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Skepticism and Caution Greet India’s New Policy on Retailers

By VIKAS BAJAJ

MUMBAI, India — When Indian policy makers announced last week that they would allow big-box foreign retailers like Wal-Mart into the country, they pledged that it was the beginning of a long-awaited second wave of economic reforms that would make the country more hospitable to business.

If they follow through, it could prompt a new economic boom in India, where once-brisk growth has slowed markedly in recent years.

But it is a big if.

Just a few days into the effort, concern is growing about whether the latest steps, which also include reductions in fuel subsidies and changes in aviation policy, go far enough, and whether the government will be able to carry out even these limited proposals in the face of stiffening opposition from political allies and opponents.

On Tuesday, an important regional leader, Mamata Banerjee, announced that she would withdraw her support from the governing national coalition on Friday afternoon if policy makers did not abandon their change agenda. Ms. Banerjee, a tenacious politician from West Bengal, last year helped torpedo an earlier effort to open the doors to foreign retailers.

Even if the governing coalition, led by the Indian National Congress Party, retains power, it is unclear how it will push through more changes with the help of other partners. And if it keeps Ms. Banerjee in the alliance by accepting her demands, the Congress party will find it difficult to make the case for bigger changes in taxation and policies governing land and natural resources. Skepticism of the government’s commitment to change runs deep, given a long history of disappointments.

“I am grossly underwhelmed,” said Arvind Singhal, chairman of Technopak Advisors, an Indian consulting firm. “This is just the tip of the much larger thing that needs to be done.”

But analysts and executives say the new thrust is critical to reviving flagging business confidence and persuading companies to dust off mothballed investment plans. India’s economy, which recovered quickly to an 8.4 percent annual growth rate after the financial crisis, is now slowing sharply and could grow as little as 5.4 percent in the fiscal year that began in April, economists say.

The Congress-led alliance has struggled to approve any significant economic policies in the eight years it has been in power. So letting foreign supermarkets enter the country, in particular, had become a litmus test of sorts for many investors and credit rating agencies about its commitment to liberalizing India’s economy.

“This will be a game changer not because of its immediate impact but because it redefines the feasibility of reforms in the current political environment,” said Eswar Prasad, an economist at Cornell and the Brookings Institution who advises the Indian government.

Still, analysts complain that as politically difficult as the most recent changes were to enact, they do not go far enough.

The new retail policy, for instance, will allow each of India’s 29 state governments to block stores owned by foreign chains like Wal-Mart and Tesco. In aviation, the new policy would allow foreign airlines to buy only a 49 percent stake in their Indian counterparts, most of which are losing money. That restriction, with India’s seemingly limitless financial support for the beleaguered state-owned Air India, is expected to deter many would-be investors.

Some in the government appear to recognize that they must do more. On Monday, Palaniappan Chidambaram, who recently was named finance minister and helped undo some of India’s socialist and protectionist policies during a previous stint in the job, said that the government would announce more changes before the end of October.

If the new retail policy does take effect as announced, companies like Wal-Mart and Ikea could be big winners.

Retail sales in India total about $500 billion a year, but less than 10 percent take place in modern stores. Much of retailing is made up of small shops owned and run by families that have long opposed foreign investment. But young Indians are increasingly drawn to air-conditioned malls and department stores where couples and gaggles of teenagers can hang out openly without worrying about offending their more conservative parents and grandparents.

Wal-Mart, which with an Indian partner has 17 wholesale stores in India, is expected to be the biggest immediate beneficiary of the new policies, which will allow it to take a 51 percent stake in an Indian retail operation. Retail chains with a foreign investor will be allowed to open stores in and near cities with at least one million people as long as states give consent, and both New Delhi and Mumbai are expected to get new outlets.

Rajan Bharti Mittal, an executive of Wal-Mart's Indian partner, Bharti Enterprises, said the conditions imposed by the government — including a requirement that foreign retailers spend at least $100 million, with half of that going to processing and other back-end operations — were acceptable.

Mr. Mittal said the companies would soon begin negotiating a new agreement and planning their expansion. Bharti already operates more than 200 retail stores that are supplied by Wal-Mart and operate under the Easy Day brand.

Though only 10 Indian states have said they will allow foreign-backed retail stores, Mr. Mittal said he expects many more to do so in the coming years once they realize that the stores will create jobs and help subsistence farmers by buying directly from them at higher prices than the wholesale traders who have a monopoly on most food trade in India.

"I am quite certain that other states will see the advantages" of foreign investment in retailing, Mr. Mittal said. "The naysayers will become yes-sayers."

Another beneficiary is Ikea. The Swedish furniture retailer, which is allowed to set up wholly owned stores under current Indian policies for companies that sell only one brand of products, announced in June that it would invest about $2 billion in India. But its plans had been stuck because of a requirement that foreign retailers buy 30 percent of their merchandise from small Indian businesses. Last week, the government said that obligation would now be voluntary.

Other foreign companies seem less eager to enter the Indian market even after the recent changes. Tesco, the British supermarket chain that has a partnership with India's Tata Group, issued a statement saying it would not announce new plans until it received "further detail on the conditions" imposed by India.

And Lufthansa and British Airways, major European airlines that have many flights to and from India, have said they are not interested in investing in Indian airlines.

The United States ambassador to India, Nancy Powell, said the recent changes were welcome. However, she added a note of caution, born of experience: "American companies are going to look very closely at the fine print."

Analysts say that hesitation is understandable because poor infrastructure, widespread corruption and a weak judicial system make India a hard place for foreign investors to do business, especially in industries like retailing and aviation.

"Strategic investors will wait to see some clarity," said Vikas Khemani, president of wholesale capital markets at Edelweiss Securities here. "A lot of investors like Wal-Mart have already expressed interest in India, but I don't see anything happening immediately until the policy environment is cleared up."

Neha Thirani contributed reporting from Mumbai and Jim Yardley from New Delhi.