



ROUND TABLE

# Distribution challenges and workable solutions

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## KEYWORDS

Distribution channels;  
Channel management;  
Indian retail;  
FDI in Indian retail

**Abstract** An effective distribution channel can be a source of strategic advantage for companies. However, little research exists about the distribution channel structure in India, which is largely traditional and quite unique. The first part of this round table article provides an overview of distribution channels, particularly their constituents and structure, with a special focus on distribution channels in India. The second part of the article reports on a panel discussion with eminent academic and industry experts on the challenges that companies in India face in designing, constructing, and managing distribution channels on the ground.

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## Academic perspective

### Introduction

Distribution channels are pathways along which products travel from producers and manufacturers to ultimate consumers. They are routes along which products, information, and finance flow. While some manufacturers deal directly with their customers, most manufacturers use a distribution channel to take products to consumers. Considerable

thought, effort, and investment are required to create and maintain a distribution channel. Channel margins and the expense of sales efforts in managing channels can form a substantial proportion of total marketing costs. An effective channel can be a source of strategic advantage for companies. Channel design and channel management are therefore important elements in a company's competitiveness. Channels are also important from a public policy perspective since they employ a large number of people and are critical to the unhindered availability of food items and other products to customers across the socio-economic spectrum. Although channels are very important, little research exists about Indian distribution channels. This note and the accompanying round table presentations therefore attempt to focus on distribution channels in India, especially on the challenges that companies in India face in designing, constructing, and managing distribution channels. The aim is to identify important challenges, examine the relevance of research findings, and develop an agenda for future channel related research in India.

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## Distribution channels

Distribution channels can be understood by analysing their constituents, structure, functions, and contributions. Channels consist of networks of different types of independent businesses which need to be aligned to assist manufacturers in fulfilling and creating consumer demand for products and services. Channels consist of three categories of entities: agents, merchants, and facilitators. Agents promote products and generate sales but do not themselves buy and stock products. Agents can be independent or they may be employees of the company. Merchants such as retailers, wholesalers, and distributors buy, stock, and sell goods to others in the chain or to ultimate consumers. Merchants are usually independent but some companies may have their own wholesale trading units or retail outlets. Facilitators such as logistics service providers, independent warehouses, carrying and forwarding agents, and transporters facilitate movement, storage, and delivery of products but are not involved in promoting or trading. Distribution channels are configured by putting together agents, merchants, and facilitators in specific ways depending on the market, product, and competitive context.

Channel structures vary across countries and industries, but all channels can be described using simple concepts such as directness, levels, density, variety, and novelty. Directness refers to the process of direct sales between manufacturers and consumers without any intervening channel member. Indirect distribution occurs when a manufacturer uses channel members to sell to consumers. Researchers have identified a number of conditions which influence whether direct distribution or indirect distribution is appropriate (Rangan, Menezes, & Maier, 1992). The concept of levels indicates the number of different buying and selling entities that exist between a manufacturer and a consumer. In the automotive industry, manufacturers sell to franchised exclusive dealers who in turn sell to final consumers. This is termed as a one-level channel. In the FMCG industry it is common for companies to sell to stockists who sell to retailers who in turn sell to consumers. This is an example of a two level channel. Density refers to the number of outlets within a certain geographic area. The fewer the number of outlets, the more exclusive is the distribution, and the more the number of outlets, the more intensive the distribution. The distribution of luxury cars with just one or two outlets in a district or city can be termed as exclusive while the distribution of matchboxes with thousands of outlets may be termed as intensive. Variety refers to the number of different types of outlets. Biscuit distribution may exhibit high variety since biscuits are available in paan stores, groceries, general stores, supermarkets, canteens, vending machines, and even online; while distribution of silk sarees may exhibit low variety in terms of channels used. Novelty refers to the utilisation of new types of channels. Online channels and vending machines are comparatively new in India and would therefore be considered to have a higher level of novelty compared to direct marketing or network marketing channels. Distribution channels are evaluated using three major criteria: effectiveness, efficiency, and adaptability. There is little research in the Indian context

on the factors that affect channel effectiveness and efficiency. A good understanding of the factors will aid in modifying channel structure in response to changes in the channel or environment.

A major challenge in channel management is keeping channel members motivated to support the principal, especially when markets are tough. Channel member profitability is a major driver but not the only factor affecting channel member satisfaction and motivation. Skilled channel managers make concerted efforts to measure and monitor channel profitability and channel members' return on investment (ROI). In addition to ensuring healthy ROI, firms utilise a variety of financial and non-financial incentives to motivate channel members. Channel incentives can range from credible channel policies, market development support, supplemental contact, high powered incentives, and end-user contact (Gilliland, 2004). Research is required in the Indian context about the motivational effectiveness of various types of channel incentives. Conjoint studies of channel member margin and incentive packages may be useful.

The nature and characteristics of channels also depends on the level of economic development. Research has suggested that channels in developed countries are likely to have larger wholesalers, larger retailers, and fewer levels in the channel when compared to channels in less developed countries (Olson & Granzin, 1992). Channels in developed markets are also characterised by organised retail and wholesale chains, considerable use of technology and data by channel members, informed customers, high Internet penetration, sophisticated logistics, and strong implementation of laws and regulations. Distribution channels in emerging markets are characterised by unorganised retailing and wholesaling; smaller, independent retailers and wholesalers; more levels in the distribution chain; less use of technology and data by channel members; scantier penetration of Internet; evolving logistics infrastructure; and poor implementation of laws and regulations. Emerging markets also have large base-of-pyramid (BOP) and rural markets which pose unique challenges for distribution. Channels change over time even if changes appear to be very slow. Channel change may be influenced by market drivers such as volatility in consumer needs, consumer sophistication and channel sophistication; environment drivers such as volatility in competitors' strategies and environment conflict; and firm drivers like company size and scope economies (Coelho & Easingwood, 2008).

## Distribution channel structure in India

The distribution channel structure in India is largely traditional and quite unique. The major channel components are the retail network, wholesale network, and the logistics infrastructure. The retail network in India consists of over nine million outlets. These include traditional outlets like paan shops; grocers or kirana stores; general stores; specialised shops for footwear, clothing, jewellery, watches, mobile phones, and consumer durables; newer formats like supermarkets, hypermarkets, and online stores; and service outlets like fast food outlets, beauty parlours, fitness centres, coaching centres, and so on.

Traditional outlets are spread across urban and rural India but the newer formats are mostly located in urban areas. The penetration of organised retail in India which is less than 8% is quite low even in comparison to other emerging markets. The average retail outlet in India is very small in terms of area, number of employees, and number of stock keeping units (SKUs) stocked. Traditional retail in India offers consumers a number of advantages like convenience, home delivery, credit, and personalised service. On the other hand, modern retail offers periodic promotional offers, lower prices, wider assortment, a better ambience, and higher quality brands. The continued existence of traditional retail in India has been based on factors such as lower rentals, lower labour costs, credit from suppliers, low or no liability on taxes, and a legal framework which prevented foreign direct investment (FDI) in retailing until quite recently. Traditional stores have managed to hold their own against organised Indian retailers so far by making some changes in their operating practices. It will be interesting to see how traditional Indian stores will fare in future after the entry of price aggressive international retailers. Research in Latin America suggests that small traditional stores have lower sales per floor area and lower gross margins compared to modern retailers but they survive because of higher inventory turnover (D'Andrea, Lopez-Aleman & Stengel, 2006). Research in Chile suggests that local retailers can successfully compete with foreign retailers by implementing best practices and focussing on the requirements of local customers (Bianchi & Mena, 2004).

Notwithstanding the many advantages offered by traditional retailers in India, modernisation has picked up in many sectors such as apparel retail, watch retail, and footwear retail. Modernisation seems to have resulted from both supply side and demand side factors. Supply side factors supporting modernisation are the large investments in retail made by brand owners in watches, textiles, and footwear; development of malls and shopping centres; and the entry of large Indian business groups into grocery and electronics retailing. Demand side factors include increased disposable income among consumers, greater brand consciousness, greater appreciation of ambience and air conditioning, and perception of shopping as a rewarding leisure activity. One important sector where the pace of modernisation has been very slow in India is the food retail sector. The bulk of food purchasing in India still happens from traditional kirana stores and traditional commodity markets. Preliminary research in India suggests that format choice in food products is influenced by consumer demographic and psychographic factors, and by distance travelled to the store (Prasad & Aryasri, 2011). The popularity of traditional retail in India could be explained by the presence of a large rural and BOP consumer segment which does not have access to modern food retail outlets. Cultural barriers may also prevent consumers from lower socio-economic strata from patronising modern retail stores. Research in Israel has found that cultural factors and distance from modern stores influence consumers' purchase of perishable food items from traditional stores (Goldman & Hino, 2005). Other factors which affect consumers' channel choices are retail brand image, store loyalty, store status hierarchy, variety seeking behaviour and leisure and

entertainment habits of consumers. More research is required to understand Indian consumers' preferences regarding traditional and modern outlets. In this context, biological models and simulation studies may help in forecasting growth of modern retail.

