Confederation of Indian Industry

e-Commerce in India
A Game Changer for the Economy

April 2016

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e-Commerce = efficient commerce, empowering commerce

India is a shopper's paradise now, albeit, online. The unrivalled population in India armed with smart gadgets is spoilt for a choice. Aided by declining broadband subscription prices and launch of 3G and 4G services, consumers have become the driving force of e-Commerce in the country. From buying groceries to furniture, movie tickets, trains tickets to steel, coal and tea – e-Commerce has empowered the consumers. As per reports, India will see more people come online than any other country in the next 15 years. With digital device and social media, online sellers are getting unprecedented opportunity for growth and have thus become continuously more attractive for investors. Even though B2C is getting all the attention B2B is not far behind. Both in Direct and Online Marketplace B2B have significant presence. The marketplace model gives customers a plethora of choice and the best prices under a single platform. It also gives vendors a level playing field. Most B2B players have tied up with banks and financial institutions for supply chain finance that helps in improving access to credit. B2B e-Commerce has brought in efficiency, convenience, choice, reach and lower transactional cost for buyers. For SMEs, B2B portals is one of the best things that have happened. For any SME, marketing and advertising costs are huge and many do not have adequate technical expertise to reach out to larger markets. Those areas are now taken care by B2B portals. Basically, B2B wipes out the weaknesses of SMEs. Having a B2B platform takes care of the distribution, advertising and gives access to markets. B2B has enabled SME's growth in sales and helped them acquire new customers. The steady growth of e-Commerce in the country is, thus, ultimately seen at both ends of the spectrum.

With the launch of Digital India and Make in India, the Government of India has been active in bringing out solutions that will help SMEs. Digital India will provide improved internet accessibility while Make in India will help in indigenizing product manufacturing. The technology centric framework by the Government will provide cloud based platforms for SMEs. All this is assisting the growth of small businesses in the e-Commerce era.

However, the tax laws in the country lead to a fair bit of complication. And for that one vital reform – the introduction of GST (Goods and Services Tax) will bring in much awaited relief for the e-Commerce sector.

Coming back to the empowered consumer – they will not be obscure anymore. SMAC will take the lead – Social, mobile, analytics and cloud computing.

- Social media has become a platform for active engagement between the buyer and the seller. It will continue to be one of the biggest influencer to connect to the end user
- Mobility – One in four Indians carry a smartphone. That data itself proves how large the mobility wave is and the scale of transactions it can execute
- Analytics – Predictive analytics will help e-Commerce players to optimize their marketing strategy for targeted advertising that will influence consumers to buy. For B2B companies the analytics will develop more reliable sales buying
- Cloud computing – Reducing costs and increasing speed of business, especially on big traffic days, is one of the major advantages of Cloud computing

Further technologies such as Machine learning, Artificial Intelligence, Robotics, Internet of Things … are yet to be leveraged in a meaningful and scale-able way by e commerce companies and that will be the next frontier.

India has long suffered from the 'missing middle' syndrome. SMEs were not evolving to become mid-sized enterprises for many years. For the millions of SME's e-Commerce platforms along with favourable Government policies will give that significant push to become mid-sized businesses and generate employment. That will be the actual revolution.

Mr. Viresh Oberoi
Co-Chairman, CII National Committee on e-Commerce

Message from CII

Confederation of Indian Industry

The Government of India has taken several initiatives for modernisation and for improving sustainability of the e-Commerce sector. The Digital India project aims to offer online government services that will have mobile phone as the backbone for its delivery. The programme will give a strong boost to the e-Commerce market by bringing internet and broadband to remote corners of the country, which is expected to give a rise to an increase in trade and efficiency.

e-Commerce industry has been directly impacting the MSMEs in India and has a favourable cascading effect on other industries. It is helping connect small merchants with customers across India. The long-term impact of this on the economy would be-increase in employment, growth in export revenue, better products and services to customers and increase in tax collection by ex-chequers.

CII is committed to support the government in this endeavour. We have engaged with key stakeholders to discuss the framework of e-Commerce sector that could accelerate its development.

I am hopeful that that this report will provide useful inputs to make e-Commerce a major contributor to the economy in the coming years.

Mr. Chandrajit Banerjee
Director General, CII

II. Message from Deloitte

Indians are known for their "street smart" frugal innovative mind-set that enables them to find solutions to seemingly impregnable challenges despite the prevailing constraints.

This is the same "innovative instinct" which is making Indian entrepreneurs embrace Digitisation, Analytics and Technology to develop platforms and deliver products & services to the end customer – thus creating a new online buying behaviour.

In context, India's retail opportunity is substantial and spurred by several factors such as the demographic dynamics (hyper-connected young population, rising standards of living and upwardly mobile middle class), deeper internet penetration, explosion of social-media platforms, and increased smartphone penetration. Thus, a significant growth of e-Commerce is imminent in the next two years.

From an investment perspective, considerable funding in the e-Commerce ecosystem has led to emergence of new business models across B2B, B2C, Logistics Service Providers, Payment Wallets, Digital Advertising and Analytics. These investments have enabled the e-Commerce companies to leverage leading technology and related practices to reach out to millions of new online customers by delivering services more effectively and efficiently.

Micro, Small and Medium Enterprises (MSMEs) form the backbone of the Indian economy by contributing over 8% to the GDP and employing over 22% of work-force[1]. In this context, e-Commerce platforms play a crucial role in connecting MSMEs with buyers in India and globally. However, MSMEs need to be empowered through training, technological awareness and financial assistance to enable and accelerate their adoption of the e-Commerce platforms.

The Government of India (GoI) policymakers are trying to develop a conducive regulatory framework and a level playing field for all stakeholders in the ecosystem. In the recent guidelines issued by Department of Industrial Policy & Promotion (DIPP), 100% FDI in B2C e-Commerce marketplace model has been allowed. Additionally, DIPP has clearly defined e-Commerce, marketplace and inventory based models.

Thus, at a stage when India is rapidly becoming a digital economy, the role of the government is critical to enable a conducive and sustainable environment for the entire e-Commerce ecosystem. The recent Government Initiatives such as Digital India, Make in India, Start-up India, Skill India, Innovation Fund and e-market platform for agro-commodities are positive steps in this direction.

Deloitte is privileged to collaborate with the Confederation of Indian Industry (CII) as a Knowledge Partner to create this report that will be recognized as a repository on the Indian e-Commerce industry. In this report, we have presented the point of view of major stakeholders in the Indian e-Commerce industry, along with the key challenges faced by them and key recommendations that will help strengthen this nascent industry to scale and sustain.

We take this opportunity to thank each stakeholder for making this endeavour possible by sharing important insights for this report.

Mr. Neeraj Jain
Partner
Deloitte Touche Tohmatsu India LLP

III. Executive Summary

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.

Key Success factors for e-Commerce industry

- Continuous innovation
- Digitisation and integration of processes
- High-end and disruptive data analytics to spot 'real-time' opportunities
- Nimbleness to scale and sustain
- Training and technological advancement of merchants

Thus, it is imperative for e-Commerce companies to focus not only on business-as-usual but also on disruptive growth to remain differentiated and build a legacy

IV. Current e-Commerce Market Landscape

e-Commerce and the Indian economy

The Indian economy has been consistently showing good signs of growth, with the average GDP growth rate at 7.5% in 2015-16[3]. 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 2020[4]. 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, 2015[5]. Additionally, during the same time, India beat the United States of America to become the 2nd largest market after China[6], 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, 2015[7].

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 mobile[2].

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 environment[8]. These factors have positively impacted Private Equity and Venture Capital investments into the country touching USD 20 Billion in 2015[9]. 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 2020[8]. 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 2015[10].

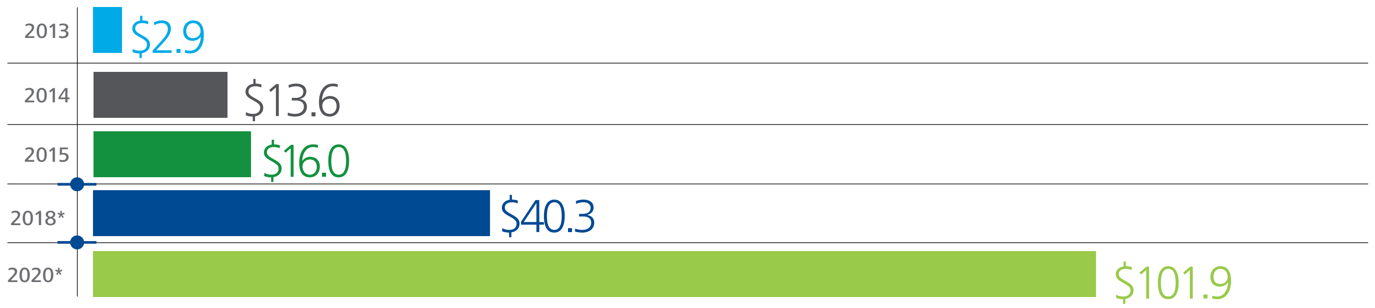
This trend however does not hold true for the B2B e-Commerce companies which are profitable with greater GMV values. The Indian B2B e-Commerce market potential was valued at USD 300 Billion in 2014, and is expected to reach USD 700 Billion by 2020[11]. The higher profitability in the B2B segment is attributed to reasons such as lack of heavy discounts, greater emphasis on quality rather than on price, and higher volumes of purchases.

