

Chapter 2

Modern Organised Retail and Its Impact on Agriculture

C. Rangarajan

We would prefer to use the term ‘modern organised retail’ to what has been referred to as ‘organised retail’, as traditional retail is also organised but perhaps in a different way as compared to modern retail. The present system of retail has been able to reach out to millions of consumers not only in the urban areas but also in the remote villages. The essential difference between traditional retail and modern organised retail is that in traditional retail, marketing passes through a number of intermediaries, whereas modern organised retail follows the practice of direct procurement or procurement through big procurement agencies.

Modern retail in all commodities in 2008 constituted about 4 % of the total retail in India, while in the food and grocery segment the ratio was less than 1 %. It is, however, projected that if the current trend of high growth rate in this sector continues, retail in food and grocery segment could rise to up to 15–20 % of the total retail. According to a report by BCG and CII (2011), in the last 3 years modern retail has grown at the rate of 24 % as against traditional retail which grew at the rate of 10–12 %.

If we look at the supply chain, the stakeholders in the chain would be the consumers, retailers, processors, wholesalers, commission agents, logistics providers, and primary producers or farmers. Other entities such as input dealers, bankers, and insurance companies support the supply chain in various ways. The growth of modern retail impacts all stakeholders—some positively and some negatively. The calculation of gains and losses is often complex and difficult. However, the ultimate test is the impact it has on producers and consumers.

Inaugural address delivered at the international seminar on ‘Organized retailing vis-à-vis farm economy of India’ at the Centre for Economic and Social Studies, Hyderabad on September 21–22, 2012.

C. Rangarajan (✉)
Madras School of Economics, Chennai, India
e-mail: c.rangarajan@mse.ac.in

© Springer India 2015
N. C. Rao et al. (eds.), *Organised Retailing and Agri-Business*, India Studies
in Business and Economics, DOI 10.1007/978-81-322-2476-1_2

2.1 Forms and Aim of Organised Retail

Modern organised retail can take several forms, from small neighbourhood stores (like Mother Dairy outlets) to air-conditioned malls (like Big Bazaar). The aim of modern organised retail should be to offer better prices to both consumers and producers and to reduce the gap between the two. Modern retailers are able to offer better prices to consumers and producers because of the economies of scale in procurement, handling, and logistics.

The main demand-side factors driving the rise of super markets are rising incomes, a burgeoning middle class, greater participation of women in the work force, and increasing urbanisation. Big modern retail chains tend to begin operations in large cities and then move onto intermediate towns and rural areas which are more price sensitive. They focus first on high-income customers and then move onto middle- and low-income customers. Similarly, they first begin operations with the marketing of processed items, and then move on to semi-processed and then fresh items.

2.2 Consumers and Modern Retail

The Indian consumer spends more than half of his expenditure on food items. Here, it is worth noting that the prices of vegetables, fruits, milk and eggs, meat, and fish have been rising faster than cereals. This is so in spite of the fact that India is the second highest producer of fruits and vegetables (about 200 million t p.a.) producing 17 and 14% of the global total vegetables and fruits, respectively. The existing channels of trading perishables are restricted by (a) the application of the APMC Act to perishables in many states, and (b) shortage of adequate cold storage facilities. For fruits and vegetables, the price at the first point of sale in large *mandis* as a proportion to the final retail price is in the range of 25–40%.

Modern retail has been found to offer better prices to consumers than traditional retail, thus helping to contain inflation. The supermarket chains build regional and global procurement networks which reduce costs, they de-seasonalise offering and increase product diversity. Modern retail also helps in conveying consumer preference to the producers. This helps producers in channelising their resources towards production of those crops/items that would guarantee them reasonable returns. Modern retail also ensures quality and safety standards for different products for the consumers. Thus, modern organised retail out competes traditional retail on price, variety, and quality. They offer greater convenience and better shopping environment to the consumer.

