



## The Legal Structure and Framework of Luxury Goods Market in India: Competitive or Restrictive Growth?

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## The Legal Structure and Framework of Luxury Goods Market in India: Competitive or Restrictive Growth?

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### Abstract

It has been evident from our long human history that luxury has been present in one or other form of consumption practices and that the luxury goods have existed for ages, dating back to Roman times, where luxuries such as silks were consumed for status, respect, and pleasure to the reformation in Europe (during the 1600s), where luxuries were consumed secretly, since their extravagant nature seriously compromised consumers' modesty and equality, important values at the time. Since the early 1990s, the luxury goods sector has been growing at an unprecedented pace. The Indian market for luxury goods has proved to be a very lucrative market and the rate of growth has outpaced that of other consumer goods categories. According to the ASSOCHAM-KPMG study, the Indian luxury market growth is estimated at 30 per cent and projected to reach \$14 billion by 2016. This rate of growth has been triggered by accelerating influence of the affluent class, high net worth individuals with an appetite for luxury good consumption, ever growing middle class population, sophisticated consumers with a desire for exclusive products and several other related factors. But, still it is in a nascent stage of development in India and presently estimated to have just one-two per cent share in the overall share of the global luxury market. While the Indian market for luxury goods depicts business opportunities, it is also accompanied with a lot challenges which necessitates formulation of a strong legal structure and framework of intellectual property protection.

A key dilemma here in this scenario is that unless one understands the Indian Luxury market from various perspectives like key supply side/demand side trends, international product segmentation policies and overall market drifts; it is hard to evaluate the present legal structures and economic policies. Possible explanations for restrictive growth of Indian Luxury market would be (1) Constraints pertaining to Luxury Infrastructure, (2) Lack of policy support for Maximum Retail Price, (3) Not being viewed as policy/regulatory friendly by Luxury retailers, (4) High Import duties, (5) FDI policy of 30% sourcing tough for International luxury players (6) policies regarding Intellectual property rights, (7) Measures taken for the presence of counterfeit luxury goods and (8) Emergence of channels- Online and Grey.

The explicit premises on which our research intends to concentrate would be the following aspects:

1) Would the infrastructure of international standards encourage the luxury brands from setting outlets in the Indian market?

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- 2) Would the revisiting of few policies related to luxury market be conducive enough for thriving of Luxury retailers?
- 3) Would reforms in the taxation environment put us on the road ahead in the luxury sector?
- 4) Would high import duties encourage affluent class to go to abroad destination to shop?
- 5) Would the recent modification in the FDI rules pertaining to single brand and multi-brand retailers facilitate the stakeholders in the luxury market?
- 6) Would internet retailing prove as a key distribution channel in the luxury retailing sector? What would be the impact of the emergence of channels - “Online and Grey” for the luxury goods market in India?
- 7) Would the business environment masked by pervasive corruption and red-tapism affect the luxury investment?

This paper will firstly pinpoint the overall luxury market in India; secondly it would highlight the challenges faced by the luxury players in today’s legal as well as economic environment and finally emphasize the zone of attention. The authors through this paper do not aim at offering definite solutions to any of above questions but would improve understanding by delivering an encompassing outlook over the opportunities and issues highlighted in the Indian luxury market.