- e-Commerce has become a key driver to create new markets in erstwhile unreachable geographies
- Smartphones, Mobile devices and Internet penetration together driving disruption in the marketplace
- GMV of B2C e-Commerce companies is growing but so are the losses
- Though B2B e-Commerce is slowly catching up, the companies in this space are more profitable with greater GMV, compared to B2C e-Commerce

"*Across the globe the e-commerce industry is a force which continues to grow, which investors cannot afford to ignore. This is especially true in India where there are so many opportunities. For example, just focusing on B2B e-commerce, the market is both large and broad which provides the potential for amazing innovations. Prime Minister Modi's vision for India and the 'Make in India' and 'Invest India' initiatives have swayed the world's attention on the opportunities provided in the sub-continent. B2C e-commerce in India is changing the ways brands reach consumers and has made it faster and easier for them to make purchases wherever they are, not just when they are in stores. The B2B opportunities are even bigger.*"

Nilesh Gopali, cloudBuy, CountryHead, India

Total e-Commerce size ($ Billion)



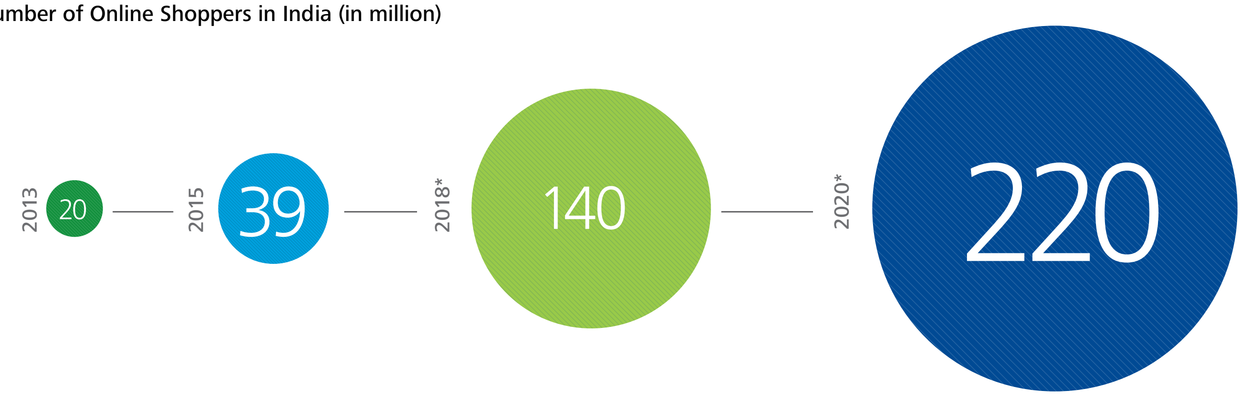
CAGR 34%

Figure 1.Size of e-Commerce industry in India (includes only B2C e-tail excluding online travel and classifieds)

A 6X growth over 5 years is envisaged for e-Commerce driven by factors like new-age technology, convenience, higher adoption rates and larger reach

Source – IAMAI, Deloitte analysis *Estimated Numbers Indicates skip in consecutive years

Number of Online Shoppers in India (in million)



CAGR 41%

Figure 2. Number of online shoppers in India (includes only B2C e-tail excluding online travel and classifieds)

Rise of the middle-class consumers and changing shopping habits are adding to the online shopping demography. Increased access to global products and services at a click of a button, and delivery to even remote locations would further drive up this number

Source – Euromonitor, IAMAI, Media reports *Estimated Numbers

Online shoppers of total internet users (as a %)

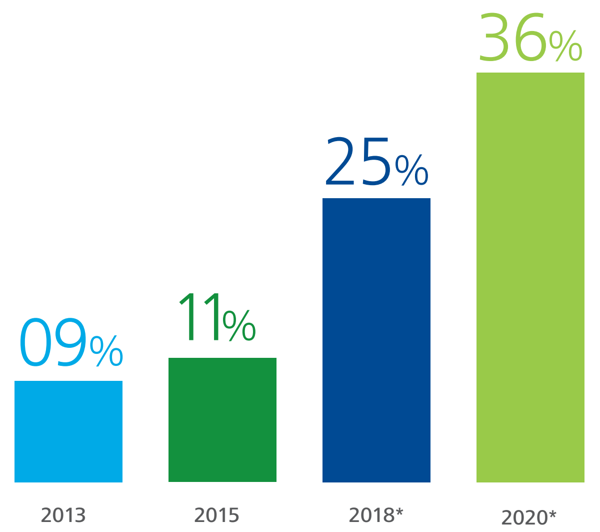


Figure 3. Online shoppers as a % of internet users in India (includes only B2C e-tail excluding online travel and classifieds)

Average spend per online shopper in India (in USD)

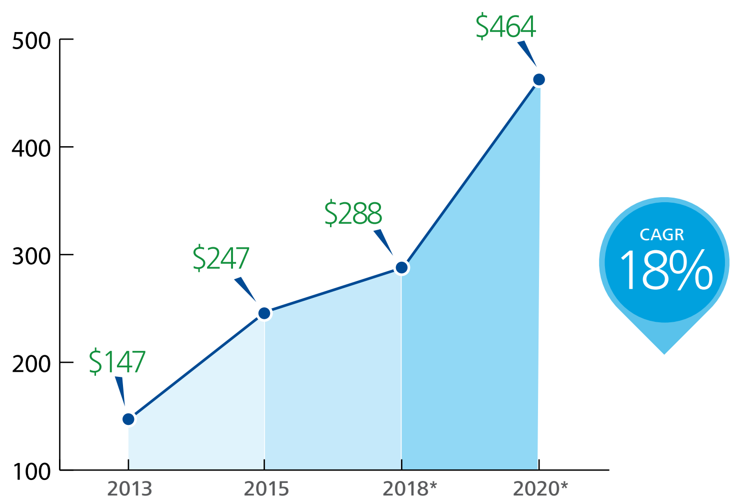


Figure 4. Average spend per online shopper in India (includes B2C e-tail, online travel and classifieds)

Online shopping is increasing its share in the total internet usage in India. Improved data connectivity in both urban and rural parts of India, will further boost this trend. Along with the increase in basket size, the average spend on online shopping is increasing, although not at the same rate

Source – Euromonitor, Deloitte Analysis, Media reports

*Estimated Numbers

Existing and Emerging e-Commerce business models

Globally, e-Commerce has been operating via various models such as B2B, B2C, C2C, Aggregators, and Hybrid.

In India, leading current e-Commerce companies under different business models are enumerated:

E-Commerce models	Leading companies*
B2C e-Commerce marketplace	Snapdeal.com, Amazon.com, Flipkart.com
B2C e-Commerce Inventory Led	BigBasket.com, FirstCry.com, Zovi.com
B2C e-Commerce Aggregator	Uber.com, olacabs.com
C2C e-Commerce	Cloudacar.com, quickr.com, olx.in
B2B e-Commerce	mjunction services limited (metaljunction, coaljunction, buyjunction, etc.), cloudBuy.com, tolexo.com, industrybuying.com, power2sme.com, Amazonbusiness.com
Omni-channel Retailers	Shoppers Stop Ltd., Infiniti Retail Limited Croma, Raymond Limited

Table 1: Indicative list of current leading e-Commerce models in India

Source: Deloitte Research *Note: Domain names

Verticals	Leading companies*
Online Travel	Makemytrip.com, yatra.com, cleatrip.com, goibibo.com
Online Real Estate	Magicbricks.com, 99acres.com, commonfloor.com, Housing.com
Online Fashion	Jabong.com, Myntra.com, Zovi.com, yepme.com, limeroad.com
Online Furniture	Fabfurnish.com, Pepperfry.com, urbanladder.com
Online Education	Purple Squirrel Eduventures , Plancess.com
Online Food and grocery	Zomato.com, Foodpanda.in, TinyOwl.com, BigBasket.com, Grofers.com

Table 2: Indicative list of emerging Vertical Specific e-Commerce companies in India

Source: Deloitte Research *Note: Domain names

The growth of the B2B e-Commerce segment is relatively slower compared to the B2C e-Commerce segment in India. This is because the entry barriers in the B2B e-Commerce are more than those in the B2C e-Commerce industry. A B2B e-Commerce company has to have a strong business model, long term logistical arrangements with rail, road and ports and also adhere to stringent regulatory and taxation governance.

With an aim to tap the huge potential in the B2B e-Commerce market in India, apart from the existing B2B companies, leading B2C companies have also started to build their own platforms for small business owners and traders. This is expected to be supported by rising expectations among growing number of companies to conduct buying and selling online and a shift to conduct procurement transactions through internet rather than the erstwhile Electronic Data Interchange (EDI).

Understanding this untapped potential of the B2B e-Commerce industry, the Government has allowed 100% FDI in B2B e-Commerce which has enabled global successful B2B e-Commerce companies such as Walmart and Alibaba to evince interest in the India B2B e-Commerce industry.

Online retailers going 'offline' and vice-versa

Several e-Commerce companies are opening physical offline stores. Such 'Experience Centres' offer online buyers the touch-and-feel experience, thus offering an integrated shopping experience especially for products with high-price points. Companies such as FirstCry, Pepperfry, Flipkart etc. have opened physical stores to complement the online sales and experience. Similar option of click-and-collect is extended by Amazon in India by providing physical locations for customers to pick up the products at a time convenient to them. On the other hand, various offline retailers have started their online ventures or partnered with leading e-Commerce companies to attract customers at all touch points. For example, Future Group inked an exclusive deal with Amazon while Tata Group owned Croma, partnered with Snapdeal to sell private brands online.

e-Commerce aggregators digitising traditional offline businesses

Besides the conventional services for utilities, fashion & lifestyle, electronics, etc. there is a new trend of emerging e-Commerce aggregators that are aiming to digitise several offline services and creating a convenient ecosystem for consumers. In areas such as truck booking, healthcare, real-estate to name a few which have been traditionally offline, there has been a rise of online aggregators.

Enumerated are some of these aggregators:

Emerging verticals	Leading Companies*
Online Health	Portea.com, Healthkart.com,
Online Laundry	Wassupondemand.com, DoorMint.in, LaundryWala.co.in
Online Entertainment	Netflix.com, ErosNow.com Hooq.com
Online Truck Booking	TruckSuvidha.com, TruckMandi.in, The Karrier.com, Fortigo.com

Table 3: Indicative list of emerging Online Aggregator Models in India
*Note: Domain names

Online aggregators besides providing comparison of price and features across service providers, are also connecting buyers directly with sellers, thus reducing costs to consumers by obviating middle-men.

Evolving e-Commerce ecosystem

Mergers & Acquisitions (M&A)

Like any high-growth, the e-Commerce industry has witnessed consolidation in the past 2-3 years. Consolidation has been taking place in the form of larger e-Commerce companies acquiring smaller companies to either diversify the offerings or to enhance their business operations. These mergers and acquisitions have largely focused on companies in the logistics, payment solutions and digital advertising space.

It is estimated that a total of 930 M&A deals with a cumulative value of USD 26.3 Billion took place in India in 2015, of which 259 deals worth USD 2.43 Billion pertained to the e-Commerce industry[12]. Also, many strategic deals took place in the hyper-local, food-tech and real estate listing segments.

Private Equity /Venture Capital (PE/VC) Funding

In yet another record of sorts, the PE/VC investments reached an all-time high in 2015 at USD 20 Billion[7]. The key sectors in which investments were seen were Information Technology with 666 deals of value USD 4.49 Billion, followed by Consumer Goods with 280 deals worth USD 4.69 Billion[13]. The majority of these investments have been concentrated in e-tailing (70% of investment), followed by online classifieds (17%) and lastly online travel & taxi (9%)[10]. However, with growing importance and push from investors for profitability and early break-evens, the leading e-Commerce companies are aiming to cut down their burn rates by as high as 50%. This aggressive drive comes at a point when capital is becoming scarce for top venture-backed online retail companies. There is also a reduction in the dependence on discounts as a growth strategy.

