

MANAGING RETAILING

3rd
Edition

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Preface to the Third Edition

Retailing is an ever-growing and expanding industry with changing formats and consumer demand. The last decade has seen seismic changes in how retailing is being practised. Internet and e-commerce has changed the landscape. Social media is forcing retailers to adapt or get absorbed in the stream. These require retailers to build innovation, authenticity, excitement, and convenience in their strategy and operations.

The book provides a wholesome understanding of retailing as an industry and business. It gives an overview of retailing around the world with the focus on Indian market. It gives knowledge about various aspects of retailing—like different formats, category management, supply chain management, retail communication, pricing and shop location, layout, design, and various uses of technology. The book also gives an insight on shoppers' behaviour and marketing strategy. The focus is on using the concepts to solve retailing decision problems.

ADDITIONS TO THE THIRD EDITION

Chapter 6: Online Retailing

The chapter gives an overview of the online retail industry. It illustrates different formats and business models in online retailing. It provides an insight to the consumers and shoppers of online retail. The chapter has sustainable marketing strategies for online retailers. It also emphasizes the importance of omni-channel retailing and provides implementation strategies.

New Case Studies

The following new cases are added in the third edition:

- BigBasket.com: Redefining the Business Model
- Samsung Electronics in India: Challenges of Multi-channel Retailing
- Hippo on Twitter: Tracking Product Stock-outs in Retail Stores

New Sections in Chapters

New sections are added in the following chapters:

Chapter 2: Indian Retail Industry The following three sections are added in the chapter:

- Impact of FDI in Globalization of Retailing
- Debate in India
- Impact of FDI in Other Developing Countries—Russia and Chile

Chapter 3: Retailing in Other Countries The following two sections are added in the chapter:

- Retailing in Singapore
- Retailing in Hong Kong

Chapter 5: Delivering Value through Retail Formats A section on Electronic Retailing is added to the chapter.

Chapter 7: Deciding Location A numerical on Converse's Breaking-point Model is added to the chapter.

Chapter 8: Category Management The following sections are added to the chapter:

- Private Label Brands
- Numerical on Assessing Economic Performance

Chapter 9: Supply Chain Management The following sections are added to the chapter:

- Third Party Logistics/Warehousing
- Numerical on Economic Order Quantity

Chapter 11: Store Layout and Design A section on Planogram is added in the chapter.

Chapter 12: Retail Marketing Strategy Full revision of Social Media Marketing section is provided.

Chapter 16: Technology in Retailing The following two new sections are added:

- New In-store Technologies
- Mobile Retailing

Revised Sections

The following sections are revised in the chapters:

Chapter 2: Indian Retail Industry

- In Structure of Indian Retail Industry, section on Size is revised.
- The sections on Impact of FDI in Other Developing Countries and FDI in China are revised.

Chapter 3: Retailing in Other Countries The following sections are revised in the chapter:

- | | |
|-------------------------------|------------------------------|
| • Retailing in Philippines | • Retailing in Germany |
| • Retailing in Indonesia | • Retailing in France |
| • Retailing in Malaysia | • Retailing in Brazil |
| • Retailing in China | • Retailing in Russia |
| • Retailing in Taiwan | • Retailing in Chile |
| • Retailing in Japan | • Globalization |
| • Retailing in United Kingdom | • Major Global Retail Trends |

Chapter 4: Understanding Shopping and Shoppers The following sections are revised:

- The whole section on Demographics of Indian Shoppers
- The section on Shopping Pattern in India

Chapter 9: Supply Chain Management The section on Private Label is revised.

Chapter 10: Retail Buying The Buying Calendar in the chapter is revised.

All the data throughout the book is updated to the latest available information on the topic.

Acknowledgements

Several organizations and individuals have significantly contributed to the third edition of the book. We are grateful to our reviewers for their valuable and insightful suggestions and comments. The assistance of Kopal Agrawal Dhandhanian in preparing the third edition is appreciated. We would like to thank the people at the Vikram Sarabhai Library and Indian Institute of Management Ahmedabad Case Center for their support in collaborating data and cases. Our sincerest thanks to the team at Oxford University Press for editing, designing, and printing of the book. They have tirelessly worked to ensure the quality and relevance of the book for students of retailing in management schools. We acknowledge their commitment and initiative. Readers can send their suggestions and feedback at pxsinha@iima.ac.in and dwarika.uniyal@iimkashipur.ac.in

Cases of the Indian Institute of Management Ahmedabad are prepared as a basis for class discussion. Cases are not designed to present illustrations of either correct or incorrect handling of administrative problems.

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Preface to the First Edition

Retailing is an integral part of the value chain in an organization. It is a function that provides the 'last mile connectivity' between an organization and its customers. In many parts of the world, retailers have emerged as one of the most potent forces in influencing the performance of the value chain.

Retailing is undergoing unprecedented change in developing economies. In India, this change is very perceptible. Fuelled by the growth in consumer income and changes in their spending patterns, the retail industry is growing at a rapid pace. The economic liberalization of the country has not only facilitated the entry of international retailers but also provided Indian retailers the opportunity to adopt the best practices and formats of some of these successful international retailers. This is a phenomenon that is being witnessed in all parts of Asia.

Retailers in Asia face issues that are unique to the continent. Traditional stores exist in the same space as new format stores. Retailers have been small in size and several in number. In India alone, there are more than 15 million retailers and, with the advent of new format retailers such as Shoppers Stop, Big Bazaar, and Crossword, their number is rising. However, the share of organized retailing, including that of online retailing, has remained the same throughout the last decade. This poses a problem for the manufacturers as they need a different set of skills and competencies to sell through different formats.

With the emergence of large retail chains and malls, retailing is fast emerging as an important area of study in business schools. Today, there is growing interest in retailing among MBA students as it has opened up several new avenues of employment. An understanding of the developments in the world of retailing, especially from a localized perspective, would help all those involved in the management of retailing as a business as well as a function. A study of retail operations, store location, shopper behaviour, pricing and communication strategies, and the functioning of the supply chain would help students and practitioners understand the management of store operations.

About the Book

Managing Retailing is designed to meet the needs of management students for a comprehensive textbook on retail management. It provides an in-depth coverage of retail theory based on original research. The book presents concepts that are clearly explained through illustrations, examples, exhibits, tables, and figures. With its problem-solving approach, the book will also be useful for practitioners involved in retail businesses.

Some chapters are unique to this book. The chapter on category management provides a different perspective from the conventional merchandise planning described in most available textbooks. The chapter on store loyalty would help students and practitioners understand how loyalty programmes can be managed successfully. A new dimension to retailing has been added in the chapter on shop as a social entity. The chapter on technology discusses recent developments in retail technology, with special emphasis on in-store technologies.

The end-chapter case studies have been selected to suit the learning requirements of the readers for each chapter. These cases cover different aspects of developing retail markets. With their focus on decision-making, the cases illustrate the application of concepts discussed in the book in actual situations. The cases on FoodWorld and Planet Health bring out the challenges faced by a first mover and highlight how retailers can carve a niche for themselves by providing enhanced customer value. The case study on Akaash Book Depot has been provided to illustrate the process of deciding the store location. Girish Food Store is a case that would help readers gain an insight into the strategic and

minute detailing required for category management. The case study on Crossword has been discussed to highlight the strategic role played by loyalty programmes in enhancing the performance of a store.

Coverage and Structure

This book has been structured along the retailing decision process. The world of retailing has been explored in Chapter 1. The chapter describes retailing as a value creation and delivery process, indicating that retailers need to create utilities for the customers. The chapter outlines the history of retailing and discusses various theories that have been propounded to describe the evolution of retailing. It also discusses various decisions that retailers need to take in order to make their operations efficient and their business sustainable.

Chapters 2 and 3 describe the retailing industry in India and some other Asian countries. The retailing scenario in the US and some European countries has been described as a reference point. These chapters provide an insight into the world of retailing in developing nations and highlight the opportunities and challenges faced by retailers in these nations.

Chapter 4 is aimed at understanding shoppers and the phenomenon of shopping. The chapter views shopping from different dimensions to provide a holistic view of the phenomenon. It describes the demographic, psychographic, and values and lifestyle (VALS) profiles of Indian shoppers.

Chapter 5 discusses the formats available to retailers in the current scenario. The retail format is a tangible aspect of the value proposition of a retailer. The format of a store is the face of the retailer. It helps retailers realize their objectives. The chapter classifies retail formats into store-based and non-store-based retail formats. It delves into the benefits and limitations of each of these formats. It also discusses emerging formats such as Internet retailing and supercentres. It discusses electronic retailing, or e-tailing, in detail and provides a comprehensive view of the e-tailing business. The chapter suggests a process for deciding on a format that would best suit the retailer's objectives, resources, and target market.

Chapter 6 explains the process of identifying a location that would be most suitable to the retailer. It describes the process in terms of two broad steps: (i) deciding the trading area, and (ii) identifying a site for the store. It also discusses various models that are utilized for this purpose.

Chapter 7 discusses how category management helps retailers provide the right mix of products, at the right price, with the right promotions, at the right time, and at the right place. Category management, as a cornerstone of efficient consumer response (ECR) initiatives, is designed to devise suitable merchandise offers.

Chapter 8 discusses supply chain management, which is another important aspect of ECR. It describes the supply chain as a system of adding value to the business. While the focus is on managing cost and continuous supply, it also highlights the importance of forecasting demand. In addition, the chapter deals with the phenomenon of private branding, which has seemingly emerged out of the vacuum left in the supply chain when manufacturers fail to consider the requirements of every retailer. The chapter discusses how retailers can use the supply chain to develop competitive advantage.

Chapter 9 is devoted to the buying function of a retailer. It focuses on the criticality of the purchasing activity to retail businesses. The chapter describes the role of the buyer and the characteristics that retailers look for in such a person. It goes on to describe the process efficient retailers would follow in developing a buying plan. This involves demand forecasting and detailing down to the stock keeping unit (SKU) level so that the store has the lowest inventory cost and is never out of stock.

Chapter 10 discusses store layout. The emphasis of the chapter is on arriving at a layout that reduces the stress experienced by customers while shopping. The chapter describes several plans available to the retailer for managing the circulation. It discusses the elements of store layout, such as planning and circulation, storefronts and entrances, merchandise display, materials and finishes, and graphics and signage. It also delves into the role of factors such as scent, music, and lighting.

Chapter 11 discusses the role of external and internal communication in building store image, with special focus on point of purchase (PoP) communication. It discusses the various tools of

external communication in terms of their advantages and limitations. The chapter discusses the role and packaging and the considerations involved in designing a product pack. It provides a framework for developing appropriate strategies for PoP communication and suggests the right tool of communication in a given condition. The conditions are described on the basis of the level of customer involvement and the value proposition that the store provides to the customers. Further, the chapter provides a 3×3 matrix to suggest options for PoP communication in various situations.

Chapter 12 elaborates the process of developing pricing strategies and policies. It also highlights the impact of pricing on other elements of the retail mix. The chapter discusses the bases of pricing, such as demand-oriented pricing, cost-oriented pricing, and competition-oriented pricing. It also discusses the options available to retailers in implementing a pricing strategy, such as everyday low pricing (EDLP) and high–low pricing. In addition, the chapter discusses the phenomenon of reference price in detail and explores various studies on the impact of reference prices on shoppers' behaviour with regard to store and merchandise choice.

Chapter 13 deals with the management of customer loyalty. The chapter first delineates the factors affecting the store choice behaviour of customers. It goes on to discuss the store choice behaviour of Indian customers. It then explains how loyalty is different from patronage. The chapter also provides a framework for managing shopper loyalty.