The public distribution system in India requires immediate attention from the Central and State governments. India was one of the earliest among emerging countries to think of making essential food grains and edible oil available to its citizens at affordable prices. A comprehensive system of procurement, storage, and distribution via Central and State agencies and a large network of fair price shops was set up across the country. This system has however been plagued by inefficiencies and leakages. Several modifications have been made to the original scheme to ensure better targetting of people below the poverty line. Research suggests that much still needs to be done in view of the substantial leakages in many states.

Regulations regarding FDI in Indian retail have now been eased; foreign companies can now freely participate in single brand retail. Foreign direct investment in multi-brand retail is also possible in large cities subject to clearance by the State government, provided the foreign company meets conditions regarding the size of the investment; investment in the back-end, and proportion of sourcing in India. It is too early to say if these new regulations will attract substantial FDI in Indian retail. The Indian market is not an easy one to understand, and according to press reports, several large Indian business groups who made significant investments in retailing are yet to attain profitability. There are some fundamental differences between retailing in developed countries and retailing in India. Consumers in developed countries tend to spend more per purchase occasion as they purchase a wider assortment, larger quantities, and higher value products. Retailing in the developed countries is characterised by large format supermarket, hypermarket, and category speciality stores in suburban locations with ample parking. Large format stores are unlikely to be successful in India because of constraints of transport, lack of storage space at home, and lower income levels. Format choice is likely to be an important decision in the Indian market and research findings in this area will be useful for retailers who want to enter the Indian market. Format preferences of consumers are difficult to forecast a-priori but conjoint analysis has been used successfully for examining format choices.

The e-retailing format has made significant strides in developed markets especially in categories such as books, durables, phones, and apparel. Many brick and mortar retailers have started e-retail operations in response to the growth of stand-alone e-tailers. Internet penetration in India was traditionally considered too low to support e-retailing but the rapid growth in the smart phone category allows mobile phone owners to access the Internet easily. This may have implications for growth in e-retailing in India.

Wholesalers have always been an important part of the distribution channel in India. Wholesalers purchase products from manufacturers and sell to retailers. They perform services like storage, bulk breaking, credit provision, and information provision for manufacturers. Most wholesalers in India are small in relation to their counterparts in developed countries and they operate in a limited

geographical territory. Wholesalers may specialise in a narrow product range across a few brands and deal with a small number of retailers. Fast moving consumer goods (FMCG) companies in India have developed a category of exclusive wholesalers called stockists or redistributors. These stockists are expected to operate in a defined geographic territory and service a defined set of retailers by providing regular product delivery to retailers using dedicated transport units which ply on fixed routes. Stockists are expected to employ sufficient number of salespersons and promotional personnel to ensure proper stocking and display of the manufacturer's products. The number of stockists used by a single FMCG manufacturer for all-India distribution may run up to a few thousand and these stockists may cover over a million retailers using systematic physical distribution. In recent years, there have been reports that even while pursuing value and volume growth, companies are reducing the number of stockists they employ. The implication is that stockists now have a larger territory to operate in and will actually or potentially be handling a larger turnover as compared to previous years. Controlled distribution through stockists is usually supplemented by using non-exclusive traditional wholesalers who cater to retailers who are not covered by stockists. Traditional wholesalers can help in expanding brand presence by several million more outlets. Practitioner wisdom suggests that traditional wholesalers operate on very low margins, yet provide useful services. Traditional wholesalers are an important element of distribution in India but there is hardly any published research about their business models and operating strategy.

A new breed of organised, pan-India, professionally managed wholesale companies have made their appearance in the electronics trade, specifically in IT hardware, technology products, and mobile phones. Large organised international companies have also entered the cash and carry wholesale format with a pan-India footprint. If this trend continues, we can envisage the appearance of professional wholesaling in other sectors of the Indian economy in the not too distant future. The growth of large, organised wholesalers has profound implications for manufacturers in India. So far manufacturers have had to deal with relatively small stockists and wholesalers with the power balance firmly lying with manufacturers. The power balance can change drastically when manufacturers have to deal with large, powerful wholesalers. The growth of organised wholesaling offers research opportunities for future distribution research in India.

Logistics is an important part of distribution channel management in India. The design of the warehouse network in India has hitherto been influenced more by the taxation structure and less by actual distance, transport, and demand considerations. Due to the presence of the inter-state Central Sales Tax, companies have tried to avoid inter-state sales by setting up warehouses in almost every state. This has necessitated the location of warehouses in almost every state. For cost reasons, these state level warehouses are usually outsourced to specialist entities called carrying and forwarding agents (CFAs). The location of CFAs within a state is determined by demand factors and transportation considerations. The tax structure distorts rational network design and can give rise to cost inefficiencies (Avittathur, Shah, & Gupta, 2005). Future changes in the tax regime

may permit companies more freedom to redesign their distribution for locating distribution centres to minimise costs and maximise service.

Many leading companies have implemented technology initiatives in their distribution channels. These include provision of computer systems and billing software to CFAs and stockists and connecting CFAs' and stockists' computers with their manufacturing databases, providing handheld devices to stockist salespersons for accurate billing, using GPS enabled transport vehicles, and so on. Companies are also experimenting with analytics and big data to understand retail demand. Firms must also address the softer aspects of channel capabilities through upgrading the channel human resources and management capabilities of stockists and wholesalers via in-house or outsourced training initiatives. Informal surveys among channel members suggest that the human resources area is a bottleneck for most channel members.

Only a few of the millions of retail outlets in India are registered with a national authority. Hence data on the size and measurable characteristics of the distribution channel in India is very difficult to obtain. Consequently retail audit measurements are extremely important for companies in estimating their volume and value of market share, distribution coverage, and retail presence. Sophisticated retail audit services with pan-India urban and rural sampling covering various types of retail outlets and products are now available in India for most FMCG categories. This needs to be extended to cover many more product and service categories. In addition to sample based audits, census of retail and wholesale outlets is required to understand the Indian distribution system. The Central Statistical Organisation of the Government of India has in the past carried out a trade census which yielded useful information on the scope and characteristics of trade in India. The census was supposed to be carried out on a periodic basis but no fresh data has been available since 1996–97. The trade census requires updating at the earliest. Other interesting areas for study in the context of Indian retail and distribution channels are franchising and franchisee operations; transaction cost analyses; horizontal integration; retail employee satisfaction and validity of the service profit chain framework; store location models; factors affecting private label activity; and retail access of BOP consumers.

The round table discussion with eminent panellists from industry and academia which follows will seek to answer the following questions:

- How is the distribution system in the particular industry currently structured? What are the major changes that have occurred? What are the main issues in distribution that have been addressed in recent years? How has the company handled these issues?
- What are the factors that will affect the distribution system in the future? What are the challenges going forward? What is the thinking about how to address these challenges?
- How is retailing in India structured? What are the implications of foreign direct investment for Indian retailers?
- How is distribution performance measured? What is the scope of retail audit in India?

## Distribution challenges and workable solutions: discussion

### Anchor

Avinash G. Mulky

### Panellists

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Faculty and doctoral students from IIMB, and invited observers were part of the audience, and they participated in the discussion.

## Avinash Mulky

We have been teaching a course on sales and distribution for 10 years and despite the changes we make, we feel that there is a gap between the theory we teach and what is happening on the ground. Therefore, we thought that a round table discussion on this subject with the experts who iron out practical problems would help in bridging the gap. The second objective of the discussion is to understand the best practices that have been used in the last few years and see what implications that has for theory building and research.

We have an eminent panel here. Mr. Rajendran, the Chief Marketing Officer for Acer Computers, has been in the industry for over 30 years and will speak from the point of view of IT and durables. We have Mr. V. Jaigopal from Madura Coats and his product is a mix of both FMCG as well as B2B. His product goes to every nook and corner of the country and the distribution system I am sure is extremely deep and wide, so we will get perspectives from there. We have Ms. Banupriya, from Nielsen and she runs the Nielsen retail audit, so we look forward to perspectives on how to measure distribution, and so on. For the theoretical perspectives, we have Professor R. Nargundkar, Senior Dean-Academics at IMT Ghaziabad. He started his career in the market research industry and has a unique perspective on the practical issues of retail and distribution. We also have Professor Ashis Mishra from the Marketing area of IIMB who teaches retailing – he is going to talk about the changes in the retail scenario and their implications on distribution.