Investors are currently focussing on start-ups that may scale slowly but have sound fundamentals and strong business models. In essence, these start-ups should have the ability to survive any scenario for e.g. recession etc. Therefore, investors today are interested in start-ups in sectors like health care and education which by the nature of their offerings will provide sustainable models and create legacy firms.

Recent corrections in valuation is a sign that investors not only want continuous market penetration but also want e-Commerce companies to focus on profitable growth. According to a recent ROC filing, Flipkart, Snapdeal and Paytm had a combined loss of USD 557 Million. Therefore, e-Commerce companies need to leverage continuous innovation, analytics, technology and digitisation to realise profitable orders for a sustainable growth

Table 3: Major M&A deals in e-Commerce in India since 2014

Buyer	Target	Industry	Year of deal
Flipkart	Myntra	Fashion & Lifestyle	2014
Snapdeal	Exclusively.com	Fashion & Lifestyle	2015
Olacabs	TaxiForSure	Online Cab booking	2015
Housing.com	Indian Real Estate Forum	Real Estate	2015
Snapdeal	RupeePower	Digital Financial Distribution	2015
Snapdeal	Unicommerce	Logistics, Warehousing	2015
Snapdeal	Freecharge	Payment Solutions	2015
Grofers	Mygreenbox	Mobile Grocery	2015
Zomato	MapleGraph	Cloud-based POS	2015
Makemytrip	MyGola	Travel guide	2015
Zomato	NexTable	Cloud based table management & reservation	2015
Flipkart	Appiterate	Mobile application marketing platform	2015
Myntra	Native 5	Mobile application development	2015
Flipkart	WeHive Technologies	Mobile advertising	2015
Snapdeal	Martmobi	Mobile applications for vendors	2015
Big Basket	Delyver	Hyper-local delivery	2015
Snapdeal	Letsgomo Labs	Mobile technology	2015
Jugnoo	BookMyCab	Online Cab booking	2015
Flipkart	FX Mart	Payment Solutions	2015
Mahindra	BabyOye	Maternity & Childcare	2015
Flipkart	MapmyIndia	Digital Map Platform	2015
Paytm	Near.in	Hyper-local app	2015
Paytm	Shifu	Consumer Analytics	2016
UrbanClap	Handy Home	Services for households	2016
ShopClues	Momoe Technologies	Mobile Payments	2016
Magicbricks	Properji.com	Property Analysis Platform	2016
Future Group	FabFurnish.com	Furniture and Furnishing	2016

Source: Deloitte Research, DealCurry.com

India is going to become the start-up capital of the world. e-Commerce is not only taking India to the next level, but is also causing a global paradigm shift. We can leverage e-Commerce to change lives of our citizens. How can we have cost-effective, consumer friendly, value-add-services at the tip of our finger– This is what Digital India should be.

Padmaja Ruparel,
President, Indian Angel Network

Key trends driving e-Commerce in India

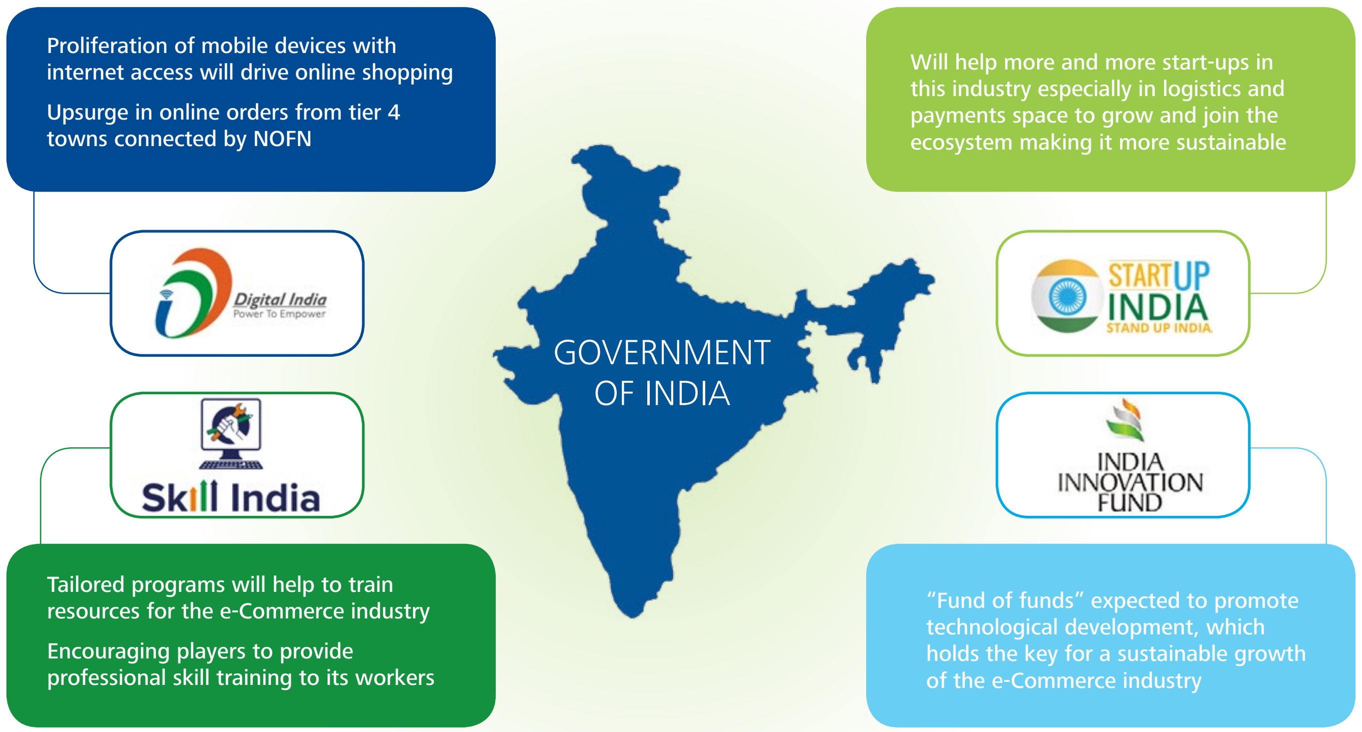
Trend 1. Government initiatives gaining momentum

The Government of India has been proactive in embracing and leveraging e-Commerce digital platforms to transform and organize traditionally offline markets such as those of agricultural produce, etc. The Government has launched an e-market platform to connect farmers with the mandis of various states to sell agro-commodities. Besides these, flagship initiatives such as Digital India, Start-up India, Innovation Fund, Skill India, etc. are contributing to the growth of e-Commerce industry. Enumerated is a brief description of these initiatives:

- **Digital India:** One of the highly ambitious and biggest ever conceived projects is Digital India which focuses on transforming India to a digitally empowered and knowledge economy. The three key areas that have identified are to Build Digital Infrastructure as a Core Utility, enable Government Citizen Services on demand and Digital Empowerment of citizens
- **Start-up India:** This program intends to build a strong eco-system for nurturing "innovation" and "Exponential Start-ups". The Government of India has taken steps such as providing funding support through a "Fund of Funds" (with a corpus of INR 10,000 Crores); "Start-up India Hub" (a single point contact for the start-up ecosystem), tax exemptions for the initial 3 years, faster exits for start-ups are some steps besides many others
- **Make in India:** Aimed at India's industrial development, the key steps taken by the Government of India are: Improving the business environment in the country, enabling manufacturing, and allowing FDI in key sectors. Key pillars of this program worth noting are "research and innovation" and "a conducive business environment"
- **Skill India:** To bridge the shortage of skilled manpower, the Government of India has set a target to train 40.2 Crores people under the new National Policy for Skill Development by 2022. The initiative includes National Skill Development Mission, National Policy for Skill Development and Entrepreneurship 2015

Success of the e-Commerce industry to significantly contribute to the Indian economy will be accelerated by the effective and timely implementation of these Government initiatives

Figure 5. Initiatives by Government of India impacting the e-Commerce industry



Trend 2. Increase in internet penetration

The e-Commerce industry in India has been propelled by the rise in internet penetration due to major improvements in the telecom infrastructure. With 3G and 4G services making way into India along with declining data tariffs, spend on internet data is growing significantly. While India ranks the lowest in Asia when it comes to internet speed, data rates in India are 2X cheaper than in China and 3X cheaper than in the US. Government schemes such as National Optical Fibre Network (NOFN) can significantly increase internet penetration in the rural communities as well as provide a means to

e-Commerce companies to tap the huge market potential there.

Number of 3G and Mobile Internet Users (in million)

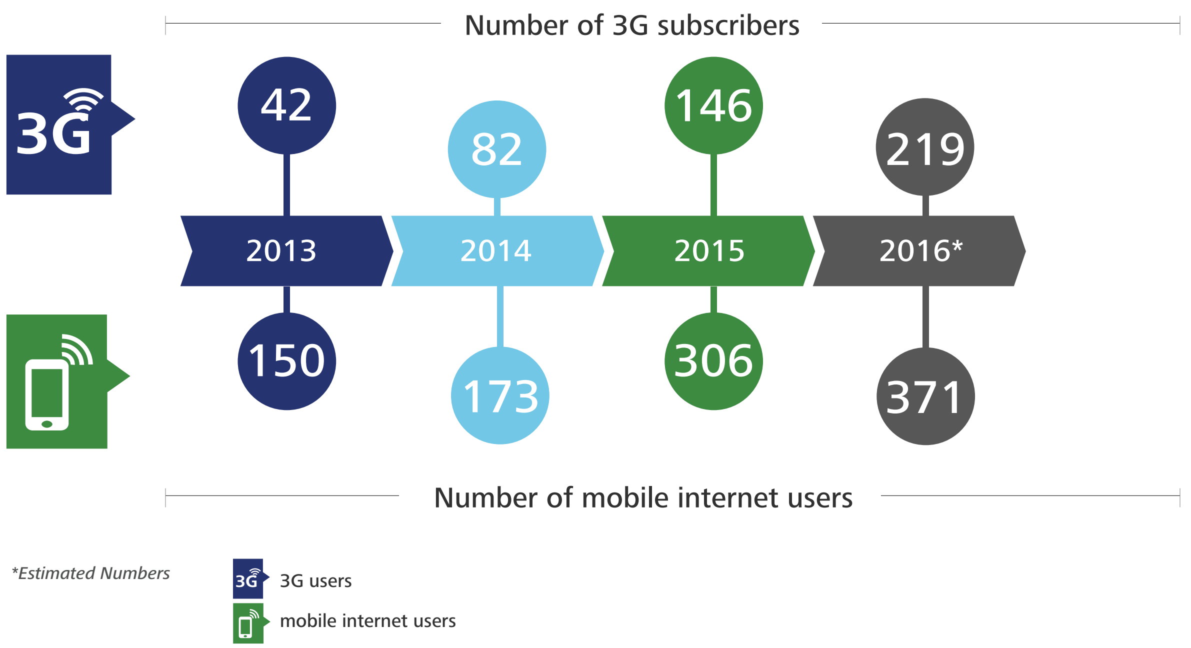


Figure 6. Number of 3G and Mobile Internet Users in India
Source: Mobile Internet in India, 2015 IAMAI

High-speed data (3G/4G) connectivity in rural areas is a challenge as well as a huge opportunity

Given the cultural and language diversification in India, localized online content and customized e-Commerce services is a significant opportunity to enhance the online buying experience

Trend 3. Growth in smartphone adoption driving mobile based e-Commerce sales

Smartphones are outpacing feature phones and are expected to exhibit massive growth in the coming years. The widespread adoption of smartphones is being propelled by several factors such as – high competition leading to low prices, prevalence of internet enabled services and ease of accessibility to content. According to a report by venture capital firm KPCB, India has the highest share of mobile based e-Commerce sales globally at 41%[14]. The leading e-Commerce companies state that almost 70-75% of their online traffic comes from mobile phones and thus higher revenues are coming from mobile applications. For e.g. 50% for Flipkart while 70% for Quikr[15].