The main concerns that emanate from modern retail are the possible displacement of middlemen (and their consequent unemployment), and the implications of the new channels on the farmers' wellbeing. The chief merit of a good distribution system is to ensure that the benefits of increasing demand are passed on to the

farmer. At the same time, the benefits of higher production and productivity must accrue to the consumer.

2.3 Impact of Organised Retail on Traditional Retail

An overwhelming percentage of food and grocery being sold in this country is through traditional retail outlets such as kirana stores, street hawkers, and wet market stall operators. Once the share of overall modern retail in food reaches about 25–30%, it is bound to alter the way the traditional channels of retail function. These kirana stores, street hawkers, etc. can also become a part of the modern retail change story if they (a) can be assimilated into organised retail; (b) are upgraded through infusion of capital, better training, etc.; and (c) can organise themselves under their banner through franchises, etc. The existence of large retail chains even in advanced countries has not wiped out the small shopkeepers or what are called ‘Mom and Pop’ stores. They retain a personal touch which is absent in large retail outlets. Also their proximity to where people live is a great advantage.

2.4 Farmers and Organised Retail

The experience of other countries in organised modern retail of food shows that processed food occupies the largest share of retail (roughly 65%), followed by semi-processed food (about 20%), and fresh food (about 15%). Farmers are increasingly realizing the gains from not only direct links to organised modern retailers but also to processors. A study commissioned by the World Bank in 2007 showed that in India the average price received by the farmer in a typical horticulture product is only 12–15% of the price paid by the consumer. It has also been found that there is a wide disparity in the prices of horticulture products across markets in the country. For instance, on the basis of available data, the mandi prices for brinjal averaged ₹ 1187 per quintal in December 2010. However, prices aggregated by states ranged between ₹ 342 (Uttarakhand) and 3554 (Tamil Nadu) per quintal and the coefficient of variation was 62%. It may be recollected that in the winter of 2010–2011 there was a most unusual runaway price increase in vegetables which began with onion but rapidly spread to tomato, brinjals, and other items. However, even in December 2009 where seasonal price behaviour was normal, while the average price was ₹ 541 per quintal, the range was between ₹ 242 (Madhya Pradesh) and 2223 (Tamil Nadu) and the coefficient of variation was 62%. Thus, the emergence of modern retail will cut the middle men out of the chain thereby giving better remuneration to the farmers as their bargaining power goes up. However, modern retailers tend to procure more from large farmers. Hence, gains from modern retail go to a privileged section of farmers. Therefore, there is a need for farmers to organise themselves into groups or clusters so that they can maximise their bargaining power with modern retail chains.

2.5 Cooperatives and Organised Retail

The success of Amul and Mother Dairy clearly bring out how organised retail can be very beneficial not only to the consumer but also to the farmer. Operation Flood pioneered by Dr. Verghese Kurien changed the entire dimension of the dairy sector in India. The National Dairy Development Board (NDDB) has transformed India from a nation suffering milk shortage to be the largest producer of milk in the world. The processing units procure milk from dairy cooperatives, chill and homogenise the milk, and sell it through their retail outlets which have wide spatial and market penetration. These retail outlets under recognisable brand names carry a lot of credibility with the public. This model is worth emulating in other agricultural products. Safal is an example of successfully organised retail of fruits and vegetables.

2.6 Contract Farming and Organised Retail

Various International Food Policy Research Institute (IFPRI) studies (on Mother Dairy, Nestle, and Venkateshwara Hatcheries) have shown that contract farmers earn higher as compared to noncontract farmers. Contracting reduces cost of production by cutting down marketing and transaction costs. Contracting also gives them access to global markets as against local markets which offer them the best prices. An IFPRI study on Mahagrapes done in 2006 found that annual profits earned per acre by the contract growers was 38% higher than the noncontract growers because Mahagrapes caters to the global markets as against noncontract workers catering to the local markets.

Modern retail also helps farmers learn about consumer preferences. This enables them to diversify into the more remunerative crops. Clustering of farmers into viable size enables farmers to match their supplies with the type and size of demand. Farmers gain twofold when they sell to organised retail: (a) they get better prices than what they would otherwise get for the same produce; (b) there is minimal wastage as procurement agencies have the wherewithal for timely lifting the produce and storing it in ideal conditions, for offloading it into the market in future, or for exporting it to other destinations.

