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India’s e-commerce war

How Flipkart, Snapdeal and Amazon are engaged in a fierce three-way tug-dominance of India’s booming online retail market

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The three online marketplaces have spent—and are spending—hundreds of millions of dollars on expanding product range and discounting in a windfall for Internet shoppers. Photo: iStock

Bengaluru/New Delhi: In July 2014, the Indian unit of Amazon.com Inc. joined a high-stakes game of poker with Flipkart Ltd, India's largest e-commerce firm.

A day after Flipkart announced a record $1 billion fund raising, Amazon's founder and chief executive officer Jeff Bezos said the Seattle-based Internet retailer would pump as much as $2 billion into its India business.

"We see huge potential in the Indian economy and for the growth of e-commerce in India," Bezos said. "With this additional investment of $2 billion, our team can continue to think big, innovate and raise the bar for customers in India."

At that time, Amazon, with its technology expertise, vast experience and large war chest, was seen as the biggest threat to Flipkart's market leadership in India, where the world's largest Internet retailer had set up its online marketplace in June 2013.

Then, in October 2014, Snapdeal, India's second largest e-commerce firm, announced its entry into the big league by raising as much as $627 million from Japan's SoftBank Group, which is also the largest investor in Chinese online giant Alibaba Group Holdings Ltd.

What was seen as an eventual head-to-head fight between Flipkart and the deep-pocketed Amazon India turned into a three-cornered contest in a country where, according to UBS AG, online retail could increase to anywhere between $48 billion and $60 billion by 2020 from $4.47 billion last year.

Since then, Flipkart, Snapdeal and Amazon have spent hundreds of millions of dollars to expand their product range, built massive warehouses, hired thousands of people and splurged lavishly on advertising and discounting to attract customers and win market share.

Their spending spree has resulted in a windfall for Indian shoppers, who have got used to deep discounts throughout the year for shopping online.

Since these three companies are privately held, the exact numbers are tough to get hold of. But the pecking order has largely remained the same: Flipkart, the market leader, followed by Snapdeal and Amazon India, then everybody else.

Flipkart and Snapdeal, owned by Jasper Infotech Pvt. Ltd, can't afford to rest easy, though.

Amazon Seller Services Pvt. Ltd, the locally registered entity of Amazon, is offering more than 30 million products across some 35 categories, includingelectronics and apparel, and also claims to have the largest product assortment in 15 of these categories, among them books and toys.

In the quarter ended June, sales at Amazon India grew more than fourfold, according to the company, showing that it was gaining significant market share in its high-stakes, e-commerce war with Flipkart and Snapdeal. Rupee or dollar figures aren't available.

The company's sales—net of discounts, product returns and taxes—surged more than 300% in the fiscal first quarter, compared with the year-ago period, according to Amazon India. In the same quarter, unit sales at Amazon India surged more than 500%.

In comparison, Flipkart and Snapdeal have lagged. Flipkart's unit sales rose 150% in the first seven months of 2015, compared with the year-ago period, according to the company. Snapdeal reported an increase of 222% in gross merchandise value (GMV) in the April-June quarter. GMV refers to the value of goods sold on a site, but does not account for discounts or even product returns.