Smartphone Shipments vs. Average cost of Smartphones

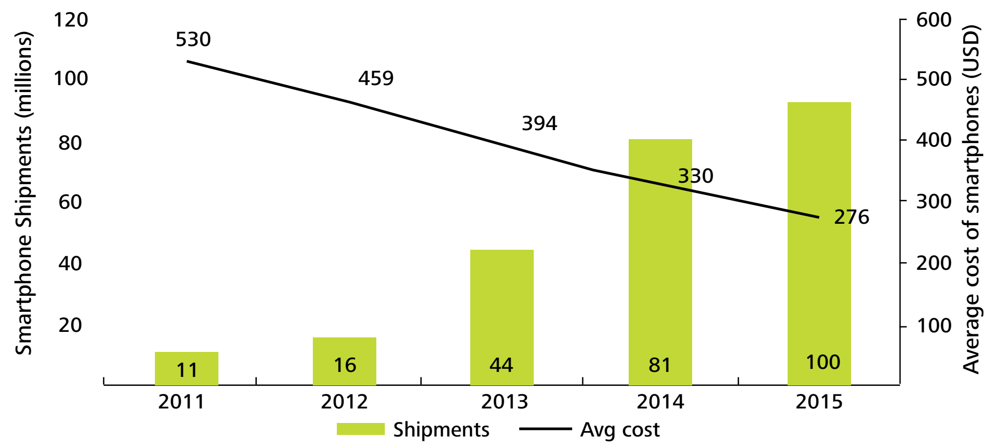


Figure 7. Smartphone shipments and change in average cost of high-end smartphone in India Source – Statista.com, Media Reports

Mobile based e-Commerce sales in different countries

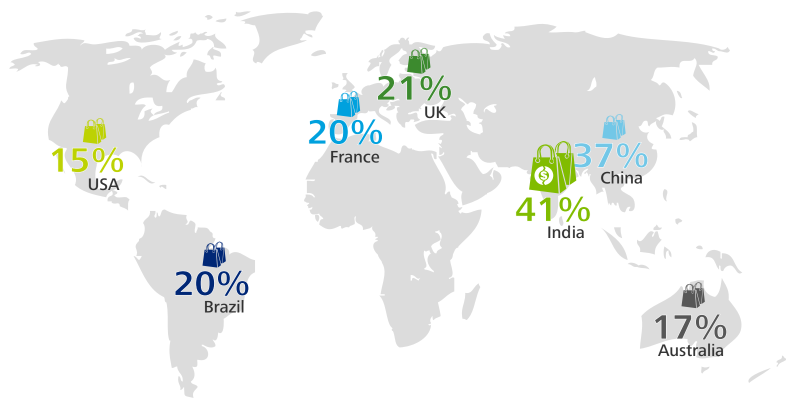


Figure 8. Mobile based e-Commerce sales in different countries as of 2015 Source – Internet Trends 2015, KPCB

India already ranks No.1 globally for the highest share of mobile based e-Commerce transactions

A Deloitte study indicates, customer purchases worth USD 9 Billion in India were impacted by digital & mobile technology in 2015

Modes of payment for e-Commerce

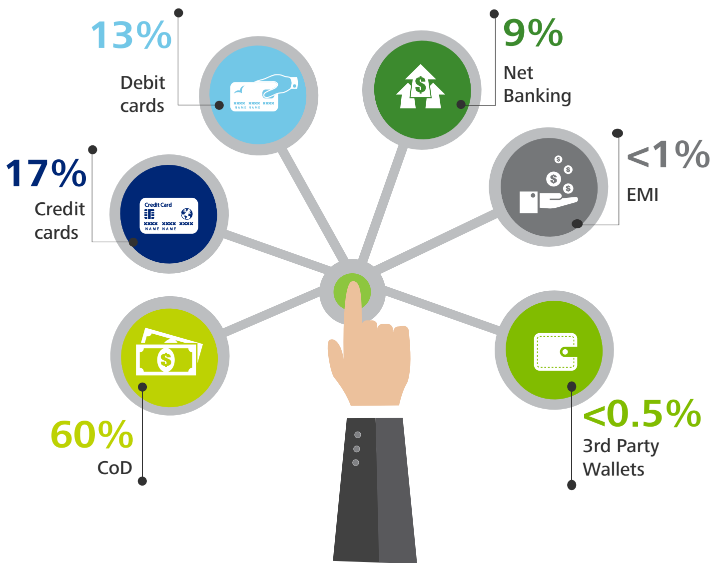


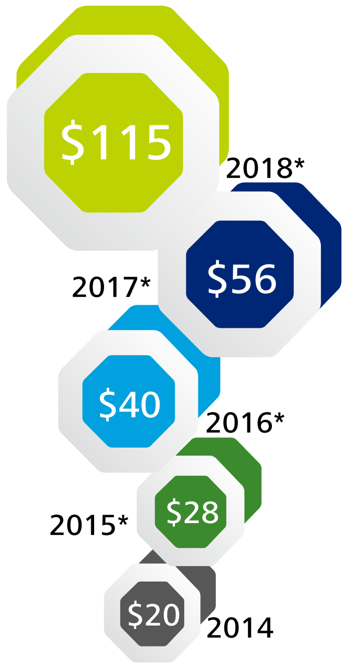
Figure 9. Modes of payment used in e-Commerce in India

Source – Company data, Deloitte Research

Growth of Digital Payment Services (*USD Billion)

Figure 10. Size of Digital Payment Services in India

Source – IAMAI, Media Reports



* Estimated numbers

Trend 4. Evolution of new payment solutions

Cash-on-Delivery (CoD) remains a popular mode of payment for Indian e-Commerce transactions. Cash transactions result in high administration costs even for the e-Commerce companies which reduces their margins. Hence, new digital payment solutions are evolving to address these challenges.

Further, the Indian government's initiative to extend banking facilities to its previously unbanked citizens through the 'Jan Dhan Yojna' scheme has added significant number of debit cards (over 110 Million) thereby providing these customers access to electronic payments. There has been launch of electronic wallets and also digital payment products from traditional banks for faster check-in and check-out of e-Commerce transactions to ease the payment process in e-Commerce.

The launch of Unified Payments Interface (UPI) by Reserve Bank of India is aimed to transform the mobile banking. UPI is expected to benefit the e-Commerce industry as well by reducing the number of failed e-Commerce transactions due to complicated transaction flows in the current payment systems. The implementation of UPI will enable the e-Commerce delivery staff to collect money electronically for even CoD transactions. For early adaptability, several e-Commerce companies have already started building applications that will facilitate mobile payments on UPI. However, the challenge will be to balance safety, integration and mass-adoption.

CoD still winning the race with a 60% share as a preferred mode of payment, followed by credit & debit cards and net banking. Overall size of digital payments estimated to grow from USD 40 Billion in 2016 to USD 115 Billion in 2018

While EMIs and digital wallets account for less than 2% share currently, they will grow faster than plastic money

Trend 5. Logistics space witnessing partnerships with hyper-local companies and India Post

Customers are getting accustomed to next-day delivery of products. Due to challenges in terms of handling huge volumes of delivery, return orders and higher standards of customer service, the industry has seen rise of several third-party logistics service providers (3PLs) who handle last-mile deliveries.

There is an increasing incidence of partnerships of e-Commerce companies with the 3PLs in order to reach the hinterlands of the country mainly in tier 2 and 3 cities. Also leading e-tailers have set up their own logistics arms for greater control on deliveries and for enhanced customer experience.

India Post with its extensive reach of 19,000 pin-codes and 1,54,725 post offices across the country has set-up dedicated processing centres to handle last-mile deliveries of the e-Commerce companies.

Even in the B2B e-Commerce space, logistics service providers are beginning to partner with online truck aggregators and freight marketplaces such as Freight Tiger to build trust and accelerate intercity freight transactions. Such aggregators are increasingly poised to become leading B2B marketplaces for the logistics industry in India.