Chapter 14 looks at the shop as a social entity. Shoppers have been found to modify their behaviour on the basis of the type of store environment they are in. They tend to alter their behaviour as they move from one store to the other. The chapter attempts to explain this phenomenon by exploring the various tangible and intangible aspects of this 'society'. It views the store as a world with its own code of conduct, language, and norms. With the customers at the centre of activity, the chapter explores the world of retailing.

Chapter 15 discusses the role of technology. Retailing has witnessed the adoption of several technologies that help in managing the supply chain and product displays and make shopping an enjoyable activity.

A common thread that runs along all the chapters in the book is the process of delivering value to the customer, where manufacturers and retailers are strategic partners. The book has been designed to aid prospective retailers and manufacturers in taking effective retailing decisions. In order to develop a holistic understanding of various aspects of retailing, it is suggested that the text be used along with the cases. Readers are requested to read this book with an eye to understand and implement the best practices of new format businesses as well as traditional retailers.

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The publishers have made every attempt to ensure the quality and suitability of the book for students of retailing in management schools. We acknowledge their initiative and commitment.

Readers can send their suggestions and feedback at pksinha@iimahd.ernet.in and uniyal.dwarika@gmail.com.

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1

The Domain of Retailing

LEARNING OBJECTIVES

After studying this chapter, you will be able to

- understand the concept of retailing
- understand the history of retailing
- discuss the utilities and dis-utilities provided by retailing
- elucidate the theories of retail development
- gain an insight into the retail management process

INTRODUCTION

Retailing as an activity can be traced back to the times when human beings stopped producing all their requirements by themselves and trading came into being. Communities such as potters, blacksmiths, and fishmongers sold their products to households. This was different from wholesale trade that led to spice routes from Malabar (Kerala) to Europe and beyond through Afghanistan and to silk routes in India and China. Retailers have now become an integral part of society.

RETAILING DEFINED

Retailing involves the sale of merchandise from a fixed location, such as a store, for direct consumption by the customer. It can be defined as an activity that ensures that customers derive maximum value from the buying process. This involves activities and steps needed to place the merchandise made elsewhere into the hands of customers or to provide services to the customers.¹ Retailers organize the availability of merchandise on a large scale and supply them to consumers on a relatively small scale. In the process, they provide the accessibility of the location and convenience of timing, size, information, and lifestyle support. When retailers perform these activities, they create value for their customers, who pay for these services. These values are created continuously through a combination of service, price, accessibility, and experience.²

One of the major roles played by retailers is to enable the adoption of products and services. Unless the product is made available at the store and is adopted by the retailers themselves, it is difficult to derive high values out of the marketing expenditure. The phenomenon, known as *dual adoption*, states that when a product is launched, customers adopt it symbolically, the actual adoption happens only when the retailers put forth the product in the right perspective.³

With more and more customers making purchase decisions at the store, retailing has gone beyond being a part of distribution function. It merits an independent marketing activity that is a combination of distribution

and communication. Moreover, the changing canvasses of marketing, where physical products and the physical space of activity are also being joined by services and non-store retailing formats, pose new realities for retailers. They need to re-orient their perspective. There has to be a clear shift from a *distribution-oriented perspective*, where the physical aspects of merchandise availability and supply chain play an important role, to a more *consumer-value-oriented perspective* for attaining sustainable competitive advantages.

RETAILING AND DEVELOPMENT

Retailing has always played an integral part in economic development. Nations with strong retail activity have enjoyed greater economic and social progress. Retail activity provides a clear indication of the spending pattern of the consumers of a country. Retailing contributes to development by making the goods/services from the producers and suppliers of merchandise available to the population, catering to their individual requirement. By bringing the product to the customers, retailers help create demand for new offers, leading to the expansion of markets. Some of the benefits of a thriving retailing sector are:

- access to products,
- better merchandise,
- not having to settle for a second or third choice when shopping for a particular product, and
- greater customer satisfaction and higher levels of customer service.⁴

Retailing symbolizes consumerism. The East European countries experienced a low rate of growth when they were under the Communist regime. After these countries opened up to the market forces and became part of the emerging economies, retailing became one of the forces driving consumption. Many international retailers gained instant popularity as they provided the customers a different shopping experience. A similar situation is now being witnessed in India, where new format stores, such as Shoppers Stop, Big Bazaar, and Crossword, have become places to see and be seen in, and customers are deriving a significant hedonic utility out of shopping. Shopping is taking on a new meaning in many categories. It now occupies a major part of the customers' leisure time.⁵

UTILITIES OF RETAILING

Retailing provides several utilities to customers. These utilities have been described as *distribution service outputs* by Louis P. Bucklin. Bucklin classified the utilities provided by retail decentralization into better product availability, waiting time, lot size, and variety. This implies that retailing ensures wider product availability to customers, reduced waiting time, provides them the desired lot size, and enhances variety, that is, the merchandise mix available to customers.⁶ These service outputs evolve around the utilities of form, place, time, and size that a customer wants to optimize. Bucklin's classification was further refined into accessibility, product assortment, assurance of product delivery at the desired time and in the desired form, and availability of information and ambience.⁷

The discussion so far indicates that manufacturers are not the only agencies that add value to the product through production and communication. Retailers convert the merchandise received from manufactures into desired forms and also get involved in the communication function by providing information about availability and delivery of merchandise. In addition, retailers also communicate through store ambience and point of purchase communication. Thus, retailers play an important role in adding value to the merchandise produced by manufacturers. Through ambience, retailers also add a new dimension of non-economic output.

A framework for channel selection suggested by Rangan et al. indicated that customers tend to choose a particular channel based on eight attributes: (i) product information, (ii) product customization, (iii) product quality assurance, (iv) lot size, (v) assortment, (vi) availability, (vii) after-sales service, and (viii) logistics.⁸ Thus, customers base their channel selection on the presence of these utilities. A similar classification of distribution

services by Oi groups them into exchange, product line, convenience, auxiliary services, and production.⁹ The performance of some of the distribution services by retailers instead of manufacturers has been referred to as the postponement of the manufacturing function so that the value to customers is delivered in the best possible manner. Thus, it is evident that retailing is not just about storing and distributing products. It is an extension of all the functions that would be carried out by the manufacturer, though in a different form. A retail store can be considered as a separate entity that is an integral part of the value delivery system that ensures that customers are satisfied with the promises made by the members of the channel. Retailers, therefore, provide the last mile connectivity of the brands with their customers.

Managing Values

Distribution services create utilities as well as dis-utilities, that is, negative (perceived) values for the customers. Several authors have attempted to classify these values.¹⁰ The most acceptable description has been provided by Sheth, who states that consumer choice is a function of multiple values, including values that extend beyond economic utilities. The five values are (i) functional (in perceived terms, economic), (ii) emotional, (iii) social, (iv) epistemic, and (v) conditional. Functional values are related to economic needs; emotional values address psychological needs; social values satisfy the need for a sense of belonging; epistemic values address the need for novelty and ego satisfaction; and conditional values satisfy the needs arising out of a particular condition.

A combination of positive and negative values, as shown in Table 1.1, brings out several dimensions of retail business that affect value design and delivery to customers.

TABLE 1.1 A Generic Perceived Customer Value Grid

	<i>Positive Functional Values</i>	<i>Positive Social Values</i>	<i>Positive Emotional Values</i>	<i>Positive Epistemic Values</i>	<i>Positive Conditional Values</i>
Negative Functional Values	Convenient opening hours, but expensive	Place to be, but expensive	My late father's favourite supplier, but too expensive	Newly opened store, but inconvenient location	Extreme cheapness of available produce because of glut, but too narrow range
Negative Social Values	Good merchandise, but 'not-my-kind-store'	Many habituals who are good acquaintances, but also the opposite	My late father's favourite supplier, but many dubious clients these days	Newly opened store, but 'not-my-kind-store'	Extreme cheapness of available produce because of glut, but 'not-my-kind-store'
Negative Emotional Values	Good prices, but unpleasant salespeople	Lifestyle store, but unpleasant sales personnel	My late father's favourite supplier, but unpleasant sales representatives	New interactive kiosk at store, but unpleasant visitors	Extreme cheapness of available produce because of glut, but unpleasant visitors
Negative Epistemic Values	Good prices, but never any new item	Lifestyle store, but never any new item	My late father's favourite supplier, but no innovative items at all	Always has lots of new items, but not accessible for inspection	Extreme cheapness of available produce because of glut, but never any new item
Negative Conditional Values	Good merchandise, but air conditioner out of order	Place to be, but music system out of order	Touching opera performance, but air conditioner out of order	Winter fashion show, but music system out of order	Extreme cheapness of available produce because of glut, but electrical doors out of order

Data sourced from van Waterschoot, Walter, Piyush Kumar Sinha, Joeri de Haes, Annouk Lievens, and Steve Burt, 'Revisiting the Concept and Classification of Distribution Service Outputs', Working Paper No. 2004-12-02, IIMA.

HISTORY OF RETAILING

Retailing as an occupation came into existence when farmers started producing more food than they required. Trading was an important part of daily life in the ancient world. Different people had different skill sets, and people who had a surplus of one good desired the goods they did not have or could not produce.¹¹

In India, the existence of the current *kirana* format and other shops can be traced to the *Manusmriti* and Kautilya's *Arthashastra*. These texts provided guidelines for dealing with customers, after-sales service, and quality and price guarantees. Such scholarly works provided the equivalence for exchange in case of barter. They also defined the tax structure for retail and wholesale transactions. Kautilya commented on the location of stores dealing in specific products in a city. He also discussed the manner in which funds and investments could be managed for better results. Memoirs of traders who came from Europe indicate that Indian merchants carried out business with low margins in order to enhance sales. Indian history and archeology record the existence of markets during the Harappan civilization also. Elaborate descriptions of local and periodic *haats* have also been found. These were the places where commodity exchange was carried out and people congregated and derived several non-economic values.

The new retail formats that are now seen in India have their genesis in Europe. The earliest traders were believed to be the Cretans who sailed across the Mediterranean and carried on trade with the people of the area. They flourished for 2,000 years, and their culture influenced other great trading civilizations. The Phoenicians followed the Cretans as civilization's major traders. They distributed the goods of Egypt and Babylonia. Tyre, Sidon, and Carthage were the principal trading cities of this empire. After the Phoenicians, came the Romans. The Romans established a different form of retailing. They set up numerous small shops with centres. In fact, ancient ruins indicate that the world's first department store was in Rome. With the fall of this empire, retailing disintegrated.

During the period after the fall of the Roman empire, independent peddlers were the only retailers. They carried their merchandise around on their back. They went from village to village selling their wares. By the twelfth century, artisans and traders began to organize into 'guilds' and opened up small shops. These guilds helped them gain social and economic advantages. During the thirteenth century, fairs and markets flourished. Early fairs often had a religious foundation. People would gather at churches and exchange goods on feast days. People travelled long distances to participate in larger markets called fairs. Tea centres run by Lipton were the first chain of stores. At the start of the twentieth century, markets were witnessing the precursors to the present-day retailing scenario:¹²

1. The retailer, and not the products he/she sold, was the brand.
2. Family-owned retail units dominated the market, but large retail corporations were also emerging in the form of corporate and cooperative stores.
3. Small retailers were resisting the entry of large retailers.
4. Many retailers and manufacturers had direct relationships.
5. New technologies in transport and construction were influencing store decisions.
6. International sourcing by retailers was also witnessed.
7. City centres were becoming major points for comparison buying.
8. Shopping centres were coming up at city centres and railway stations.

