Indian cities COMING OF AGE

Manufacturers and marketing firms are increasingly eyeing the growing demand for a host of products and services in Tier II and Tier III cities across India, writes **Dipta Joshi.**

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INDIA'S second and third rung cities are coming of age. Given their historical importance, many of these cities — Kanpur, Mysore and Surat, for instance — boast of an illustrious past. It is now time for them to regain their past glory, as a host of industries and brands reach out to them. Gearing to compete with the metros, Tier II and Tier III cities are the new growth centres of resurgent India.

Indeed, nearly 35 Indian cities with a million-plus population are proving to be as lucrative a market as the Tier I cities or metros. A recent report released by the economic research group at McKinsey Global Institute (MGI) titled 'The Bird of Gold: The Rise of India's Consumer Market' notes: "While India's two largest conurbations (an extended urban area, where several towns merge with the suburbs of a central city), Delhi and Mumbai, will continue to be the country's biggest markets and the top eight cities will remain the dominant locations for upper-income global consumers, we estimate that almost two-thirds of India's middle-class opportunities will lie outside those top-Tier urban areas."

Not surprising as half of India's 10.7 million households with an annual income of up to $23,000 in the year 2006 were living in smaller cities such as Vadodara, Nagpur, Ahmedabad and Vijayawada, according to the National Council for Applied Economic Research (NCAER).

The current small-town boom is also a reflection of India's free-market prosperity. Powered by healthy economic growth of 9.6 per cent for fiscal 2006-07, disposable incomes across India have been rising. This has fuelled the purchasing power of the 50-million strong middle class. The spending binge has already taken India's total consumption to $380 billion, and is expected to touch $1.5 trillion in 2025.

This is good news for the organised Indian retail market, which is expected to touch $30 billion by 2010 from the current $14 billion. Retailers are also not overlooking the fact that the past few years have seen India's retail growth graph led largely by consumers in Tier II and Tier III cities instead of the metros. Organised retailing in smaller towns and cities is estimated to grow at a staggering 50-60 per cent a year compared to 35-40

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READYING FOR THE RACE: Each player wants to have the first-mover advantage and establish strong brand loyalties

per cent in the large cities. The second and third rung cities are fast emerging as India's new growth centres. The arrival of consumer brands is helping fulfill the aspirations of a burgeoning affluent class in smaller towns and cities, and has also opened new markets for entrepreneurs. Jagdeep Kapoor, managing director, Samsika Marketing Consultants, believes demand has existed since long. It is retailers, who seem to be re-discovering these markets only now. "With the spread of television, consumers in these cities became aware of these brands. Now that these brands are in their markets, they are being lapped up," he says.

Most of these cities have been growth centres for some time now. Ludhiana, Punjab's largest city, is also an industrial hub with knitwear, bicycle and auto parts manufacturing factories. Nashik is deemed the third most industrialised city of Maharashtra after Mumbai and Pune. Tirupur in Tamil Nadu accounts for 90 per cent of India's cotton knitwear exports, earning an annual $800 million plus in foreign exchange. In such a scenario, "Price of a product was never an issue here, they were always willing to pay, the issue was availability," explains Kapoor.

That is precisely what retailers are now trying to address in every segment be it food, apparel or even lifestyle. Large numbers of departmental stores, hypermarkets, supermarkets and even speciality stores are being set up in the smaller cities. The bigger players include Wills Lifestyle (ITC's retail division), the RPG Group, the Kishore Biyani-owned Future Group, the AV Birla Group's 'More' brand of retail stores and Mukesh Ambani's Reliance Retail. The race is on as each player wants to have the first-mover advantage and establish strong brand loyalties in these relatively new markets.

Brands are now even finding takers in the traditional jewellery market, fast replacing the family jeweller. Established players like D'damas and Asmi are looking forward to increasing their presence through franchises and even individual stores in some Tier II and Tier III cities.

"For any retail business `accessibility' and `availability' are important logistically," says Vivek Padgaonkar, a professor at Mumbai's Narsee Monjee Institute of Management Studies. "Retailers today understand this and are paying attention to these factors. As a result, we are seeing one-stop malls that offer both convenience and comfort to consumers in smaller cities too."

