PGDM (IB), 2019-21
FRANCHISING & GLOBAL RETAILING
IB-433
Trimester IV End Term examination, September 2020

Time allowed: 2 hrs 30 min

Max Marks: 50

Roll No: ___________

Instruction: Students are required to write Roll No on every page of the question paper, writing anything except the Roll No will be treated as **Unfair Means.** In case of rough work please use answer sheet.

Section A

Attempt any three. Word limit: 300 words M M =10* 3 = 30

1. (A) Some factors of retail internationalization can act as both barriers and drivers. Explain this statement with three appropriate examples. (CILO-1)
   Or
   (B)Choose a retail operation which you are familiar with, that does not have international retail outlets till date. Using the Simpson and Thorpe's PLIN model's four factors, assess the company's international viability. (CILO-1)

1. (A) New franchisors often expand because of a solicitation from a businessperson in a foreign country. What could go wrong in this method of selection of a franchisee? (CILO -2)
   Or
   (B)How are international retailers impacted by currency fluctuations? What strategic changes can a retailer take to reduce the negative impacts? (CILO -2)

2. (A) Discuss the criteria used to rank the countries in the GRDI table. What other measures could be used to rank the countries? Give reasons for your choice.(CILO-3)
   Or
   (B)Discuss three of the main consumer trends in the 2020s as per the reports, and assess the impact such trends will have on retail in emerging countries like India and China.

Section B

M M= 10* 2 =20 Case Study is compulsory and is for 20 marks.

1. How should Tesco sustain the advantage of being the first global multi-brand retailer to be allowed to invest in India?

2. How should it fine-tune its tried and tested global business model to suit the Indian retail market? How could the company avoid the kind of failure it had recently experienced in its U.S. business?

TESCO PLC: STRATEGY FOR INDIA[1]

In March 2014, Tesco PLC (Tesco), the largest retailer in the United Kingdom and the third largest supermarket group in the world, had signed an agreement for setting up a 50:50 joint venture (JV) in Indian retail with Trent Hypermarkets (Trent), the retail division of the Tata Group, a leading Indian business conglomerate.[2] Tesco was committed to investing £85 million[3] (US$110 million) as its share of capital. The JV was being formed close on the heels of Tesco securing a clearance from the Foreign Investments Promotion Board (FIPB) of the Indian federal government. The FIPB clearances in the retail sector were confined till then to what was known in India as single brand retailing (see Exhibit 1). Tesco was the first global retailer to be cleared to invest in multi-brand retailing.

The clearance stipulated three conditions: (1) Tesco would invest 50 per cent of its capital in back-end infrastructure; (2) it would source at least 30 per cent of the value of procurement from small and medium enterprises (SMEs) within India; and (3)it would open its retail outlets only in cities with a population of over a million.[4] As it got down to the nitty-gritty of execution, the management of Tesco, headquartered in London, United Kingdom, was facing the dilemmas of sustaining advantage, business model and how to avoid failures.

BACKDROP

Even after nearly two decades of internationalization, Tesco had not been able to recover the cost of its capital outside the United Kingdom.[6] The company was in the middle of optimizing its assets in each of the 11 overseas markets where it had established a presence ever since it started to go global in 1995 in search of revenues and margins. Under Philip Clarke, a company veteran who had taken charge as the chief executive officer in March 2011, Tesco had taken some hard decisions. It had divested fully in Japan, the third largest grocery market in the world, in December 2012. It had exited the United States, the second largest grocery market, in April 2013. It was restructuring its operations in China, the largest grocery market in the world, by negotiating a minority stake of 20 per cent in a joint venture with the local partner. It had put a hold on expansion plans in Poland, Czech Republic and Turkey; it was focused on maintaining the growth rate in Malaysia and retaining leadership positions in Hungary, Slovakia and Thailand. It had the biggest share of problems in South Korea, its largest international market by sales, where the growing fascination for online shopping among consumers had affected the flow of cash at its checkout counters.[7]

The situation was also daunting on the home front. The rate of growth in the United Kingdom, the company's core market that was generating 68 per cent of consolidated revenues, was stagnant at less than one per cent per annum. Overall, grocery retail in the United Kingdom was highly concentrated, with the four leading players — Tesco, J Sainsbury, Wm Morrison and Asda — accounting for 59 per cent of total retail value sales in 2013, a proportion which had remained static since 2012.[8]

INDIAN RETAILING INDUSTRY

India was the second largest country in the world by population (see Exhibit 2). The Indian retailing industry was growing at a compound rate of 15 per cent per annum. Its revenues were expected to reach US$1.3 trillion by 2020 from US$500 billion in 2012.[9] The industry, however, was fragmented. India had the highest number of retail outlets per capita in the world, at about 12 million serving a population of 1.3 billion. A bulk of them consisted of 'mom and pop' establishments which did not have access to institutional financing. Driven by entrepreneurial zeal, they leveraged personal relationships with vendors and customers for working capital.

