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Potential and challenges of e-commerce in India

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Abstract

The study seeks to search and look at the potential and challenges of e-commerce in India. The e-Commerce sector has seen unprecedented growth in 2014. The growth was driven by rapid technology adoption led by the increasing use of devices such as smart phones and tablets, and access to the internet through broadband, 3G, etc, which led to an increased online consumer base. Furthermore, favored demographics and a growing internet user base helped aid this growth. In terms of highlights, the growth shown by homegrown players such as Flipkart and Snapdeal and the huge investor interest around these companies displayed the immense potential of the market. With the entry of e-Commerce behemoths such as Amazon and Alibaba, the competition is expected to further intensify. Both these international players come with deep pockets and the patience to drive the Indian e-Commerce market. Also, their strong domain knowledge and best practices from their international experience give them an additional edge. Additionally, these companies have been part of markets where they have seen the e-Commerce market evolve and are aware of the challenges and strategies to address issues thereof. This study explores the current status, potential and the challenges faced by e-commerce in India and is based on the analysis of secondary data mainly obtained from the professional reports and e-commerce literature available.

Keywords: e-commerce, potential of e-commerce and challenges of e-commerce

1. Introduction

1.1 E-commerce Overview

Over the last decade, the Internet has changed the way people buy and sell goods and services. Online retail or e-commerce is transforming the shopping experience of customers. The sector has seen unprecedented growth especially in the last two years. The adoption of technology is enabling the e-commerce sector to be more reachable and efficient. Devices like smartphones, tablets and technologies like 3G, 4G, Wi-Fi and high speed broadband is helping to increase the number of online customers. Banks and other players in e-commerce ecosystem are providing a secured online platform to pay effortlessly via payments gateways.

The homegrown players have shown tremendous growth and attracted some big investors. The entry of global biggies like Amazon and Alibaba has taken the competition to a new level. E-tailers are differentiating themselves by providing innovative service offerings like one-day delivery, 30-day replacement warranty, cash on delivery (CoD), cashback offers, mobile wallets, etc. The supply chain has improved significantly and e-tailers are even leveraging on the services of Indian Post for greater reach across the country. In 2014, Indian Post collected ` 2.8 billion through CoD option of payment.

India slipped from 14th to 20th rank among the top 30 developing countries in 2014 Global Retail Development Index (GRDI) that looks at measures for retail investments worldwide. 2 Chile and China are leading in the GRDI rankings. The sector is still in its growth stage in India and has enormous potential to offer in the coming years. The government's most prestigious Digital India project could take the sector to new heights.

The digital commerce market in India has grown steadily from \$4.4 billion in 2010 to \$13.6 billion in 2014. As per industry estimates, the digital commerce market in India is expected to reach \$16 billion by the end of 2015 on the back of growing Internet population and increased online shoppers. Online travel accounts for nearly 61% of e-commerce business while e-tailing contributes about 29%. 3 Visa India spend data showed 53% growth in the number of e-commerce transactions in 2014.

Similarly, there is an almost similar growth trend of e-commerce in the global market. The eMarketer report had predicted that the business-to-consumer (B2C) e-commerce sales worldwide will reach \$1.5 trillion in 2014, increasing nearly 20% over 2013. As the e-Commerce players from the US, Europe and Japan are seeing slower growth in home markets, they are increasingly looking to enter developing economies of India, Brazil and China which have forecasted growth rates of more than 20% over coming years. Most popular e-commerce categories are non-consumable durables and entertainment related products.

2. Objectives of the study

The objectives of the study are:

1. To study the current status and growth potential of e-commerce in India.
2. To study the challenges faced by e-commerce in India.

3. Methodology

Secondary data is mainly collected from publications of national and international research organizations like Deloitte and ASSOCHAM, CRISIL, Technopark and CII. Different

reports have been collected from a variety of sources like various publications of the government and publications of various associations connected with telecommunication (mobile and internet) department like TRAI. Qualitative Analysis of various available literatures (documents and reports) has been done using the techniques of statistical compilations and manipulations, reference and content analysis.
The current status has already been discussed in introduction part, is section 4 covers the first objective and the section 5 discusses the second objective while section 6 discusses the conclusion.

