

A CONCEPTUAL PAPER ON INDIAN ECOMMERCE ECOSYSTEM FOR ACCELERATED BUSINESS GROWTH

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Abstract

As a result of globalization, Indian eCommerce sector has experienced unprecedented growth during 2014 - 2016. The growth driver was quick technology adoption complemented by the rising use of electronic devices like tablets and smart phones, and easy access to the internet through broadband, 3G, etc. This enhanced online consumer base. In addition to these, favourable demographics and a growing number of internet users played a catalytic role in boosting this growth. The growth registered by domestic players like Flipkart and Snapdeal in addition to the intense investor interest in these firms indicated the immense potential of the market.

With the entry of eCommerce giants like Amazon, the competition has further intensified. International players like Amazon and Alibaba entered with big budgets and the sufficient patience to drive the Indian eCommerce market. Their domain expertise and customer centric practices based on their international experience provide them a cutting edge. These firms have been a part of markets and have witnessed how eCommerce markets evolve. These firms are familiar with the challenges and strategies to address them. Indian firms has realised this and are focussing on

- *enlarging vendors base and*
- *selection on their platforms,*
- *innovating on multiple customer touch points, and*
- *providing seamless and rapid delivery services in order to compete with the international entities.*

Competition is expected to continue, and therefore these eCommerce firms are experimenting different approach to attract customers and increase online traffic.

The Government of India's ambitious Digital India project and the modernisation of India will also influence the eCommerce sector. The Digital India project aims to provide a one-stop shop for government services that will have the mobile phone as the backbone of its delivery mechanism. The programme will give a strong boost to the eCommerce market.

This paper has attempted to discuss the present state of the eCommerce landscape in India and industry concerns. Additionally, it looks at the industry's key drivers and challenges, and suggests efforts which will help eCommerce companies accelerate and sustain growth.

Key Words : *Globalization, eCommerce, drivers for growth consumer base, Digital India, eTail.*