Number of parcels handled per month by India Post

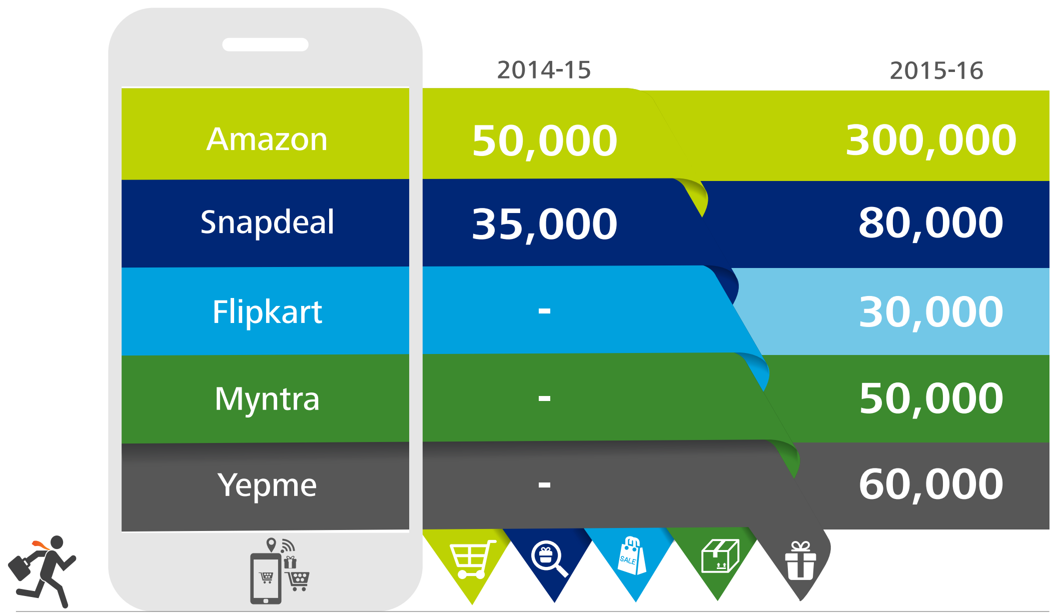


Figure 11. Association of India Post with leading e-Commerce companies
Source – Department of Posts, Company data, Deloitte Research

Each of the players (e-commerce companies) needs assistance to build end-to-end networks. Forming partnerships for last-mile deliveries enable LSPs to provide same-day delivery and reach hinterlands. However, hyper-locals cannot entirely serve these smaller areas as they don't have economies of scale. Large delivery players will have to co-exist with smaller delivery players

Pritam Banerjee,
Senior Director Corporate Policy South Asia, DHL

Logistics challenges in meeting customer expectations of next-day delivery

India Post shaping up a large opportunity in terms of remote location accessibility and wider coverage to untapped markets, thus reducing the need for e-Commerce companies to 'own' last-mile delivery

New age entrepreneurs entering online aggregator platforms for freight transactions

Trend 6. GST expected to enhance the growth of e-Commerce

GST will enforce a single comprehensive indirect tax regime that will be applicable across all states on the supply of goods and services. The implementation of GST is expected to subsume the central excise duty, service tax and additional customs duty at the central level and VAT, CST, entry tax etc. at the state level.

GST will enhance operational efficiency of the e-Commerce industry in the enumerated ways:

- Transparency and simplification of taxes across the borders in India
- Elimination of the incidence of double-taxation and improvement in the efficiency of supply chain
- Logistics service providers can leverage seamless hub-and-spoke models for delivery resulting in lower costs and fewer bottlenecks. Warehouses can be set-up keeping in mind business objectives rather than for reduction in incidence of tax

Trend 7. Empowerment of MSMEs

MSMEs are characterised as a highly fragmented and unorganised sector across vast geographies but account for almost 8% of India's GDP[1]. With the advent of e-Commerce, many MSMEs are exploring the option of selling online and thus accessing new customers across the country.

It has been observed that MSMEs that adopt advanced level of digital engagement experience annual revenue growth that is 27% higher than those of offline businesses due to factors such as reduction in marketing and distribution costs, shorter time to market, etc. The leading e-Commerce companies are taking major initiatives to tackle some of the adoption challenges that MSMEs face:

- They are assisting MSMEs in procurement of loans, training and integration of technology
- They are also encouraging MSMEs to engage with customers on a real-time basis by providing analytical tools for better preparedness and insights on future trends

Additionally, the government is making attempts to make MSMEs more familiar with technology through initiatives such as Technology Centre Framework that will provide support for adoption of cloud based technology by MSMEs. The B2C marketplace, MSMEShopping.com was launched by National Small Industries Corporation (NSIC) with no transaction costs and expects to on-board 5,000 – 10,000 MSMEs by 2016.

- The much-awaited GST implementation to impact and shape e-Commerce through a uniform tax structure, simpler inter-State goods transfer, merchant compliances and easier tax refunds
- MSMEs to join the e-Commerce bandwagon in larger numbers
- Lack of financial training and technological understanding pose a challenge for the adoption of the e-Commerce way of doing business

V. Existing Tax, Forensic and Regulatory Landscape

Direct Tax Landscape

There are no distinctive incentives or special governing provisions that have been set out as such for the e-Commerce industry. However, the e-Commerce companies are subject to regular provisions of the Income-tax Act, 1961. Withholding tax provisions are also relevant to e-commerce companies in India. As the e-Commerce companies typically are technology driven, their operations entail payments for various online services and facilities, many of which are sourced from non-resident service providers. As a result, withholding tax provisions assume relevance for them.

Withholding Tax

Under the domestic tax law, withholding tax is inter alia attracted on payments that are in the nature of royalty or fees for technical services. Also, in the case of non-resident payees, withholding tax is applicable for any payment which is chargeable to tax in India. In this context, the provisions of the tax treaty with the relevant country need to be evaluated, if applicable, since these can be invoked to the extent they are more beneficial.

Nonetheless, for payees who do not have a Permanent Account Number, withholding tax applies at a higher rate. Generally, foreign payees do not prefer to have a Permanent Account Number in India as they may have only few and sporadic transactions with Indian payers.

The characterisation of payments plays a key role in determining applicability of withholding tax. For example:

- **Copyrights** - If a payment towards a software is for the use of copyright, and therefore 'royalty', withholding tax would trigger. However, if the payment is

Some services / facilities which attract the question of withholding for an e-Commerce player

1. Website hosting and maintenance
2. Online Advertisements
3. Server/Cloud arrangements
4. Bandwidth and communication
5. Online use/ download of software

Figure 12. Applicability of Withholding Tax to an e-Commerce company

- No special provisions for taxation on e-Commerce companies
- Ambiguity in applicability of withholding provisions
- In most cases, the tax cost is commercially agreed to be borne by the Indian payer (particularly where non-resident payees are involved). This also requires grossing up of income, if taxes are to be withheld
- Owing to the significant increase in cost in such arrangements, the question of withholding tax is of great concern to Indian payers
- Equalisation levy of 6% proposed to be applicable on certain online services
- Proposed tax incentives for eligible start-ups companies

categorised as for purchase of a copyrighted article, and therefore 'business profits', generally, there would be no requirement to withhold tax

- **Server** - Similarly, if a payment for storage on server is regarded as use of equipment, withholding tax on royalty would apply. However, if the payment is construed as payment for a standard facility of storage on server, it would not attract withholding tax

Equalisation Levy

Recently, the focus has been on taxation issues concerning e-Commerce transactions that are undertaken from outside India i.e. without requiring physical presence of the service provider in India. A committee was constituted to examine these issues and to suggest a workable approach to deal with them.

The committee proposed imposition of an equalisation levy (in the range of 6 – 8% of gross payment) on the payer availing specified digital services and facilities, including online marketing and advertisements, cloud computing, website designing, hosting and maintenance, digital space, digital platforms, etc. As proposed in the Committee's report, the levy would not be a tax on income, and therefore, not governed by the Income-tax Act, 1961. However, the income would be exempt in the hands of the payees, in case of payments that have been subjected to the equalization levy

Indirect Tax Landscape

The e-Commerce industry typically serves as a platform to enable B2B, B2C and C2C to interact and enter into a transaction for supply of goods and services. e-Commerce companies have transformed the traditional stock-and-sell model to multi-model platforms such as market place/services model attracting VAT/CST, service tax etc. However, indirect tax laws have not kept the pace with the evolving business complexities. This has resulted in significant business challenges. Ambiguity of tax laws coupled with delays in business clarifications by tax authorities poses significant challenges to the e-Commerce companies.

Service Tax

Presently all services, except those specified in the negative list and specifically exempted, are chargeable to service tax at the rate 14% and Swachh Bharat Cess at 0.5% and proposed Krishi Kalyan Cess at 0.5% (with effect from 1 June 2016), thereby summing the effective rate to 15%. Typically, service tax is applicable to e-Commerce operators engaged in providing a platform for facilitation fee or commission, online travel portals, online intermediaries, digital content service providers, online advertisers, aggregators and so on.

Relevant Proposals of Finance Bill, 2016

- **Tax incentives for eligible start-ups: Deduction of 100% of the profits derived by such start-up in three out of initial five years**
  - o Could apply to e-Commerce companies that meet the eligibility criteria including developing and commercialising a new / significantly improved service or process and hold a patent in their area of business
- **Introduction of an equalisation levy of 6%**
  - o Presently, the levy is proposed to be applicable only with respect of payments for online advertisements or any provision of digital advertising space or any other facility / service for the purpose of online advertisement
  - o The proposed provisions allow extending the levy to any other online service that may be notified by the Central Government

Value Added Tax / Central Sales Tax

Sale of goods is subjected to VAT/CST, wherein VAT is levied on intra-State sale and CST is levied on inter-State movement of goods. Typically, rate of VAT/CST ranges from 0% to 15%.

Excise Duty

Excise duty is a federal levy and is levied on the goods manufactured in India. At present the standard rate of excise duty is 12.5%.

Customs Duty

Customs duty is levied on the import of goods from country other than India. Customs duty is determined based on the percent of 'assessable value' and is to be paid by the importer of the goods.

Goods and Services Tax

Goods and Services Tax (GST) is proposed be a consumption based unified tax which would be levied on both goods as well as services. GST proposes to subsume most of the current indirect taxes like excise duty, service tax, VAT, etc. and a single tax would be levied called GST.

GST is expected to possibly eliminate, simplify and streamline multiple indirect tax regimes in India. GST is a single comprehensive tax that will be applicable across all States in India, hence, e-Commerce companies will not have to struggle with the complex regulatory structure. Moreover, sourcing, distribution and warehousing strategies that are currently designed by companies from the perspective of minimising the tax liability, will undergo a change. Going by this, it is expected that the e-Commerce companies stand to gain tremendously from GST.

Presently, the Constitutional Amendment Bill is passed by the Lower House of the Parliament and it is placed before the Upper House in order to empower Centre/ State Governments to roll out the GST law.