## S. Rajendran: IT distribution

My presentation consists of two modules: one is a profile of Acer both worldwide and in India. I will then talk about IT distribution at Acer India, the evolution of IT distribution, the challenges we faced, and our outlook for the future.

### About Acer

Acer was established in 1976, headquartered out of Taiwan. What has been very consistent is our brand mission of

breaking barriers between people and technology. With the changing times, we have adopted different tag lines to make it relevant for the market and for the consumer. We started off with the tag line “We hear you” about two decades back; right now it is “explore beyond limits”. The philosophy behind the tag line is as follows: People want to be empowered and we have adopted the tag that says we will provide the gadgets, the hardware product solutions to help each individual explore beyond limits.

Acer’s brand value has been consistent for the last three decades and it represents being curious, progressive and human. In our approach to products and solutions, and in our communications, we try to portray these values.

### Profile of Acer

- Established in 1976
- Revenues – US\$15.7 billion (2012)
- 8000 Employees
- 95,000 Retail stores in 70 countries
- Brands: Acer; Packard Bell; Gateway; Founder

We are one of the leanest companies in the world, given our turnover of \$16 billion. This links into our business model where we leverage the strengths of various other people in the eco-system and focus on our core strength at the same time. Acer is the prime brand but with the change in the industry, particularly the widespread consolidation, we found a strategic fit in some geographies and we took over brands such as Packard Bell in Europe, Gateway in the US and Founder in China three years ago. As a brand, we were an original design and equipment manufacturer (ODEM), manufacturing for others but over time we realised that one needs to have one’s own brand and we aligned ourselves to the world of sports. For instance, we are strongly tied up with Ferrari, integrally connected with them to supply the hardware for their F1 races. The other association in the world of sports is the London Olympics where we were the exclusive hardware partners.

### Acer India

Acer came to India in 1999, out of a joint venture (JV) with Wipro. In India we have understood the need to be close to

the market physically so we have headquartered at Bangalore but we have branch offices in 21 cities. Our manufacturing unit is located in Pondicherry, and we call it the re-configuration centre because it is not manufacturing in the true sense of the word. (Table 1 gives details of the Acer India profile.)

### IT distribution: evolution over the years

During the early days (1999–2001), our business model reflected a salient carry over from the JV legacy. Wipro-Acer was a joint venture and Wipro was a very enterprise focussed company by virtue of which the consumer segments we focussed on were the large B2B or institutional buying such as insurance, government, and infrastructure. The Acer philosophy in India was to be an indirect business model company with a focus on our strengths in terms of product technology, understanding the customer and after sales support, yet leverage the other members in the ecosystem to deliver value to the market. Therefore we had a clutch of system integrators who took our products and created solutions around them. However, this was contrary to the Acer philosophy worldwide which was a consumer oriented, small and medium businesses (SMB) oriented company, with retail presence. So, during those three years, we started re-inventing ourselves to build on our strengths through a new initiative called a customer oriented distribution structure. This is a conventional structure with some parallels with an FMCG or a white goods distributor. We wooed several best-in-class distributors such as Ingram and Redington. But distribution was fairly unstructured at that time. We had *dealers*; between distributors and customers there used to be one level of dealers who would pump in materials directly to the customers. But given the geography and the complexity, we also had *resellers* who did the re-distribution, catering to the hinterland and the smaller geographies, the suburbs or to small dealers.

Over the next five years (2002–2007) we tried to bring in some refinement in the distribution channel, according to the nature of the buying and consumption habits of the end customer. We brought in channel segmentation in the distribution; those distributors who were purely retail oriented, were called *IT Specialty Stores* (ITSS) and we also gave them an Acer branding and categorised them as Acer

malls and Acer points. Acer malls were exclusive to Acer and Acer points were multiple branded stores. The ITSS also included the other retail outlets category, which consisted of those outlets that had a good footfall print, and good shopping ambience. The idea behind this segmentation was that the value-add and the engagement framework were different as compared to some of the other normal non-Acer branded outlets selling Acer products; we were giving them support in terms of merchandising, promotion, training of sales personnel and so on. We had another set of distributors, *resellers and dealers* who continued from before, who formed the unstructured part of the market and went into places which were hard to reach by distributors.

We also brought in some refinement to the commercial segment within the stock and sale business through *value-added re-sellers*. The value added reseller would have trained engineers to understand customer requirements and cook up the product according to specification, and provide a complete solution. Broadly speaking, he had lot of similarity with the system integrator except that he was much smaller in scale. The value added reseller was not pan-India, not very large and was typically operational in geography or a city where the focus was mostly on the SMBs and corporates.

Our current structure is as follows (Fig. 1: Acer channel structure: present). Consumer sales are indicated by the lighter shaded boxes and commercial in the darker shades. With the market evolving, we have large format retailers also as one big breed of channel partners reaching out to consumers – Croma, Reliance, Vijay Sales, Hypercity and so on. We have a very strong engagement with them but through Tier 1. The master re-sellers have become refined today as we have a programme to identify them and we know how we want the product to move in the market. We ensure that the brand touch and brand consistency are not lost, even if the product goes to smaller towns. In this we have brought another identity to a channel partner much like Acer malls and points, and we call them Acer galleries. They are smaller formats of Acer branded stores but in a Tier-3 or Tier-4 city.

We have also brought in some structure to categorise the consumer durable or the consumer electronic stores who may not sell much but they have an IT products category. This is more prevalent in places like Delhi or Mumbai where such stores could sell stationery, some media, and some

**Table 1** Acer India: profile.

- Acer India (Pvt) Ltd. was incorporated on 9th September 1999, a 100% subsidiary of Acer Inc.
  - A 3 year joint venture with Wipro
- AIL is a part of the Asia Pacific (AAP) region – the largest entity among other Acer national subsidiaries
- Acer India has grown to be close to the market: HQ at Bangalore; Branch offices – 21 of them with local touch
- India Reconfiguration Centre at Pondicherry
- India operations: ~ INR 3500 crore (Rs 35000 million) revenue in 2011–12
- Market standing
  - Desktops No.1 to 3; Notebook No 3; No. 1 in Monitors & Net books
  - No. 1 in Desktops
  - No. 1 in TFTs for some 14 quarters
  - No. 1 in Net books in 12 of the last 12 quarters (>60%+ m.s. in Q3'12)

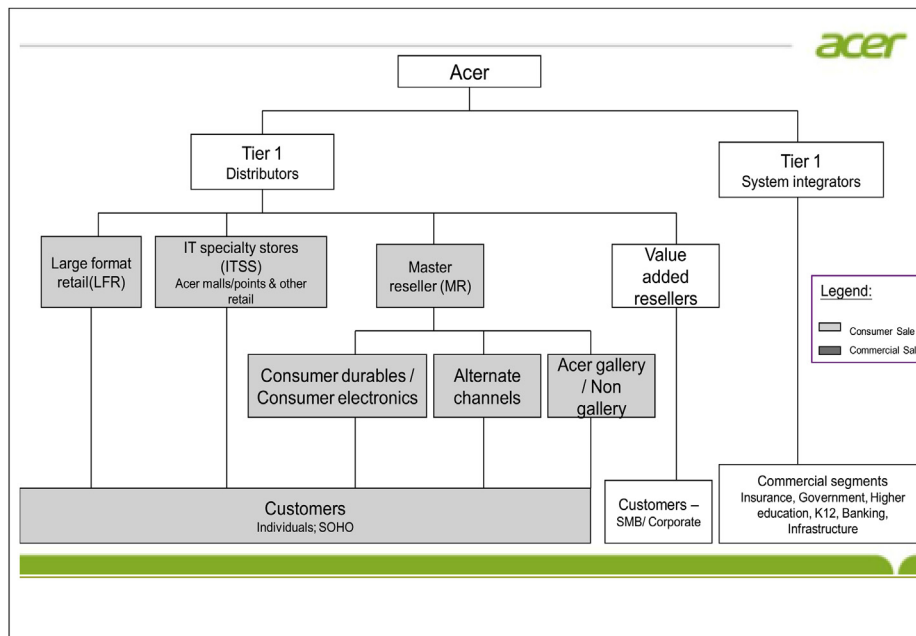


Figure 1 Acer channel structure (present).

low-end computers, and since they are perceived as reliable outlets by the customer, they become consultants even for hardware.

The commercial part continues as before without much change.

What are the *challenges* that we faced? Internally, the movement from “enterprise” to “consumer” was a big cultural change because we were moving from a semi-direct business model to an indirect business model. This involved changing and fine tuning several processes, including our lexicon when we talked of becoming a consumer oriented indirect business model company.