**Key Words:** Indian Luxury market, Luxury Retailing, Luxury Brands, Foreign Direct Investment, India

## **The Legal Structure and Framework of Luxury Goods Market in India: Competitive or Restrictive Growth?**

Our long human history in India has shown us that luxury has been existent in one form or the other when it comes to practices related to consumption. Luxury goods market has been evident in the market for centuries (Bernard, Sandor and Gilles, 2005). The word “Luxury” in English, “Luxe” in French and “Lusso” in Italian are all derived from the Latin term “LUXUS” which according to Oxford Dictionary (1992) connotes “soft or extravagant living, over-indulgence” and “sumptuousness, luxuriousness, opulence”. The concept of a luxury product is “perceived to be the extreme end of the prestige brand category where brand identity, awareness, perceived quality and loyalty are important components” (Phau and Prendergast, 2000). Luxury goods have existed for ages, dating back to Roman times, where luxuries such as silks were consumed for status, respect, and pleasure to the reformation in Europe (during the 1600s), where luxuries were consumed secretly, since their extravagant nature seriously compromised consumers’ modesty and equality, important values at the time (Berry, 1994). Since the early 1990s, the luxury goods sector has been growing at an unprecedented pace. The market for luxury apparel brands has proved to be a very lucrative market for the marketers and the rate of growth has outpaced that of other consumer goods categories. (Wadud and Nair, 2003) The rate of growth has been triggered by high net worth individuals with an appetite for luxury brand consumption. Accordingly, luxury brands have eventually started to become highly competitive and significantly required to be run like businesses. It is very significant to understand the attitude process and function that supports and creates the luxury brand. The processes according to which consumers acquire and consume luxury items remain unfathomable. It seems particularly difficult to predict the situations under which dreams about luxury generate and how such dreams finally materialize into purchase actions (Bernard and Claire, 1995).

Luxury products are well crafted and cultivate a highly desirable image of exclusivity (Bearden and Etzel, 1982). Clothing represents symbolic value reflecting the status of one who is wearing it (Solomon, 1983). When the clothing is transformed into luxury brand apparel, consumers become motivated to desire to impress others with high priced prestigious products (Mason, 1981). There has been a tendency of more consumers moving away from traditional low-cost brands to luxury brands (Speece and So, 1998). The studies that represent luxury apparel goods depict the purchase consumption dependent upon various needs of the consumer

status (Coelho and McClure, 1993), expression of identity (Piacentia and Mailer, 2004) and self-esteem (Taylor and Cosenza, 2002). Vigneron and Johnson (1999) define luxury brand as highest level prestigious brand consisting of values like perceived conspicuous value, perceived unique value, perceived social value, perceived hedonic value and quality value.

The Indian market for luxury goods has proved to be a very lucrative market and the rate of growth has outpaced that of other consumer goods categories. According to the ASSOCHAM-KPMG study, the Indian luxury market growth is estimated at 30 per cent and projected to reach \$14 billion by 2016. According to the Euromonitor International, the Indian Luxury goods market is the fastest growing and ranked 17 among 26 countries studied by Euromonitor International's Luxury Goods research. According to Euromonitor International, the luxury product categories which have recorded considerable growth are luxury jewelry as well as timepieces, luxury writing instruments/stationery; super premium beauty/ personal care, luxury electronic gadgets and luxury tobacco. This rate of growth has been triggered by accelerating influence of the affluent class, high net worth individuals with an appetite for luxury good consumption, ever growing middle class population, sophisticated consumers with a desire for exclusive products and other factors like unaccounted or black money in the economy. But, still luxury goods market is in a nascent stage of development in India and presently estimated to have just one-two per cent share in the overall share of the global luxury market. While the Indian market for luxury goods depicts business opportunities, it is also accompanied with a lot challenges which necessitates formulation of a strong legal structure and framework of intellectual property protection.

A key dilemma here in this scenario is that unless one understands the Indian Luxury market from various perspectives like key supply side/demand side trends, international product segmentation policies and overall market drifts; it is hard to evaluate the present legal structures and economic policies. Possible explanations for restrictive growth of Indian Luxury market would be (1) Constraints pertaining to Luxury Infrastructure, (2) Lack of policy support for Maximum Retail Price, (3) Not being viewed as policy/regulatory friendly by Luxury retailers, (4) High Import duties, (5) FDI policy of 30% sourcing tough for International luxury players (6) policies regarding Intellectual property rights, (7) Measures taken for the presence of counterfeit luxury goods and (8) Emergence of channels - Online and Grey. These would be the explicit premises explained below on which the authors aim to concentrate through this research:-

### **1) Would the infrastructure of international standards encourage the luxury brands from setting outlets in the Indian market?**

The mounting infrastructure and operation costs act as a barrier in the growth of luxury outlets in India. The rental costs and other operation costs are considerably high and the luxury centers are limited to certain destinations particularly Metros. The shortage of well trained staff in Indian market becomes the biggest drawback for luxury retailers to handle their business activities. Although there is overall increase in the level of education in India, still would still require a longer time for the Luxury retailers to witness considerable impact towards staffing issues. Moreover, there is also a limitation of people postponing their purchase to buy luxury goods during their travel to international destinations. Another phenomenon which is evident recently is the emergence of large format stores of multi-brand outlets dealing in luxury brands. Similarly another change which is evident is the increasing pressure of rental expenses has led the luxury outlets to move out of the hotels as well as shopping centers to the busy shopping streets of the bigger cities in India. The depreciation of rupee is also one of the major factors affecting the growth of luxury infrastructure in India.