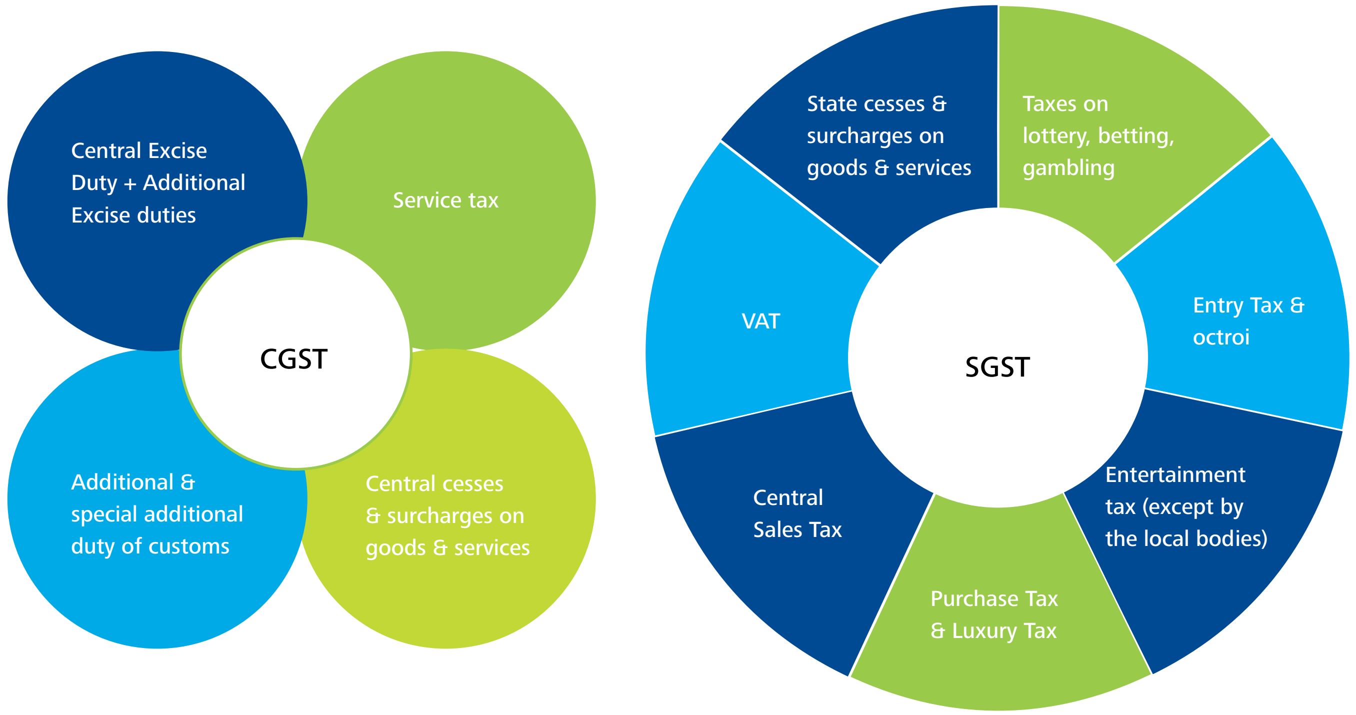


Figure 14. Taxes which are proposed to subsumed under GST regime

Forensic Landscape

Frauds pose a real threat to the financial health and reputation of organisations, whether large or small. The Association of Certified Fraud Examiners' 2016 Report to the Nations on Occupational Fraud and Abuse estimates the average loss due to fraud to be as much as 5 % of annual revenues, which globally translates to approximately USD 6.3 Billion.

The present economic climate, while fostering competition and growth, has also exposed organisations to fraud, misconduct and noncompliance. Given the mounting pressure on margins and the need for cost optimisation, losses due to fraudulence can significantly impact the profitability of organizations, in particular in emerging industries such as e-Commerce.

In case of e-Commerce businesses, the inherent nature of complex business operations, sophisticated use of technology, reliance on multiple stakeholders and third parties, and limited sector-focused regulation, have made e-Commerce businesses susceptible to the risk of fraudulence all the more.

An indicative list of fraud risks faced by the e-Commerce industry is enumerated:

"As digital technology advances, e-Commerce companies need to think beyond the fundamentals in order to compete successfully. Fraud risk needs to be recognized as a key concern and comprehensive fraud risk management processes need to support all activities within the life cycle of the business, in order to mitigate the risk (of fraud) effectively. The focus needs to be on building a cohesive and consistent approach addressing emerging issues such as data privacy, compliance protocols on sellers, training and awareness standards; to name a few."

Rohit Mahajan,
APAC Leader, Partner and Head,
Forensic – Financial Advisory, Deloitte India

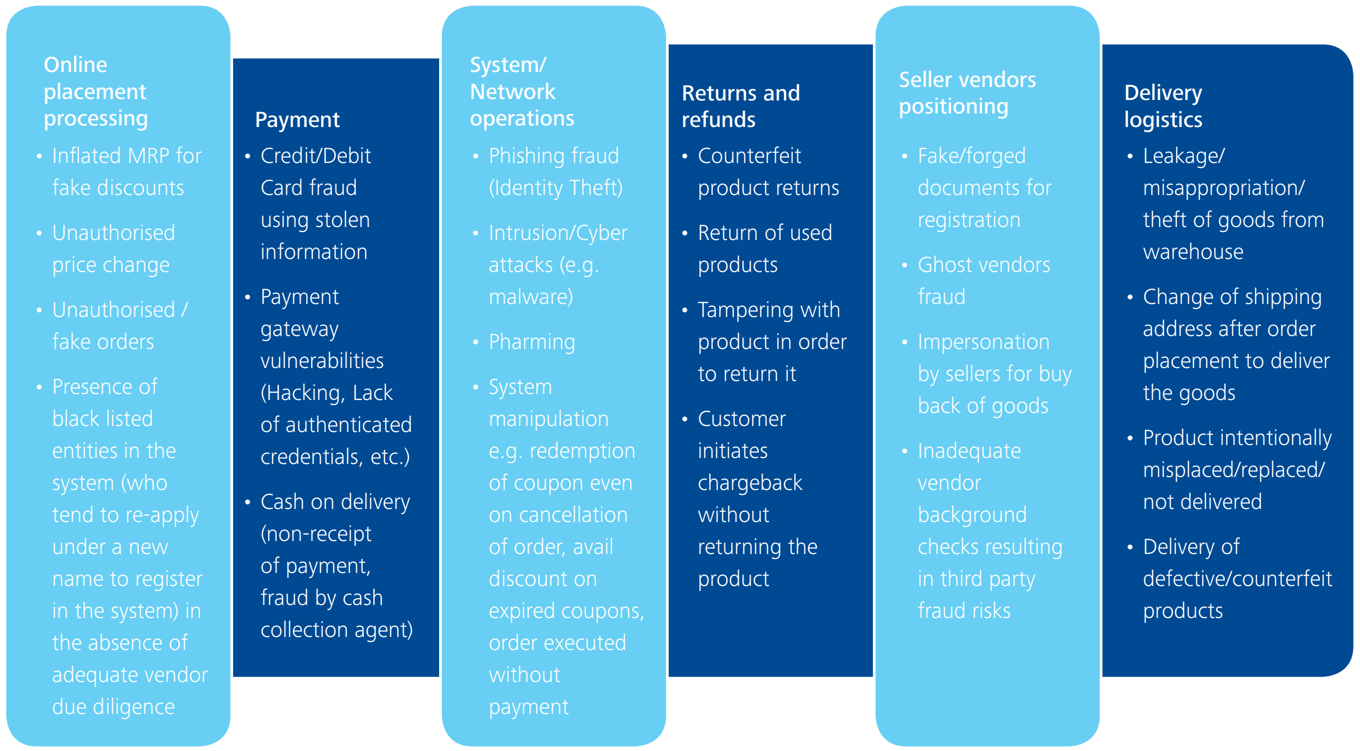


Figure 15. Fraud risks involved in the e-Commerce Industry

Regulatory Landscape

Under the FDI policy, different caps and conditions are provided for different categories of trading viz. wholesale trading, single brand retail trading and multi-brand retail trading. Within these guidelines, the e-Commerce activities are carved out and treated differently.

Further clarity on the existing policy has been provided through guidelines by DIPP in the circular released on 29th March, 2016. The recognition of the online marketplace model and permissibility of FDI in such cases are certainly welcome clarifications. Broad regulatory framework for e-Commerce in India as per the above mentioned circular is:

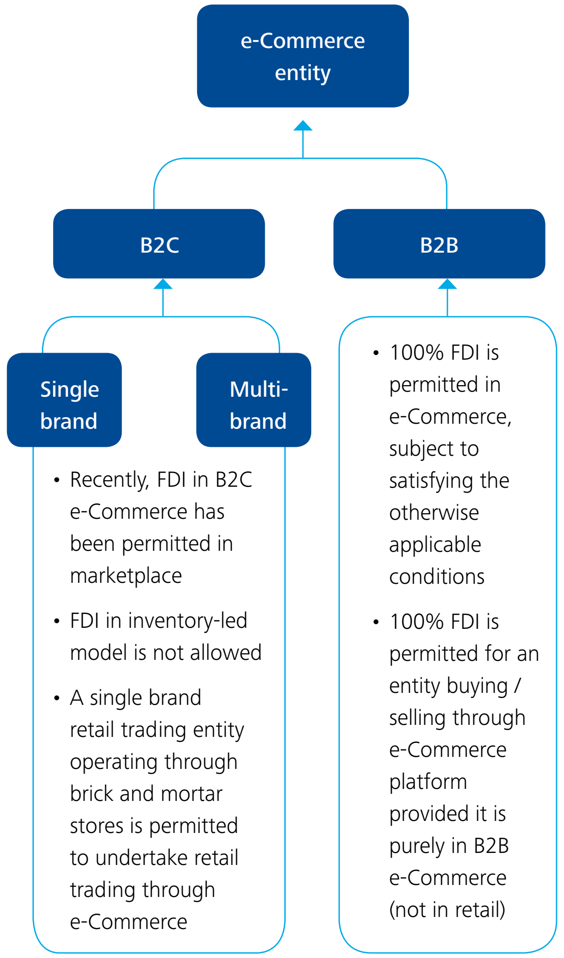
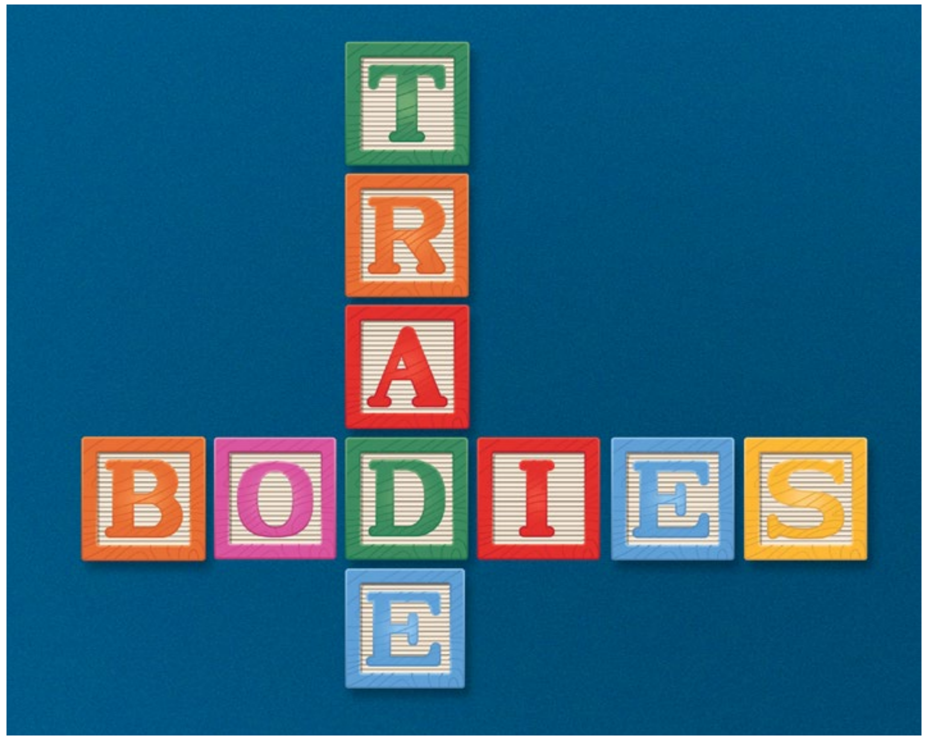


