

Business Opportunity of Retail Franchising in India

Reetu Mehta¹ and Rajiv Kaushik²

¹Research Scholar, IMSAR, MDU Rohtak, Haryana, India

²Professor, Department of Management Studies,
Vasih College of Engineering, Rohtak, India

International Journal of Research in Management Sciences
Volume 3, Issue 4, October-December, 2015, pp. 01-05
ISSN Online: 2347-5943 Print: 2347-8780, DOA : 29102015
© IASTER 2015, www.iaster.com



ABSTRACT

Retailing in India is one of the pillars of its economy. The Indian retail market is among the largest and the fastest growing sectors in the world. India has occupied a remarkable position in global retail rankings. The country has high market potential, low economic risk, and modest political risk. The organized retail segment in India is estimated to be worth \$24 billion, only 2.5% of total retail sales are driven through franchise formats compared with nearly 50% in the US, representing significant potential. Growing awareness, easier access, and changing lifestyles have been the key growth drivers for the consumer market. The Indian retail Industry which comprises organised and unorganised retail is presently estimated at US\$ 490 billion. It has experienced high expansion with a noticeable shift towards organised retailing formats. With bulk of the brands taking the franchise route, the growth forecast in retailing has grown even better. This paper provides a study on franchising business, growth prospectus and factor affecting the franchising business.

Keywords: Franchising, Foreign Direct Investment, Retailing.

1. INTRODUCTION

India's liberalization policies started in year 1991 and have brought the far-reaching changes in Indian economy. The Foreign Direct Investment (FDI) has improved the business opportunities and leading to exciting entrepreneurial accomplishments. Franchising is in the centre of a market revolution in India. The prospects of the expansion in franchising are further boosted by a ample supply of energetic, home grown entrepreneurs making India an exciting market place [1, 2, and 3]. Retailing in India is one of the pillars of its economy and accounts for about 22 percent of its GDP growth. The Indian retail market is estimated to be US\$ 500 billion and one of the top five retail markets in the world by economic value. India is one of the fastest growing retail markets in the world, with 1.2 billion people. India's retail market is expected to expand and reach the market cap of \$1.3 trillion by 2020. Moreover, the GDP is set to grow at 8 per cent over the next three years, making it the world's fastest-growing major developing market. The current retail sales in India is worth \$925 billion and had grown at 5.8 per cent on compounded annual growth rate in 2010-2014. India represents a good opportunity for international retailers in single-brand retail. After two years of latency, Wal-Mart will open a new outlet in Agra and plans to add 50 wholesale stores to its existing 20 in the next five years. Retail sector's high growth potential is attracting investors due to the many reasons. India has occupied a remarkable position in global retail rankings. The country has high market potential, low economic risk, and modest political risk. In terms of market potential, India ranks eleventh after United States, China, Canada, UK, Brazil, Germany, Austria and Mexico [3]-[7]. India's net retail sales are quite significant among emerging and developed nations and the country is ranked third after

China and Brazil. Overall, given its high growth potential, India compares favourably with global peers among foreign investors. By the year 2020, India is projected to be the world's third largest middle-class consumer market behind China and the USA. Further, by the year 2030, India may even surpass both countries with an aggregated consumer usage projected to be nearly US\$13 trillion.

2. RETAIL FRANCHISING

The franchise business in India is becoming more and more popular among domestic and international players across various sectors. As a result, some of the major industries credit successful franchising for their rapid progress in India. According to KPMG India, the key industries with the highest prospects of successfully franchising in India are retail, food and beverages, health, beauty, and wellness, consumer services and education and training. As a business model, franchising is becoming especially widespread in India's metropolitan areas gaining a firm foothold since the government started loosening financial regulations in the early 1990s to encourage a free-market economy. Notably, in 2009, the Indian government lifted the restriction on foreign franchisors to charge royalty rates above certain levels without needing precise governmental approval. Now, foreign franchisors may charge a lump-sum fee and royalty for the transfer of technology and use of a trademark or brand without any maximum limit through the automatic route. Today India is home to more than 3,000 brands which adopt the franchising model.

KPMG India estimates that the franchising industry is expected to quadruple between 2012 and 2017, and will contribute to almost 4% of India's GDP in 2017, growing from a current estimated contribution of 1.4% of GDP. According to the Franchising Association of India, growth of franchising in India are worth US\$13.4 billion in 2012 and expected to witness of 30 percent over the next 5 years.

3. BUSINESS OPPORTUNITY

Retail, food and beverages, health, consumer services, and education are predicted to be the key sectors [8]-[11]. The organized retail segment in India is estimated to be worth \$24 billion; only 2.5% of total retail sales are driven through franchise formats compared with nearly 50% in the US, indicating considerable potential, the KPMG report said. There are presently more than 3,000 brands in India that have adopted the franchise model. Bata, NIIT, Apollo Hospitals, and Titan watches were among the first Indian franchisors. Several leading global companies already have an established presence in India. Recent FDI reforms in single- and multi-brand retail are expected to support this growth, although recent clarifications allowing foreign retailers to only open company-operated outlets could pose a hindrance.

