



Socio-Economic Impact of Direct Selling: *Need for a Policy Stimulus*

Arpita Mukherjee, Tanu M. Goyal, Divya Satija, Nirupama Soundararajan



Executive Summary

India is one of the fastest growing economies in the world. Over the past decade, the gross domestic product (GDP) and per capita income has grown at an average annual rate of seven per cent and five per cent, respectively. By 2015, with a projected GDP of \$2.18 trillion, India is expected to be the 11th largest economy in terms of GDP based on the market exchange rate and the fourth largest in terms of purchasing power parity (PPP).

With the increase in growth rate, per capita incomes rose, urbanisation increased and the percentage of people below the poverty line declined. In addition, the Indian consumer market underwent changes. There has also been a shift in the pattern of consumption – from necessities to discretionary consumption. In 2007, India was ranked the 12th largest consumer market in the world and it is expected to be the fifth largest consumer market by 2025 after the United States (US), Japan, China and the United Kingdom (UK).

With economic development and growing consumerism, the retail sector in India also underwent significant changes. Various store and non-store retail formats have evolved to cater to this growing market and direct selling is one such non-store retail format. Direct selling refers to the selling of goods and services to the consumers away from a fixed retail outlet, generally in their homes, workplace, etc., through explanation and demonstration of the product by direct sellers. This sector is one of the fastest growing non-store retail formats, recording double-digit growth in the post-reform period. The growing Indian market has attracted a large number of Indian and foreign direct selling companies.

Globally, direct selling is a labour-intensive industry and has a positive socio-economic impact in terms of higher employment, women empowerment and skill development. This report examines the socio-economic impact of direct selling sector in India focusing on how the benefits can be leveraged through appropriate policies. Since there is hardly any primary data on this sector, the report is based on a pan-India primary survey of more than 2500 respondents including direct selling companies, their manufacturing and supply chain agents, direct sellers, consumers and policymakers.

The study found that direct selling is a relatively new sector in India but is growing at a fast pace. Companies are spreading their operations from Tier I to smaller cities and are even trying to explore rural markets. The number of products sold through this route has increased. A number of foreign companies have already established their presence in India and many more are exploring this lucrative market.

Direct selling offers self-employment opportunities to a large number of people, especially women. The number of direct sellers in India has almost doubled between 2004 and 2009. In terms of the number of direct sellers, India ranked 11th among the top direct selling countries in 2009-10. In future, this sector is expected to offer employment opportunities not only in urban areas but also in rural areas. Indirect employment is expected to be generated in manufacturing and the supply chain, as direct selling companies develop India as a sourcing hub. The direct selling industry not only offers an alternative employment opportunity but has also contributed in terms of increased incomes for those who have entered the industry as direct sellers. The survey revealed that most direct sellers are happy with the quality of their employment. Financial independence, development of personal and business skills, flexible timings and an improved ability to take care of families are other benefits of direct selling. Direct sellers have pointed out that direct

selling has helped them to build self-esteem and confidence and develop their sales skills. It has enabled women to be financially independent and increased their ability to save. Direct selling also provided a safety net during the global slowdown as a large number of direct sellers joined this sector during that time. In fact, the number of direct sellers increased by 4.84 per cent during the slowdown period (2008-10). An interesting finding of the survey is that although, direct selling has benefited women in terms of financial independence and improved self-esteem, Indian women, unlike women in other countries, do not think that they have achieved equality of status with men. The flexible working hours that direct selling offers has helped women achieve a balance between their work and family lives.

The survey of consumers showed that Indian consumers are ready to explore various formats of retail. Although only a few are at present using the direct selling mode, the consumer base is likely to increase in the future with a rise in incomes, growing awareness and changes in the consumption basket. Those who use this mode have pointed out that direct selling offers several benefits such as personalised service, products of good quality, convenience and time saving.

The survey also found that direct selling companies are investing in setting up manufacturing units in India and are streamlining the supply chain. A substantial part of the products are sourced locally from contract manufacturers and this is leading to the percolation of technology, the concept of branding and packaging, etc., to Indian small and medium enterprises (SMEs).