Figure 16. Regulatory Framework for e-Commerce in India

Guideline	Impact
Definition for e-Commerce entity – DIPP has clearly defined "marketplace" and "inventory" based models of e-Commerce	• Existing e-commerce companies will have to re-look at their business models to ensure compliance with the guidelines issued. It would help in bringing certainty to exposure had in the past
100% FDI is allowed in the marketplace model via the automatic route	• Owing to certainty with regard to FDI in e-Commerce marketplace and conditions to be fulfilled, foreign companies will be more open to investing in Indian e-Commerce marketplace
100% FDI is permitted in B2B	• There have been no amendments in this area and the Government continues to support and allow FDI in B2B e-Commerce
B2C e-Commerce marketplace model cannot influence sale price	• Reduce heavy discounting that was used previously • Create a level playing field between offline and online sellers • Pricing decision will rest on seller
e-Commerce entity will not permit more than 25% of the sale from its marketplace model from one vendor or their group companies	• Currently many e-Commerce companies are depending on sellers that contribute at times greater than 40-50% of their sale. They will now have to restructure the sales process to look at options such as on-boarding multiple merchants to ensure the 25% threshold
In marketplace model goods/services made available for sale electronically on website should clearly provide the name, address and other contact details of the seller	• The entire onus of quality and originality of goods delivered rests on the seller • Customers are empowered to reach out to sellers directly in case of faulty delivery
The post sales, delivery of goods, customer satisfaction, warrant/ guarantee of goods and services sold will be responsibility of the seller	• Brings clarity on responsibility of counterfeits, after sales - services, warranty, guarantee, etc. on e-Commerce platforms • The e-Commerce marketplace model may provide support services to sellers with respect of warehousing, logistics, order fulfilment, call centre, payment collection and other services. However, primary responsibility remains with the seller
FDI in not permitted in inventory based model of e-Commerce	• Provides a level playing field for large offline retailers

Additionally, in a notification issued by the Directorate General of Foreign Trade (Ministry of Commerce and Industry) dated 11th April, 2016 - the definition of e-Commerce with respect to Foreign Trade and export of goods via e-Commerce platforms has been clearly articulated. This indicates that the Government of India is aware of the power of e-Commerce and is attempting to foster a favourable regulatory framework to facilitate exports leveraging the e-Commerce industry.

VI. Role of Trade Bodies



Given the complexities and dynamic environment in the e-Commerce ecosystem, active participation of all stakeholders is critical. The Industry Trade Bodies collectively represent the interest of all stakeholders in the ecosystem. B2B and B2C e-Commerce industry sell varied products from different sectors which requires an active and collaborated participation of Trade Bodies to shape a conducive framework in India.

The Trade Bodies as a catalyst through:

Industry representation

Trade Bodies represent interest of all members, consumers and sellers. They create a significant impact in the industry by increasing transparency and efficiency amongst different members

Ensuring level playing field

By representing both offline and online companies, Trade Bodies play a huge role in ensuring a level playing field in doing business for all

Empowering and enabling the ecosystem

Trade Bodies support the ecosystem in ways such as encouraging healthy competition, availability of skilled manpower, driving adoption of new technologies and continuous awareness and education on global trends and best practices to its members

Assisting manufacturers, MSMEs

Manufacturers and MSMEs find support and guidance from Trade Bodies in adoption of technology, use of new-age payment mechanisms, and access to capital and migration to online platforms

Facilitator and solution provider

In the event of industries facing challenging situations Trade Bodies play a primary role to arrive at a feasible and conducive solution framework through a consultative approach with all stakeholders

VII. Challenges faced by major stakeholders

Broad overview of challenges faced in the B2C e-Commerce ecosystem

Key Challenges	
Scaling of organizations and profitability	• B2C e-Commerce companies have raised and infused capital from investors to scale operations. However, from a profitability perspective, the losses have grown faster than sales. Majority of the companies rely on discounting for customer acquisition leading to an absence of long-term sustainable business models
Tax framework	• Due to the absence of a uniform tax structure, States have adopted different tax frameworks and Inter-State goods movement is a challenge. It not only increases operational and compliance costs but also delays timely delivery of goods
Counterfeit goods	• There is an increasing incidence of cyber thefts and payment thefts in the industry today. Additionally, supply of fake, counterfeit products by the merchants on the platform are on a rise

Broad overview of challenges faced in the B2B e-Commerce ecosystem

Key Challenges	
Highly technical barriers to market entry	• The B2B e-Commerce ecosystem currently is highly fragmented with fewer companies due to factors such as the requirement of domain expertise, detailed knowledge of product features and specifications.
Lack of robust technology integration	• Users are likely to be using standalone systems prior to adopting B2B e-Commerce for handling inventory and orders. Integrating existing systems with B2B e-Commerce is critical, but is usually not implemented efficiently for sharing information and selling online
High costs associated with complex logistics fulfilment	• The challenge in delivering orders quickly and efficiently often depends on size, scale and location that demands the use of specialist freight services increasing cost considerably.
Long customer acquisition process	• Impulse purchase is less likely to happen in B2B e-Commerce, owing to the bulk nature of orders, and slow decision making process. This makes the customer acquisition process longer.
Rigid Procurement Processes in Large Corporates	• Large corporates have stringent procurement and approval processes for buying goods in bulk which restricts the procurement teams to buy on B2B e-Commerce platforms
Lack of level-playing field	• There is a lack of level-playing field for doing B2B e-Commerce business as compared to a traditional B2B offline business establishment

Challenges faced by key stakeholders

Platform owners – B2C

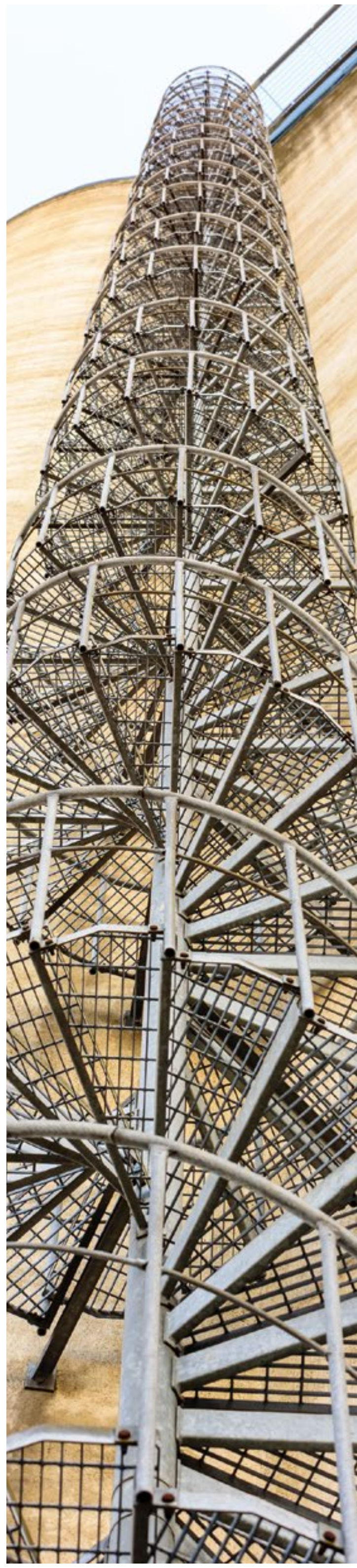
Key Challenges	
Cash on Delivery (CoD) as a mode of payment	• Customer's preference for CoD increases chances of return and results in locking up of working capital for both the platform and the sellers.
Network and bandwidth dependency	• Access to e-Commerce platforms, through desktops, mobiles, and other devices are dependent on the network bandwidth
Merchant's lack of online experience	• Small merchants are uncomfortable and unfamiliar with technology and need to be trained on the use of e-Commerce technology
Digital payment transaction failure	• Due to lack of high-speed bandwidth and inefficacies in payment gateway technology, the e-Commerce industry is facing high transactions failure rates leading to customers dissonance
Dependence on Telecom Operators for rural penetration Navigating Procurement Process of companies	• E-Commerce companies, who want to expand into tier 2 & 3 cities, are dependent on the Telecom Operators to roll out 3G/4G into such areas for connectivity
Reverse logistics	• Currently, reverse logistics is highly inefficient, which results in high inventory and increased costs
Lack of customer loyalty	• Currently customers are mainly attracted through discounts and have very little brand loyalty. Customers easily and frequently switch among platforms based on best discount offered by them.
High cost of customer acquisition	• Intense competition and heavy discounting has resulted customer acquisition and retention costly for e-Commerce companies.

B2C Aggregators

Key Challenges	
Dependence on Network and bandwidth	• Lack of coverage and network congestion, especially in tier 2 & 3 cities, leads to incomplete transactions
Regulatory challenge	• B2C aggregators like taxi-hailing category have faced business suspension in many states due to lack of definition in the regulatory framework
Cash on Delivery (CoD) as a mode of payment	• Indian consumers prefer paying in cash as opposed to using digital payments resulting into cash handling risks as well as locking up of working capital
Dependence on multiple entities	• The e-Commerce aggregator model is heavily dependent on multiple technological integrations and data dependency with several entities, both online as well as offline.
Lack of high-skilled manpower	• There is a scarcity of skilled human resources who have expertise in the area of analysing consumer data, study user patterns, analytics, algorithms, simple interface, machine learning, and rules/laws of online platforms

Micro, Small and Medium Enterprises - Merchants

Key Challenges	
Unskilled staff	• MSMEs typically cannot afford high-skilled staff to mandate e-Commerce operations such as product upload, online marketing, shipment and after-sales service
Lack of expertise in peripheral activities	• As the merchants move to online channels, they lack expertise in peripheral activities where they seek the support of e-Commerce platforms and logistics partners such as managing inventory, handling invoicing and providing consumer insights
Technology integration and perception gap	• Merchants are not well versed with e-Commerce technology frameworks and business operations • Merchants also have the perception that offline recovery is faster than online recovery. • Small merchants fear that their transactions will fall in audit trail
Lack of training	• Lack of training for doing e-Commerce transactions is a critical roadblock for the migration to online platforms
Differential delivery rates charged by different platforms; inadequate coverage of platforms or their delivery partners	• Merchants have to deal with different rate cards with different platforms, which becomes an operational challenge • Merchants also have to deal with multiple platforms as often one platform might not adequately cover the areas as per their requirement.
Higher "Returns" due to Cash on Delivery (CoD)	• Higher "Returns" due to CoD; all add up to logistics costs of SMEs • Returns of goods alone account for an estimated loss in the range of 5% on the MRP of goods sold, with a typical rate of return of goods of 15-20% expected by platform owners
High cost of finance	• Access to finance is difficult from banking due to lack of collaterals and stringent documentation requirements • Cost of finance increases due to high interest costs on working capital
Mobile apps by platforms	• There is an increasing focus on mobile applications which gives an advantage to big merchants who can afford the cost of developing a mobile app, something smaller merchants find much harder to do.