In a study done by Ghosh and Vadivelu in the Mother Dairy outlets in Solan district of Himachal Pradesh, it was found that the farmers selling to Mother Dairy bore 30% of the marketing costs as against 65% borne by the farmers selling via the traditional retail route.

2.7 Markets for Agricultural Commodities and APMC Act

Most vegetables and fruits are currently marketed through transaction systems governed by the Agriculture Produce Marketing Committee (APMC) Act regulations. Market yards or *mandis* set up under the act are supposed to play a vital role in price

discovery by creating an environment where there is a free play of market forces of supply and demand and transparency in transactions. It was started as a protective regime for farmers to enable them to secure fair prices.

However, the supply chain in the *mandis* involves a large number of intermediaries between farmer and consumer, namely a sequence of commission agents and traders at the wholesale level and the retailer. At every stage, there is a price mark-up and delay due to transportation, packing/unpacking, market charges, etc. Both the wholesaler and retail traders have to buy farm produce from the *mandis*. Similarly, farmers have to sell in the *mandis*. However, many *mandis* are dysfunctional and maybe even nonexistent in practice. The *mandis* have not encouraged the cleaning, sorting, grading, and packaging of agricultural produce before sale by the farmers. Thus, the APMC regulations have had some undesirable consequences.

In a bid to provide more competitive choices to farmers and to encourage private investment, the Ministry of Agriculture circulated a Model Act in 2003 amending certain portions of the APMC Act. These reforms deal with direct marketing, contract farming, and markets in private/cooperative sector. Seventeen states have already amended the APMC Act as per the provisions of the Model Act. Some others have made modifications only through administrative orders.

The 12th plan Working Group on Horticulture and Plantations is of the view that certain common standard operating procedure (SOP) for all markets, i.e. the modern and regulated markets under APMC Acts, must be introduced. As against the 12th Plan Approach Paper, the 12th plan is not in favour of removing perishables from the purview of the APMC Regulations. However, I do believe that there is a strong case for removing perishables from the purview of APMC regulations as the nature of the commodity requires speedy transaction in order to minimise wastage. It would be in the best interest of the producer either to conclude the transaction speedily or to keep the produce in cold storage till he can earn a more remunerative price. Two examples of direct marketing from producers to consumers are Rythu Bazars in Andhra Pradesh and Shetkari Bazar in Maharashtra. These markets have enabled both ends of the supply chain gain better prices and the delivery of fresh produce to the consumer.

Direct marketing of produce to modern organised retail networks also helps the farmer in getting a better price than through *mandis*. Regular supply agreements with groups of farmers and modern retail outlets will help farmers have an assured minimum income besides cutting down on wastage, transportation costs, and providing fresh supply of food items to consumers.

2.8 Modernisation of Procurement Systems

Modernised procurement systems form the base on which successful organised retail system operates. The traditional logistic systems suffer from various inadequacies, namely (a) multiple handling of produce, inadequate cold chains leading to high wastage; (b) institutional shortcomings flowing from the existing APMC Act has perpetuated a framework with uncompetitive and non-transparent markets; and

(c) inadequate processing facilities. The weakness in the food logistics system has led to temporary shortages which have resulted in the rise in prices.

The existence of an efficient cold chain storage network is a prerequisite for an effective market in horticultural commodities. The number of cold storages has increased from 600 in 1965 to 6284 in 2012. The installed capacity in 1000 million ton has increased from 682 to 29,305 over the same period. In terms of spatial distribution, north India accounts for 47% of the total number of cold storages and 52% of the capacity of cold storages in the country.