In spite of these benefits, the survey found that there are several barriers, which restrict the growth of this sector. While some of them can be addressed by the direct selling companies, the others need government intervention. Barriers such as sale of limited products through this mode, need for better product marketing, streamlining the supply chain and logistics have to be addressed by the direct selling companies. The companies should also make basic training mandatory, which will improve the quality of direct sellers and facilitate brand building. Since the direct sellers represent the direct selling companies, it is in the interest of the companies to follow a stringent verification procedure for appointment of direct sellers to minimise frauds. Personal information and contact details of direct sellers can be made available in the direct selling companies' websites so that consumers can identify legitimate direct sellers.

There are broadly four areas that need government intervention. These are: (a) the provision of a clear definition of direct selling, (b) streamlining of the foreign direct investment (FDI) policy (c) the enactment of a governing legislation for the sector and (d) the establishment of a nodal ministry or single point of contact.

a. Need for a clear definition:

There is no clear and holistic definition of direct selling in India; as a result, the classification of direct selling is also unclear. While the Department of Industrial Policy and Promotion (DIPP) classifies direct selling under wholesale trade for the purpose of FDI inflows, according to the National Industrial Classification (NIC), 2008, direct selling is classified under retail trade (non-store format retail). This has benefited the sector, partially because 100 per cent FDI is allowed in wholesale trade. However, the definition of wholesale trade itself has undergone several changes and direct selling is not clearly specified in the consolidated FDI policy of DIPP dated April 2010. Moreover, direct selling, especially the multi-level marketing format has both business-to-business and business-to-consumer operations. Thus, it is neither a part of retail nor wholesale trade; rather it is, *sui generis*, shares properties of both retail and wholesale. Some experts, therefore, define direct selling as neither wholesale nor retail but as a specialised channel of distribution.

There is need for a proper definition of retail and wholesale trade and of different components of retail trade. This is needed because FDI is presently allowed in some segments of retail while there are FDI restrictions on others. In fact, while designing the FDI policy, the DIPP should follow either the NIC classification (which is compliant with the international industrial classification) or the United Nations Central Product Classification (UNCPC) classification. These two classifications are broadly similar. Different formats of retail and wholesale trade should be clearly defined for the purpose of FDI inflows.

b. Need to streamline the FDI policy:

At present, FDI is not allowed in multi-brand retail and is only partially allowed in single-brand retail. It is allowed in wholesale cash and carry. This has led to multiple back door entry routes. As of now, many retail and direct selling companies have entered the Indian market through routes such as test marketing, sourcing from SMEs, franchising, wholesale cash and carry, 51 per cent FDI in single-brand retail and setting up of manufacturing facilities. The survey found that the FDI restriction on retail is not an entry ban but it has led to grey market operations. Some traditional, family-owned retailers have also become direct sellers. As long as retail is treated as a sensitive sector (irrespective of the products sold) and there are multiple entry and operation routes, the sector will suffer from operational uncertainties. The FDI policy should be clear and transparent and should ensure a stable operating environment. Otherwise, India will not be able to attract the desired FDI and foreign companies in India will continue to face operational uncertainties.

Since most direct selling companies are 'single-brand', they would benefit if 100 per cent FDI is allowed in single-brand retail. It is also easier to allow 100 per cent FDI in single-brand retail since most single-brand retailers, including direct selling companies, do not operate in sensitive sectors like fresh fruits and vegetables. This will increase sourcing from India, percolation of technology and the concept of branding. This sector will benefit even more if partial FDI is allowed in multi-brand retail since there will be more clarity on the entry route. Partial FDI in multi-brand retail will not adversely impact the traditional sector since direct selling companies operate only in branded products and they have a selling model that is different from that of traditional, family-based retailers. On the other hand, it will lead to inflow of FDI, technology and best management practices. Since direct selling is labour intensive, it will create employment.