The malls have taken over the tradi-

MILLION-PLUS CITIES

CITY	POPULATION
Greater Mumbai	11,914,398
Delhi (Urban)	9,817,439
Kolkata	4,580,544
Bangalore	4,292,223
Chennai	4,216,268
Ahmedabad	3,515,361
Hyderabad	3,449,878
Pune	2,540,069
Kanpur	2,532,138
Surat	2,433,787
Jaipur	2,324,319
Nagpur	2,051,320
Indore	1,597,441
Bhopal	1,433,875
Ludhiana	1,395,053
Patna	1,376,950
Vadodara	1,306,035
Thane	1,261,517
Agra	1,259,979
Kalyan-Dombivli	1,193,266
Varanasi	1,100,748
Nashik	1,076,967
Meerut	1,074,229
Faridabad	1,054,981
Haora (Howrah)	1,008,704
Pimpri-Chinchwad	1,006,417

SOURCE: Census of India: 2001

DEFINING CITIES

State/Union Territory	A-1	A	B-1	B2
ANDHRA PRADESH	Hyderabad		Vijayawada Visakhapatnam	Warangal Guntur
ASSAM			Guwahati	
BIHAR			Patna	
CHANDIGARH				Chandigarh
CHHATTISGARH				Durg-Bhillai Nagar Raipur
DELHI	Delhi			
GUJARAT		Ahmedabad Surat	Rajkot Vadodara	Jamnagar Bhavnagar
HARYANA			Faridabad	
JAMMU & KASHMIR				Srinagar Jammu
JHARKHAND			Jamshedpur Dhanbad	Ranchi
KARNATAKA	Bangalore			Belgaum Hubli-Dharwad Mangalore Mysore
KERALA			Kochi	Kozhikode Thiruvananthapuram
MADHYA PRADESH			Jabalpur Bhopal Indore	
MAHARASHTRA	Greater Mumbai	Nagpur Pune	Nashik	Amravati Aurangabad Bhiwandi Solapur Kolhapur
ORISSA				Cuttack Bhubaneshwar
PUDUCHERRY (formerly Pondicherry)				Puducherry
PUNJAB			Amritsar Ludhiana	Jalandhar
RAJASTHAN		Jaipur		Bikaner Jodhpur Kota
TAMIL NADU	Chennai		Coimbatore Madurai	Salem Tirupur Tiruchirapalli
UTTARAKHAND				Dehradun
UTTAR PRADESH		Lucknow Kanpur	Meerut Agra Allahabad Varanasi	Moradabad Ghaziabad Aligarh Bareilly Gorakhpur
WEST BENGAL	Kolkata		Asansol	

SOURCE: Ministry of Finance

> Our own surveys have shown that acceptability of newer products is faster in smaller cities where people have more time to visit shopping malls.

tional grocery store culture in these cities, thus powering the retail expansion. Ludhiana already has 14 malls and plans are afoot for more. Within the next four years, Pune, considered a satellite city of Mumbai, will have 42 malls, more than Mumbai (as per current plans). During the same period, close to 660 malls are likely to come up at various places across the country. Of these, almost 450 malls will be in cities like Kanpur, Ahmedabad, Indore, Agra, Vadodara, Jalandhar, Amritsar and Surat. According to Arif Sheikh, director, Plaza Center NV, a Europe-based development company that plans to invest over $1.25 billion over the next three years for building malls, the availability of space, lower marketing costs and surety of footfalls adds to the attraction of these cities. "Our own surveys have shown that acceptability of newer products is faster in smaller cities where people have more time to visit malls. Besides, I could put up 30 billboards about my brand in a place like Visakhapatnam for the same money that just one at Colaba (in Mumbai) would cost," says Sheikh. Of the 52 malls Plaza Center NV is currently developing, 42 are in Tier II cities across India.