Externally, we had to engage with our partners – distributors, dealers, retailers – to come on board, to accept our brand, and to accept us as long term partners. Internally we focused on communication, talking about return on investments (ROI), inventory, turns, cycles, ageing, margins and so on because that is what the “enterprise” mindset would not understand. It took a lot of time to get the communication going across the entire spectrum of stakeholders, internally and externally, and senior management invested a lot of time in it. We spent a significant amount of time getting an Ingram or a Redington on board. We also made some upfront investments in retail stores though it often did not make good business sense since we were just moving into retail, but we had to convince people that we were committed. Based on consumer buying behaviour, we also refined the channel structure, as explained earlier.

While we do not sell online, companies such as Flipkart and Homeshop 18 have started engaging with us. We have started on a very small scale to give business to them directly. We have made a very small beginning and we have to see how it evolves.

What is our outlook on our *distribution structure*? We think the market has reached a stage where it is ripe for

some consolidation. IT hardware is a business where you need to have economies of scale because the net margins are typically about 1%, and not all players are able to scale up. The other change we are seeing is a redefinition of roles. Earlier “national” meant that the distributor would carry our products across all territories. Now we have started focussing regionally, allocating to them only those regions in which they are strong. Otherwise we get a national player playing in a regional role or we get a home grown player who is a regional distributor there. Exclusivity, along with its pros and cons, has started to play a role. For example, a pan India distributor could get exclusivity for a particular product or a specific region. Another trend being observed is convergence of products, which means a convergence of channels for the distributor, which is a very big challenge.

*Channel dynamics* are playing out through the emergence of *chain stores* at city/state/region levels. This would mean the distributor’s role of feeding these stores may become redundant. There could be big players who would start feeding them directly. *Large format retailers* (LFRs) are becoming much larger in terms of size and scale and there may be a need to engage directly with them. *Specialist stores* would continue to be in business and *e-tailing* is an emerging trend. Right now there are some vendors who are engaging the Tier 1s to feed the e-tailer, like Flipkart but I am not too sure whether the margin structure can sustain so many levels.

The challenges we see in *IT hardware distribution* are multi-faceted starting with *technology changes*, where a lot is happening in terms of form factor and device capability. *Boundaries are becoming blurred*. What is IT? Is it a product? Is it a service? The *supply chain dynamics* sees supply chain players also wanting to fulfil the role of a distributor and competing with them, thus bringing efficiency into the system. Today, a plain vanilla distributor fundamentally

does one or all of three things: warehousing, logistics, and credit extension, and a dynamic supply chain player could perform the first two. The *Internet* is becoming an important source today for information, comparison, and convenience of buying. There are *alternate players* who are coming into the eco-system, such as the Telco channel, white goods channel, and online stores. Telco channel is one where there is some convergence happening. White goods players are coming into the space and some of them are able to camouflage the price through bundling or cross-promotions which is becoming a challenge. The *business model changes* include cloud computing, mobile devices, content consumption (vs. content creation). Flat macro-economic conditions will be the new normal. Players will need to reinvent themselves and see how they are going to be relevant to the new changing landscapes.

## V. Jaigopal: Distribution challenges: the Coats India experience

We are a textiles and thread business serving both institutional and domestic consumers and accordingly have a different perspective on distribution challenges. My presentation aims to bring to life our distribution system and experiences in the market.

### Coats: fact sheet

The parent company Coats is a UK based British multinational, which has been around for 250 years globally and since 1880 in India. We are global leaders in sewing thread, present in over 100 countries. We are the world's leading player in the industrial and textile crafts business. The Coats Group revenue in 2011 was \$1701.6 million, with a growth of 7%. We have a large industrial business where the key segments are apparel, automotive, health care, food and beverage, luggage, home furnishings, sporting and outdoor goods and protective clothing; we are now moving into more high-end areas like fibre optics, energy cables and so on. The revenue from our industrial division in 2011 was \$1142.3 million, with a growth of 8%.

We also have a crafts business which generated revenue in 2011 of \$559.3 million with 6% growth and which covers activities such as hand knitting, crochet and needlecraft.

### Coats India: the consumer business

Coats India, which is my division, is a part of Madura Coats Limited which is part of the UK-based Coats plc. The Indian business consists of industrial products, consumer threads, accessories, craft threads and global exports. We have a consumer business with an intense countrywide distribution network.

Given the unique presence of tailors in our country, we sell a large number of small tubes of thread, 100–400 m or 800 m in length, and a few other products including craft threads, zippers, interlinings, and eyebrow thread (a huge and growing business) through a quasi FMCG channel.

We also have a B2B business catering directly to large manufacturers and smaller ones through resellers but the

unique flavour of our distribution lies in the consumer business.

We have vast product variety which creates distribution challenges and we have segmented products across premium, mid range and economy as relevant for the industry. We have industrial manufacturing locations in all four regions of the country, but for the consumer part of the business, the manufacturing end of the supply chain is concentrated in the South for economies of scale. We have clusters of manufacturing facilities, controlled by the company which is fairly typical of FMCG companies operating in a country like India which is so price sensitive. Material moves from these factories to a central warehouse in Hosur just outside of Bangalore from where it is distributed to 16 depots or stock points all over the country. We are in the process of opening more stock points.

### Tailoring: unique to India

All over India, in big cities and small towns, we find small tailoring outlets, which are workshops of 10 tailors or fewer. Tailoring activity of this scale is unique to India, and they even sustain some high end retail outlets. An estimated 2.5 billion tubes of thread are sold in a year to such outlets. The tailor population is estimated to be well over 1 million, and the number of outlets could be 400,000. Despite the inroads of readymade garments (RMG) the small tailor is not under threat – our estimates show that they are growing at a small level even in smaller towns with more people moving from unstitched to stitched apparel. So, we have to think of ways of reaching out to them through our distribution network. Reaching out to tailoring shops is a challenge and since they are spread across the vast geography of India, mass media is ineffective and is prohibitively expensive. Our distribution channels consisting of Coats sales representatives and dealer salesmen take on the job of tailor contact. The mechanisms of contact, home-grown and tailored to suit unique needs, include tailor meets, collar workshops, group canvassing activities to introduce new products, ready stock retailing and so on. Tools like style guides, product brochures, and cabinets are utilised.

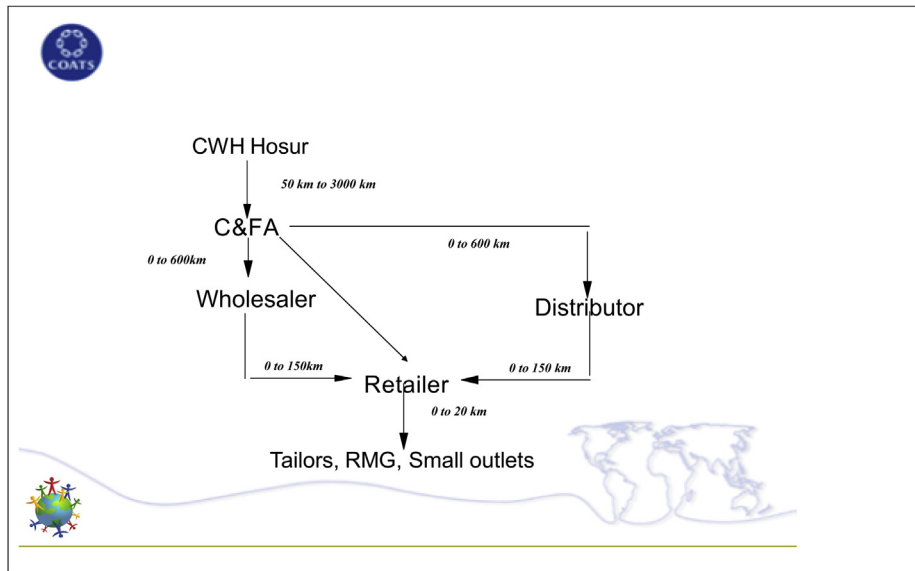
### Coats' distribution channel

We have a fairly traditional distribution channel (Fig. 2), with a central warehouse (CWH), 16 or 17 stock locations which are managed by carrying and forwarding agents (C&FA). We also have to work with wholesalers.

In a pure FMCG company you are selling through your channel to a final customer, usually through a restricted channel. But we have to work with a hybrid mix; you might be selling through geography specific distributors or open channels (dealers) and in turn they would reach out to retailers and small tailors and outlets around the country. We also have to deal with distances. For us, a distance of 3000 km, or from Hosur to Guwahati takes 16 days! These are stock challenges in the distribution and we are constantly thinking of ways to come up with a more efficient distributing model.

