# India seen relaxing rules for retailers

## Govt appears anxious not to scare off Ikea, which has baulked at sourcing requirement

[MUMBAI] India's government appears set to relax heavily criticised sourcing rules for retailers, anxious not to scare off Ikea – one of the few big name firms that has said that it will invest in the country – or any others willing to follow.

India kicked open the door to foreign retailers in January when it removed an investment cap for single brand chains to set up shop but then shot itself in the foot by imposing a requirement that companies had to source 30 per cent from small local firms.

Ikea and others have baulked, and the government's response is being seen as a test case of how well it can revive flagging investor confidence at a time when economic growth has slowed to its weakest in nine years.

Signs point to backtracking on the part of the government, with a top official closely involved in framing retail policy telling Reuters that key clauses may be relaxed although the government was still discussing the pros and cons as well as the extent of any relaxation.

"We are in the process of finalising our views about all this," said the official, asking firms to "be a little patient".

Analysts are confident that there will be an easing of the rule.

"The government is in damage control mode. It realises it has sent out a wrong signal by putting the 30 per cent sourcing requirement for foreign retailers," said Saloni Nangia, senior vice president for retail at Technopak consultants.

Prime Minister Manmohan Singh this month also held up the Swedish furniture giant's planned US$1.8 billion investment as an example of investor confidence, while the trade minister said that its already substantial amount of sourcing from India would be taken into account.

New Delhi is also pushing to resuscitate a reform to allow foreign retailers that sell many brands – supermarkets such as Wal-Mart Stores – to invest in the country with a 51 per cent cap on ownership. At the moment, they are only allowed to operate in a wholesale capacity.

The government's plans were scotched last year by a political backlash but India could launch the policy within weeks if the political climate is right, the official involved in retail policy said.

"We are pushing to the extent we can," he said. "Multibrand retail is only a pause. There are no major issues there."

The sourcing rule for single-brand retailers currently stipulates that local suppliers must not have more than US$1 million invested in plant and machinery.

The rule was designed to ensure that India's manufacturing sector, which pales next to China's, benefits from foreign money rather than being muscled aside by imports. But it represents a headache for retailers looking for scale and reliable, high quality suppliers.

Ikea has asked for a 10-year window to comply with the rule – a timeframe that the government has said is too long.

"It will take us time to fully live up to the requirements," said Josefin Thorell, a spokeswoman for Ikea. The company has declined to comment on how it would respond if it did not get 10 years.

UK-based footwear retailer Pavers, the only other retailer besides Ikea to apply for wholly owned operations since the rule change, is asking that sourcing not be measured based on the value of goods sold.

"Our request along with the industry is that 30 per cent of that should be on the cost price instead," said Utsav Seth, chief executive of Pavers' Indian operations, although he added that Pavers would comply with the current rule if its request was denied.

In addition to ironing out these policy matters, the government is also rethinking what to do if a supplier grows beyond its original size. According to a policy document in November, an Indian company would be disqualified from supplying a foreign firm if it grew beyond its original US$1 million investment.

"I would call it penalising success," said Devangshu Dutta of Third Eyesight, a retail consultancy. "If you are successful in actually helping small companies grow, they would be penalised because they would not be able to supply you any more. And you would be penalised for helping them grow."

Another rule, one that says that an investor must own the brand that it is proposing to bring to India, may also be relaxed, said the official involved in retail policy.

This has tripped up Spain's Inditex SA which applied for permission to bring a second clothing brand, Massimo Dutti, to India in addition to its flagship clothing brand Zara.

The government has put that proposal on hold after the application was not submitted by brand owner Inditex but by its wholly owned unit Zara Holdings BV. – *Reuters*