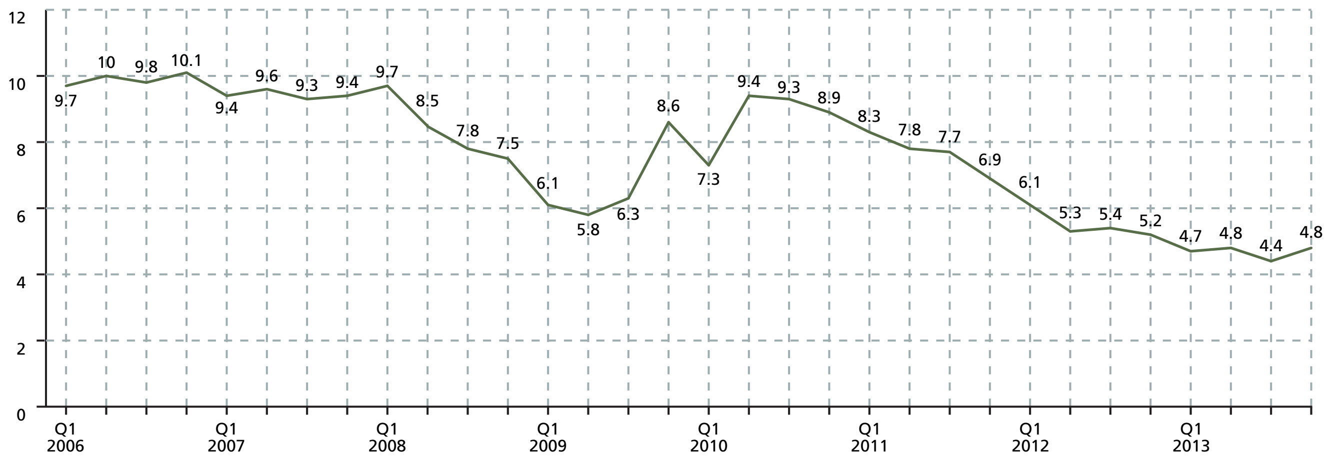
India's Foreign Direct Investment (FDI) policy for retail companies has had a tortuous past, with uncompromising positions held across the spectrum of political parties and frequently changing legislation. Highly vocal opponents of foreign entrants argue that foreign-owned retail stores could lead to the closure of tens of thousands of local corner shops across the country and endanger the livelihood of millions of shopkeepers. The debate has caused legislative indecision for decades. (To wit: A 2011 cabinet decision to allow 51% FDI in multibrand retail was rolled back within a month due to pressure from opposition parties.) Finally, in the last quarter of 2012, the Indian government overturned the ban on majority foreign ownership in multibrand retail, and also allowed 100% FDI in single-brand retail. Since then, 18 single-brand retail FDI proposals have been approved for companies such as Promod, Fossil Inc. and Decathalon.

Nonetheless, most large format supermarket operators such as Walmart and Carrefour are waiting for more clarity in policy before launching stores in India. In December 2013, Tesco unveiled a $110 million plan for a joint venture with a subsidiary of the TATA group to operate a chain of supermarkets. The central government's ruling on FDI in retail allows the state complete discretion in the application of this policy. Uncertainty persists. As recently as January 2014 a change in the state government in Delhi saw the unexpected roll-back of a previously approved FDI policy in multibrand retail in the city-state.

Despite these complexities and challenges, the great Indian bazaar still harbors the latent potential of a billion hopefuls who are optimistic about their future. A boisterous democracy, an aspiring populace and a fast-emerging market make India an enticing global retail opportunity. Yet India poses significant barriers to foreign consumer goods and retail companies that fail to distinguish between India's current reality and its future promise.

Figure 3

India GDP Growth (%)



Source: Trading Economics

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