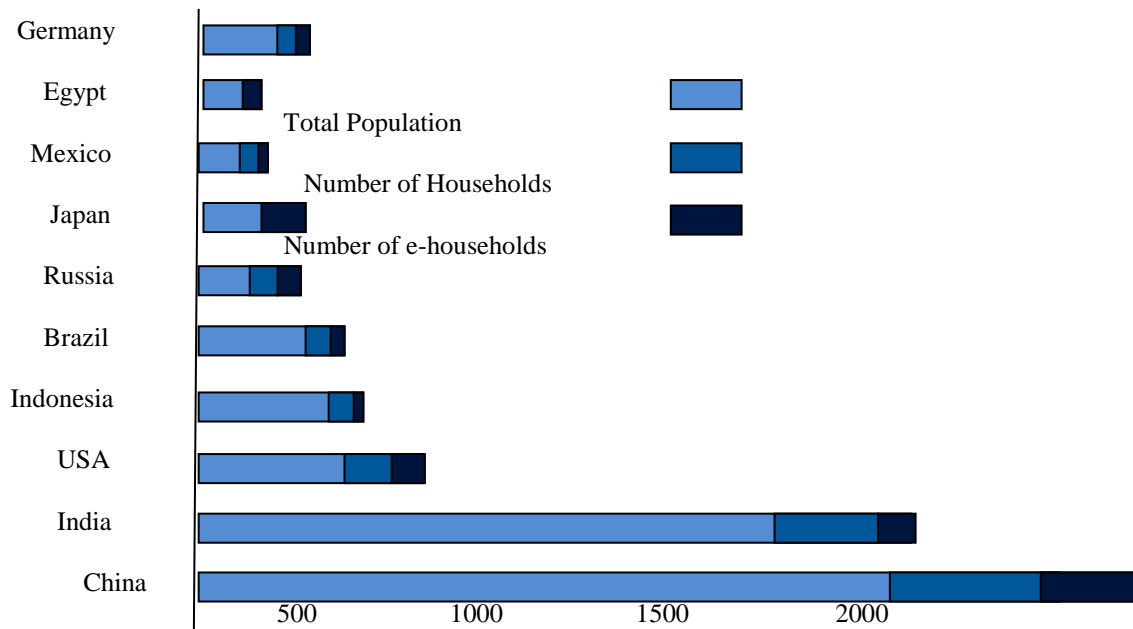
Industry on an upturn

In 2013, Asia-Pacific has emerged as the strongest business-to consumer (B2C) eCommerce region in the world with sales of around 567.3 billion USD, a growth of 45% over 2012. Globally, B2C eCommerce sales increased by 24% over 2012. This reflects the huge untapped potential of eCommerce by retail companies, both in their country of origin and across borders. eCommerce deals with the procuring and selling of goods and services, over an electronic platform, mainly the internet. These business transactions are categorised into either business-to-business (B2B), business-to-consumer (B2C), consumer-to-consumer (C2C), consumer-to-business (C2B) or the recently evolved business-to-business-to-consumer (B2B2C). eCommerce processes are conducted using applications, such as email, online catalogues and shopping carts, electronic data interchange (EDI), file transfer protocol and web services and e-newsletters to subscribers.

As indicated in Ecommerce Europe,

- *country-wise, the US, UK and China together account for 57% of the world's total B2C eCommerce sales in 2013.*
- *In comparison, India had sales of only 10.7 billion USD, 3.3% of that of China in 2013 with fifth position in Asia Pacific. This is despite the fact that India enjoys high demographic dividends just like China.*
- *India's internet penetration with total e-households at 46 million against China's 207 million is one of the reasons behind India's poor B2C sales growth.*

Top ten countries in terms of population and corresponding e - households



(Source : Ecommerce Foundation 2014)

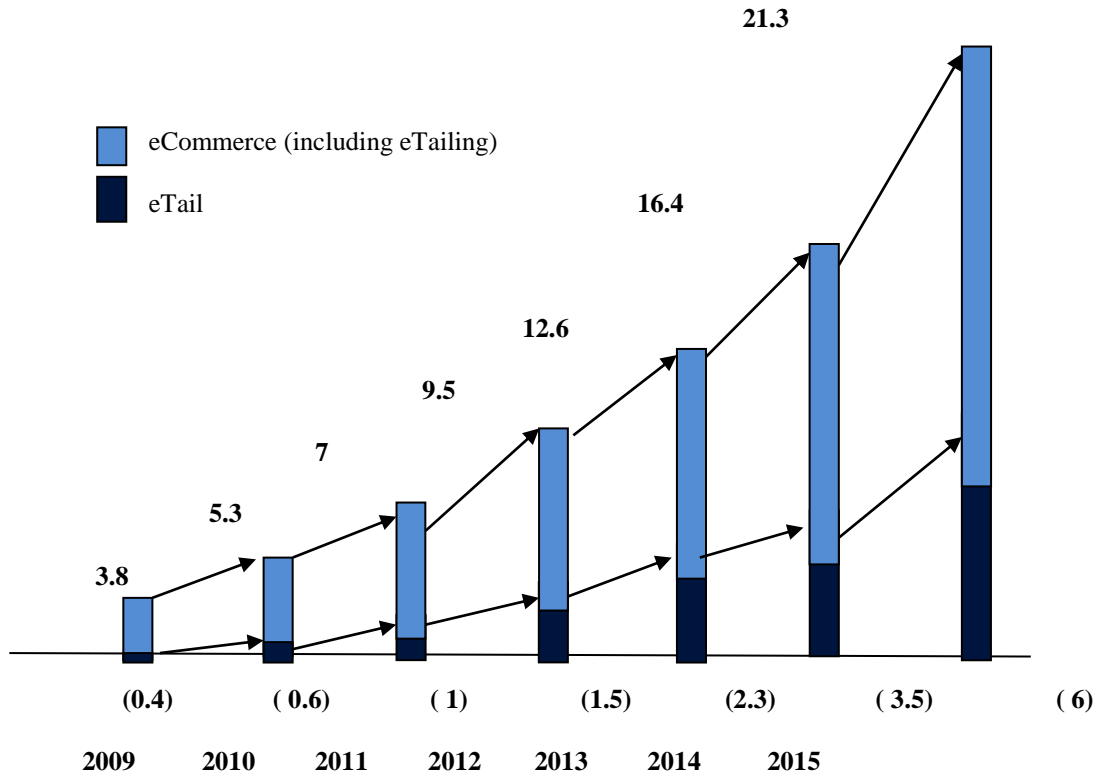
According to Forrester Research, an independent technology and market research firm, only 16% of India’s total population was online in 2013 and of the online users only 14% or 28 million were online buyers. India, therefore, was still in a nascent or immature stage of evolution of online retail spending. China was in ascending stage at 50%, whereas Japan (69%), Australia (57%) and South Korea (70%) were in mature stage.