These developments were also witnessed in other countries, especially in North America. Large corporations were entering into retailing in the USA and Canada in the early twentieth century. The history of American retailing can be traced back to shops located near ports where merchants from Europe would dock their ships and sell the merchandise. Many American retailing institutions originated after 1850. Prior to that,

most Americans lived on farms and were self-sufficient. During this time, peddlers and general stores were the only retailers in the country. Department stores started gaining prominence after 1850. As department stores grew in cities, rural citizens used the first form of direct catalogue/mail order marketing. This allowed them to get the goods they needed without the hassle of travelling long distances into the city.¹³

The development of railroad systems and refrigeration between 1890 and 1920 enabled shoppers to travel more widely and choose from a greater assortment of merchandise. The first set of department stores opened during this time. They offered more convenient and consolidated locations, longer hours, and better prices. American retailing witnessed the proliferation of other formats such as supermarket chains and shopping malls between the two World Wars. National brands such as Wonder Bread and Hostess were introduced in the market during this time. The first convenience store, 7-11 (Texas), and the first McDonald's (Illinois) also opened.

The time between 1950 and 1970 witnessed the emergence of major players and formats. The first indoor regional mall was set up by Southdale. The next big retail shift came when Sam Walton opened the first Walmart and discounters, such as Kmart and Target, opened their stores. These stores used low costs and high turnovers to provide customers with lower prices. Kroger installed the first retail bar code scanner and the first GAP store opened in San Francisco. Walmart integrated computer systems to its operation. These mass retailers also set up independent distribution systems to gain the volume necessary for negotiating with suppliers, track inventory, and allow for just-in-time (JIT) replenishment. In the next decade (1970–1980), the retail industry witnessed the emergence of category killers and wholesale club stores such as Toys “R”Us, Home Depot, Circuit City, and Sam’s Club. The industry started getting consolidated at this time.

During the 1980s, superstores and retail category killers made up about one-third of the US retail revenues. In response to these price players, other formats such as malls, speciality stores, and grocery stores started stressing on ‘retailtainment’. Mall of America—one of the largest malls in the world—opened in Minneapolis. Sears exited its general merchandise catalogue business. This was the time when the retailers started focusing on the ‘store as brand’ strategy. The 1990s can be termed as the times of the Internet. Amazon.com launched its book retailing business using e-commerce. This period also witnessed major internalization efforts by large retailers. The 1990s witnessed a lot of turbulence in the American retail industry. Retailers turned into multi-format entities, especially with the help of the Internet. The focus has now shifted to the emerging economies and retailers are searching for a different business model to succeed in these markets ruled by small retailers.

From the year 2000 onwards, the pace at which traditional retailing is getting transformed into modern retailing is incredible. This is evident from the straggling shopping centres, multi-storey malls, and huge complexes that offer shopping, entertainment, and food all under one roof. Along with the striking transformation in the demographics of the Indian population, we are also experiencing the advent of large corporate houses and superior IT management in the retail sector. This sector has grown at a compound annual growth rate (CAGR) of 11.2 per cent during the period 2007–09, with food and grocery accounting for the major share. The Indian industry is dominated by unorganized retailers, but the organized retailing revenues have also increased at a CAGR of 19.5 per cent during the period 2007–09, with the apparel and footwear segments accounting for the major share.¹⁴

THEORIES OF RETAIL DEVELOPMENT

The retail scenario keeps changing continuously. These changes are brought by ever-changing customer requirements, economic development of the nation, falling borders, new technologies, and by entrepreneurs. Countries like India and many other Asian and East European countries are witnessing unforeseen changes in the landscape of retailing. The traditional retailers, recognized as mom-and-pop stores, are now sharing the

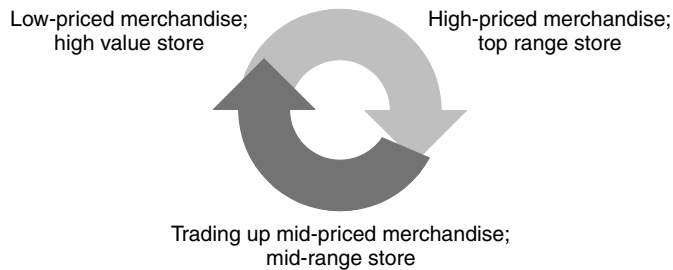


FIG. 1.1 The Wheel of Retailing

canvas with malls, departmental stores, and large price format stores. Several theories have been propounded to explain such developments. We shall now discuss some of these theories.

Wheel of Retailing

The wheel of retailing theory is one of the oldest and most acceptable theories of the development of retailing. It postulates that retailers enter the business at a fairly low status, low prices, and with low price operation. This helps them compete against the established retailers. With time, when such retailers succeed, they acquire more sophisticated and elaborate facilities. Finally, they mature as high-cost, high-price retailers who become vulnerable to new entrants, who, in turn, go through the same process.¹⁵ This happens because these stores are usually established by entrepreneurs who are aggressive and cost conscious and do not want unprofitable frills. However, they tend to lose the control over cost as they acquire age and wealth. Their successors turn out to be less competent. Either the innovators or their successors fail to adapt to the changed environment and the laxity in management lead them along the wheel.¹⁶ Figure 1.1 shows the wheel of retailing.

The Retail Accordion

Retail development is linked to human habitation. It expands or contracts in line with the geographical expansion of the society. When a new area or location is developed and customers start living in that area, the early stores deal in almost all products needed by these customers. Few stores that come up match the offerings of these early retailers. Most of them attract customers due to convenience, as the travel and search costs from other localities are more. In most cases, these stores deal with consumer non-durable products and several emergency or infrequently purchased products such as hardware and electrical products. However, as the locality evolves, a set of stores starts and offers merchandise that does not necessarily overlap with that of the existing retailers. These stores also specialize in a particular category. In most cases, these are consumer durable and household appliances. Petrol pumps, restaurants, shops selling gifts and other lifestyle products, and beauty salons are some of the retailers that emerge. This trend continues till the trading area witnesses a good growth. As the growth tapers, the retailers turn their attention from acquiring more customers to maximizing the value per customer. This starts a phenomenon where retailers start adding unrelated merchandise to their offering and slowly a large number of them become 'general' merchants.¹⁷ The cycle continues, and after some time, 'specialist' retailers emerge, which add significant value to one category of merchandise and attract clientele on the basis of either range or value added products. Some of them become price players and some emerge as category killers.

Melting Pot Theory

According to this theory, a new value proposition by one retailer gives rise to two new retailers with the same proposition.¹⁸ This theory, also called the *dialectic process*, suggests that retail firms adapt mutually

to the emerging competition and tend to adopt the plans and strategies of the opposition.¹⁹ This was epitomized in the earlier *avatar* of Tesco, where it would simply match what Sainsbury would offer. Their policies became similar in terms of facilities, offerings, supplementary services, prices, and even the loyalty programme rewards.²⁰ It took almost ten years for Tesco to recover from this and become the most respected retailer. This phenomenon of melting pot is also very evident in the white goods sector, catalogue stores, and petrol pumps. This gives rise to a process where a successful retail 'formula' catches like wildfire and many retailers adopt it without really finding out the key success factors. Thus, after some time, the mortality rate increases and many of them are not sure of the reason for its failure. In the grocery sector, India is facing a price-led dialectic process. The instant success of the model attracted several retailers and just buying in bulk and selling it cheaper than the current retailers has not led to many facing closure.

Polarization Theory

This theory suggests that, in a longer term, the industry consists of mostly large and small-sized retailers. The medium-sized becomes unviable. This is called polarization. The large-sized retailers take advantage of large and direct purchases from the manufacturers and offer a large range at very competitive prices. This phenomenon has led to an increase in the size of retailers and reaction in their numbers. Larger stores offer one-stop shopping. The smaller retailers tend to offer a limited range of products, but add value to their offers with other services, or tend to specialize. It is found that firms tend to be more profitable when they are either smaller in size or they are big. The mid-size firms fall into the Bermuda Triangle.²¹

The *Bermuda Triangle Effect* refers to the phenomenon where the performance of mid-sized firms suffers if big mid-sized firms continue to 'act small', or small mid-sized firms set up costly big-firm practices. Informally organized firms have low fixed costs. Small firms that are informally organized have low operating costs, but as size increases, the need for coordination within the organization increases, and informal organization often leads to errors and confusion. Thus, the cost of operating informally increases as a convex function of scale. Conversely, formal organizations incur fixed costs such as the cost of running an information system. For a small firm, this fixed cost is distributed over a small output, so that the cost per unit of revenue is high. However, as the firm increases in size, the fixed cost is distributed over a larger volume, thus lowering operating cost as a fraction of revenue.

Ideally, small organizations should be managed informally and large organizations should be managed formally. As a firm grows in size, it should have a transition at the cost cross-over point from informal to formal management. However, organizations do not have a transition at the optimal point. Some move from informal to formal too early, others wait too long before making the transition. The result is that mid-sized firms face higher costs and lower profitability. This leads to the Bermuda Triangle of management—many firms enter it, not all get out of it from the other end. There is plenty of evidence to suggest that small independent retailers have been affected by large retailers. However, it is expected that specialized stores would grow to and fill the mid-size segment.²²

India is witnessing a peculiar phenomenon where both independent and large format stores are increasing by leaps and bounds. However, it is too early to predict whether polarization would occur in India as well.

RETAIL MANAGEMENT PROCESS

Retailing is a complex business. The complexity comes not out of the activities involved, but out of the detailing and precision involved in implementing each of the decisions. It is about every customer that visits

the store and about every transaction that the customer gets involved in. While most retailing businesses involve products, the act of retailing is essentially a service that the manufacturer asks the retailers to perform. The product, which is the centre of activity for most of the manufacturers, becomes just one of the elements in the delivery of retailing service to the customers. In this business, the customer is always present during the process of delivery of the service. The presence of customers in the premises or during the process makes retailing a very involving business.

Compared to manufacturers, retailers have to take much better care of their customers because, unlike manufacturers of brands, the trading area of a retail store is limited. There is a high likelihood of exhausting the store’s potential faster. Thus, the business has to depend far more on repeat purchase. Manufacturers are generally concerned about the market share arising out of the number of customers or the rate of usage. Retailers are more concerned about deriving more value out of their limited customer base. This makes it imperative that opportunities are assessed more accurately and customers are well cared for.

The retailing process involves several decisions. Figure 1.2 provides a framework for retailing decisions. At the core of the framework is the *retail value proposition*. The proposition is derived keeping in mind the market profile and expectations, opportunities present in the market, competitive stances and activities, and the retailer’s objectives and resources. Based on the proposition, retailers decide on the formats, merchandise, location, supply chain, pricing, promotion, and other aspects of the retailing mix.