It is important to know that retail – both in the store and non-store formats – is regulated across the world. However, clubbing the FDI policy with domestic regulations makes the FDI policy non-transparent and cumbersome. The retail regulation should be equally applicable to domestic and foreign retailers and should be separate from the FDI policy. This will also strengthen India's position in international negotiations like the World Trade Organization (WTO) where FDI issues are covered under market access or entry-level barriers while domestic regulations are addressed separately. Further, clubbing the FDI policy with domestic regulation may lead to differential treatment for foreign and domestic companies, which is not desirable since at present the sector is highly competitive. Besides, it will worsen India's bargaining position in the WTO and other international negotiations.

c. Need for a governing legislation:

Like retail, direct selling falls under the purview of state legislation and is governed by a large number of ministries/departments at the centre, state and local levels. The multiplicity of regulatory bodies has resulted in multiple regulations governing this sector. These should be streamlined for the smooth performance of this sector and for setting up a pan-India supply chain and manufacturing facilities.

In spite of the large number of regulations, the direct selling sector in India does not have a comprehensive Act as in the case of countries like Malaysia. This study found that the Prize Chits and Money Circulation Scheme (Banning) Act, 1978, which is sometimes cited for regulating this sector, is not applicable to direct selling and is outdated. India should have a comprehensive Act focussing on banning fraudulent practices such as pyramid schemes. The Act should have a clear definition of pyramid and other money circulation schemes and draw a distinction between fraudulent schemes and legitimate multi-level marketing (including direct selling). Since, the number of pyramid schemes and the modes of operation of fraudulent players change frequently, it may be easier to lay down the procedures for identification of legitimate direct selling companies. Such procedures can be drawn up by carefully studying the code of conduct for direct selling companies across the world. The India Direct Selling Association (IDSA) has laid down a code of conduct but this is voluntary and is only applicable to IDSA members. There is need to have a proper regulation in place that lays down conditions for identification of a legitimate direct selling company. A majority of survey participants felt that registration of direct selling companies with a central authority, based on a clearly specified procedure and nominal registration fees, would help identify legitimate operators in the sector.

The Consumer Protection Act, 1986, and the Consumer Protection (Amendment) Act 2002, which came into effect in March 2003, need some modifications in order to protect consumers of products sold through direct selling. For example, it does not clearly specify the cooling-off period for purchases through direct selling mode. Apart from this, legal cases in India take time and there is need to speed up consumer court proceedings. In this context, the Indian government can learn from the regulatory experiences of other countries. The industry, government and consumers suffer because of the activities of fraudulent players. Therefore, the government can collaborate with industry associations and independent legal experts to design an appropriate regulation. Collaboration and co-operation between the industry and government is crucial for the smooth functioning of the sector.

d. Need for a nodal ministry:

There is no single nodal ministry at the centre and hence, the grievances of this sector go unheard. Companies are not sure whether it is the DIPP or Ministry of Consumer Affairs, Food and Public Distribution that governs them. Therefore, survey participants feel that the sector should have an independent regulator like Telecom Regulatory Authority of India (TRAI), which can be a single point of contact. The retail sector in India is also making similar demands. There is no doubt that there should be a nodal ministry or single point of contact at the centre. This can either be the DIPP or the Ministry of Consumers Affairs, Food and Public Distribution. However, since the sector does not have entry or exit barriers, is highly competitive and has no network or interconnection requirements, there is no need for an independent regulator.

During the survey, a number of survey participants pointed out that the sector should have “industry status”. Unlike retail, the demand for “industry status” is not because of a shortage of funds but because companies and direct sellers feel that this will give them a sense of security and legitimacy. At present, there are many fraudulent companies that operate under the garb of direct selling. This issue can be addressed if there is a nodal ministry and a governing legislation.

Overall, the study found that the direct selling sector is growing at a fast pace and the number of direct sellers are increasing. In the light of the high employment generation potential of this sector, any policy decision should take into account the effect of the policy on employment in a country where unemployment rates are high.



**Indian Council for Research on
International Economic Relations**

Core – 6A, 4th Floor, India Habitat Centre
Lodhi Road, New Delhi – 110003, India
Tel: 011-43112400, Fax: 011-24620180
Website: www.icrier.org