India’s growth potential

Since the eCommerce industry is fast rising, changes can be seen over a year. The sector in India has grown by 34% (CAGR) since 2009 to touch 16.4 billion USD in 2014. The sector is expected to be in the range of 31 billion USD in 2017.

eCommerce ecosystem

- **Online travel, ticketing, etc.**
 Ticketing for air, rail, bus, movies, events
- **Online retail**
 Retail products sold through online route
- **Online marketplace**
 Platform where sellers and buyers transact online
- **Online deals**
 Deals purchased online, redemption may or may not happen online
- **Online portals classified**
 Includes car, job, property and matrimonial portals.



(Source : IMAI, CRISIL, Gartner, PwC Analysis and Industry Expert)

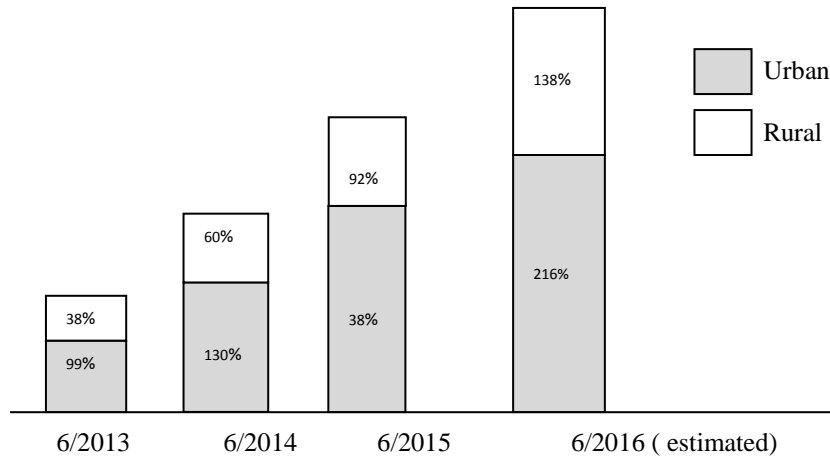
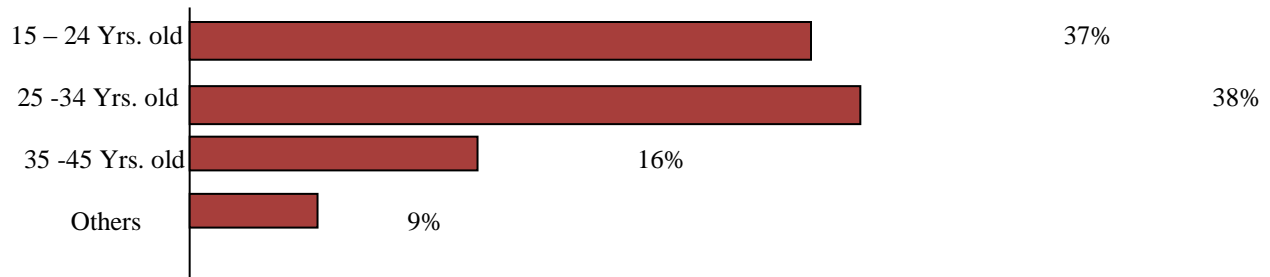
At present eTravel comprises 70% of the total eCommerce market. eTailing, which comprises of online retail and online marketplaces, has become the fastest-growing segment in the larger market having grown at a CAGR of around 56% during 2009-2014. The market size of the eTail market was around 6 billion USD in 2015. Books, electronics apparel and accessories are the highest selling goods through eTailing, and constituted around 80% of product distribution. The ever increasing use of smart phones, tablets and internet broadband and 3G and now 4G has led to developing a strong consumer base and is likely to expand further. Thus combined with a larger number of home grown eTail firms with their innovative business models, a robust eTail market in India is roaring to expand at further greater speed. Some of the factors that fuelled growth a significantly low (19%) but fast-growing internet population of 243 million in 2014 is an indicator of the sector's huge growth potential in India.