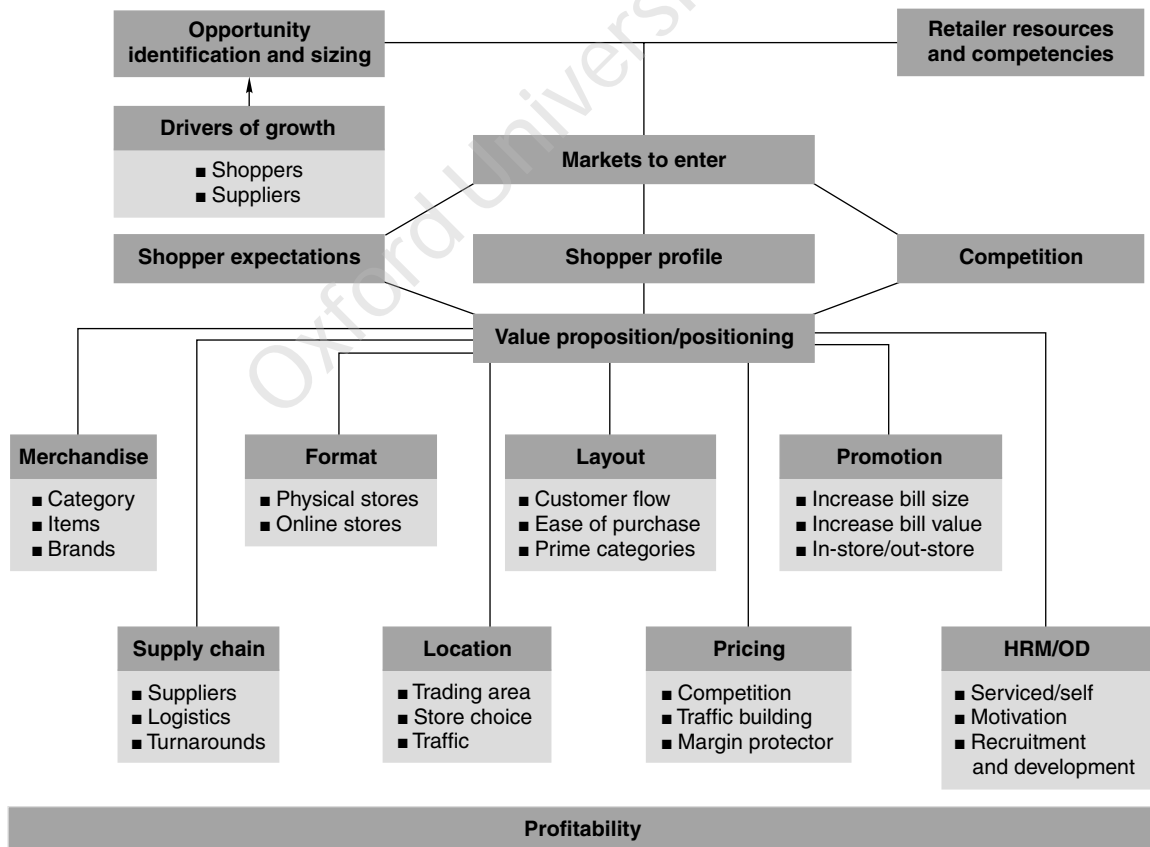


FIG. 1.2 Retailing Decisions

Retail Performance and Profitability

The profitability of a retailer is based on a judicious use of its three main resources of inventory, space, and people. A good management of inventory and efficient consumer response by a retailer would help not only in getting better markups due to the right merchandise, but also higher sales at full price and lower markdowns. A higher inventory turnover benefits the customers by providing them merchandise that is fresh and as per their requirements in terms of stock-keeping units (SKUs) and items. For the retailer, it translates into a higher return on inventory. The return on the investments on the store, called the real estate, is determined on the basis of the sales or return per square or cubic feet of space. This reflects the usage of the space in a way that allows shoppers to feel comfortable while shopping as well as to find the required merchandise easily. It involves not only the amount of space allocated to a department or a category, but also the way the space is being utilized for stocking, displays, promotions, creating the right ambience, and administrative offices.

The third major resource of a retailer is the people and the investments in technology. People in the store are the ambassadors of the store. They play a very crucial role in delivering the desired experience to the customer and provide a human touch to the operations. In consonance with technology, they help in achieving efficiency as well as effectiveness in the operations of the store. In several formats that are chosen primarily on service, people and technology become the competitive weapon to win over other formats that use price or merchandise as key choice criteria for the customers.

Tables 1.2 and 1.3 provide a glimpse into the financial performance of some select retailers. The key performance parameters are the operating profit margin (OPM) per cent, gross profit margin (GPM) per cent, and net profit margin (NPM) per cent as an overall measure of their performance. In addition to these, a retailer would also look at the performance at its department or category level, and would compare it to that of its competitors to assess its competitiveness. An example of such a comparison is shown in Table 1.4. In such a scenario, it would evaluate the performance in terms of its markups, markdowns, and inventory turnover contribution to assess its efficiency. The contribution earned becomes critical in retail business since the competitive pressure forces retailers to take quick decisions with regard to promotion and pricing, and the contribution represents the money that the retailer has at its quick disposal.

TABLE 1.2 Financial Performance of an Apparel Retailer

NSE 299.00	Apparel Retailer		Market Cap: 98.60B	
	Financial Performance in ₹ Cr			
Quarterly	Jun '17	Mar '17	Dec '16	Sep '16
Total sales	499.16	454.12	430.21	435.12
Other income	16.03	8.04	13.17	23.43
Operating profit	64.51	11.88	51.7	39.14
Gross profit	48.48	3.85	38.54	15.71
P/L after tax from ordinary activities	38.15	25.26	37.23	21.07
Equity share capital	33.23	33.23	33.23	33.23
OPM (%)	13	3	12	9
GPM (%)	10	1	9	4
NPM (%)	8	6	9	5

(Contd)

(Table 1.2 Contd)

<i>Annual</i>	<i>Mar '17</i>	<i>Mar '16</i>	<i>Mar '15</i>	<i>Mar '14</i>
Total income	1,851.36	1,587.01	1,475.03	1,345.39
Operating profit	122.63	93.51	54.89	26.76
Profit before tax	135.04	96.92	138.89	68.25
PBDT	172.65	132.18	178.73	93.85
Reported net profit	106.87	77.85	100.03	54.24
Equity dividend (%)	100	90	100	70
<i>Balance Sheet</i>	<i>Mar '17</i>	<i>Mar '16</i>	<i>Mar '15</i>	<i>Mar '14</i>
Equity share capital	33.23	33.23	33.23	33.23
Preference share capital	0	0	0	0
Reserves	1,507.60	1,380.55	1,338.69	1,283.19
Total debt	290.69	75	75	225
Total liabilities	1,831.52	1,488.78	1,446.92	1,541.42
Net block	456.26	465.51	387.77	342.94
Investments	1,112.67	1,059.05	1,037.45	862.4
Net current assets	223.44	-89.43	-24.48	299.72
<i>Ratios</i>	<i>Mar '17</i>	<i>Mar '16</i>	<i>Mar '15</i>	<i>Mar '14</i>
OPM (%)	7	6	4	2
NPM (%)	6	5	7	4
Basic EPS (₹)	3.22	23.43	30.1	16.32
Return on networth/equity (%)	6.93	5.5	7.29	4.12
Total debt/equity (X)	0.19	0.05	0.05	0.17
Dividend/share (₹)	1	9	10	7
Current ratio (X)	1.02	0.83	0.92	2.5

Data sourced from <http://www.moneycontrol.com/financials/trent/profit-loss/T04>; http://bsmedia.business-standard.com/_media/bs/img/article/2014-08/19/full/1408392506-9981.jpg

TABLE 1.3 Performance of Multi-format Retailer

<i>Particulars</i>	<i>Multi-format Retailer</i>			
	<i>Mar '17</i>	<i>Mar '16</i>	<i>Mar '15</i>	<i>Mar '14</i>
Total income	6,638.40	6,304.21	1,917.93	1,703.84
Sales turnover	6,632.98	6,060.71	1,850.73	1,661.21
Net sales	6,602.86	6,060.05	1,850.73	1,661.21
Other income	38.15	11.95	2.78	5.13
Operating expenditure	659.34	1,694.74	2,309.34	2,551.50
Financial expenses	507.61	488.86	669.04	692.54
Personnel expenses	59.96	279.44	381.87	423.94
Operating profit	953.31	1,011.84	1,116.04	1,039.75
Reported net profit	53.50	-104.14	-228.14	-187.73
Earning per share (₹)	0.69	-1.35	-24.59	-20.23
Operating margin (%)	25.20	12.13	10.79	8.98
Gross profit margin (%)	8.46	5.57	5.83	5.48
Net profit margin (%)	1.15	0.14	0.71	0.02
Reported EPS (₹)	0.92	0.27	1.79	0.12

Data sourced from http://www.sify.com/finance/stockpricequote/Pantaloon_Retail_India_Ltd-PFO/ratios.html; https://www.indiafoline.com/article/capital-market-results-analysis/pantaloon-retail-india-ltd-114022109806_1.html

TABLE I.4 Department-wise Comparison of a Retailer's Performance: An Example

Particulars	Comparison of Financial Performance (Figures in ₹ Crore)									
	Store	Benchmark Competition	Department A	Benchmark Competition	Department B	Benchmark Competition	Department C	Benchmark Competition	Department D	Benchmark Competition
Net sales	270	300	27	30	25	22	18	24	40	35
Percentage of total store sales (%)	100	100	10.00	10.00	9.26	7.33	6.67	8.00	14.81	11.67
Markup (%)	40	39	39	37	36	38	28	27	33	33
Markdown (%)	25	23	22	25	21	22	25	23	11	12
Gross profit (%)	22	20	40	35	18	17	20	20	23	22
Cash discount (%)	2	1.87	2	1.9	2	2	2	1.9	2	1.8
Marketing promotion expenditure	5.4	7.5	0.5	0.75	0.3	0.35	0.2	0.3	0.7	0.9
Manpower expense	17.55	18	1.755	1.8	1.625	1.32	1.17	1.44	2.6	2.1
Inventory turnover	2.5	2.1	3	2.8	1.2	1.6	1.8	1.6	4.2	4
Interest on inventory (%)	11.50	11.50	11.50	11.50	11.50	11.50	11.50	11.50	11.50	11.50
Inventory carrying cost	10.8	12.99	1.08	1.299	1.0	0.88	0.72	0.96	1.6	1.4
Contribution (%)	18	16	22	21	20	20	14	16	23	19

SUMMARY

Retailing is a crucial function that marketers perform in order to deliver the promised offer to their customers. In most cases, it is performed by firms called retailers. These entities make the suitable product available to the customers through packaging, stocking, and other distribution outputs described as ‘decentralization’, ‘waiting time’, ‘lot size’, and ‘variety’. Retailing is an integral function of marketing that creates utilities in terms of economic, social, emotional, conditional, and epistemic values sought by customers.

Retailing has been linked to the economic development of a society. It represents a consumption-oriented economy.

Shopping has been regarded as a chore as well as an enjoyable experience. Some have used terms such as ‘shopping therapy’ to signify relief from monotony. A customer seeks different values from shopping, based on the motive of purchase. Retailers use different value propositions to remain competitive in the market and design strategies for delivering these values through a judicious mix of the retail management elements. The unique value proposition is derived on the basis of the

target market and shoppers’ profile and expectations. It takes the shape of merchandise, location, format, service, ambience, and other elements that help the customer choose a retailer and decide on patronizing it.

Several theories have been posited to explain how retailing develops. One of the most prominent among them is the wheel of retailing theory. It postulates that retailing serves a very utilitarian and basic function of availability in the beginning and slowly develops to deliver hedonic experiences, and then again gets into the loop of being utilitarian till some retailers redefine the business again.

A retailer uses three main resources—inventory, real estate, and people—to deliver value to its customers and to remain competitive. A retailer should assess its performance at the corporate level, store level, and also at the department or category level. It is also advised that it carries out a comparison of its performance with competitors to find out whether it has been efficient in its operations, and whether the strategies have been effective in providing the desired results.