Festive sales

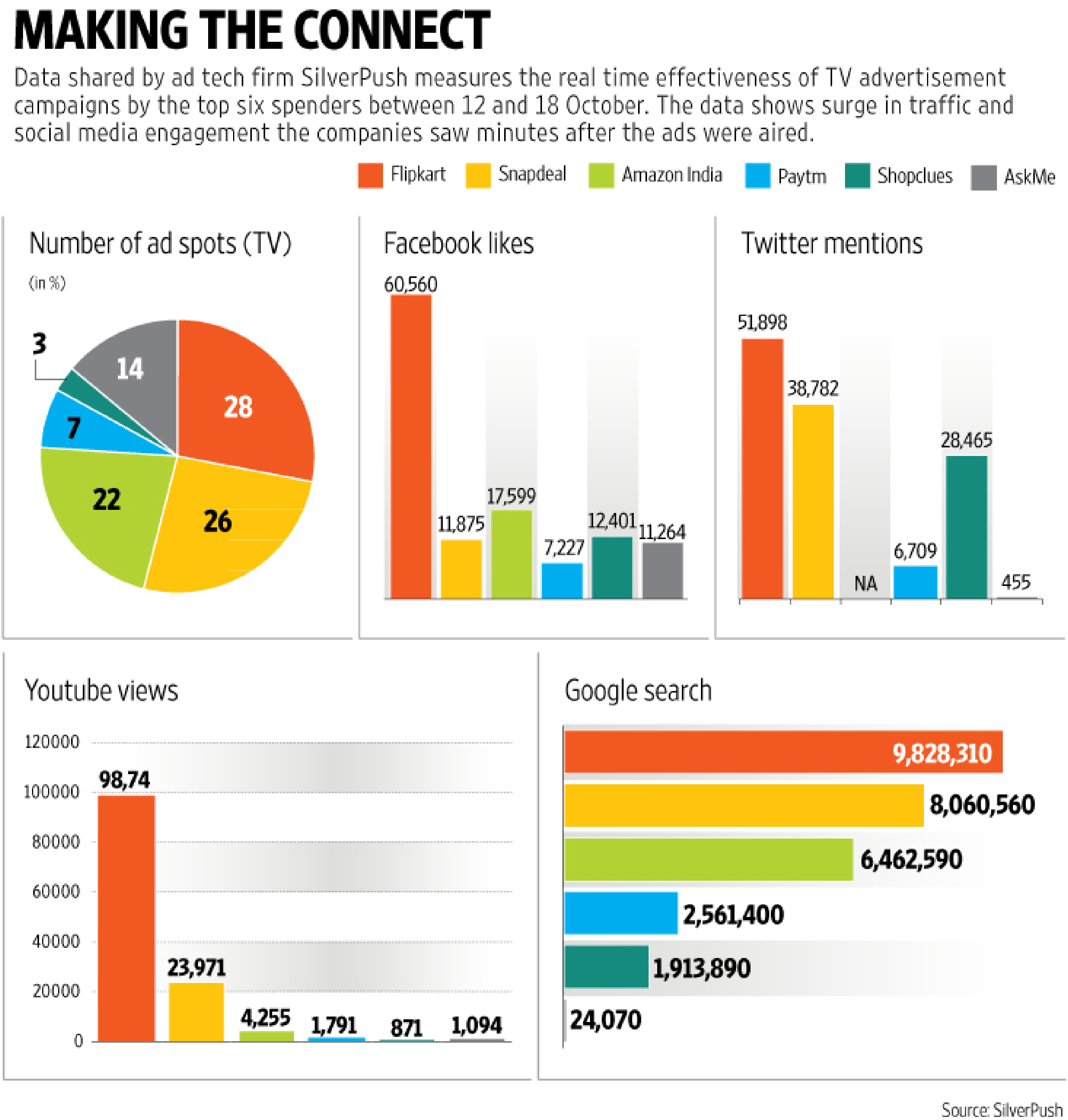
Amazon India's market share gains heaped pressure on Flipkart and Snapdeal to generate bumper sales in the ongoing festival period, when India celebrates Dussehra and Diwali in October and November, followed by Christmas and year-end holidays in December. E-commerce firms generate more than half their annual sales in the October-December quarter.

Flipkart already had a point to prove that it could execute a big sales event successfully. Last year, it spent the equivalent of several million dollars on marketing its one-day Big Billion Day sale in October, touting deep discounts on all kinds of products.

The company took just 10 hours to hit its target of $100 million in gross sales (excluding discounts) on the day of the sale, which is inspired from similar shopping events such as Cyber Monday and Black Friday in the US and the Singles' Day sale held by Chinese e-commerce giant Alibaba Group.

But Flipkart was unprepared for the rush of customer traffic and the company's founders, Sachin Bansal and Binny Bansal, were forced to apologize to customers for pushing up prices of some products, cancelling orders, inadequate stock and other glitches.

Flipkart tried it again this year. The company said last month that this year's version of the Big Billion Day sale will be open for five days from 13 to 17 October and will be limited to shoppers on its smartphone app.



After last year's snafu-ridden sale and Amazon's market share gains this year, Flipkart couldn't afford anything less than a stellar festival quarter. To make things tougher for the firm, Amazon India held a competing five-day sales event on the same dates as Flipkart.

Judging by last week's numbers, Flipkart has passed the first, and most important test, with flying colours.

The company reported more than $300 million in value of goods sold over the five days, at least three times more than last year's single-day sale.

Restricting the sale to its app helped Flipkart drive as many as five million app downloads, Flipkart chief product officer Punit Soni said.

"We have exceeded all our targets. The idea to go app-only was validated. We took the app and tweaked and fixed and optimized it such that it became a 10MB app from 25MB earlier. When we did that, we started seeing more and more people adopting it. The Flipkart app is No. 1 in the iOS App Store as well as on Google Play Store, above Facebook and WhatsApp which are high-frequency social messaging apps," Soni said.

Amazon India, too, saw a surge in sales. It reported a fivefold increase in the number of new customers on its site, compared with traffic on a non-sale day. Sellers on its platform saw sales grow 8-10 times last week, compared with non-sale days. The company, which has more than 30,000 sellers, declined to specify the sellers that generated the surge in sales.

Amazon India had its biggest ever daily sales on five consecutive days last week, country manager Amit Agarwal said.

"This is turning out to be the greatest sale we have seen both from experience and demand perspective. Pretty much all our categories have been hitting their biggest days and beating them in consecutive days. And what is even more exciting for us is that despite the massive surge in demand, we are continuing to make sure that customers get it right and very fast," he said.