There is also further increase in the competition for the limited space available in the luxury shopping centers with the entry of single brand (100%) and multi brand (51%) luxury retailers in the Indian market. The luxury destinations also have an impact in terms of more and more luxury players choosing internet retailing because of the rising costs of setting up the luxury outlets. A new phenomena presently witnessed in the Indian market has been the clustering of brands leading to the formation of multi-brand outlets like Luxxe Box promoted by Genesis Luxury Fashion Pvt Ltd or other multi brand outlets like The Collective. As per the research carried by Euromonitor International in India; Delhi, Goa and Mizoram have higher capacity for luxury spending when compared with other states in India. Euromonitor International predicts that India will achieve a quite high paced growth in luxury goods sales among the emerging markets between the period from 2014 and 2018. It is expected to grow by 63 percent ahead of China's 59 percent during the above mentioned period. The rise in the disposable incomes of Indian population and the increase in the high net worth individuals would provide as a promising opportunity for Luxury Retailers as per the Euromonitor International report.<sup>4</sup>

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<sup>4</sup> [www.euromonitorinternational.com](http://www.euromonitorinternational.com)

## **2) Would the revisiting of few policies related to luxury market be conducive enough for thriving of Luxury retailers?**

The FDI policies allow luxury players to expand through 100% in single brand retailing and 51% in multi-brand retailing. Luxury Brand retailers are attempting to offer higher range of products within the outlets although multi-brand retailers would have limited amount of space within the outlets because of 51% restriction in the Indian market. It is good to evaluate as to why back-end aggregator like Wal-Mart wanted to partner an Indian company. It was flexibility in terms of scaling up in India which counted the most to a bigger player like Walmart. The key determinant in organized retail lies in creating efficiency gains via scale and better logistics, and passing on some of the gains to the end-consumer in the form of cheaper products while retaining the rest along with the large volumes of thin margins in retail sales. How much of value is retained in the cash-and-carry back-end of the business and how much realized from retail is a function of competition.

India's investment rules which is 100% FDI in cash-and-carry but only 51% in retail acts as a barrier for players like Walmart as a result of which Walmart has not been able to find a strategic partner in India. This above subject of revisiting the policies for luxury market has been dealt in under Question 5 in a comprehensive manner.

## **3) Would reforms in the taxation environment put us on the road ahead in the luxury sector?**

In terms of the taxation environment compared to other countries, India has the highest tariff barrier after Brazil. Here we could evaluate the impact of taxes on various luxury goods in India. There is a heavy 38 percent custom duty levied on leather goods in India compared to China where it is 17 percent and Japan where it is 11 percent.<sup>5</sup> Again if we compare the luxury car segment, most of the luxury car makers are blaming the high taxes in India the reason for their slow market growth although there is willingness among the Indian luxury buyer segment. For instance the Italian super-luxury sports car maker Automobili Lamborghini SpA is

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<sup>5</sup> <http://www.livemint.com/Industry/fs4D5KWoifwnyrsq86XeGL/High-custom-duty-barrier-to-luxury-brands-in-India.html> accessed on 15th March, 2015.

drastically affected by high taxes, approximately up to 170 per cent which is restricting growth in this segment.<sup>6</sup>

Again if we take the sales of luxury watches in India the sales are affected due to the custom duty as high as 49% in this segment. Raymond Weil, President Olivier Bernheim while comparing Indian with other luxury destinations said "The Indian luxury goods market is not growing the way it should due to high customs duty. This makes it complicated to trade in luxury goods like watches. No other market poses such a situation".<sup>7</sup> While comparing, the modern commercial principles followed by countries like China is the luxury goods market has led to its becoming a successful luxury destination in the world.