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CONCEPT REVIEW QUESTIONS

1. Define retailing. What services does a retailer provide?
2. Describe the theories of retail development. Which do you think describes Indian retailing in the most appropriate manner?
3. Describe the retail management framework given in Fig. 1.2. What is the fulcrum of the business of retailing?
4. How can a utility become a dis-utility? Using the framework given in Table 1.1, describe the net value that a customer would get.
5. What are the main performance criteria for a retailer? Do they remain the same at the store as well as category level?

CRITICAL THINKING QUESTION

Critically examine the retail management framework given in Fig. 1.2. Divide the model into strategic and operational decisions and provide your logic for the same. Would this be applicable to small retailers?

PROJECTS

1. Meet a retailer/store manager and find out the decisions made by the enterprise. Fit them in the model given in Fig. 1.2. Find out who makes each of these decisions in the organization and build a hierarchy of decisions.
2. Visit a place that has a cluster of retail outlets. Figure out the bases of the formation of the cluster using one or a combination of the theories of retail development.

CASE STUDY

Nirantar Agrasar Retail*

Purushottam Bhatnagar, CEO of Nirantar Agrasar Group of Industries Limited (NAGIL), was following the Indian retail growth story intently. He observed that it was interesting to see how the shopping landscape was evolving rapidly with the emergence of new opportunities for organized retailers. In 2008, India topped AT Kearney's annual Global Retail Development Index (GRDI) for the third consecutive year, maintaining its position as the most attractive market for retail investment. Exhibit CSI.1 indicates the evolution of India's retail sector across the past few years. The untapped scope of modern day retailing in India had been led by several large corporations such as Pantaloon, Tata, Aditya Birla Group, RPG, and Reliance. Several regional and local chains such as Ebony and Khadims had also emerged. While most of these developments were taking place in large cities, some companies such as Sriram, ITC, Godrej, and Tata had also ventured into rural areas. Most of the rural retailers dealt primarily in agro inputs. However, some, such as Godrej, sold non-agro products like FMCG and consumer durables too. These companies saw value in providing products and services to more than 700 million of the population of rural India. In his observation, Purushottam was very much impressed with Sam Walton. He admired the way Walmart had started in smaller towns and slowly emerged as the largest retailer.

Triggered by these factors, Purushottam started nurturing his dream to take NAGIL to the retail sector. The company was a prominent player, especially in the Hindi belt¹. It had already been doing well in the FMCG, leather, wind energy, and construction sectors. In the year 2006–07, FMCG accounted for about 65% of its ₹10 billion² turnover. Its detergent was one of the largest brands in the category with a market share of about 15%. Its leather shoe brand had established itself

with middle-class office-goers. Since NAGIL had a very well established business in UP, Purushottam thought it was prudent to explore the possibility of starting the business in this state. The demography of UP indicated that it consisted mostly of small towns and cities. Only two cities, Lucknow and Kanpur, had a population of more than 1 million³. Headquartered at Kanpur, he wanted to explore the possibility of starting the venture from places where he had spare landholdings, such as Kannauj, Chhibramau, Bhongaon, Madhoganj, Sandila, and Bilgram (See Exhibit CSI.2). With these thoughts in mind, he called up one of his old friends, Acharya Bhatt (henceforth referred to as AB), who was an IIMA alumnus and had started retail consulting.

Puru: AB, I plan to enter the retail business. I believe that the large cities are or would very soon become very competitive. Given the very low instances of retailers entering the small towns and rural areas, I would like to explore that arena. I would be glad if you could find time to come over on Monday?

AB had just returned from Shimla from his summer break. He was still getting used to the Delhi heat when he got this call.

He called his secretary, Meghna.

AB: Meghna, see if Priyank⁴ is in his cabin, I wish to see him. Get the SUV ready by evening; put two crates of Bisleri⁵, one large tube of Odomos, and a dozen packs of Allout. We are going on a safari across UP. Please do keep a map of UP.

Meeting with Purushottam

AB: Puru, meet Priyank, who has been my partner in the retail consulting business for six years now.

Puru: Nice to meet you, Priyank. So AB, have you thought of what I had proposed?

* Sinha, Piyush Kumar and Bhattacharya, Ipsit, 'Nirantar Agrasar Retail', Indian Institute of Management, Ahmedabad. Reproduced with permission.

1. Consisting of the states of UP, Bihar, MP, and Rajasthan, which account for almost a third of India's population.
2. 10 million = 1 crore
3. 1 million = 10 lakh
4. Priyank, who was also an IIMA alumnus, was Acharya's partner in the consulting firm.
5. Bisleri is a popular mineral water brand, Odomos is a mosquito repellent cream, and Allout is a mosquito repellent coil.

EXHIBIT CSI.1 India's Retail Growth Story

<i>India Retail (₹ Billion)</i>					
<i>Unorganized Retail (₹ Billion)</i>	2003–04	2004–05	2005–06	2006–07	CAGR (%)
Food and grocery	7,028	7,064	7,418	8,680	7.3
Beverages	212	309	373	518	34.7
Clothing and footwear	777	993	1,036	1,356	20.4
Furniture, furnishing, appliances, and services	512	656	746	986	24.4
Non-institutional healthcare	950	972	1,022	1,159	6.9
Sports goods, entertainment, equipment, and books	212	272	308	395	23.0
Personal care	371	433	465	617	18.5
Jewellery, watches, etc	530	610	655	863	17.7
Total	10,592	11,309	12,023	14,574	11.2
<i>Organized Retail (₹ Billion)</i>					
Food and grocery	39	44	50	61	16.5
Beverages	11	12	13	16	14.7
Clothing and footwear	168	189	212	251	14.3
Furniture, furnishing, appliances, and services	67	75	85	101	14.8
Non-institutional healthcare	14	16	19	24	20.0
Sports goods, entertainment, equipment, and books	25	33	44	63	37.0
Personal care	11	15	22	33	46.9
Jewellery, watches, etc	18	24	33	49	40.5
Total	353	408	478	598	19.5

<i>Organized Retail Increase in Area ('000 sq. ft)</i>			
	<i>Average Size (sq. ft)</i>	2001	2006
Supermarkets/Convenience stores	1,000	400	4,751
Hypermarkets	40,000	0	3,000
Discount stores	1,000	48	1,472
Speciality stores	800	2,121	16,490
Department stores	30,000	780	4,980

Source: 'Impact of Organized Retailing on Unorganized Sector', ICRIER Report 2008.

EXHIBIT CS1.2 Map Indicating Prospective Locations

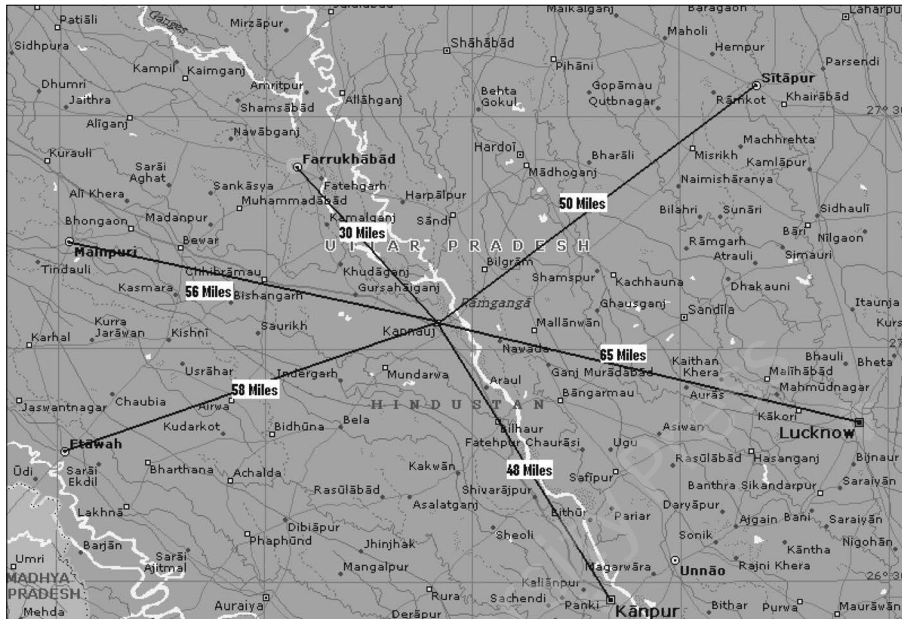
AB: Puru, after talking to you the other day, we conducted a preliminary study of the six locations you have in mind. We have divided the geography into two belts, eastern and western. By our definition, three of your locations, Sandila, Bilgram, and Madhoganj, lay close to the eastern belt, i.e., the Hardoi–Sandila–Lucknow belt (east side of the river). The other three, Kannauj, Chhibramau, and Bhongaon, lay close to the western belt, i.e., the Farrukhabad–Kannauj–Kanpur belt (west side of the river). Taking into account factors such as demographic and economic profiles, political scenario, extent of commercialization, cropping pattern, area requirement, connectivity, and availability of necessary infrastructure, we feel that NAGIL should venture in the western belt. Although, for long, the western belt has been largely agrarian and the eastern belt more commercialized and industrialized, many retailers have started eyeing the western belt now. We have some news of Vishal Megamart and RPG Spencer's coming to Etawah and Farrukhabad. We find it better to enter and establish the business in the western belt before competition intensifies.

Puru: In that case, what is your opinion about a rural retail model in Kannauj?

AB: We do not know in detail yet. However, we do see considerable scope in Kannauj because it boasts of an almost half a century old perfumery industry with old established players primarily supplying to intoxicant manufacturers. As a result, it is economically stronger with respect to other locations making the possibility of a retailing venture more viable. It is also better connected by rail and road than the other two. It is about 80 km from Kanpur. You may eventually cover the other areas through smaller formats, typically a spiral expansion approach.

Priyank: I guess AB and I would move on to conduct a scenario analysis of Kannauj. We shall meet you again with our findings by the end of this fortnight.

Puru: Take one of my young associates, an MBA graduate, Vishwa, along with you for that. He maintains my distributor contacts in western UP. Using his contacts and resources, you would be able to meet people and garner information much faster and easier.

EXHIBIT CSI.3 Map of Kannauj**The Kannauj Block⁶**

The town was located on NH91⁷ on the banks of The Ganges (Exhibit CSI.3). Once in Kannauj, while Vishwa met the government officials to gather the demographic and trade data and arrange interaction with some businessmen, AB and Priyank, started exploring the terrain. They went about the place through its lanes, by-lanes, and crowded markets.

AB: Evidently retailing in Kannauj district is in its evolutionary phase. Much of it looks scattered and unorganized in terms of supply chain, quality, and reliability of costs.

Priyank: I agree. You can observe that typical of a small town market, majority of the retailing takes place in the main bazaar with shops ranging between 100 and 350 sq. ft. Most of them specialize in a particular merchandise; though some of them apparently have been at this place for long as general merchants, reminiscent of variety stores. These numerous small-sized shops and narrow roads make the market look very clustered. I also noticed that there were

several shops dealing in agri-inputs and implements. On enquiry, a retailer told me that in Kannauj block, fertilizers and seeds are disbursed through 12 cooperatives and 60 private retailers, while crop protection chemicals (insecticides, fungicides, and herbicides) and plant growth regulators (PGRs) are distributed through only 12 private retailers. Very few retailers deal in liquid fertilizers. Consumer durable and farm equipment stores appear larger in size. A significant number of shoppers in most of the shops are men.

AB: Did you notice a number of general grocery, agri-input, durables, and other shops on the national highway? People say, in the past few years, as the city has expanded towards NH91, retailing has also been spreading to that region. One of the shopkeepers says that the block serves several villages within a radius of about 25 kilometers, except on the east due to the river.