Internet users by country: In million during 2014

In absolute terms, India's internet users was short by just 36 million as compared with 279 million in the US and higher than that in Japan, Brazil and Russia. However, in relation with its population, only 19% Indians use the internet. This indicates the potential of internet use in India and as internet penetration increases, the potential of growth for the eCommerce industry will also increase.

An analysis of the demographic profile of internet users clearly indicates that eCommerce is rising very rapidly in India and will continue in coming years. Around 70 - 76% of Indian internet users are in the age group of 15 to 34 years. This age group people shops more than the rest population. Peer pressure, rising aspirations with career growth, fashion and trends encourage this segment to shop more than any other category and India, therefore, clearly enjoys a demographic dividend that favours the growth of eCommerce. In coming years, as internet presence increases in rural areas, rural India will yield more eCommerce business.

Demographic Profile of India Online Users (As On September 2013)



(Source : IAMAI – IMBR)

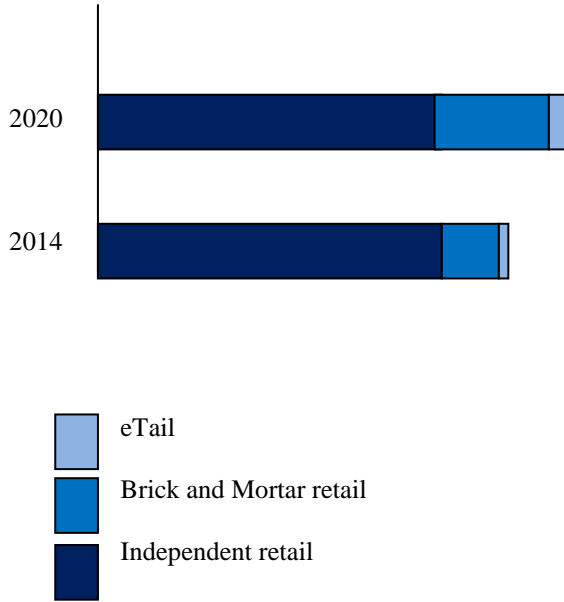
Geographical distribution of internet users in India (million)

It is expected that By 2020, eTail in India will account for 3% of total retail. Further, orders per million are expected to grow more during 2015-16 which will mean more opportunities for both consumers and eTail companies. While the share of online shopping in total retail has increased at a fast pace in the last few years, it is still miniscule compared to the figure in China, where the share is 8-10%.

Share of eTail in Indian retail

	2014	2020
Independent Retail	91.6%	83%
Brick & Mortar Retail	8%	14%
eTail	0.4%	3%

(Source : Technopak, Accel Partners)



Orders per month (in Million)

Year	no. of orders
2012	4
2013	5
2016	12

(Source : Technopack, Accel Partners)

Online business models

To get the maximum benefit from eCommerce business, a large number of companies are adopting different innovative ideas and operating models including partnering with online marketplaces or setting up their own online stores. Some key operating models include the following:

- **Marketplace and pick-up & drop** is a model where sellers often partner with leading marketplaces to set up a dedicated online store on the latter's website. Here sellers play a key role of managing inventory and driving sales. They leverage on high traffic on the marketplaces' website and access their distribution network. However, the sellers have limited say on pricing and customer experience.
- **Self-owned inventory** is a model where the eCommerce player owns the inventory. The model provides better post-purchase customer experience and fulfilment. It provides smoother operations due to ready information on the inventory, location, supply chain and shipments, effectively leading to better control over inventory. On the flipside, however, there are risks of potential mark downs and working capital getting tied up in inventory.
- **Private label** reflects a business where an eCommerce company sets up its own brand goods, which it sells through its own website. This model offers a wide-ranging products and pricing to its customers and competes with branded labels. Here, margins are typically higher than third-party branded goods.
- **White label** involves the setting up of a branded online store managed by the eCommerce player or a third party. The brand takes the responsibility of generating website traffic and providing services by partnering with payment gateways. It helps build trust, customer affinity and loyalty and provides better control of brand and product experience.

Political ecosystem point of view, with the new government, business confidence towards investments in the eCommerce sector has significantly increased. During the year 2014, investors aggressively funded the eCommerce sector because of strong growth prospects. In addition to the traditional online formats of retail and lifestyle, new online business segments like healthcare, grocery and real estate, were also tapped.

Top 20 PE deals in the eCommerce sector in 2014

Month & Year	firms	Amount in million USD	Key investors
Jul-14	Flipkart	1,000	Morgan Stanley, GIC, Tiger Global, Accel India, Iconiq Capital, DST Global
Dec 14	Flipkart	700	Tiger Global, Iconiq Capital, DST Global, Steadview, Qatar Investment Authority
Oct-14	Snapdeal.com	637	Temasek, PremjiInvest, SoftBank Corp
May-14	Flipkart	210	Tiger Global, Iconiq Capital, DST Global
Oct-14	Olacabs	210	Tiger Global, Matrix Partners India, SoftBank Corp, Steadview
Feb-14	Snapdeal.com	134	Kalaari Capital, Intel Capital, Nexus Ventures, Bessemer, Saama Capital
May-14	Snapdeal.com	100	Temasek, PremjiInvest
Nov-14	Housing.com	90	Helion Ventures, Nexus Ventures, Qualcomm Ventures, SoftBank Corp, DST Global, Falcon Edge Capital
Mar-14	Quikr	90	Warburg Pincus, Norwest, Matrix Partners India, Nokia Growth Partners, Omidyar Network, Kinnevik
Sep-14	Quikr	60	Warburg Pincus, Norwest, Tiger Global, Matrix Partners India, Nokia Growth Partners, Omidyar Network, Kinnevik
Nov-14	Zomato Media	60	Sequoia Capital India, Vy Capital
Feb-14	Myntra	50	Kalaari Capital, Tiger Global, IDG Ventures India, Accel India, PremjiInvest
Aug-14	Snapdeal.com	50	Ratan Tata
Jul-14	Olacabs	41.6	Sequoia Capital India, Tiger Global, Matrix Partners India, Steadview
Nov-14	Proptiger Realty	37	SAIF, Accel India, Horizen Ventures
Sep-14	Freecharge.in	33	Sequoia Capital India, Ru-Net Holdings
Sep-14	BigBasket	32.7	Helion Ventures, Ascent Capital, Zodius Capital, Lionrock Capital
Jun-14	Amazon.com India	30	Catamaran Ventures
Oct-14	CarTrade.com	30	Warburg Pincus, Tiger Global, Canaan Partners
Sep-14	CommonFloor	30	Tiger Global

Key developments in 2014

During 2014, India witnessed many developments that gave a fillip to the eCommerce industry. eCommerce has increasingly attracting buyers from Tier 2 and 3 cities, because of limited access to brands that could not satisfy high aspirations. According to eCommerce companies, these cities have seen a 30% to 50% rise in transactions.

Since last one or two years, there has been a trend of exclusive tie-ups between eTailers and established boutiques, designers, and high-end lifestyle and fashion brands. For example, during 2014, Jabong included international fashion brands like River Island, Miss Selfridge, Dorothy Perkins, Blue saint along with domestic fashion brands through Jabong Boutiques. Also, Myntra benefited from exclusive tie-ups with brands such as Harvard Lifestyle, Desigual and WROGN from Virat Kohli.