Distribution is the key, however. Currently we have 3500 direct outlets, and 20,000 indirect accounts. We have





**Figure 2** Coats distribution channel. Notes: CWH: central warehouse; C&FA: carrying and forwarding agents; RMG: readymade garments.

largely “open” distribution, the reasons for which are historical. We have some covered geographies and very little modern format retail. We have outlets specific to tailoring and apparel trade. The influence of wholesale markets is high, so we understand that reaching out to small retailers is vital. The distribution channel is powerful for demand activation because the way you set up your distribution channel, the way you interact with small retailers in the absence of mass media is very important. We have an extensive geographical coverage and make a redistribution effort. We run over 17,000 van retail journeys a year, with over 60,000 man days of retailing by dealer salesmen. But our redistribution sales, though important, form about 25% of primary sales.

### Distribution challenges

The principal challenge is that of *distribution reach* or cost effective reach because in India effective pricing is very important.

We have a higher portion of the sales coming from the South and the West (each with 35% of sales with 22% population distribution). In a traditional market which is moving up, our growth markets are the North (19% of sales and 30% of the population) and the East (13% sales and 26% population). However, with emerging garment clusters and growing urbanisation, there are new distribution challenges, where our old wholesaler, retailer, dealer distribution model is inadequate and calls for alternate solutions.

Another interesting challenge is *rural affluence*. The latest indicators say that 70–75 predominantly rural districts have started to move towards urban in terms of their per capita income and purchasing power. We have to stay on top of such trends to see how we would distribute our products, particularly our premium products.

A standard distribution template would map at the town level, the rural district level, would map outlets and retail

audits. However, in our industry, we have to arrive at our own *internal benchmarks for distribution*.

Overall sales benchmark for a district or a territory is based on population and market potential value (MPV) data. The MPV data gives you an index of purchasing potential of a particular market, based on which you could refine the data on premium sales by adding the market intensity index (MI). This would give you an indication of the way forward with premium products and you could work out a broad distribution template. While a *frequency coverage plan* would help plan your daily response to distribution, a long range plan would suggest opening depots in certain locations, and increasing your warehouse space or changing your stock policies.

Besides mapping for the width of distribution, you also try to map for the depth in order to ensure that you are reaching out across the span of product categories. This would give you an index, and a combination of the mapping exercises would give you a frequency coverage which is applicable for a sales cycle as well as an order taking or a van journey where towns or markets have to be covered on weekly/bi-weekly/fortnightly beats. To illustrate with one district of the Punjab, we have categorised towns with direct Coats dealers, small towns with dealers which are part of the company reimbursed van coverage, towns not covered by reimbursed company vans but which have dealers with historical contact, and finally towns or new routes that we have yet to explore and which we need to focus on.

What has given us traction in the area of distribution is the *deployment of technology* to process orders and come up with distribution solutions. Once you have a long range demand forecast, with the use of a basic ERP and the advanced planning optimiser (APO), you could generate the heuristics for a production plan for the number of threads and finished goods stocks to be produced on a daily basis. Based on the orders which are flowing through the system, you could have a supply chain diagnostic that would generate a sequence of alerts. The production planning

daily scheduler (PPDS) acts on these alerts to produce the right sequence of shades and colours which would help you move your stock to the central warehouse and forward. The right use of technology enabled us to improve availability and fill rates from 80 or 85% to over 95% with minimal increase in inventory and cost.

We also look to leverage advancements in our industrial business to aid selling efficiency in the consumer business. We have come up with a digital colour matching device, which would help detect the closest match from the shade or the stock that is available, to improve retail outlet efficiency. After establishing this with manufacturers, we have started deploying it with large resellers and are working on more cost effective solutions for smaller stock points to improve sales productivity. Coats counts colour physics and colour technology as one of its core competencies and plans to deploy this competency in the consumer distribution network.

Which brings us to the next critical challenge: *channel profitability*. Channels are becoming highly competitive and since branded products offer wafer thin margins, the preference is to push unbranded, higher margin goods. Here, sticky retail price points make channel margins and price increases a “zero sum” game. Particularly in an inflationary environment like our country, focus on overall return on capital employed (ROCE) and stock turns, absolute margin rather than margin percentage is the solution. In channel segmentation, what is critical is to grow the right partners who facilitate demand activation, retail advocacy – that is those who would create traffic for your consumer business. Stable pricing policies are important and we have created automated scheme settlements.

Another distribution challenge is the *high cost to serve*. Our business is constituted of thousands of small players with annual turnover of below Rs 1 million. Sales has to really be earned; we have over 20,000 transactions per month with bill value less than Rs 10,000/-. The casual payment behaviour of the players requires disproportionate collection effort.

*Sales force attrition and effectiveness* is another challenge, with attrition ranging from 20 to 40%. There is a lack of rigour in the sales process, and weak opportunity conversion. There is a *lack of market intelligence* – with sales force attrition, we also lose market intelligence and visibility. We are trying to deal with the sales force problem with sales force automation tools. For the B2B and the industrial part of the business, we already have a [salesforce.com](#) deployment. For the consumer part of the business, for various reasons, we might choose a local partner with devices which will stand the test of dust and grime of India and make it simple for application from our channels.

*Other key issues* include dealer relationships, taxation such as VAT and GST, weights and measures, legal metrology, and counterfeiting. We do not know how effective a tax like goods and services tax (GST) will be. However, such legislation actually helps in forcing the channel partner to move to official ways of billing and record keeping. Counterfeiting has been included under distribution because the distribution channel is an important means of countering counterfeiting.

Despite having the best IT systems, maintenance of records especially in a channel that exclusively sells thread

products is a challenge, and maintaining an appropriate level of relationship, especially with long standing dealers and distributors of the past is important.

## R. Nargundkar: Distribution: a demand side perspective

My presentation is from the point of view of the much neglected customer but a few pointers might emerge for companies as well. In a sense I am talking from a strategic perspective, from a demand side view of distribution rather than the supply side. I will touch upon different types of industries, FMCG, durables, B2B, and services marketing.

*FMCG distribution* has vastly improved in the country and in many large towns it might be as good as its Western counterpart though we might not have the same reach in terms of organised retail; however we have substitutes in terms of forms of retail stores that sell FMCG products. The major difference could be that we have more stages of distribution partners compared to the more developed countries of the world in that category. Distribution is generally considered a poor cousin of the glamorous advertisement world but it is actually as critical or even more critical for consumers because they are directly affected by what happens on the distribution front. The push factor in a sale and after sales satisfaction are the responsibilities of the point of contact whatever name you give him - retailer, dealer, or distributor. In the case of durables for example, the process-based view of a dealer's sales service has improved customer experiences in many cases. For example, a couple of decades ago, car sales happened through monopoly dealers. I once had occasion in Bangalore to go to a Toyota showroom and was impressed with the sales process which was rigorously adhered to by the trained salesperson for any customer who walked in. It was not a mandatory process in many showrooms of other brands at the time so in some ways the customer was getting a better experience here, which was close to a global experience of being sold a car.

In the *B2B sector* we also have a few other companies which have done well given the lacunae in the system in India. In B2B distribution, including after sales, companies such as Cummins, Kirloskar and Caterpillar for example, are globally known for after sales service and managing the delivery of spares, which forms a critical cost component for the customer.

Moving on to *services* such as life insurance, for example, customised advice is critical for individuals who want to invest their money. The industry needs trained individuals at the point of contact with a consumer, who do not parrot the company tag line blindly and try and understand the customer and his unique needs. This is needed much more in the Indian context because a lot of mis-selling happens here. Customised advice and refraining from mis-selling can be a differentiator for those companies who want to capitalise on this in some way so that they gain the trust of their consumers. Similarly big retail stores should consider not just the assortment of products but other important things such as convenience of location, parking space, number of checkout counters and so on. So innovations in distribution can happen on all

these fronts. Further, in many cases, democratisation of distribution or disintermediation has happened due to companies such as Flipkart and Jabong, or in the case of travel, Yatra and Make mytrip. This is actually welcome for the consumer who might be more comfortable shopping from home and has the means and the ability to do it. (But then even a Flipkart found that they had to innovate by adding cash on delivery, in order to multiply their existing market.)

In the case of banks, non-branch services have improved over the years but the in-branch services seem to have complexities which were not present in the old world banking. Service providers seem either untrained or confused at times even in providing routine services. Of course the ambience has improved hundred fold during the same time. Online services are another major irritant and simple processes are often difficult to complete. One possible solution to some of these issues, given the Indian situation, is the home delivery of goods and services. There is no reason why somebody cannot make home delivery a differentiator (in any industry) and forge ahead of competitors.