Modern retail formats, characterized by shopping malls, supermarkets and hypermarkets, were confined to urban and semi-urban India. They formed less than five per cent of the country's total retail operations, as compared to 85 per cent in the United States, 80 per cent in the United Kingdom, 55 per cent in Malaysia, 40 per cent in Thailand, 35 per cent in the Philippines, 25 per cent in Indonesia, 20 per cent in China, and 15 per cent in South Korea.[10] Modern retail formats in India were forecast to grow in the order of US$220 billion by 2020. Their growth was driven by trends prevalent among the Indian middle class, such as rising personal incomes, evolving consumption trends, changing lifestyles and increasing levels of urbanization.

In 1997, the Indian government approved 100 per cent Foreign Direct Investment (FDI) only in wholesale stores, keeping the retailing out of reach of foreign retailers. In 2006, the government allowed 51 per cent FDI in single- brand retailing. A number of international retail brands such as IKEA and Carrefour were excited to enter the Indian market and announced their plans to start talks on investment proposals with the concerned ministries as well as the state governments. In September 2012, the government announced 100 per cent FDI in single brand retail and in December 2012, 51 per cent FDI in multi-brand retail. In August 2013, the guidelines for FDI in multi-brand retail were revised by the government in response to the view of both overseas investors and local industry associations that the conditions were stringent. For example, the rule about sourcing 30 per cent of products from small-midsized enterprises was relaxed for some categories. They included fruits and vegetables. The latter were categories on which Tesco was focused.[11]

FOOD RETAILING

The Indian food retailing sector was of the order of US$311.8 billion in 2012. Growing at the rate of about 10 per cent per annum,[12] it was different from other global food markets in several ways.

First, a large part of the food consumption in India happened within homes unlike in countries of the developed world where most of the food was cooked and consumed outside homes. An estimated 30 per cent of Indian population was also vegetarian.[13] Second, each of the 29 states in the country had its own cuisine and, even within a state, there were wide variations in tastes, eating habits and use of cooking ingredients. One-size-fits-all national brands typical of Europe, and also of North America, would not generally work in India. Most food brands were regional rather than national.[14] Third, the factors shaping where, how and what people bought were also different. For example, less than 10 per cent of the population owned a vehicle, so very few drove for shopping. Approximately 95 per cent of customers visited a store within a three to five kilometres radius of their homes.[15] Shopping for household requirements was done in weekly frequencies, rather than monthly as in Europe. Fourth, while deep promotions and leisurely shopping experience were the main tools to draw shoppers to supermarkets and hypermarkets in the developed economies, customer service was the key factor in retaining customers in India. The service included free home delivery and deferred payments.[16] Fifth, Indians shopped for groceries in a very narrow band. As a result, a grocery store did not have to stock more than 10,000 products. Having an abundance of space and then filling it up with merchandise, a common practice in the developed retail markets of the world, were not conducive to success in Indian retail.[17]

Finally, 35 per cent of Indians were less than 15 years of age and 70 per cent less than 35 years of age.[18] The proportion of the young was higher in India than not only the countries of the developed world which was graying, but also the emerging economies such as Brazil, Russia and China.

A common factor in food retailing between India and the developed markets, however, was the concept of value for money among consumers. It prevailed across all demographic and income segments. When Indian consumers experienced the perfect mix of quality and price, they would exclaim "*paisa vasool*!" which translated into "I got my money's worth!" It was the highest form of praise for a company and a benchmark of customer satisfaction to which its peers aspired.[19] However, unlike in the developed world, private labels were less common in India. India had several 24-hour food networks on its various television channels. Cooking competition shows were becoming popular on television. Increased exposure to foreign foods was expected to lead to continued growth in the sector.[20]

There were seven major grocery chains nationwide: Reliance Fresh, More, Spencer's Fresh, Food World, Namdhari Fresh, Star Bazaar and ITC Choupal Fresh (see Exhibit 5).