Enhanced shopping experience

Besides general online shopping, customers are also shopping online for weddings and festivals, thanks to wider range of products being offered and aggressive advertisements. The free and quick shipment and wider choice of products, along with the ease of shopping online as compared to in-store shopping, is also helping eCommerce gather momentum. Further, eCommerce companies are doing rapid business due to sales. New concepts such sales on weekends, holidays and festivals are attracting a lot of new customers and building customer loyalty among existing customers. Television and social media, particularly Facebook, are playing a proactive role in promoting eTailing through aggressive advertisements. This has helped several eCommerce companies build substantial brand image.

Mobile will continue to be the most influential aspect of eCommerce in coming years

With mobile apps being developed by most eCommerce websites, smartphones are increasingly replacing PCs for online shopping. In 2013, only 10% of the mobile users used smartphones, and only 5% of the eCommerce transactions were made through a mobile device. All eCommerce transactions today happen via mobile has reached 18% level.

According to some industry players, over 50% of the orders are being placed through mobile apps, this is leading not only to substantial customer acquisition but also building customer loyalty for various brands. Note that the most mobile transactions so far are for entertainment (booking movie tickets and music downloads). This trend will change soon with more and more merchandise being ordered online.

Key market factors to be evaluated before entering a new eCommerce business

To achieve their vision, eCommerce companies will need to understand the intricate landscape of new markets in addition to their own internal capabilities and limitations. The following factors must be considered:

<ul style="list-style-type: none"> Market size: Before moving too aggressively into a new market, it is important to consider how sizable the 	<p>eCommerce readiness: It is essential to fully understanding the payment and logistical infrastructure, consumer behaviour, retail opportunity and technological developments.</p>	<p>Scope of growth: It is also important to look at the internet penetration, demographics of the online buying population and understand which phase of development each market is in.</p>
<p>Barriers to entry: Players should understand the regulatory environment and connect with solution providers, content distribution networks, and digital agencies.</p>		<p>Competition: There is also a need to do an in-depth assessment of what competitors are doing, their online strategy and the nature of each offering.</p>

Product basket Expansion

It is a current trend of relatively newer products such as grocery, hygiene, and healthcare products being bought online. Similarly, Indian jewellery and lingerie are in great demand among customers outside India. Export comprises 95% of cross-border eCommerce, with the US, UK, Australia, Canada and Germany being the major markets.

Exclusive partnerships with leading brands

Over the year or so, there has been a trend of exclusive tie-ups between eTailers and established boutiques, designers, and high-end lifestyle and fashion brands. For instance, in 2014, Jabong added international fashion brands such as Dorothy Perkins, River Island, Blue saint and Miss Selfridge, along with local fashion brands through Jabong Boutiques. Similarly, Myntra benefited from exclusive tie-ups with brands such as Harvard Lifestyle, Desigual and WROGN from Virat Kohli.

Expanding the product basket

There is a recent trend of relatively newer products such as grocery, hygiene, and healthcare products being purchased online. Similarly, lingerie and Indian jewellery has also been in great demand among customers outside India. Export comprises 95% of cross-border eCommerce, with the US, UK, Australia, Canada and Germany being the major markets.

Industry opines

Few of the eCommerce firms and industry observers have raised concerns about the free shipping, deep discounts, intense competition and higher rejection rates due to cash on delivery (CoD) have impacted online eTailing adversely. Some of these concerns are specific to India and are more difficult to overcome.

Findings and Discussion

Some of the key concerns are listed below:

- **High cost of customer acquisition :** Due to intense competition by the relatively better off companies with more funds the cost of customer acquisition is increasing.
- **Generation & sustenance of traffic:** Competition from established eCommerce players is making it difficult for private label brands to generate traffic on their white-label websites.

- **Low profitability:** High cost of customer acquisition, free shipping and high rejection rate of CoD orders is resulting in negative profitability.
- **Last-mile delivery:** Indian eTailers faces another problem of poor last-mile connectivity, in remote areas with larger population.
- **High payment cost:** CoD services impose substantial financial cost. In India, CoD continues to be a preferred route of payment.
- **Skilled manpower:** A serious issue faced by all major players is lack of availability of talent manpower. Also high attrition are causing manpower crunch.
- **Regulatory barriers:** Specifically in India, regulatory barriers in the eCommerce market are higher as compared to more mature markets.