Indeed, smaller cities and towns are offering a better cost advantage over bigger cities. According to real estate consulting firm Jones Lang LaSalle, Tier II and Tier III cities often offer higher returns on rentals. Thus, the returns in Tier II cities like Hyderabad, Chennai and Pune are in the range

FROM VILLAGES TO MEGALOPOLISES

IN simpler times, you lived in a city, a town or a village. But with millions of people migrating from rural areas to urban centres, the classification of cities has undergone a dramatic change. Urban centres are now called metros, mini-metros, major cities, Tier I, II and III cities, towns, and also megalopolises (or megapolises).

The Registrar General and Census Commissioner of India uses the term urban agglomeration to describe cities, which could range from metropolitan areas (cities with a population of over one million – there are 26 such cities), to cities (population of over 100,000 – about 300 such cities exist), to towns (less than 100,000, numbering over 3,500). A megalopolis is used to describe a metropolitan area with a population exceeding 10 million; in India, Mumbai, Delhi and Kolkata are megapolises. A metropolis in India means a city with a population exceeding four million – which besides the three megalopolises, include Bangalore and Chennai.

The Indian government uses a different classification for cities for payment of House Rent Allowance (HRA) and City Compensatory Allowance (CCA) for its employees. The major classifications include A-1 (metros), A (large cities) and B-1, B-2 and C (smaller cities). For the purpose of CCA, currently there are six A-1 cities, seven A-class cities, 23 B-1 cities and 39 B-2 cities.

The services sector – especially information technology, ITES and real estate services – has a different classification for cities in India: Tier I, Tier II and Tier III. Tier I cities correspond roughly with metros, and are the most expensive in terms of rentals and capital values. They account for about 60 per cent of the total real estate space.

Tier II cities are the mini-metros and large cities (roughly the 23 B-1 cities), which have seen significant IT and real estate construction activity in recent years. Tier III cities are the emerging IT destinations, corresponding roughly to 39 B-2 cities.

Marketing firms and the media use another classification for cities, one that has been defined by the Media Research Users Council, which publishes the Indian Readership Survey (IRS) and other such studies. The Council uses a Socio-Economic Classification (SEC) and urban areas are segregated into A1, A2, B1, B2, C, D, E1, and E2 categories.

SEC A and B, accounting for a quarter of the urban population, refer to high-class consumers; SEC C – about a fifth of the urban population – refers to middle-class; and SEC D and E refer to low-class. About 80 per cent of high-class consumers live in seven cities – Mumbai, Delhi, Bangalore, Chennai, Kolkata, Ahmedabad and Hyderabad.

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of 10.5-11.5 per cent of the capital value of the commercial real estate asset. In cities like Kolkata and Ahmedabad returns could scale up to 12 per cent of the capital value, higher than the returns of 9.5 to 10 per cent of capital value on rental income in Tier I cities.

Tier II and Tier III cities are also attracting manufacturing and IT companies. IBM launched its outsourcing centre in Noida in the National Capital Region, and also made a foray into Coimbatore in Tamil Nadu, with its global small and medium business unit. Honeywell and General Electric have set up operations in Madurai and Jaipur.

Besides, even business process outsourcing (BPO) companies are looking towards smaller towns. MphaSis, Satyam, Wipro, Tata Consultancy Services and Infosys opted to set up their BPO facilities in relatively smaller places like Mangalore, Thiruvananthapuram, Chandigarh and Visakhapatnam. Apart from cheaper rents, the second rung cities offer an employable stream of educated workforce (thanks to the presence of good colleges), which is easier to retain due to proximity with their families.

Also, many Indian states are offering incentives to investors wanting to relocate to Tier II and Tier III cities. Funds are also being allocated to launch a number of urban development projects aimed at improving the local infrastructure in these places. The move to decongest large cities and attract the software and BPO industries to secondary centres has received support from both the central and state governments. Software Technology Parks of India (STPI), the agency that offers dedicated infrastructure and facilities, is setting up parks in Tier II cities.

Both international and domestic real estate developers are also planning major commercial, retail and residential projects in Tier II and Tier III cities across the country.

The benefits of India's buoyant economic growth are not restricted to the major metros, and a more inclusive growth is likely to be more sustainable in the long run. This translates into greater opportunities for companies as they enter new, untapped markets. For the smaller cities it is time to regain their place in the sun.