While Flipkart went head-to-head with Amazon India last week over the five-day sale period, some other e-commerce companies avoided competing directly with the two retailers.

Snapdeal is holding its sale over several weeks by offering single-day sale events. Last Monday (12 October), Snapdeal said it generated roughly $100 million in GMV during its Electronics Monday sale, which offered discounts on smartphones, laptops, other electronics and home appliances.

According to Snapdeal, it saw over 17x increase in volume, with over 350% increase in first-time buyers. The app was downloaded about 5 million times during this sale period.

The company saw 4x growth in mobile phones; it sold five devices per second during the Electronics Monday sale; mobiles worth ₹500 crore were sold on this day.

According to the company, last Diwali, it processed 30 orders per second while the number in the pre-Diwali sale this year is 300 orders per second.

Discounts of between 30% and 80% drove the traffic for all three online retailers.

Losses abound

Since the beginning of 2014, Flipkart has raised roughly $2.6 billion in capital and Snapdeal about $1.7 billion.

Flipkart boosted its market leadership in May 2014 by buying India's largest online fashion retailer, Myntra, for an estimated value of more than $330 million. Snapdeal snapped up mobile recharge firm Freecharge for more than $400 million this year.

These two deals helped Flipkart and Snapdeal boost their sales growth and acquire new customers. Flipkart and Snapdeal have also invested in a host of other firms, partly to boost their technology functions. While the two e-commerce firms continue to experience healthy sales growth, the absence of profits, or even signs of costs reducing relatively, has been a point of concern.

Their investors have talked up the vast market size and the explosive growth in the number of Internet users, mainly because of the increasing penetration of inexpensive smartphones. The number of mobile Internet users in India is projected to double and cross the 300 million mark by 2017 from 159 million users at present, according to an August report by the Internet and Mobile Association of India (IAMAI) and consultancy firm KPMG.

What is missing in this rosy picture is any discussion about whether any e-commerce company in India has built, or is in the process of building, a business model that can generate profits.

The jury is out on that, judging by the way companies are changing tack and the continued lack of restraint in spending on acquiring customers through advertising and discounts.

Valued at $15 billion, Flipkart is undergoing a complex transformation where it is not only moving from an inventory model to a marketplace one, but is also trying to shift to an advertising-led model from a commission-based one, which is the mainstay of a marketplace.

Flipkart started out as an online retailer, directly selling products to customers; but, since 2013, it has been shifting to a marketplace model where it simply connects customers to third-party sellers on its platform.

Snapdeal, too, is tweaking its business model. The company is aggressively investing in logistics through specialty logistics provider GoJavas. Snapdeal, which bought a 20% stake in GoJavas for ₹120 crore in March, increased it to 42% earlier this month.

All these moves will either require hundreds of millions of dollars in fresh funds, which will only delay any chances of these companies cutting losses.

Marketing expenses and deep discounts are also unlikely to abate meaningfully until consolidation brings about moderation in spending.

This level of uncertainty about business models of the two largest venture-backed companies is worrying and finally prompting investors to step back.

Flipkart's negotiations with new investors to raise funds failed to make progress since talks began in March, while Snapdeal was forced to settle for a valuation in its latest round that was lower than what it initially sought.

Who will make money?

Flipkart closed a $700 million round from its existing investors led by Tiger Global in August; while Snapdeal raised $500 million from Alibaba, Foxconn and SoftBank in the same month at a valuation of $4.5 billion.

For the fiscal ended March, losses at the two e-commerce firms are expected to soar from the few hundreds of crores of rupees reported in the year before. In all likelihood, losses for the ongoing year will also increase significantly.

Both companies are private, so their results can only be obtained once they make regulatory filings later this year.

In the obsession over vague metrics such as the growth in smartphone users and GMV, sound business practices have taken a backseat. These metrics had given the illusion that businesses can be valued in new ways rather than traditional metrics such as price-to-earnings ratio and cash flow.

As these two companies mature, this argument is starting to ring hollow.

What compounds the sales-profit dilemma for Flipkart and Snapdeal is that Amazon isn't likely to slow its spending.

It's particularly important for Amazon to build a large business in India, which is considered to be the last big unconquered market in the world, after it lost out in China to Alibaba.

Amazon has also spent less than $700 million in the country since it announced its $2 billion investment in July 2014, leaving a lot of leeway for the company to continue its aggressive expansion.

"While it is very clear that Flipkart, Snapdeal and Amazon are the market leaders, the jury is still out on who will turn out to be the winner," said Sumchit Anand, founder and managing director of Acquisory Consulting India Pvt. Ltd.

"The one who starts making money will be the winner. Look at the airlines industry; while most airlines are bleeding, IndiGo has emerged as the winner because it managed to start making money."

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