E Commerce Drivers and Challenges

While the growth in this sector excites entrepreneurs and financial investors alike, some serious challenges are beginning to weigh down on the sector. eCommerce players in India need to address eight key aspects of their business, both internal and external.

External challenges

External forces impact how eCommerce firms plan their growth strategy and offer seamless customer experience both onsite as well as post transaction.

- **Product and market strategy:** eCommerce firms have to address problems related to rapidly evolving customer segments and product portfolios; information access on market intelligence on growth, size and share; manage multiple customer engagement platforms; focus on expansion into new geographies, brands and products; and simultaneously tackle a hypercompetitive pricing environment.
- **Customer and digital experience:** firms have to ensure a rich, fresh and simple customer experience, not geared towards discovery; manage inconsistent brand experience across platforms; manage proliferation of technologies; and handle time-to-market pressure for new applications. Presently, social media has become more influential than paid marketing.
- **Payments and transactions:** eCommerce firms may encounter issues around security and privacy breach and controlling fictitious transactions. Further, RBI restrictions for prepaid instruments or eWallets act as impediments. From a transactions perspective, cross-border tax and regulatory issues, and backend service tax and withholding tax can have serious implications.
- **Fulfilment:** Firms need to check if the physical infrastructure gets affected by the internet speed. Also, the lack of an integrated end-to-end logistics platform and innovation-focused fulfilment option could cause delivery issues. Challenges around reverse logistics management and third party logistics interactions could also act as barriers to growth.
- **Internal challenges:** Internal forces impact how eCommerce companies can organise to drive and sustain growth.
- **Organisation scaling:** eCommerce firms have to make sure organisation design is in line with the rapidly evolving business strategy, along with fluid governance, strong leadership and management development. From a growth angle, identifying acquisition opportunities, fund raising and IPO readiness becomes necessary. From a technology angle, it is important to transform IT as an innovation hub and address the lack of synergy between business, technology and operations functions of the enterprise.
- **Tax and regulatory structuring:** eCommerce firms need to address issues around sub-optimal warehouse tax planning; imbalance between FDI norms vis-à-vis adequate entity controls; inefficient holding, IPR or entity structures; and international tax inefficiencies. Future challenges include the new Companies Act, policy on related-party transaction pricing, and the uncertainty around GST roadmap.
- **Risk, fraud and cyber security:** From a risk perspective, eCommerce firms could face challenges around brand risk, insider threats and website uptime. Issues around employee-vendor nexus, bribery and corruption make companies vulnerable to fines. Cyber security also raises some concerns around website exploitation by external entities.
- **Compliance framework:** eCommerce firms have to comply with several laws, most of which are still evolving. Potential issues around cyber law compliance, inefficient anti-corruption framework, legal exposure in agreements or arrangements, indirect and direct tax compliance framework and FEMA contraventions and regularisation could pose problems. Also, uncertainty around VAT implications in different states due to peculiar business models could cause issues.

Suggestions

Following steps are recommended for eCommerce firms to accelerate business growth

1.Customer experience

As the buyers progress from research to purchase to fulfilment stages, their expectations change fast. eCommerce firms need to understand these change drivers and adapt their proposition accordingly. Simple transitions between ordering on tablets, mobile phones or PCs will have to be facilitated. Besides, convenient multichannel returns and delivery options need to be developed along with the provisions of touch and feel the product before buying. They should also ensure sufficient after sales service and support. Online product reviews and ratings, videos, more advanced sizing and fitting tools should be provided.

2.Technological advancements

eCommerce firms have to upgrade their offerings continuously with changing technology. e.g, shopping through mobiles has truly arrived and therefore firms need to devise customer friendly mobile apps for their websites. They need to ensure that their websites have the required speed to do fast business, especially during sale, deals and discounts. Solutions enabling seamless integration of back-end and front-end infrastructure, customer experience enhancement initiatives, integrated inventory management and analytics would be crucial for the eCommerce firms.