#### **4) Would high import duties encourage affluent class to go to abroad destination to shop?**

There are 196 nations in the world from which Indian need visa for 50 countries. Hong Kong, Egypt, Fiji, Sri Lanka and Thailand are some of the prominent countries out of those 50 nations where Indian are able to travel visa free for shopping<sup>8</sup>. Due to high import duties on luxury goods in India, it is believed that affluent class travels abroad for their tourist as well as luxury shopping interests. Presently there are more and more companies emerging which help people shop luxury products at tax free rates. (Global Blue operates one of the world's biggest and most trusted Tax Free Shopping networks, providing its customers with savings of up to 19% on everything they purchase abroad at any of Global Blue's 270,000 shopping partners and also helps travelers to find the brands they are most interested in, whether those are globally famous fashion brands or niche designers that are unique to a certain city.<sup>9</sup>)

Holiday destinations also happen to be shopping destinations and it is preferably one of the reasons why Indians choose to go to international destinations. The activities like river rafting, scuba diving, para sailing as well as skiing would be factors propelling to travel abroad but accompanying that, luxury shopping seems to be catching up with Indians. The hotel room rates are another determinant while choosing destinations. The rising hotel costs in India is

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<sup>6</sup> <http://www.newindianexpress.com/business/news/2014/11/26/High-Taxes-Stall-Growth-of-Super-Luxury-Car-Sales-in-India/article2540700.ece> accessed on 15th March, 2015.

<sup>7</sup> [http://www.business-standard.com/article/news-ians/high-customs-duty-hindering-growth-of-indian-luxury-market-raymond-weil-president-ians-interview-114092800414\\_1.html](http://www.business-standard.com/article/news-ians/high-customs-duty-hindering-growth-of-indian-luxury-market-raymond-weil-president-ians-interview-114092800414_1.html) accessed on 15th March, 2015.

<sup>8</sup> <http://travel.siliconindia.com/travel-article/Top-Visa-Free-Hot-Spot-Destinations-for-Indians-aid-688.html> accessed on 15th March, 2015.

<sup>9</sup> <http://www.globalblue.com/> accessed on 15th March, 2015.



another factor which allows travelers to compare the high costs and choose international destinations over domestic travel.<sup>10</sup> The total number of Indians travelling overseas was 12 million in the year 2012. The hot destinations essentially are in South-East Asia, Europe and United States while half of the outbound Indian tourists are going to Thailand, Malaysia, Colombo, Dubai and Singapore. The newer destinations chosen from these for Indians largely are Hong Kong, Macao, Manila, Istanbul and Greece.<sup>11</sup>

##### **5) Would the recent modification in the FDI rules pertaining to single brand and multi-brand retailers facilitate the stakeholders in the luxury market?**

Out of the 189 countries analyzed for starting a business, “The World Bank’s Doing Business 2014” indicates that India is among the most difficult countries to operate and ranked it as 179. The foreign firms are mostly suggested to hire a professional services firm to support with setup and investment in the India.<sup>12</sup> The rental costs in India have been the major barrier for international luxury retailers because heavy rental costs could eat away 10-15% of retailer’s revenue when compared with the global average of 4-10%.

The multi-brand retailing changes made in 2012 allowed up to 51 percent FDI with prior government approval. Companies were required to invest at least 30 percent of the total FDI proceeds into ‘back-end infrastructure’. This has to be incorporated within three years and the minimum FDI investment has to be up to US\$100 million. These activities included mix of investments ranging from distribution, logistics, design improvements, quality control, warehouses, manufacturing, processing, packaging and storage. This was the major change that happened in FDI after which there have been a series of changes in the legal framework which just escalates the confusion of multi brand retail business. It has been very evident that changes in FDI have an impact on how India can address its legal and economic barriers.

The decision making when it comes to Central and State Governments has been a major hurdle in the path of progress for Luxury brand retailers. Although the Central Governments have

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<sup>10</sup> <http://www.nriol.com/blogs/indian-tourists-in-foreign-nations.asp> accessed on 15th March, 2015.

<sup>11</sup> <http://www.dailymail.co.uk/indiahome/indianews/article-2318536/Get-ready-summer-stampede-Indians-flock-book-overseas-flights-holidays-abroad-work-CHEAPER-staycations.html> accessed on 15th March, 2015.

<sup>12</sup> Shawn Greene (21<sup>st</sup> Nov. 2013), “2013 Changes in Indian FDI Policy”, <http://www.india-briefing.com/news/2013-changes-indian-fdi-policy-7149.html/> accessed on 15th March, 2015.

allowed the FDI in multi brand retail, the State Governments have been reluctant to carry forward the decisions. The international retailers also have a limitation of conducting their business in cities with a population of more than one million and a mandatory requirement of a minority Indian partner.