The publishing industry in India is another one which could do with professionalisation of marketing and distribution. On the flip side however, the rise of e-books or e-commerce sites like Flipkart, and self publishing (sites such as [pothi.com](http://pothi.com) that let you publish your own books) will bring in a new set of issues into publishing.

I will close with the point that technology is not critical in all industries and even with technology, what is important is customer satisfaction. Technology does help if it is used well but at the basic level or the strategic level what is important is checking what the consumer would be happy with in terms of touch points, distribution, after sales service and then trying to deliver it in a way that does not bleed your company. The field of innovation is infinite and I do not think we have even tapped a fraction of it.

## Banupriya Sudhakar: Retail audits

I belong to the retail audits division or retail measurement service of Nielsen and head the retail measurement service in the South. I am going to talk about the Nielsen retail audit, and the Indian retail structure.

Let me begin by highlighting different touch points in the distribution channel and their needs as relevant to Nielsen. A *distribution channel* is conventionally envisioned as a series of intermediaries, who pass the product down the chain to the next entity until it finally reaches the consumer or end user. Each element of the chain has its own specific needs, stimulus, and ability to deliver in a unique operating environment, which the producer must take into account, along with those needs of the end user.

Recent innovations in rural distribution models have expanded the role of the distribution partner. The distributor role is no longer restricted to physical distribution of products, but has expanded to provision of several other inputs which influence a consumer's purchase decision, such as credit and post-sales service.

## Retail measurement services

What is a retail measurement service (RMS)? An RMS tracks the consumer off take for FMCG products through retail trade on a monthly basis, on the basis of audits of retail outlets in the country. Our RMS tracks 40,000 stores every month and projects the information on a universe of 9.2 million retail stores in India.

What do we measure in a retail audit? We visit the 40,000 stores that form our panel of retail outlets every month and we collect details on stock and purchase and arrive at sales for about 100 odd FMCG categories. The estimated size of the retail outlets which stock any FMCG product in the country is about 9.2 million. We report to the manufacturers on the market sizing in terms of the volume, the value, the penetration of the category, company brand and SKU, and the price at which it is reported.

How do we conduct an RMS? We conduct a physical audit, and the auditor manually counts the SKUs in the outlet, the stock available and he traces the purchases by checking the purchase records for receipts and kachha bills and arrives at sales. What value does the Nielsen RMS deliver? What does this data basically mean to any manufacturer? The Nielsen RMS provides essential data on sales, competition, price, penetration, and market share trend. It provides a company- and brand-wise sales performance within and across markets, the manufacturer's category sizing across markets, it helps compare the sales performance of key competition, helps him estimate opportunities to increase or decrease price, find out the reach of his brand's SKUs in the market, potential markets to increase distribution, and the market share trend – in that it estimates the volume and value share trend for a company or brand.

## Retail landscape

The retail landscape broadly looks as represented in Fig. 3 (Fig. 3: Retail landscape). This is restricted to FMCG. To describe our panel of outlets, a grocer is somebody who stocks and sells loose products such as rice and dal, and who physically weighs products and gives it to the consumers. He also stocks branded products but more of his turnover comes from products sold as loose items. A general store mostly stocks packaged branded foods. Chemist stores sell ethical allopathic drugs and possess a license. Stores that sell ayurvedic, unani or homeopathic medicines but not allopathic drugs are excluded from this category.

A modern format store by our definition, should have a self-service facility, electronic billing and a shopping trolley or basket for people to use. Paan plus, another channel type peculiar to our country, is a paan kiosk which has evolved over the years. Our retail census reveals that the movement of FMCG products in these kinds of outlets is very brisk.

We have a category called food stores which began as bakeries and now sell packaged food and groceries as well. The panel also consists of cosmetics retailers which stock cosmetics and toiletries.

Nielsen RMS does not include wholesale channel as retailers buy from them and including them would lead to double counting of off takes.

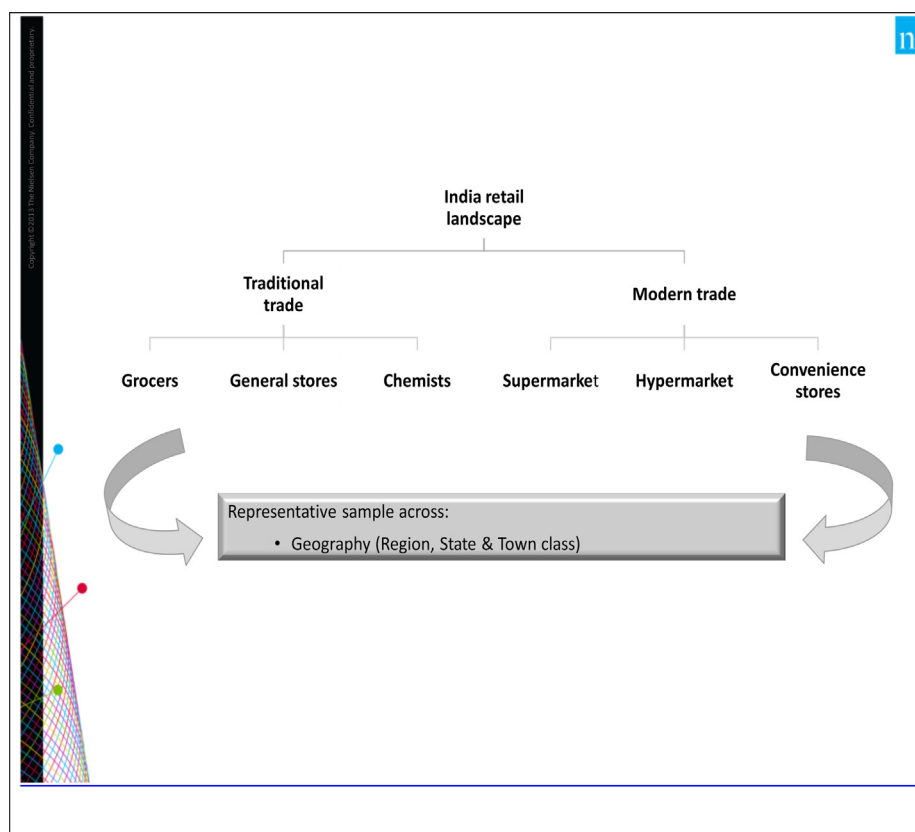


Figure 3 Retail landscape.

Broadly, an FMCG distribution structure would be as follows: from the factory goods can go directly to consumers, to corporates, to the wholesaler, distributor, or retail. Our retail audit does not go to a direct institution sales point or direct to consumers sales; our touch point is what is sold from the retailer to the consumer, so the end channel in the distribution structure is what we track.

### Methodology of Nielsen retail audit

The methodology of our retail audit is given in Fig. 4. We conduct a census of outlets to arrive at our base data. Every year we conduct a retail outlet census to estimate the FMCG outlets in the country. Then we classify these retailers by the type of outlet (such as grocer, general store etc) and by the turnover (high, medium, low) of the outlet. Once the outlets are classified, we select the outlets based on the universe number in a particular centre. This is done across the country. The data collection process involves collection of monthly data from outlets; the data is processed and cleaned, and it is projected to the universe and the reports are delivered to the clients every month.

We use an electronic hand held terminal to collect the stock purchases from the outlet, which is processed and reported in software called the Nielsen advisor.

Our panel covers a specific set of outlets which cater to the manufacturers' needs. However, there are several channels which we do not cover but which could be critical for some of the manufacturers. These include exit points such as railway and bus stations, highways, tourist towns, school canteens, and so on. We do not visit these channels unless a manufacturer asks us for distinct, one-time information.

Channel types such as chemists and paan outlets, and modern stores are critical and evolving channels. Another important channel is the online channel. Queries from manufacturers prompted a Nielsen survey to check on purchase intent of a connected device and the responses revealed a high intention to buy in the case of mobile phones (50% of respondents), computer games and entertainment tickets. There is a huge potential for the online channel, even in the FMCG category.

In rural areas the following six entities are identified as viable distribution channels: non-government organisations; co-operatives; self help groups; micro finance institutions; and rural retail.

Looking at future trends, in the near term we see the following trends shaping demand: personal consumption mindset, nutrition and wellness, digitisation, partaking in global brand culture, premiumisation and lifestyle upgrade, and emphasis on time saving. Connectivity will be the key, with telecommunication, social media, and the online medium affecting trends in the long term.