Hindrance in Franchising Business

Nevertheless, there still remain a number of legal, political, business, and cultural barriers that foreign franchisors must consider before implementing a franchise program in India. Franchising in India is still in its emerging stage. Only 10% of the businesses in India are franchised as compared to 70% in the United States. Education sector which accounts for the maximum portion of the total franchised business in India is only 38% franchised as a sector as a whole.

Indian franchising story has just started and it has a long way to go. India would be able to do so with its huge population, the growing aspirations and prosperity of the middle class, changing lifestyles, growing entrepreneurial culture, and the shifting of gears to small cities and towns [12]-[14]. All these factors will lead to the growth of a succeed partnership between the brand and franchisee.

In an emerging market like India, the trend of business expansion through franchising is gaining popularity and it has now become crucial to identify various economic aspects of this business model. A successful franchise business depends on the understanding between franchisor & franchisee. In education sector various professional course coaching franchisees are paying about 35-40% royalty while a pre-school franchisee and similar franchisees are paying about 15-18% but still the former is more contented as compared to the latter. What are the factors that decide satisfaction level of a franchisee? What steps do they follow before taking the big decision of buying a brand? What are the current trends in the franchising business in India? How many franchisees are planning to continue this business for a long term and what percentage of them are planning to start up their own businesses since they have gained enough expertise and exposure through this opportunity? Who could be an ideal franchisee? These are some of the important questions with which every franchisor is struggling. A franchisor has to be observant while selecting an appropriate partner for his business. On the other hand a franchisee too has apprehensions and expectations; they want profitability, cooperation, better communication and understanding from the franchisor.

4. OPPORTUNITY IN INDIA

The consumer durables market is expected to reach US\$ 12.5 billion in 2015 and US\$ 20.6 billion by 2020. Urban markets account for the major share of total revenues in the consumer durables sector in India[1]-[3]. There is a lot of scope for growth from rural markets with consumption expected to grow in these areas as penetration of brands increases. Further, demand for durables like refrigerators as well as consumer electronic goods are likely to witness growing demand in the coming years in the rural markets as the government plans to invest significantly in rural electrification. The FMCG sector has grown at an annual average of about 11 per cent over the last decade. The overall FMCG market is expected to increase at of 14.7 per cent to touch US\$ 110.4 billion during 2012-2020, with the rural FMCG market anticipated to increase at a CAGR of 17.7 per cent to reach US\$ 100 billion during 2012-2025. Food products is the leading segment, accounting for 43 per cent of the overall market. Personal care (22 per cent) and fabric care (12 per cent) come next in terms of market share. Growing awareness, easier access, and changing lifestyles have been the key growth drivers for the consumer market. The Government of India's policies and regulatory frameworks such as relaxation of license rules and approval of 51 per cent foreign direct investment (FDI) in multi-brand and 100 per cent in single-brand retail are some of the major growth drivers for the consumer market. Potential customer segment: Rural consumer: Rural consumers constitute 70% of the total population base and account for only 40 % of total consumption in India due to the minimal penetration of organised retail. Table 1 is showing the trends and facts for different type of consumers.

Table 1

Potential Consumer	Percentage of Population	Size of Business (USD)	Target Area	Remarks
Rural consumer	70%	833 million	Personal care, electronics, food and beverages	localising the product
Working population	50%	600 million	Package food, luxury products, consumer electronics, beauty and wellness	Consumer spending
Youth	28%	500 million	Food and beverages, mobile, personal care, apparels and accessories	Access to more and more money

Middle income households	-	75-300 million	Food and beverages, mobile, personal care, home care	Spending habits
Growing number of millionaires	-	156000 million	Luxury consumer electronics, home furnishing, luxury products	Numbers of millionaires are increasing very fast in India

5. FACTOR AFFECTING THE FRANCHISING GROWTH

In an emerging market like India, the trend of business expansion through franchising is gaining popularity and it has now become crucial to identify various economic aspects of this business model [4]-[8]. A successful franchise business depends on the understanding between franchisor & franchisee. Some important factors affecting franchise businesses are:

Competition: The competition among different franchise business is getting severe, as new players have joined the markets. In India the trend has been most observed in the establishment of fast food chains and retail outlets. As the competition in particular segment increases, the franchisors have to devise new strategies to keep ahead of the competitors.

Value Added Services: the transfers of technology, technical know-how and assistance have become the basic amenities to be provided by the franchisors. The franchisors have added new services like internal communication systems, software support, etc., to add value to the franchisor's services and assistance.