3.Convergence of online and off line channels

As the potential buyers progress from research to purchase to fulfilment stages, their expectations also change fast. eCommerce firms need to understand these change drivers and adapt their proposition accordingly. Easy transitions between ordering on tablets, mobile phones or PCs will have to be facilitated. Besides, convenient multichannel returns and delivery options need to be developed along with the provisions of touch and feel the product before buying. They should also ensure sufficient after sales service and support. Online product reviews and ratings, videos, more advanced sizing and fitting tools should be provided.

4.Delivery experience

In the absence of integrated end to end logistics platform, the eCommerce industry is facing problem related to procurement operations and transportation. Online purchases from Tier-2 and Tier-3 cities are expected to significantly increase, thanks to the emergence of low cost smart phones, however, poor last mile connectivity could act as a deterrent. Keeping control on logistics and on ground fleet management, especially courier companies, is essential for growth.

5.Payments and transactions

India continues to be a cash-based society due to limited banking and credit card penetration. This, combined with a lack of consumer trust in online merchants, has forced companies to offer CoD services, which imposes significant financial cost for firms in the form of labour, cash handling and higher returns of purchased items. Data protection and the integrity of the system that handles the data and transactions are serious concerns. Companies should take necessary action for management even if this imposes a cost on them.

6.Tax and regulatory environment

Laws regulating eCommerce in India are still evolving and have poor clarity. Favourable regulatory environment would be key towards unleashing the potential of eCommerce and help in efficiency in operations, creation of jobs, growth of the industry, and investments in back-end infrastructure. Furthermore, the interpretation of intricate tax norms and complex inter-state taxation rules make eCommerce operations difficult to manage and to stay compliant to the laws. With the wide variety of audience the eCommerce companies cater to, compliance becomes a serious concern. Companies will need to have strong anti-corruption programs for sourcing and vendor management, as well as robust compliance frameworks. It is important for the eCommerce firms to keep a check at every stage and adhere to the relevant laws, so as to avoid fines.

7.Operational framework

Business models are evolving rapidly in the eCommerce sector mainly due to increased competition and the inability of players to sustain high costs. Firms in eCommerce need to adapt and innovate constantly to sustain their businesses. Furthermore, several of these firms entered into the eCommerce industry as start-ups and have grown to a huge size supported by the continuous growth in the market but lack well defined capabilities and organisational structure. System building, financial and talent management become key.



1. Customer acquisition

The cost of customer acquisition in Indian eCommerce is rising rapidly due to intense competition between multiple well-funded players. Just 2% of website visits currently result into transaction. Hence, there is a gap between potential and actual buyers. Coupled with high transaction costs, this area could pose serious issues. This suggests companies should constantly work on their brand positioning.

2. Digital infrastructure

Digital disruption has driven change in the eCommerce industry with shoppers embracing multiple touch points in their purchase journeys. Firms have to spend sufficient resources on technology development as also advertising and branding, especially because the younger population is demanding. In the journey toward digital business transformation, embedding SMAC technologies in the business becomes crucial.

3. Addressable Markets

To grow businesses, the Indian eCommerce sector needs to closely watch the growth of markets in the Tier 2 and 3 cities. Sector need to improve logistics and supply chain management there, do an effective demand management to keep an eye on what products are being sought in these cities. With eCommerce largely being a borderless activity firms need to focus on customers and their needs.

Conclusion

India's overall retail opportunity is substantially growing, and coupled with a demographic dividend (youth population, rising standards of living and upwardly mobile middle class) and increasing internet penetration across the country, higher growth in eCommerce is expected in the years to come. From an investment point of view, the market is a primarily minority stake market, with maximum traction in early-stage deals. Early stage funding will support and enable firms develop a solid foundation to begin from. With such strong market prospects and an equally upbeat investor community, many more eCommerce firms from India entering the coveted billion-dollar club will become a reality within next 4 – 5 years.

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