Priyank: Now I see why I found so many tractors parked near the bus stand, about half a kilometre from the market.

6. A state is divided into districts as administrative units; which in turn consist of blocks.

7. National highway linking Kanpur and Ghaziabad.

EXHIBIT CS1.4 Basic Demographic Information for Kannauj Block

Population	200,000.0	Sex ratio (females/1000 males)	862.0
Population density (persons/ sq. km)	585.0	Literacy rate (%)	58.2
Rural population (%)	80.0	Literacy rate (males)	69.0
Average family size (urban)	6.5	Literacy rate (females)	45.0
Average family size (rural)	7.0	Area (hectares)	37,800.0

Age-wise Population Distribution across Kannauj Block

Age Group	% Total	% Males	% Females
0–9	27.5	26.7	28.3
10–19	24.0	24.8	23.1
20–34	21.4	21.2	21.7
35–49	15.0	15.5	14.4
50–59	5.5	5.3	5.7
> 59	6.6	6.5	6.8

Education Scenario in Kannauj District

	< Primary	Primary	Middle School	Higher Secondary	Senior Secondary	Graduates	Others
Males	22.52	23.27	25.56	15.17	7.96	5.39	0.13
Females	22.52	29.59	29.9	9.86	5.36	2.71	0.06

Source: District statistical office, Kannauj

AB: Among these small stores on the highway, I also found a larger store of TATA Kisan Kendra. I visited the store and was told that Hariyali Kisaan Bazar, the rural retail arm of the Sriram group, is located about five kilometers towards the west.

Vishwa: The government statistical department report indicates Kannauj to be a block with a population of 200,000 with a density of 585 persons per square kilometer (Exhibit CS1.4). Spread over an area of 37,800 hectares, it consists mainly (80%) of rural population. About 35% of the population is within the age of 20 and 50 and supports a literacy level of 58%; about 75% of which are educated till middle school. The main occupation of the population is farming (about 52%). Another 25% are marginal workers (Exhibit CS1.5). Depending upon the size of landholding, these farmers earn upto ₹2,00,000 per annum.

Priyank: I individually interviewed some farmers during the day. They say that a typical farmer saves about 60% of the income for the next crop. Their other primary

expenditures include household consumables, apparel, education of children, and savings to buy durables and construction material. Apparently, due to a highly unreliable and seasonal income the basket size per purchase is small. However, they spend a considerable amount during festivities and special occasions amongst relatives or local community. Further, a majority of the earnings of a rural household is consumed in the year itself or is converted into assets such as housing, agricultural implements, or consumer durables such as refrigerator, television, bicycles, motorcycles, and mobile phones.

AB: What about the people related with the perfumery industry?

Priyank: This is a high margin industry with the old established players primarily supplying to intoxicant manufacturers. Businessmen, though few in number, have good income. Their spending pattern is quite similar to a tier II city consumer. Also, with better cropping patterns and higher awareness due to the high penetration of

cable and satellite, especially among younger population, rural consumers are also aspiring to acquire the same status and livelihood as their urban counterparts. The role of social hierarchies, caste, religion, traditions, social norms, and customs in influencing buying behavior is also vital.

Consumption Pattern in Kannauj

AB: I have some information on the monthly per capita consumption expenditure (MPCE) classes (Exhibit CSI.6) of UP. If we translate this to Kannauj in the same proportion, we see that about 63% of the rural households spend more than ₹420 per month on personal consumption. This amounts to a total potential market of a ₹1 billion per annum (Exhibit CSI.7). However, this is just the government reported figure, and from what I see, I expect the number to be at least three times higher. My discussions with dealers and the manager of HKB provide a further indication of the share of food and non-food items (Exhibits CSI.8 and CSI.9). A typical

household would spend about 40% of the total spending on non-food items. There has also been a recent upsurge in the consumer durable market for products such as 100cc motorcycles from Hero Honda, lubricants, 175 l. refrigerators, color televisions, and building construction materials. In view of the increasing aspirations of the local consumers, local retailers have already started to shelf products on the lines of tier II city stores.

Agricultural Scenario

Next, while Priyank and Vishwa moved out to have a look at the location and meet some government officers, AB met the district agricultural officer (DAO). He indicated that Kannauj primarily lies in the potato cultivation belt. Other important crops are wheat and maize (Exhibit CSI.10).

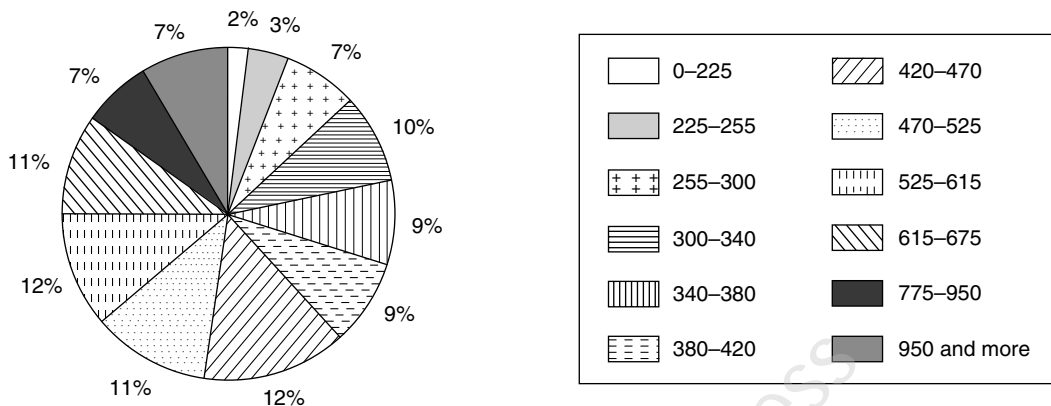
AB: With the help of data obtained from the officer and in conversation with various retailers and agriculturists of the region, I have prepared a molecule and product-

EXHIBIT CSI.5 Economic Scenario across Various Occupational Categories in Kannauj Block

Category	Annual Income (₹ '000)	Explanation			
Farmer					
Landholding	< 2 acres	60			
	2–4 acres	60–120			
	4–8 acres	120–180			
	8–12 acres	180–240			
	> 12 acres	> 240			
Landless agricultural worker	15–25	150–250 days work available at established ₹100/day rate			
Landless non-agricultural worker	20–35	200–350 days work available at established ₹100/day rate			
Industrial workers					
Skilled	60–150	5,000–12,000 salary per month			
Semi-skilled/Unskilled	20–50	2,000–4,000 salary per month			
Small shop owner	50–150	Depending upon the scale of operations and type of product sold			
Small business owner	300–700	Depending upon the scale of operations and type of product sold			
Large business owner	> 1,000	These are usually the perfume manufacturers and cold storage owners in the area			
<i>Farmers</i>	<i>Agricultural Workers</i>	<i>Businessmen</i>	<i>Marginal Workers</i>	<i>Others</i>	<i>Total Workers</i>
26,866	6,562	1,608	13,177	3,627	51,840

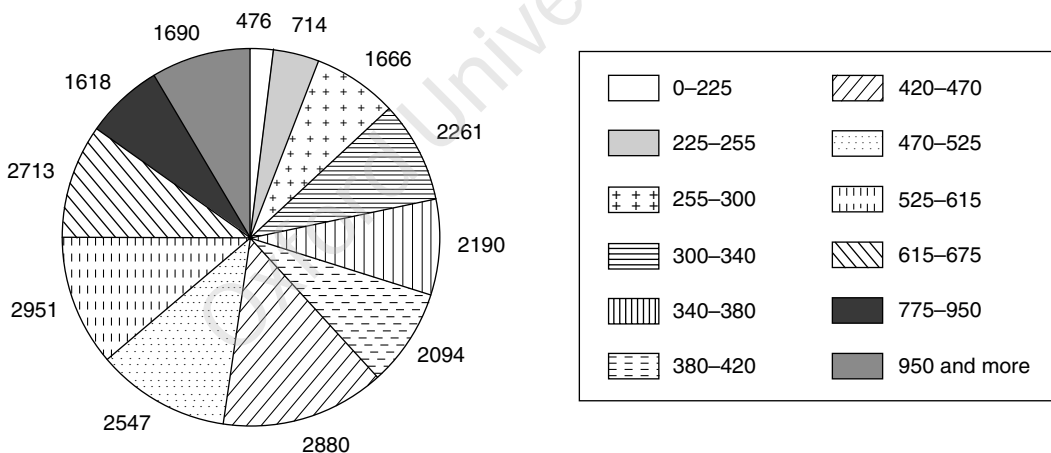
Source: Based on personal interview samples collected and district statistical office records

EXHIBIT CSI.6 Percentage Distribution of UP Rural Households in Various MPCE Classes



Source: Indiatstats

EXHIBIT CSI.7 Distribution of Kannauj Rural Households under MPCE Classification



Source: Based on discussions with dealers and HKB manager.

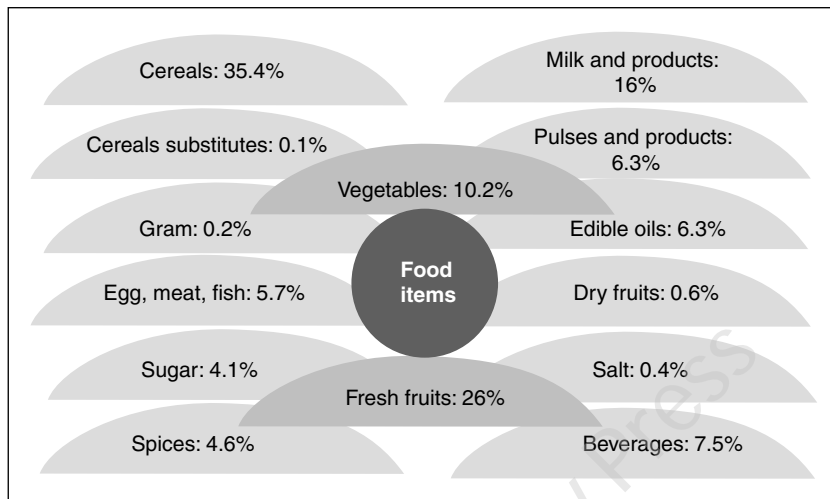
wise usage scenario for various agricultural inputs (Exhibit CSI.11). We know the usage factors for each of these inputs. Superimposing these on the landholding scenario (Exhibit CSI.12), we arrive at the annual agricultural input requirement for the area (Exhibit CSI.13). The DAO has also provided the following scenario of the agricultural and veterinary services in the region (Exhibits CSI.14 and CSI.15). This

information may help us think about some add-ons for the retailing model.

Locational Analysis

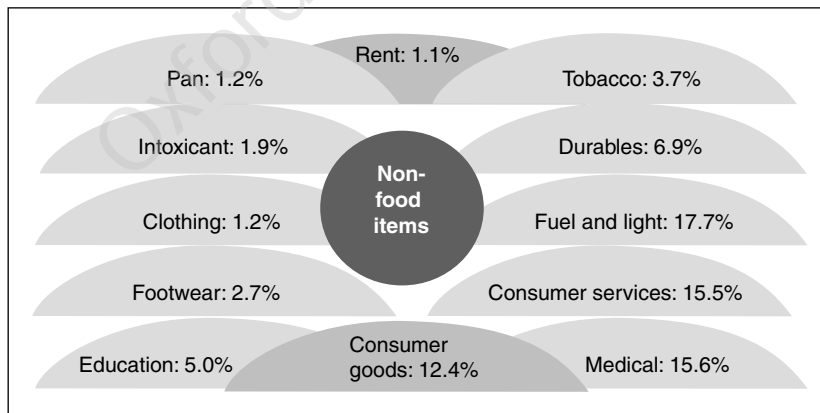
Vishwa: Kannauj is very well connected with nearby villages via all-season roads; 25 roads connect Kannauj with villages, each having a population of more than 1,500. There are another 45 all-season roads connecting

EXHIBIT CSI.8 Spending Pattern of Kannauj Rural Households under Food Consumer Segments



Source: Based on discussions with dealers and HKB manager.