**6) Would internet retailing prove as a key distribution channel in the luxury retailing sector? What would be the impact of the emergence of channels - “Online and Grey” for the luxury goods market in India?**

In India we have started witnessing many designers willing to drop their exclusive tag and join the multi brand retail outlets to attain increase in demand and visibility. This is not a common phenomenon which is evident in the luxury goods market. Jabong.com and Myntra.com have even started partnering with international luxury giants Jimmy Choo (Dorothy Perkins and Miss Selfridges – only through online route) to stimulate the overall shopping experience of the customers. The other high-end brands available in the premium section of Jabong.com include French Connection, ALDO, HiDesign, Mango, Tommy Hilfiger, GAS, GANT, Nautica, River Island and Steve Madden. The rise in online retailing in India has led to lot of international brands to adopt the online platform for brand visibility. Myntra has launched around 10 exclusive brands over the past few years like Supra, Stanley Kane and many more. The phenomenal rise in freight costs and custom duties make it improbable for retailers to launch brick and mortar stores in the country. It is yet to be seen in India, whether online presence would be an advantage for retailers to have partnerships with different brands<sup>13</sup>. Although, online platform emerges to be profitable since retailers could increase their revenue by having higher margins in luxury products and lower distribution costs. Coming to the fakes and counterfeit products in India, there have been many grey market imports which are sold through online retailers in India. There are several Brands such as Nikon, Puma and Canon which have taken legal actions those selling fake goods and cheating genuine customers. While the luxury fashion brands retailers are concerned about fakes, consumer electronics retailers are concerned about parallel imports. The online sales of these fake products affect the brand’s equity and credibility of online retail industry.<sup>14</sup>

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<sup>13</sup> Payel Majumdar (12<sup>th</sup> Oct, 2014), “The democratisation of couture: Buying luxury brands online”, retrieved from: <http://www.sunday-guardian.com/young-restless/the-democratisation-of-couture-buying-luxury-brands-online> accessed on 15th March, 2015.

<sup>14</sup> <http://www.onlineworld-glan.com/shopping-blogs-43/> accessed on 15th March, 2015.

## 7) Would the business environment masked by pervasive corruption and red-tapism affect the luxury investment?

The lobbying and bribery under political corruption is well known to Indian politics.<sup>15</sup> The retailers entering India have found a lot of difficulty in operating smoothly in the complex Indian business environment. The 30% sourcing law has been very difficult to comply with because of which we see restricted growth in business. There is difficulty for any retailer to operate in Indian business environment without transferring unaccounted amounts for acquiring real estate.<sup>16</sup> The procedural delays have been highlighted by many of the international luxury retailers who have entered India. The reports presented by Walmart to US Government had revealed that it had incurred more than Rs. 100 crore in the process of lobbying Indian lawmakers to acquire accessibility to the Indian market. The current framework under which luxury retailers could operate in India is debatable because we do not see any immediate solutions.

Henceforth, this paper has firstly pinpointed the overall luxury market in India; secondly it has highlighted the challenges faced by the luxury players in today's legal as well as economic environment and finally has emphasized the zone of attention. The Luxury retailers would have to carefully implement multiple business strategies which are tailor made for segments or target group to tap the huge potential of the Indian luxury market. The authors through this paper do not aim at offering definite solutions to any of above questions but would improve understanding by delivering an encompassing outlook over the opportunities and issues highlighted for the Indian luxury market.

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<sup>15</sup> <http://www.chakreview.com/Lifestyle/FDI-in-Retail-sector-in-India> accessed on 15th March, 2015.

<sup>16</sup> ET Bureau (Oct 10, 2013), "India too corrupt for foreign investment", [http://articles.economictimes.indiatimes.com/2013-10-10/news/42903000\\_1\\_bharti-and-wal-mart-cash-and-carry-back-end-30-local-sourcing-norm](http://articles.economictimes.indiatimes.com/2013-10-10/news/42903000_1_bharti-and-wal-mart-cash-and-carry-back-end-30-local-sourcing-norm) accessed on 15th March, 2015.

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