TESCO PLC - COMPANY BACKGROUND

Tesco was a multinational grocery and general merchandise retailer. In addition to the United Kingdom, it was present in five Asian countries (China, India, Malaysia, South Korea, and Thailand) and six European countries (Hungary, Ireland, Poland, Czech Republic, Turkey and Slovakia). It had consolidated revenues of £63.6 billion for the year ending February 2014 (see Exhibit 6).

The company had refocused its strategy in 2013 into three priorities.[21]

The first strategic priority was to "strengthen the foundations" of its core market. The company had invested £1 billion in 2012-2013 in its U.K. business towards training staff, improving services, opening new stores, designing new store formats, diversifying the product range and generally enhancing customer value. One of the major launches in the United Kingdom, of late, was grocery home shopping. Its success had provided a platform on which to build a position of leadership in the multi-channel world.

The second was to establish "a seamless blend of bricks and clicks" in all markets in the light of changing customer expectations of "being able to shop whenever, however and wherever" they wanted. Tesco had discovered that customers who chose to shop across more channels with the company not only spent more but were also more loyal. Tesco believed that it had the potential to establish leadership in multi-channel retailing in markets even outside of the United Kingdom.[22]

The third priority was to pursue "disciplined international growth." After exiting the U.S. market in April 2013, Tesco had reinforced its capital discipline by placing an overall ceiling of £2.5 billion on capital expenditure for the following three financial years.[23]

As a retailer, Tesco had four competitive advantages: a global presence, a firm foothold in the U.K. market, a range of store formats and a loyalty program known as Clubcard.[24] Its geographical diversity had enabled the company to balance the risks associated with excessive dependence on a few selected markets. The United Kingdom was an important market for Tesco not only because it was the single largest source of group revenue but also because Tesco was a market leader in the country. Consolidating its position in the United Kingdom was therefore crucial. In addition to offering several store brands such as Tesco extra, Tesco metro, Tesco express, Home plus express, and Tesco Lotus, Tesco was present in varied store formats including hypermarkets, supermarkets, convenience stores, and department stores, which together provided a cushion against certain risks such as the lingering global recession. Tesco had 70 per cent customer retention for the year 2013 and cross-sold its products and services to 64.3 per cent of its customers.[25]

ENTRY INTO INDIA

Tesco's initial foray into India in May 2004 had nothing to do with its retailing core. The company had set up a subsidiary called Tesco Hindustan Service Center, headquartered in Bangalore, a city in southern India, to provide information technology (IT) support to the store-operations of Tesco worldwide. Its mandate was to build world class IT platforms and manage the back-end operations pertaining to finance, supply chain, merchandising and checkouts. Its goal was to centralize IT competencies and leverage them across the group. The subsidiary employed 6,500 IT professionals whose role was to "make the Tesco experience better" for half a million employees of Tesco and millions of customers worldwide.[26]

In August 2008, Tesco set up a sourcing office in Bangalore to buy fresh foods (e.g. fruits and vegetables), processed foods (e.g. cheese, meat and seafood), and staples (e.g. rice and other grains) from select orchards, processors and granaries in India for its stores worldwide. The objective was to reduce the group's supply chain costs and improve store profitability. Sourcing was soon extended to general merchandise and apparel. By 2012, Tesco was buying 7 per cent of its global inventory from India.[27] Tesco also announced, in August 2008, an exclusive franchise relationship with Trent Hypermarkets wherein it would offer its know-how for improving the shopping experience at the latter's Star Bazaar stores in India.[28]

TRENT HYPERMRKETS – COMPANY BACKGROUND

Trent Hypermarkets was part of the Tata Group, an Indian business conglomerate. The group was operating in over 100 countries in seven broad business segments: information technology, engineering, materials, services, energy, consumer products and chemicals. The group had consolidated revenues of US$96.79 billion in 2013 of which 62.7 per cent was from businesses outside India. It had more than 540,000 employees worldwide.[29]

The consumer products segment of Tata had diversified into retailing in 1998 by setting up Trent, a flagship company. Headquartered in Mumbai, in western India, Trent had four retail chains - Westside (lifestyle products), Star Bazaar (food products), Landmark (books and music), and Fashion Yatra (fashion products).