EXHIBIT CSI.9 Spending Pattern of Kannauj Rural Households under Non-food Consumer Segments



Source: Based on discussions with dealers and HKB manager.

EXHIBIT CS1.10 Cropping Pattern in Kannauj

<i>Crop</i>	<i>Area under Cultivation (Hect)</i>	<i>Yield (MT/Hect)</i>	<i>Annual Production (MT)</i>	<i>Price/MT (₹ '000)</i>
Paddy	659	2.41	1,588	10.0
Wheat	8,411	3.12	26,242	6.8
Bajra	84	0.63	53	5.2
Jowar	202	0.74	149	5.7
Maize	8,160	1.81	14,770	5.6
Barley	219	3.12	683	5.6
Urad	267	0.92	246	16.7
Moong	224	0.83	186	16.5
Chana	253	1.13	286	18.6
Peas	272	1.61	438	13.2
Arhar	265	0.96	254	16.1
Mustard	1,247	1.07	1,334	18.2
Sunflower	1,705	2.05	3,495	14.2
Potato	7,141	21.14	150,961	2.4
Other vegetables	7,341	NA		
Total	36,619			

Source: District Agriculture Office

EXHIBIT CS1.11 Product and Molecule-wise Usage Scenario of Various Agricultural Inputs

<i>Various Agri-inputs</i>		<i>Agri-input Usage Scenario (in MT/Annum)</i>							<i>Total</i>
		<i>Potato</i>	<i>Sunflower</i>	<i>Paddy</i>	<i>Wheat</i>	<i>Watermelon</i>	<i>Maize</i>	<i>Flowers</i>	
Fertilizers	Urea	2,625	425	175	2,075	~0	2,150	15	7,465
	DAP	3,500	85	35	996	25	1,075	15	5,731
	MOP	875	~0	~0	~0	0	430	~0	1,305
	Zinc	175	0	9.1	~0	0	~0	0	184.1
	NPK	3,500	85	35	996	0	1,075	0	5,691
	SSP	8,750	~0	~0	~0	0	0	0	8,750
	Others	50							
Insecticides	Phorate 10G	7	1	7	2	0.2	2	0	19.2
	Chloropyriphos 20EC	1	1	1	0	0	0.2	0	3.2
	Endosulphan	1.5	1	2	0	0.2	0.2	0.1	5
	Cypermethrin	1	0.5	1	0	0.1	0.2	0	2.8
	Sulphur 80WG	1	0.5	0.2	0	0	0	0	1.7
	Monochrotophan	1.5	0.5	1	0	0.1	0.3	0	3.4

(Contd)

(Exhibit CS1.11 Contd)

Various Agri-inputs	Agri-input Usage Scenario (in MT/Annum)							
	Potato	Sunflower	Paddy	Wheat	Watermelon	Maize	Flowers	Total
Carbofuran	2	0	0.5	0	0	1	0	3.5
Dimethoate	2	0	0	0	0.2	0	0.1	2.3
Malathion	0.5	0	5	0	0	0	0	5.5
Fungicides								
Mancozeb	10	0	0.2	0	0.2	0	0	10.4
Sulphur 80WG	1	0.5	0.2	0	0	0	0	1.7
Sulphur 80WP	2	2	0.5	0	0	0	0	4.5
Carbendazim 50WP	1.5	0	0	0	0.05	0	0	1.55
Metalaxyl+Mancozeb	2	0	0	0	0.01	0	0	2.01
Copper Oxychloride	0.2	0	0.5	0	0	0	0	0.7
Hexaconazol	0.05	0	0.2	0	0	0	0	0.25
Herbicides								
Butachlor 50EC	0	0	2.5	0	0	0	0	2.5
Pretilachlor 50EC	0	0	0.2	0	0	0	0	0.2
2,4-D 80 WP (Na salt)	0	0	2	2	0	0	0	4
Isoproturon 75 WP	0	0	0	2	0	0	0	2
Metribuzin 70 WP	2	0	0	0	0	0	0	2
Glyphosate	1	0	0	0	0	0	0	1
Atrazine 50 WP	0	0	0	0	0	3	0	3
PGRs								
Amino acid base (amino cell gold, Suryamin, Biovita, Biozyme)	4	0	0	0	0	0	0	4
Seeds	178525	8.4	9.8	1662	123.5	161.2	NA	180490

Source: Based on inputs from agri-input dealers and agronomists in the region.

EXHIBIT CS1.12 Landholding Scenario

Landholding	Area (in Hect.)	Percentage of Total	Number of Plots
< 0.5	5,461	21.2	11,774
0.5–1.0	4,268	16.6	6,475
1.0–2.0	8,140	31.6	4,353
2.0–4.0	5,592	21.7	2,300
4.0–10.0	2,128	8.3	406
> 10.0	150	0.6	12

Source: District agriculture office

EXHIBIT CS1.13 Agricultural Input Requirement in Kannauj

Landholding of Farmer (Hectare)	Number of Farmers in the Category	Total Fertilizer Requirement (MT/Hect)	Total Insecticide Requirement (MT/Hect)	Total Fungicide Requirement (MT/Hect)	Total Herbicide Requirement (MT/Hect)	Total PGR Requirement (MT/Hect)
< 0.5	11,774	3,004	10	4	3	1
0.5–1.0	6,475	2,347	8	3	3	1
1.0–2.0	4,353	4,477	15	7	5	2
2.0–4.0	2,300	3,076	10	4	3	1
4.0–10.0	406	1,170	4	2	1	0
> 10.0	12	83	0	0	0	0

EXHIBIT CS1.14 Agricultural Services Situation (2005–06)

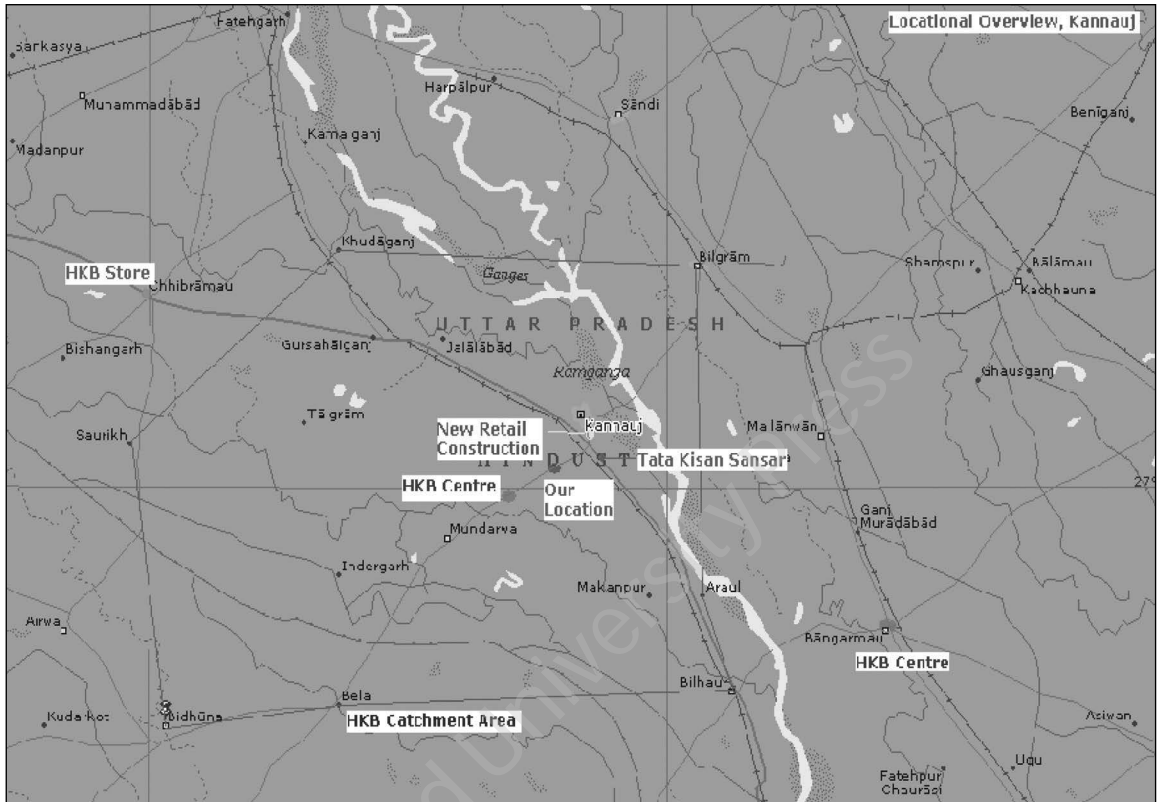
Warehousing facilities	Cooperative	0
	Agri-dept	0
	Private	12
	Total installed capacity (MT)	2,500
Crop protection centre		0
Crop services centre	Agro	0
	Others	3
Cold storage facilities	Number	50
	Total installed capacity (MT)	247,857
Mandi Samiti		0

Source: District Agriculture Office

EXHIBIT CS1.15 Veterinary Services Situation (2003)

Buffaloes	36,454
Cows	22,754
Sheep	40
Goats	52,006
Total cattle	111,254
Veterinary hospitals	0
Veterinary pharmacies	1
Cattle service centre	2
Artificial insemination centres	3
Cattle breeding centres	0

Source: District Agriculture Office

EXHIBIT CSI.16 Overview of NAGIL's Location with Respect to Other Major Retail Players

to other small villages. Government and private buses, jeeps, and shared auto-rickshaws are easily available for commuting. Due to the effective road network, most local retailers and distributors use trucks or trolleys to transport their cargo. All trading and procurement take place through these centres. Table CSI.1 provides approximate costs to transport cargo from Kannauj to various commercial centres using truckload.

TABLE CSI.1 Approximate Transport Cargo Costs from Kannauj

Kannauj to	Truck Freight Charges (in ₹)	
	Peak Season	Lean Season
Delhi	7,000–8,000	7,000
Kanpur	2,100	1,800
Farrukhabad	2,300	2,000
Lucknow	4,500	4,100

Usually, trucks are used to transport 9–15MT of cargo, whereas trolleys may help transport loads up to 7MT. GATI and XPS, two courier and cargo companies, also have good services in the region. The power supply situation is very poor and unreliable. Local retailers rely solely on diesel generator sets. During summers, one might expect an intermittent supply of electricity for only 10 hours a day, though 484 out of 693 villages in Kannauj District are electrified.

Priyank: I surveyed the location of NAGIL's plot. Apparently, we are within a radius of 80 km from major commercial centres—Kanpur and Farrukhabad. (Exhibit CSI.16 indicates an overview with respect to other major organized retail players in the region.) There is a DSCL's HKB just 3 km away from the location on the same, on the Kannauj–Tirva road. I had a look at their assortment. They seem to be targeting the villagers though they have kept certain hi-end products as well. Apparently, a new retail construction is also coming up at

a distance of 5 km on the highway towards Farrukhabad. Grapevine is that it is expected to be rented to RPG Spencer's. One disadvantage, apparent to me, with the location of the plot is that it is situated across the railway line. However, most of the recent constructions, commercial as well as residential, are being developed along the highway, which runs along the railway line in Kannauj.