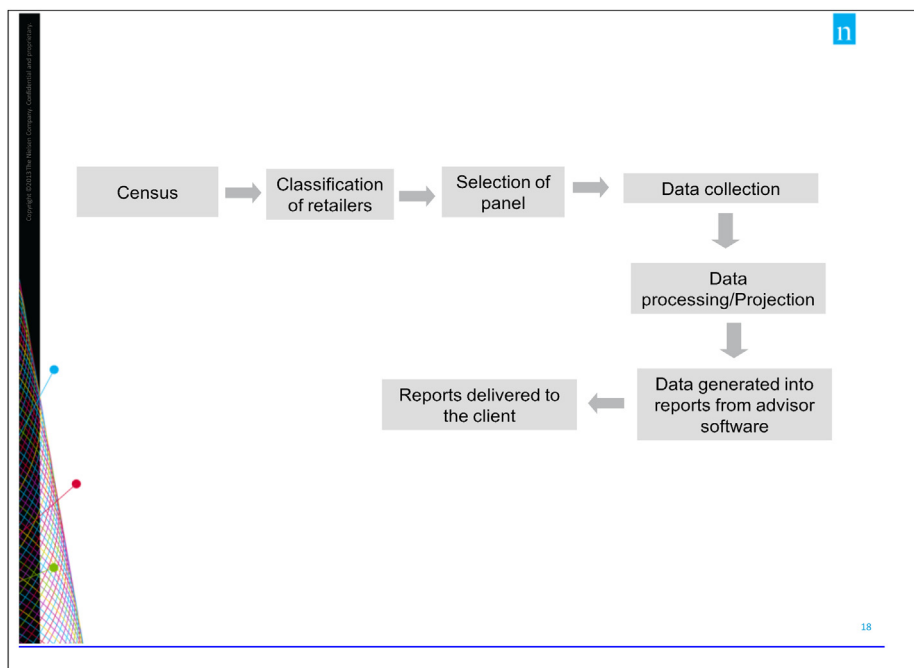


Figure 4 Methodology of Nielsen Retail Audit.

## Ashis Mishra: Distribution challenges: retail dimension

My presentation will cover the Indian retail scenario, particularly the changes that have taken place in recent years and their impact on distribution; FDI in multi-brand retail; and the expected response from manufacturers.

### Indian retail scenario

The urban face of the Indian retail sector has been steadily evolving over the last decade. While the speed and amount of change have been debatable, the indications have been positive. The indicators are: the growth of organised retail (modern retail); evolution of retail consumers; and changes in policy and guidelines. When we talk about organised retail, the first question that arises is, who is an organised retailer? While it is difficult to give a precise definition, to put it in context, we could say that modern retailers are those who have registered for sales tax, income tax etc, employed staff legally in the sense that they get paid a monthly salary, have provident fund and so on, and those with exposure to best practices in the industry, including the use of technology in the various facets of retail operations such as billing, credit card acceptance, superior management practices, and technology at back end operations. They make efforts towards building the store as a brand through appropriate product display, store layout, design and ambience, and visual merchandising. Their store concept should be replicable and scalable.

Where is the growth of organised retail, headed? The figures in Table 2 (Growth of retail sector) suggest that

organised retail is definitely going to grow. What remains to be seen is how big it is going to grow and where it is going to stop? Will the growth of organised retail consume the kirana stores and the small food and grocery stores?

### Growth of Indian retail

If we look at the retail pie (Table 3) and compare the penetration of organised retail in clothing and apparel (34%), footwear (38%) and time wear (52%) with food and grocery (1%), it gives us a picture of where distribution is today, and the major reason for the lack of growth of organised retail in India. All the large format retailers today, such as Wal-Mart, Tesco, Carrefour and so on, are big because they are in food and grocery. The point to note here is that 70% of the total disposable income in India goes to food and grocery and that is where there is only 1% penetration of organised retail.

When you look at the retail categories with the largest share percentage of organised retail to total retail, these being consumer electronics (20%), and mobile telecommunication (15%) there is still scope for growth. So also with categories such as footwear and time wear. If you look at the total retail pie, in 2011 you can say as a proxy of consumer expenses, that 68% is food and grocery followed by apparel and clothing which is 7%. However, while apparel has been tapped up to 34%, food and grocery is only 1%.<sup>1</sup>

A break up of the Indian retail market (Table 4) reveals: in the East, the organised retail market is 2.7% of the total retail market, the highest being in the South at 8%. If you look at the region wise share of the total market, the share

<sup>1</sup> India Retail Report, 2011.

**Table 2** Growth of retail sector.

	2010 (In Rs. Cr)	2012 (In Rs. Cr)	Growth %	2015 Estimated (in Rs. Cr)	Estimated growth %
Total retail	21,19,634	28,50,055	16.0	47,80,318	18.8
Organised retail	1,38,961	2,23,572	26.8	4,87,423	29.7
Share of organised retail	6.6	7.8		10.2	

India Retail Report 2013.

**Table 3** The retail pie.

Retail categories (2012)	Total market (in Rs. Cr)	Organised retail (in Rs. Cr)	Share % to total retail
Clothing and apparel	2,20,000	74,000	34
Fashion accessories	10,998	1375	12
Footwear	24,132	9300	38
Jewellery	1,28,000	12,800	10
Eyewear	33,000	2427	7
Timewear	9000	4700	52
Food & grocery	17,12,000	24,300	1
Food service	1,34,058	16,000	12

India Retail Report 2013.

of the organised market, the East is 9% and the North is 32%, which shows up the regional disparities. All our thoughts of organised retail are about the large format retailers taking over the small format retailers. Apart from the US, where organised retail forms 85% of the market; UK, France, Germany and Spain, where the share of the organised market is 75–80%, you do not see organised retail being that big. Specially, if you look at the big countries, in Brazil the share is 40–50%, in Russia, 33–38%, China, 19–23%, and at the South East Asian countries it is 30–40%. In India, the figure is 7.8%, and in relation to the West, even an optimistic estimation will not put organised retail at more than 20–25% in India. What it means is that organised retail is not going to threaten the unorganised sector. Actually it could go the other way round; given the FDI guidelines, and going by the way the government has formulated the rules, the large multi brand retailers will think twice before opening consumer facing retail stores in India.

Thus, in conclusion, we can contend that a large part of the market is still to be explored. Growth is inevitable but the pace is slow. There is serious regional disparity in the growth of organised retail. Organised retailers need to invest in food and grocery heavily if the total organised retail share has to increase.

### Sustainable business models in retail

Retailers today need to look at sustainable business models. Retail growth is going to come from Tier-2, Tier-3 cities and the rural areas and until now there has not been a sustainable model for the rural areas, the prime reason for that being the distribution network.

The way retail operates is that all goods, whether it is apparel or food and grocery, go into a central warehouse from the various procurement centres. From a central warehouse they are distributed to regional warehouses/ depots/go-downs and from that to the respective retail stores. This model is not sustainable because of the

distances and the time it takes to transport goods in India. If you look at the history of retail, and take the example of Wal-Mart, their hub and spoke model worked in the US of the 70s, but the same model would not be sustainable in India today. Our dynamics, logistics, business models, and our consumers are all different from what America was in the 70s and 80s. What we need is a different innovation model suitable to our requirements.

Moving to the consumer side, consumers have been divided into seven segments according to income, geography, education, and occupation.<sup>2</sup> They are the strugglers (121 million, 50% of the total, with an average disposable income per month of less than \$3300); the next billion divided into the large town next billion (14 million, 6% of the total), and the small town next billion (58 million, 24%), together with an average disposable income per month of \$3300 to \$7400; the aspirers comprising the urban aspirers (19 million, 8% of the total) and rural aspirers (14 million, 6% of the total) together with an average disposable income per month of \$7400 to 18,500; and the affluent divided into professional affluent (4 million, 2% of the total) and traditional affluent (9 million, 4% of the total) with an average disposable income per month of over \$18,500. Looking at this from the perspective of C.K. Prahalad's concept of bottom of the pyramid, then the struggler segment would be the biggest potential market. And the maximum expense across all segments is in food. The expenditure on food as a percentage of their consumption expenditure for the strugglers is 42%, small town 35%, large town 37%, rural aspirants 35%, urban aspirants 31% and only when you are looking at the affluent class, the food expense reduces to 17%–20%. Health, housing, and apparel are other areas of major expenditure.<sup>3</sup>

<sup>2</sup> India Retail Report, 2013.

<sup>3</sup> "Building a New India", BCG India Consumer Survey, 2010.

**Table 4** Region-wise Indian retail market.

	All India (INR Cr)	North India (INR Cr)	East India (INR Cr)	West India (INR Cr)	South India (INR Cr)
Total retail market	19,48,916	5,68,556	4,20,405	4,77,472	4,82,483
Organised retail market	1,26,680	41,582	11,363	35,320	38,414
Organised retail market in %	6.5	7.3	2.7	7.4	8
Region wise share % (total market)	100	29.2	21.6	24.5	24.8
Region wise share % (organised market)	100	32.8	9	27.9	30.3

India Retail Report 2011.