Star Bazaar had opened its first grocery store in 2004 in Ahmadabad, a city in western India. The larger goal was to open 50 stores on an investment of US$350 million by 2020. By 2013, there were 15 Star Bazaar stores in eight cities, which were generating revenues of US$130 million and a loss of more than US$1 million.[30]

Although it was expected to breakeven only at a critical mass of 25 stores, Star Bazaar had taken the slow and steady route to growth rather than rapid expansion. It had spent the first several years observing trends, learning the business and tweaking the model.[31] Star Bazaar had a focused approach to growth. It would open stores only in urban centers and in western and southern Indian cities in particular. The pace of launch of new stores would not be based on the availability of low- cost real estate, but on the likely trends in the flow of traffic, known as footfalls.

Star Bazaar had also identified specific sources of differentiation from other food retailers: offering fresh foods sourced directly from farmers; pricing them at 25 per cent below traditional markets; creating buzz around food by live demonstrations in stores; providing ‘combination offers’; launching store brands in popular categories such as staples; and a queue management system that opened the next checkout counter as soon as there were more than three people in a line.

NEGOTIATIONS WITH TESCO

From the beginning, Tesco had a favorable view of the potential of Indian retail in the long term. In the short term, however, the company preferred to wait and watch for an appropriate policy framework. In a presentation to analysts in October 2013, for example, Tesco had placed India, along with China and Turkey, as the last area of focus of international growth.[32] Korea, Malaysia and Thailand were the first area of focus because of their “significant growth potential,” and Ireland, Czech, Hungary, Poland and Slovakia were the second area of focus as part of “improving returns and holding on to market positions.” The company was of the view that modern retail in India was in its “very early stage” with only £3 billion of potential business.[33] However, by December 2013, Tesco had applied to FIPB for permission to invest in India in response to the new guidelines on FDI in multi-brand retail issued in August 2013. The company had changed its view of Indian retail within weeks. The reasons went, reportedly, beyond the rigor of its own perspective on India.

Leading news agencies in both India[34] and the United Kingdom[35] had cited evidence of pressure points in the run up to the JV. The government of India was keen on a marquee retail brand such as Tesco being among the first to sign up for its new guidelines on FDI in multi-brand retail. The Tata Group brought to bear its own influence. In addition to an ongoing partnership with Tesco in India, the Tata Group had extensive business interests in the United Kingdom since 2000, having acquired the tea firm Tetley, steel maker Corus and luxury car brands Jaguar and Land Rover. Official influences were at work not only in India but also in the United Kingdom.

ISSUES BEFORE TESCO IN INDIA

Sustaining the First-mover Advantage

Tesco had done its homework in India for a decade. It was servicing its global retail network from a dedicated IT centre in India since 2004, feeding its global supply chain from a dedicated sourcing centre in India since 2008, and was also advising Trent Hypermarkets in managing its Star Bazaar chain of stores in India since 2008. It had now tied up with Trent Hypermarkets in a JV. Together, the earlier initiatives provided a head start for the JV and also a formidable platform for success. But, sustaining the first-mover advantage depended upon how quickly the JV could achieve two goals: building scale and becoming profitable. Star Bazaar had established 15 stores so far and, by its own reckoning, could reach breakeven only at 25 stores. The largest local retailer Reliance Fresh, founded in 2006, had 705 stores. The second largest, More, founded in 2007, had established 528 stores.[36] The sector was bound to get competitive.

Fine-tuning a Tried and Tested Global Business Model

Tesco was using hypermarkets as a vehicle of international expansion. The format was basically a North American and European innovation and was known to be more suited to monthly purchases and for buying in bulk. Its appeal in India was limited because people were used to buying weekly requirements. Although there were several successful examples of hypermarkets in India, they were dealing with only general merchandise. Grocery shopping was characterized by higher frequency. Even among groceries, fresh foods were bought with greater frequency than staples. The focus on freshness — at Tesco and also at Trent — required change either in format for the JV or in the shopping habits of average Indian shoppers. Both were fundamental changes.