AB: Good you had a look at HKB's store. I too did some background research on this particular rural retail by talking to the regional dealers and the store manager. They were the first to take a step towards organized retailing in Kannauj in 2006. Spread over three acres, HKB sells all sorts of items, ranging from agri-inputs to hardware. After facing several challenges in the past two years, the number of footfalls per day has stabilized between 200 and 700. HKB operates around 25 centres and stores in western, 20 in central, and another 25 in eastern UP. Since its inception in 2006, the HKB-Kannauj centre has been able to gain considerable farmer attention through village-level campaigns. Its agronomists regularly visit farmers in its catchment area and advise them on better agricultural practices and inputs. This has helped them in developing a rapport with the local rural population. Exhibits CS1.17 (a) and (b) show the layout of the store in Kannauj.

Another important organized retail player in the area is TCL's Tata Kisaan Sansar. TCL first ventured

into the rural retailing space as Tata Kisaan Kendra in 1998. These were designed to be one-stop agricultural input shops for Indian farmers. A strategic review of the business after four years led to its transformation into Tata Kisaan Sansar (TKS). TKS was set up with the objective of helping farmers to create value by improving farm productivity through better agronomic practices, availability of farm credit, and quality agricultural inputs. TKS usually operates through a franchisee which typically operates as a branded retail outlet providing agricultural inputs, farm equipments, crop advisory services, farmer credit financing, and produce buyback arrangements. A TKS operates on over 2,000–3,000 sq. ft of space and serves a catchment area of 8–10 km.

Political, Legal, and Regulatory Scenario

Priyank: I must say I am kind of surprised. Sitting over there in Delhi, and reading through national dailies' reporting of 'Reliance Shutting Shop; Putting at Bay Its ₹130 Billion Investment due to Various Kinds of Political Hindrances', I never realized there are others who have been able to do fairly well. Problems were also witnessed by Subhiksha (which has closed down) and Spencer's, I guess. All I wonder is how are some of them able to sail smoothly while others face trouble. I always thought the UP government has not been particularly supportive of large organized retail formats because of its perceived ill-effect on small *kirana* stores. After all, which political party would play with its vote-bank by enraging the large dependent population?

EXHIBIT CS1.17(a) Hariyali Kisan Bazaar, Kannauj Site Layout Plan

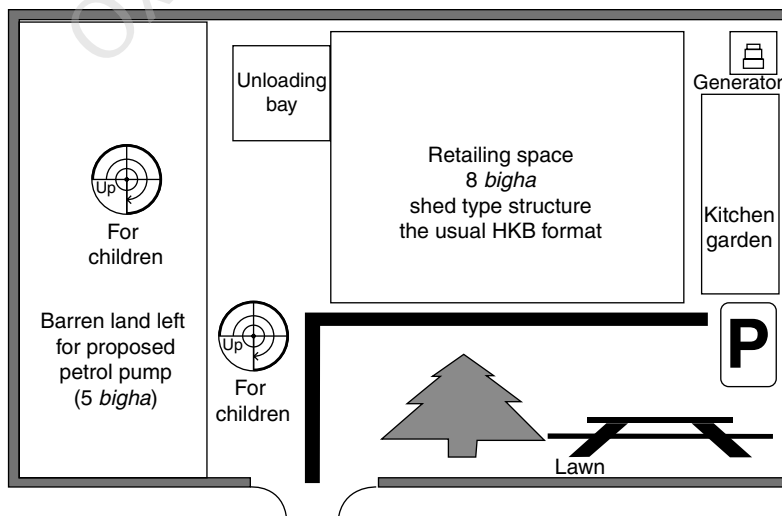
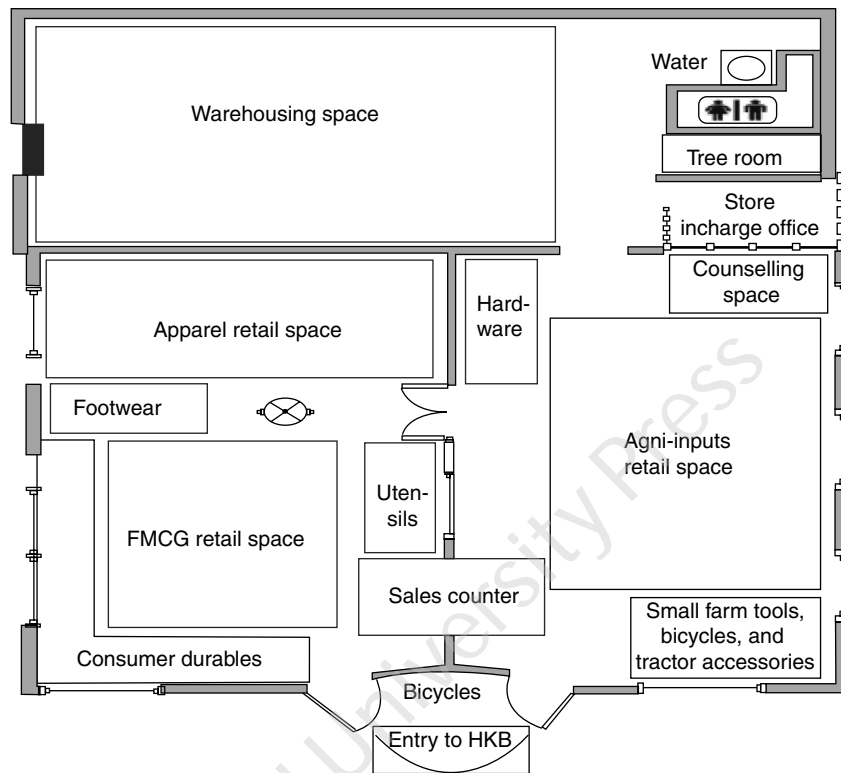


EXHIBIT CSI.17(b) Schematic View of HKB Store Layout

Vishwa: There are two major political lobbies in UP; you emphasize on one's area, the other kills you. A retailer cannot fare well in any state without understanding the political dynamics of the state. After all, the retail and wholesale sector in UP is the second largest employer (after agriculture) in the state by providing employment to about 10% of the population.

AB: Vishwa, what did you figure out about the regulatory requirements through your discussions with district regulators?

Vishwa: Litany of licenses and enforcement of acts. Applications need to be filed to

- the district magistrate for changing the land-usage pattern from agricultural land to commercial land;
- legal metrology department with affidavit on compliance of Standard Weights and Measures Act;
- inspector—shops and establishments—with affidavit on compliance of Shops and Establishments Act;

- the municipality for operating the store 360 days a year, for extending hours of work on requirement, for storage of inflammables, for selling food items, etc.;
- the state electricity board;
- the excise and sales tax departments;
- the fire department for a no-objection certificate;
- the labour department with affidavit on compliance of Payment of Wages Act and Minimum Wages Act and I am sure there is more to it!

AB: Oh sure! That is just an indicative list. There are at least 30 licenses that I see we shall need to file. Take for example, essential commodities such as staples, food grains, and sugar. The government regulates production, supply, and distribution of these essential commodities through the Essential Commodities Act, 1955. Any retailer dealing in these products would need to obtain a license. The situation is no different for agri-inputs such as fertilizers.

Priyank: You are right, AB. However, there are certain favourable regulations in the state that NAGIL can benefit from, such as the following:

- UP was the first state to modify its Agricultural Produce Marketing Act. The Government of UP allows direct sale/purchase from the farmer's fields under the Uttar Pradesh Krishi Utpadan Mandi Adhiniyam. Cargil and ITC are procuring their produce through this mechanism. NAGIL may eventually think about developing produce buy-back arrangements with farmers.
- Besides, contract farming is being practised by reputed companies for select commodities, such as Pepsi for potato.
- The government also allows public-private partnership in financing, construction, operation, and management

of agricultural markets. No fee is being levied on direct marketing of agricultural produce.

The Strategic Call

Purushottam was feeling confident with the information that AB's team had gathered. 'There seems to be potential in this place. This place is also near our headquarters and is accessible by road as well as rail. The block also seems to be a feeder town that attracts customers from all over. What about the financials?' AB provided Purushottam with a ballpark five year projection of the business and CAPEX requirements (Exhibits CS1.18 and CS1.19). He opened the envelope and started reading the report. He was into the first paragraph when his phone rang. 'I would have to leave now. It seems the meeting with the investors for this business has been advanced. In case you have some other thoughts, please mail me. I would access it on my Blackberry'.

EXHIBIT CS1.18 Anticipated Financials

Capital Expenditure Requirement (₹)	Category	% of Wallet of Customer	Expected Margins	
Site development costs	800,000	Apparel	6	70
Construction costs	4,500,000	Footwear	3	70
Furnishing and interiors	1,200,000	Building materials, hardware, and lubes	5	25
Electrification costs	100,000	Cosmetics	2	35
		Child products	2	60
Equipment costs		Toys and games	2	75
Generator	1,400,000	Gifts and novelties	1	75
Material handling equipment	50,000	Thermoware	1	30
Computers and peripherals	92,000	Agri-inputs	30	12
Other miscellaneous	90,000	Consumer durables	7	15
		Home furnishing	2	70
Insurance costs	1,000,000	Plastic goods	2	65
Licensing costs	600,000	Kitchen aids	1	70
Initial procurement costs	1,700,000	Glassware	1	30
Retail launch expenditure	200,000	Dress accessories	3	75
Manpower recruitment costs	50,000	FMCG	30	20
		Cleaning aids	1	70
Total	11,782,000	Electricals	1	75
		Average margin		30.1

EXHIBIT CSI.19 Proforma Income Statement

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
	2008–09	2009–10	2010–11	2011–12	2012–13	2013–14
Total sales	0	14,000,000	15,400,000	16,940,000	18,634,000	20,497,400
Cost of sales						
Material costs	1,700,000	9,793,000	10,772,300	11,849,530	13,034,483	14,337,931
Other direct	10,500	778,000	855,800	941,380	1,035,518	1,139,070
Total cost of sales	1,710,500	10,571,000	11,628,100	12,790,910	14,070,001	15,477,001
Gross margin	(1,710,500)	3,429,000	3,771,900	4,149,090	4,563,999	5,020,399
(As a % of sales)		24	24	24	24	24
Overhead expenses						
Selling	0	140,000	154,000	169,400	186,340	204,974
Personnel	50,000	1,590,000	1,749,000	1,706,100	1,876,710	2,064,381
General	0	68,500	75,350	82,885	91,174	100,291
Depreciation	0	718,900	718,900	718,900	718,900	718,900
Advertising costs	20,000	20,000	20,000	20,000	20,000	20,000
Insurance related costs	0	996,058	1,095,664	1,205,231	1,325,754	1,458,329
Total operating expenses	70,000	3,533,458	3,812,914	3,902,516	4,218,877	4,566,875
Net income before taxes	(1,780,500)	(104,458)	(41,014)	246,574	345,122	453,524

* *Source:* The team also indicated that the typical estimates for other established players were as follows:

- Gross margin (% of revenue) = 10–16%
- Fixed costs (% of revenue) = ~15%
- Variable costs (% of revenue) = ~5%

Questions

1. Should NAGIL move into the retail sector? Please justify your answer.
2. If NAGIL goes ahead with its proposed decision of entry into organized retail, which would be the best place to start the venture?
3. Please identify the key decision areas and analyse the competitive strategies for NAGIL as an industry.