Uttar Pradesh followed by West Bengal has the highest number of cold storages in the country. In spite of the substantial growth in the number of cold stores, they fall woefully short of their requirement. Cold storage facility is available for only around 10% of fruits and vegetables. An investment of about ₹ 14,000 crores may be required during the 12th Plan to suitably augment the existing storage capacity. A further investment to the tune of ₹ 22,000 crores will be required in order to extend cold storage facilities to 25% of the fruits and vegetables.

Seventy-five percent of the cold storage capacity is used to store potatoes, while only 23% fall in the multiproduct category. Cold storages for meat, fish, and dairy items, and for other items such as chillies and other spices account for only 1% of the total cold storage capacity. Further enhancement in the cold storage capacity would be very beneficial to both the farmer and the consumer as it minimises wastages, provides fresher and off-seasonal food items to the consumers.

Modernised procurement systems reduce costs and improve product quality. The catchment area of such procurement agencies may be at a national, regional, or global level. They shift from reliance on traditional wholesalers to nontraditional, specialised wholesalers and logistics firms. They enforce private standards on behalf of supermarkets. Normally, the modernisation of procurement systems of processed products precedes that of semi-processed and fresh foods. However, this pattern may be reversed in developing economies like India.

In order to strengthen backward integration, procurement agencies should not only connect with farmers for output but must help them in providing critical inputs like finance, insurance, technical expertise, storage facilities, etc. This would enable farmers to become more competitive both in national and international markets. Thus, supplying to supermarkets can be a springboard for exports even to small and medium farmers.

2.9 Uttarakhand Example of Modern Retail vis-à-vis Traditional Retail

The IFPRI and the Asian Development Bank (ADB) published a research report in 2009 regarding certain issues in traditional value chains of high-value crops in Uttarakhand. It was found that farmers faced transaction costs that are between 25 and 38% of the price paid by the retailer in the wholesale market. The report also

brought out the example of how modern food retailing in collaboration with NGOs had transformed the cultivation and livelihood patterns for the Rawain Valley to the north of Dehradun. Establishment of local collection centres led to a dramatic rise of cultivation of off-seasonal vegetables from 5 to about 50%. The condition of both the farmers as well as the consumers improved, and both got better prices.

2.10 Modern Retail and International Trade

As already stated organised modern retail acts as a spring board for even small and medium farmers, and industry. Global retail chains procure globally. They offer domestic producers the window to sell their products in the global markets at the best prices.

2.11 FDI and Retail

In January 2012, the Government of India (GOI) approved reforms in single brand retail with 100% foreign ownership, with the requirement that 30% of the goods should be sourced from the local suppliers (SMEs, artisans, etc). This backward linkage has been put in place to ensure that the interests of the small players are safeguarded. The bigger reform announcement which would give a substantial boost to the retail sector is the government decision to allow FDI in** multi-brand retail upto the extent of 51%. This decision would also lead to a commensurate growth in related infrastructure as 50% of the total FDI brought in has to be invested in 'back-end infrastructure' within 3 years of the induction of FDI. Back-end infrastructure includes processing, manufacturing, distribution, design improvement, packaging, quality control, logistics, storage, warehouse, and agriculture market produce infrastructure. Many farmer organisations such as the Bharat Krishak Samaj and Maharashtra Rajya Shetkari Sangathan have welcomed this decision of the government. The modern retail will give an alternative to the restrictive auction system in the *mandis*. As mentioned earlier, the fear that this could result in large-scale replacement of small retailers is misplaced. India is a vast country; there will be place both for large as well as small retailers. Each has its own advantages. There can in fact be a mutually beneficial impact.

Modern retail in the country is at a nascent stage and is evolving in terms of scale of operations, store format, and merchandise mix. The traditional systems and modern retail chains are complementary to each other and their coexistence is important for each other's functioning while providing options to producers and consumers.

<http://www.springer.com/978-81-322-2475-4>

Organised Retailing and Agri-Business
Implications of New Supply Chains on the Indian Farm
Economy

Rao, N.C.; Radhakrishna, R.; Mishra, R.K.; Kata, V.R.
(Eds.)

2016, XVI, 311 p. 29 illus., Hardcover

ISBN: 978-81-322-2475-4