Managing the Risks of Failure in India

The risk of failure prevailed due to the unpredictable nature of Indian politics and public policy. Federal elections were scheduled to be held in May 2014 for a new government that would carry the popular mandate for the following five years. The ruling United Progressive Alliance had favored 51 per cent stake for an overseas retailer in multi-brand retailing. The opposition Bharatiya Janata Party (BJP), which was widely expected to win the elections, was against it on the ground that retailing sector was providing employment to 9.4 per cent of Indian population and that FDI would undermine the role of mom and pop establishments and unsettle local livelihoods. While BJP was widely perceived to be business-friendly, its election manifesto had singled out multi-brand retail sector as one where it would “bar” foreign direct investment.[37]

EXHIBIT 1: GLOBAL RETAILERS IN INDIA

	Company	Country	Year of entry	Category	Investment (US$ million)	Venture
1	Tesco PLC	UK	2014	Grocery	110.0	Multi-brand
2	H&M	Sweden	2013	Apparel	120.0	Single brand
3	IKEA	Sweden	2013	Furniture	1,750.0	Single brand
4	Fossil	USA	2013	Accessories	4.0	Single brand
5	Decathon	France	2013	Sportswear	120.0	Single brand
6	Pavers England	UK	2013	Footwear	16.0	Single brand
7	Brooks Brothers	USA	2012	Apparel	1.0	Single brand

Source: www.tata.com/company/reportsinside/UKs-Tesco-eyes-50-50-supermarket-JV-with-Tata. accessed May 1, 2014

EXHIBIT 2: INDIAN ECONOMY - GROWTH METRICS 2011-2016

Metric	Unit	Actual		Estimate	Forecast		
		2011	2012	2013	2014	2015	2016
Population	million	1,202	1,220	1,238	1,256	1,274	1,292
Gross domestic product	US$ billion	1,876	1,855	1,927	2,139	2,530	3,022
GDP per head	US$	1,560	1,520	1,560	1,700	1,990	2,340
Personal disposable income	US$ billion	1,326	1,293	1,325	1,445	1,668	1,937
Bank lending rate	%	10.2	10.6	10.3	10.3	10.4	10.3
Exchange rate per US$	₹	46.7	53.4	58.6	60.1	58.3	55.8

Source: The Economic Intelligence Unit Country Forecast, June 4, 2014.

EXHIBIT 4: INDIA: NUMBER OF GROCERY OUTLETS & THEIR SQUARE METERAGE

Brand	Company	2013		2012	
		No of stores	Sq Mts. (000)	No of stores	Sq Mts. (000)
Reliance Fresh	Reliance Retail	705	350	620	318
More	Aditya Birla Retail	528	209	529	203
Big Bazaar	Future Value Retail Ltd	290	1,451	185	926
Spencer's	Spencer's Retail Ltd	161	94	183	96
Others		12,430,770	481,043	12,364,339	474,670
Total		12,432,454	483,147	12,365,856	476,213

Source: "Grocery Retailers in India," Euromonitor International, March 2014, accessed May 1, 2014.

EXHIBIT 6: TESCO PLC – GROUP INCOME STATEMENT

Year ending February (in £ millions)	2014	2013	2012	2011	2010
Revenue	63,557	64,826	64,539	60,931	56,910
Cost of Sales	59,547	60,737	59,278	55,871	52,303
Operating Profit	2,631	2,188	3,985	3,811	3,457
Profit before Tax	2,259	1,960	3,835	3,535	3,176
Net Profit	970	120	2,814	2,671	2,336
Business Segments (Revenue)					
United Kingdom	43,057	42,386	42,248	40,117	38,558
Asia	10,276	11,462	10,793	9,159	8,439
Europe	9,221	9,957	8,826	10,241	8,704
US	-	-	628	495	349
Tesco Bank	1,003	1,021	1,044	919	860
Total	63,557	64,826	64,539	60,931	56,910
Business Segments (Operating/TradingProfit)					
United Kingdom		1,007	2,704	2,360	2,458
Asia		661	737	570	474
Europe		329	529	527	440
US		-	(153)	(186)	(165)
Tesco Bank		191	168	264	250
Total		2,188	3,985	3,535	3,457
Retail Indices					
Number of stores	7,305	6,784	6,234	5,380	4,811

Sales area (`000 sq. ft.)	109,572	116,236	112,433	103,616	93,985
Average employees		537,784	519,671	492,714	472,094
Average FTEs		416,441	406,088	384,389	372,338

Source: Tesco Annual Report 2014, p. 69. p. 80, and p. 138;