There is a significant variation in the consumption basket across markets. In India, over 30% of the consumption expenditure is on food, as compared to China 25%, Brazil 17%, Western Europe 16%, and US 9%.<sup>4</sup>

The focus of our innovation should be on different approaches to understanding distribution and the supply chain, rather than on micro segmenting the market.

### Indian retail sector: SWOT analysis

A SWOT analysis of the Indian retail sector reveals the *strengths* as the higher purchasing power of consumers, a working population of 117 million with median age 29, and low retail penetration which gives scope for penetration.

The *weaknesses* would be the political uncertainty in the country, the regulatory requirements, and the poor infrastructure and supply chain.

The *opportunities* include innovation in retail formats, retail analytics, in-store experience, technology usage in retail and financial models, e-tailing (the threat to our kirana/mom-and-pop stores is more from e-tailers rather than the large stores), superior customer focus, and change in regulatory scenario.

The *threats* would be the availability of land and real estate, and of skilled man power. As a contrary observation, some retailers want the attrition to be high to avoid providing their employees with a career path and higher salaries, and consider a low staff turnover as the reason for their lack of growth!

### FDI in retail

Considering the question of FDI in retail, earlier it was up to 100% in cash and carry in wholesale trading and export trading, up to 51% in single brand retail with prior approval from government. Now the norms are FDI up to 100% in single brand retail with prior approval from government and up to 51% in multi-brand retail again with prior approval from the government. And with that the minimum amount to be brought by the foreign investor would be at least \$100 million. Outlets can be set up only

in cities with a population of 10 lakh (1 million) and above and at least 50% of the total FDI should be invested in back end operations within three years of the first tranche. Further, for multi-brand retail, at least 30% of the value of procurement of the products should be sourced from Indian small industries and single brand retail, looking for less than 51% investment, should source 31% of the value of goods from India, again from small and cottage industries.

However, this does not explain the position of the states, which can deny approval. Further, restricting multi brand retail outlets to cities with a population of 10 lakhs (1 million) and above limits options especially for large format retailers who succeed through scalability; their modus operandi is based on their penetration. The consequences (according to KPMG 2009<sup>5</sup>) of the new rules and regulations would be as follows: Foreign multi-brand retailers through cash and carry format will roll out consumer facing formats, investment from single brand retailers will go up; there would be consolidation in the retail industry as efficiency in business would be a hygiene factor than being a motivator, in that the issue of scalability and the depth and breadth of retail that we referred to would come into play. If a couple of large format players come in, then the retail industry will not be sustainable because all of them would be focused on the metros and big cities, and further fragmentation of the industry is not going to help anyone. As we have seen in other industries, the retail industry will see consolidation. This would benefit capital constrained Indian retailers in more ways than one (JP Morgan note, 2010<sup>6</sup>). It would increase scale and penetration. It would accelerate the pace of investment in the supply chain to meet the demands of increase in scale. It would enhance operational efficiencies, and enable sharing of expertise and best practices of foreign retailers. Hence, the coming of big retail giants will create new markets, increase penetration of retail across sectors, increase efficiency in the retail sector and the infrastructure of supply chain would improve.

<sup>4</sup> "Retailing in India", Euromonitor International, 2012; "Building a New India", BCG India Consumer Survey, 2010.

<sup>5</sup> KPMG (2009). "Indian Retail: Time to Change lanes", KPMG In India.

<sup>6</sup> Retail: India (2010), JP Morgan note.

Next we look at the manufacturer – reseller/retailer relationship. Currently, it is the “branded bulldozers” phase. The manufacturers are strong and resellers are weak. We do not have any strong organised retailers, who at 7.8% of the retail market, do not have much bargaining power. Over a period of time, what is best for a mature retail industry, is the position of strategic partnerships, with both retailers and manufacturers being strong and seeing value in each other. However, the concentration ratio in retail sector being quite low and in future too, with the organised retail being restricted to 20%–30% (estimated based on other Asian countries), manufacturers need not change their business model drastically. Changing their business model or looking at distribution differently will not be a compulsion for the manufacturers; it would be a choice of proactivity. If we see something drastically different in the next decade or after that, maybe the situation will change.

## Discussion

**Q:** In connection to the Nielsen retail audit, what is the sampling design that you use for the panel of stores when you collect the retail audit data?

**Banupriya Sudhakar:** It is a two stage sampling. First stage is a sample of the towns and based on the census population we know how many metros, class one towns, class two towns, and how many rural villages we have. The next stage sampling will be on the basis of the number of outlets. Empanelling of these outlets is done on the basis of a random sampling. We make sure that we cover 60% of the districts in a state when we take the sample towns and with outlets we make sure that these are distributed equally across a particular geography.

**Avinash Mulky:** One of the developments in this field in some other countries is the professionalisation of distribution, with distributors who operate like companies. For example you have companies like Arrow in the US which sell a large quantity of chips and other things. In your industry you have Redington or Ingram, which are corporate entities in the distribution space. But do you see that kind of trend developing in other spaces?

**S. Rajendran:** In the FMCG space, we do have big distributors as our clients in other markets, but not in India.

**V. Jaigopal:** I don’t see that happening automatically in the FMCG space in India. Two reasons – infrastructure and cost asymmetry. In India, the wholesaler’s place in the wholesale market is handed down as an inheritance. He typically works the store himself for 14 h, and that is how a huge cross section of the trade works. Nobody can spend capex and create retail space. For a company which comes from outside, to compete with these wholesalers would create an infrastructure and cost issue.

Second, with the existing fragmentation that Prof Ashis Mishra talked about, no manufacturer who currently has the balance in his favour, would actively seek to have a large organised distributor and lose out on channel power. Scalability probably comes more readily to the IT and other spaces but I don’t think it comes so easily to the FMCG and traditional format space.

**Avinash Mulky:** If you turn that question around, what were the conditions that allowed companies like Redington to find their space in that market?

**S. Rajendran:** I think it is the nature of the industry because the product inherently has a very short shelf life. Technology keeps changing very fast so the wealth of information is not in the stocking units but in the information which they are able to access about the stock keeping units. If there is a model change, which happens once in three months or so in this space, more than 50–60% of the product is rendered obsolete. So the need for timely information, to have your stock levels known on a daily basis, to have a real time view of their operations is vital and we need to make investments to be in the know. I think one more point to add here is the scope for differentiation in IT is not very high.

**Avinash Mulky:** Mr. Jaigopal, you mentioned that it is sometimes difficult to collect money from your small partners. Do you see a trend towards specialist agencies that would look after the data part, something like Factors in the US?

**V. Jaigopal:** To answer your previous question, and to take an example from say consumer durables, sometimes with large distributors or large retailers, the need for investment in stock and with an element of risk is high, so these companies probably seek out partners who will co-invest, and that is one of the reasons why you would like to have an Ingram or a Redington or somebody because when you come out with a big stock, he might be quite happy to invest in a fair bit of it.... Coming to the question of collection, factoring or asset securitisation even in the B2B space in our country is not advanced. The cost of factoring would be higher than the complete channel margin. The only option is in-house discipline and a proper in-house system, the deployment of technology, and for taxes such as VAT and GST to bring people more into the compliance net.

**Q:** Mr. Jaigopal, would you talk about price compliance, which is another aspect of distribution. How is it taken care of in your case? Do you enforce it or is it enforceable?

**V. Jaigopal:** Legally, it is not enforceable. You can only prescribe maximum retail price above which something cannot be sold in this country. If some channel partners act disruptively in a geography, and say, decide to undersell a certain product and that affects another 10–20 people in the channel, it can be a problem for which you need to have a policy which creates disincentives for such behaviour, but you cannot legally enforce price compliance. If a partner is selling above the maximum retail price, we would take immediate action.

**Q:** My question is Acer related. In which area do distributors provide post sales service?

**S. Rajendran:** If you look at distributors in the IT space, traditionally their value add, as I said, is one of three things – logistics, warehousing or credit extension, which is big for us because in India collection is a challenge. There are very few distributors who provide after sales support. More often than not the customer tags the service experience with the brand. So in IT, most brands take the ownership for rendering after sales support, it may be an indirect business model - in Acer we have about 500 authorised support partners. They are the touch points for the customer in proximity to the place he has bought the product but the ownership for the after sales experience in terms warranty



or out of warranty support, spares availability, is ours. So, with the exception of Redington, there are very few distributors who venture into that territory.

**Avinash Mulky:** Thank you all for your insights into making this such a rich discussion. It has been a very knowledgeable experience.

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