4. Current Status and Growth Potential of E-Commerce

The Indian economy has been consistently showing good signs of growth, with the average GDP growth rate at 7.5% in 2015-163. The retail sector is showing a promising trend of 11% CAGR, growing from an estimated size of USD 600 Billion now to USD 1 Trillion in 20204. Although, currently the total e-Commerce spend in India accounts for less than 2% of the total retail spending, e-Commerce has become a key driver to create new markets in erstwhile unreachable geographies.
The Indian consumers are rapidly advancing towards adopting technology. While the overall tele-density is 81.8%, the mobile tele-density is also high at 79.8% as of November, 20155. Additionally, during the same time, India beat the United States of America to become the 2nd largest market after China6, for smartphones with 220 Million users – This was attributable to the availability of highly affordable smartphones and with easy-to-use features which helped first-time smartphone users leapfrog from the desktop/laptop phase. Internet penetration is also significantly rising with the number of internet users at 354 Million as of September, 20157. In addition, there is a shift in mobile usage from voice to data. Mobile internet spend has risen from 54% to 64% from 2014 to 2015. This is due to an availability of high-speed 3G & 4G internet connectivity at affordable prices which has led to an increase in transactions done via mobile2.
India's rank for ease of doing business went up by 12 in just one year due to an improved regulatory framework thus creating a conducive business-friendly environment8. These factors have positively impacted Private Equity and Venture Capital investments into the country touching USD 20 Billion in 20159. Majority of these investments have been in e-Commerce industry.
The e-Commerce industry is expected to form the largest part of the Indian Internet market with a value of approximately USD 100 Billion by 20208. In addition to transforming and revolutionising the retail sector in India, it is also facilitating MSMEs to jump the evolution loop by providing means of financing, technology and training. Advent of technology enabled innovations such as Digital Payments, Hyper-local Logistics, Analytics driven Customer Engagement and Digital Advertisements have enabled the e-Commerce industry to grow at a much faster rate.
Within the e-Commerce industry, the Gross Merchandise Value (GMV) is an important metric for valuations especially during the early stages of growth. The majority of B2C e-Commerce companies, globally, despite being operational for 5-20 years, report low profitability. The situation in India is no different i.e. a growing GMV but at an overall loss as the e-Commerce companies establish themselves. The GMV for B2C segment in India was approximately USD 16 Billion in 201510.
This trend however does not hold true for the B2B e-Commerce companies which are profitable with greater GMV values. The Indian B2B e-Commerce market potential was valued at USD 300 Billion in 2014, and is expected to reach USD 700 Billion by 202011. The higher profitability in the B2B segment is attributed to reasons such as lack of heavy discounts, greater emphasis on quality rather than on price, and higher volumes of purchases.

5. Challenges of E-Commerce

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

5.1 External Challenges

External forces impact how e-Commerce companies plan their growth strategy and provide seamless customer experience onsite and post transaction.

i) **Product and market strategy:** e-Commerce companies have to address issues pertaining to rapidly evolving customer segments and product portfolios; access information 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.
ii) **Customer and digital experience:** Companies have to provide 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. In the recent past, social media has become more influential than paid marketing.
iii) **Payments and transactions:** e-Commerce companies may face 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.
iv) **Fulfilment:** Companies will 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 fulfillment option could cause delivery issues. Challenges around reverse logistics management and third party logistics interactions could also act as barriers to growth.

5.2 Internal Challenges

Internal forces impact how e-Commerce companies can organise to drive and sustain growth.

i) **Organisation scaling:** e-Commerce companies will have to make sure organisation design keeps pace with the rapidly evolving business strategy, along with fluid governance, strong leadership and management development. From a growth perspective, identifying acquisition opportunities, fund raising and IPO readiness becomes necessary. From a technology perspective, 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.

ii) **Tax and regulatory structuring:** Companies will 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.

iii) **Risk, fraud and cyber security:** From a risk perspective, e-Commerce companies could face issues 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.

iv) **Compliance framework:** e-Commerce companies have to comply with several laws, many 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.

6. Conclusion

E-commerce has transformed the way business is done in India. With attractive and convenient shopping options at the core of the consumer facing business, the e-commerce industry offers the power to create innovative, sustainable, consistent and seamless shopping experience across all channels. In the last 4 years, while the e-Commerce B2C segment has grown significantly leading to creation of many Unicorns, the focus of the Investors going forward seems to have shifted to profitable growth to achieve a stabilization of the economic model. This seems to be resulting in collaborations and partnerships across the value chain with the aim to optimize the costs. Simultaneously, the e-commerce B2B segment is showing signs of rapid digital adoption which is likely to feed the significant rise of MSMEs and entrepreneurs from the Indian hinterland. The growth of the e-commerce industry has been triggered by increasing internet and smartphone penetration in not only metro cities but also in tier two & three cities of India. Mobile devices are further expected to drive sales via e-commerce platforms over the next 5 years.

While the e-commerce space has rapidly evolved, several challenges have surfaced primarily in areas of taxation, logistics, payments, internet penetration and skilled man power. In taxation, for example, the lack of a uniform tax structure leads to several issues such as double-taxation or impediments in the free flow of goods across the country. However, the ensuing Goods and Services Tax (GST) is expected to help in overcoming these challenges through a uniform tax structure. Clearly defined rules for e-Commerce transactions in GST and a consultative approach while framing these rules will be favourable to both, the Government of India as well as the e-commerce companies.

Logistics lies at the heart of e-commerce and a large number of third-party logistics service providers have entered this space to provide customised last-mile deliveries. In line with the trend for increased e-commerce uptake in tier two and tier three cities, e-commerce and third party logistics service providers are partnering with players with existing infrastructure in tier two and tier three cities (e.g. India Post) to facilitate deliveries in those cities. However, the increasing logistics costs related to last-mile delivery, especially on account of return orders, requires innovative and analytical driven models that will enhance operational efficiencies in the logistics value chain. This will help e-commerce companies in their drive towards profitability.

From a payment perspective, Cash-on-Delivery (CoD) continues to dominate the payments for e-commerce sales in India which in turn presents its own set of unique challenges. Digital payments (eg. mobile wallets) are slowly gaining traction. The growing usage of mobile internet and the implementation of the UPI are expected to give further impetus to the growth of digital payments. In the last 18 months, the Government of India has announced several flagship programs namely, *Digital India*, *Make in India, Start-up India, Skill India* and *Innovation Fund.* The timely and effective implementation of these programs will support the e-commerce eco-system to overcome the challenges related to ineffective rural internet penetration and lack of skilled manpower.

As the digital eco-system evolves in India, the e-commerce companies on their part need to continually innovate, embrace digitisation and analytics to remain relevant. Further, to differentiate, the e-Commerce companies will have to in parallel, focus both, on business-as-usual and also on disruptive growth towards building legacy firms.

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