Customer Needs: As globalization continues to show its marks, the customer behaviour has become hypercritical. The customer has a number of options and loyalty can easily be breached. This has led to the customization of services and products according to the needs of the people. Franchisee plays a prominent role in it and keeps the franchisor updated with customer feedback. It is one of the major factors affecting franchise business nowadays.

Legal Environment: Though the implications of the changing legal systems have a least effect on the franchise business, but it may be significant if the laws pertain to the proprietorship or any aspect of business operations. These are some of the major factors that have shaped the franchise business in the country.

Despite the storied growth and positive growth numbers mentioned above, franchisors should take special care to understand all regulatory, legal, political, and business implication of entering the market. While India has rebounded after the global economic crisis, since 2012 it has experienced a moderate slowdown in economic growth. India's legal system is incredibly slow and there are staggering delays associated with Indian court proceedings the path to a non-appeal able final resolution may be prohibitively long. Among the 185 economies covered by the World Bank's 2013 Doing Business survey, India ranks at 184 in terms of countries in which it is easiest to enforce a contract. Further, courts at the lower level may not have the experience to handle complex commercial matters for which foreign franchisors may seek resolution, and such proceedings are not confidential. While FDI restrictions have been relieved in various sectors, India still needs to address its great infrastructure shortfalls like shortages of utilities, poor roads and bridges. Pervasive state control in business activities like number of permits and licenses that may be required to do business can be overwhelming and overly burdensome for a foreign franchisor. Further, unequal access to quality education like areas beyond metropolitan places must continue to develop to sustain growth and a qualified workforce. Excessive government bureaucracy and corruption persists at various levels and has proven to be

difficult to curb. While the Indian government continues to reform the FDI policy, more progress is sought from the business community. India has a diverse consumer base and workforce.

6. CONCLUSIONS

Despite certain concerns, the future for franchising in India is bright. Over the years, India has become an attractive destination for business investments due to the rapid growth of consumerism, globalization, and liberalization. India enjoys a positive economy, large consumer market, and loosening government restrictions. The window of opportunity in India is open. But foreign franchisors should make sure to conduct a thorough investigation and evaluation of business opportunities (taking into account the many legal, political, business, and cultural barriers that may exist) before committing long-term to franchising in India. Franchising is not an industry, so it's not treated as a sector by financial institutions, which makes it difficult for them to raise money. It is important to identify them as a separate segment to increase lending from banks and assist expansion.

REFERENCES

- [1] Collaborating for Growth Report on Franchising Industry in India 2013, KPMG India.
- [2] Consumer Markets - India Brand Equity Foundation Report, August 2015.
- [3] Franchising in India: The Time is Right By Erik Wulff and Abhishek Dube, Legal Services Newsletter, 2014.
- [4] Doherty, Anne Marie, and Nicholas Alexander. "Relationship Development in International Retail Franchising: Case Study Evidence from the UK Fashion Sector." *European Journal of Marketing* 38, No. 9/10 (2004): 1215-1235.
- [5] Alon, Ilan. "The Use of Franchising by US- Based Retailers." *Journal of Small Business Management* 39, No. 2 (2001): 111-122.
- [6] Welsh, Dianne HB, Ilan Alon, and Cecilia M. Falbe. "An Examination of International Retail Franchising in Emerging Markets." *Journal of Small Business Management* 44, No. 1 (2006): 130-149.
- [7] Sengupta, Anirban. "Emergence of Modern Indian Retail: An Historical Perspective." *International Journal of Retail & Distribution Management* 36, no. 9 (2008): 689-700.
- [8] Hoffman, Richard C., and John F. Preble. "Global franchising: Current Status and Future Challenges." *Journal of Services Marketing* 18, no. 2 (2004): 101-113.
- [9] Halepete, Jaya, KV Seshadri Iyer, and Soo Chul Park. "Wal-Mart in India: a Success or Failure?" *International Journal of Retail & Distribution Management* 36, no. 9 (2008): 701-713.
- [10] Sinha, Piyush Kumar, and Sanjay Kumar Kar. "Insights into the Growth of New Retail Formats in India." *Retailing in the 21st Century*. Springer Berlin Heidelberg, 2010. 119-140.
- [11] Westfall, Ralph, and Harper W. Boyd Jr. "Marketing in India." *The Journal of Marketing* (1960): 11-17.
- [12] Mann, Manveer, and Sang-Eun Byun. "Accessing Opportunities in Apparel Retail Sectors in India: Porter's Diamond Approach." *Journal of Fashion Marketing and Management* 15, No. 2 (2011): 194-210.
- [13] Gulati, Ashok. *The Rise of Supermarkets and Their Development Implications: International Experience Relevant for India*. Vol. 752. Intl Food Policy Res Inst, 2008.
- [14] Chari, Anusha, and T. C. A. Madhav Raghavan. "Foreign Direct Investment in India's Retail Bazaar: Opportunities and Challenges." *The World Economy* 35, no. 1 (2012): 79-90.