C2C e-Commerce (Carpooling)

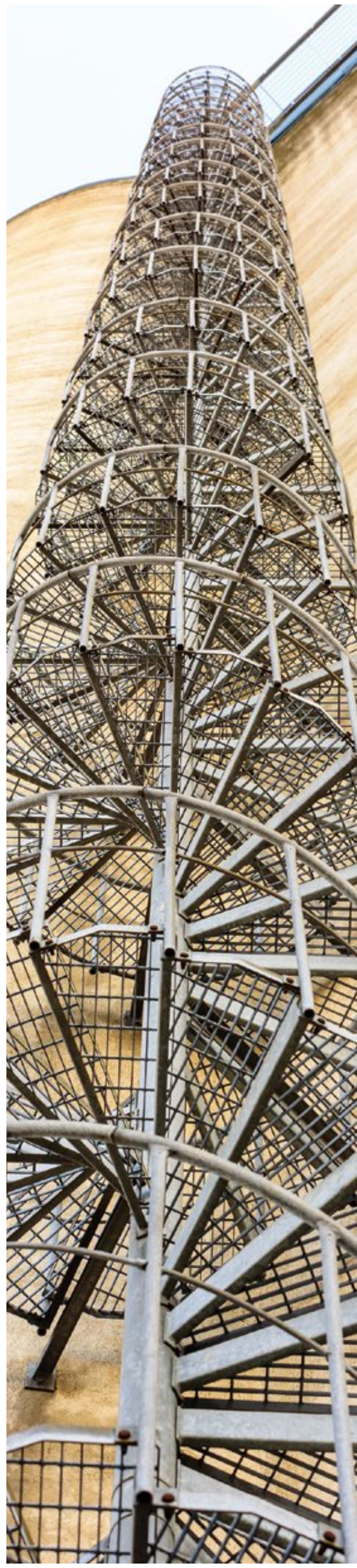
Key Challenges	
'Shortage of Supply'	• Globally, even in the most mature markets, the carpooling industry still lacks best practices • The carpooling industry in India is a new and evolving one. It faces massive 'shortages of supply' due to low penetration rates of cars in India (3 in 100 people own a car) as well as a mistrust of carpooling with only a few people offering rides.
Acceptance of "ride sharing" as a game changer	• Globally, this concept is seen as a game changer. However, In India, there isn't widespread acceptance of "Ride Sharing" yet due to lack of incentive being offered by Government or socially responsible corporate citizens in sustainable urban mobility

Platform Owners – B2B

Key Challenges	
Unorganised	• Almost 95% of the B2B market is unorganised and dominated by local vendors/mom –and-pop shops. Lack of education on the use of technologies among customers (to buy) and sellers (to list) put sellers at a disadvantage as they do not have access to buyers via the internet. Furthermore, small sellers are unable to scale up and sell to multinationals at competitive prices compared to those of bigger producers. Critical feedback for these small sellers to improve operations is also lost by remaining offline.
Preference for credit	• Historically "Credit" is a preferred mode of payment in offline B2B transactions where payment in offline trade is made 30 days after receipt of goods. In B2B e-Commerce however, payment will have to be made upfront. At the most CoD will be accepted.
Nomination for Public Sector Enterprise (PSE)	• Currently there is a lack of a transparent and efficient competitive bidding route to choose the PSEs. It restricts the Public Sector entity or the Public Exchequer from getting the best options for service providers

Logistics Service Providers (LSP)

Key Challenges	
Internet's accessibility and affordability	• Bottlenecks of Internet accessibility and affordability specially for last-mile delivery in remote areas
Poor infrastructure	• Poor infrastructure (roads) sometimes forces logistics service providers to take longer routes. Logistics service providers will also need to improve surface transportation capabilities via both, road and railway, across various geographies to create more opportunities and avenues for the growth of the sector
Railways don't allow partial usage of containers	• Presently logistics service providers are forced to lease full containers as railways don't allow partial usage of containers which does not justify costs due to lack of volumes
Air cargo not established	• Air cargo in India is not as established as compared to it in developed countries, and thus restricts the options of logistics service providers
Cash on Delivery	• Cash on Delivery (CoD) orders is a challenge for most delivery partners. Handling CoD capacities will be critical in driving volumes for e-Commerce companies, especially within the B2C segment
Reverse Logistics	• Platform owners providing reverse logistics increase the cost of delivery and operational efficiencies for the logistic providers
Geographical reach and coverage	• LSPs are not able to cater to tier 2 & 3 cities and rural areas due to infrastructure challenges and high delivery costs
Track and Trace coverage	• Logistics service providers earlier faced a problem with respect to delivery information not reaching the sender due to lack of GPS tracking. Although presently it has been made possible for as many as 25,000 pin codes for the largest logistics service provider, tracking within hinterlands still is a challenge. In some regions in the North East of India, it still takes 3-4 days to receive a status update on a delivery. Handheld devices that are solar powered are now being looked at to tackle this problem
Skilled manpower for "Delivery" and "Sales"	• The erstwhile delivery boy's role has evolved. He now wears multiple hats, including that of a sales boy, but isn't trained for the job. The e-Commerce companies struggle to recruit skilled manpower for "Delivery" and "Sales"
Long waiting times at border check posts	• Long waiting times at border check posts for stock transfers of multiple shipments can be a problem when entire consignments are held back due to certain non-compliances. This impacts the customer experience of many other stakeholders
Scaling up handling capacity	• As volume of deliveries scale up to a few hundred thousand parcels daily for logistics service providers, logistics service providers are faced with a challenge of scaling up handling capacities (collection centres, movement, scanning) within very short time frames
Cost of hardware	• Cost of handheld devices and other peripheries for fulfilment is high and hinders the rapid growth of this industry



Policy Makers

Key Challenges	
Lack of skilled manpower	• The Government ecosystem lacks technologically proficient manpower who have a deep understanding of e-Commerce business operations
Regulatory framework	• e-Commerce lacks guidelines, operational framework and policy in areas such as tax structures, broad policy recommendations, vigilance, overall governance etc.
Differentiate between local goods and inter-state goods	• A daunting task for state governments today is to differentiate between local goods and inter-state goods, especially the ones sent by parcel or speed-post. As record/registration (via TIN) of the movement of these goods is done voluntarily by suppliers, there exists a possibility of tax leakage, a significant cost to state tax authorities
Tax evasion	• Fraudulent activities adopted by few merchants in fake registrations, and fictitious activities etc. lead to difficulties in audit trail and tax collection
Inter-linkages of Government departments and agencies	• Several government departments and agencies operate in silos, which leads to lack of uniform policy recommendation and implementation challenges
Lack of digitisation	• Several government departments are not digitised and still operate on paper
	• Cost of implementation of digital technology is too high and there is resistance to upgradation from the obsolete ones
Integration of National borders	• National borders too are not integrated. For instance, the "Indo-Nepal" border doesn't have the "IceGate Facility" (Customs E-payment gateway) to file documents
Tracking road and rail transport	• Transportation on road and rail, along with border crossing, payment of toll, octroi etc., is not tracked, making e-commerce transactions inefficient. A robust transportation system is crucial for the e-Commerce industry to thrive
Price regulation and quality control	• Price regulation and quality control of core commodities such as coal are some other challenges faced by the Central Government that has a direct impact on the B2B e-Commerce industry

Direct Tax – Challenges faced by e-Commerce companies

Applicability of withholding tax:

e-Commerce company as a payer

Applicability of withholding tax is a critical issue for e-Commerce companies, given their need of various online services and hi-tech facilities. However, a number of issues crop up in this regard.

• To begin with, characterisation of payments is a contentious issue. Some guidance is available from judicial precedents. However, as courts in different jurisdictions have taken differing views on certain matters, only limited support can be drawn

• In cases where the commercial terms agreed upon require the Indian payer to bear any Indian withholding tax cost that may arise on payments to non-residents, the cost burden on the payers is greatly increased if taxes are withheld on a conservative basis

• In many such cases, the payees are not forthcoming with documentation (such as tax residency certificates) or fulfilling other conditions (such as obtaining Permanent Account Number) to enable the payer to apply a lower rate of withholding tax or a nil rate based on the relevant tax treaty provisions

• Further, there is a strong push back from the payees if the Indian payers apply an interpretation which is different from those set out in international commentaries

• If, based on judicial precedents and guidance from international commentary, taxes are not withheld, often, the matter is required to be litigated on several fronts including disallowance of expenses and levy of penalty. Such disputes emerge because the issues are extremely fact-specific

e-Commerce company as a payee

Difficulty is also faced on the other side, i.e. in respect of service fee/commission received by the e-Commerce companies in India.

Most e-Commerce companies incur significant losses in the initial years of their operations. Thus, typically, no tax is payable by them, until they become profitable and unutilised tax losses are offset against such profits

• If taxes are withheld from payments to these e-Commerce companies, cash-flow issues arise due to the time taken in obtaining refunds.

• The other alternative to e-Commerce companies obtaining lower/nil withholding certificates has its own challenges:

o The payee is required to furnish information regarding proposed payers, such that the certificates can be issued individually to each payer. This poses a practical difficulty for the e-Commerce companies who transact with numerous payers. Further, due to the dynamic nature of business, the payers may not be known or identified at the time of making the application at the start of the financial year.

o Also, a certificate is typically valid from the date of issuance till the end of the relevant financial year. In such a scenario, the period between making the application and issuance of the certificate is not covered, and therefore, withholding tax triggers on income of this period. This results in blockage of funds to the extent taxes are withheld.

Lapsing of business losses:

In case of a closely held company, the tax law[17] prohibits carry-forward of business losses for set off against future years' profits if the shareholding of the company changes by more than 49%. The e-Commerce companies are liable to be adversely impacted by these restrictions.

• e-Commerce companies usually incur sizeable losses in their initial years of operation.

• Further, there is a pressing need for additional capital to sustain and grow the scale of operations.

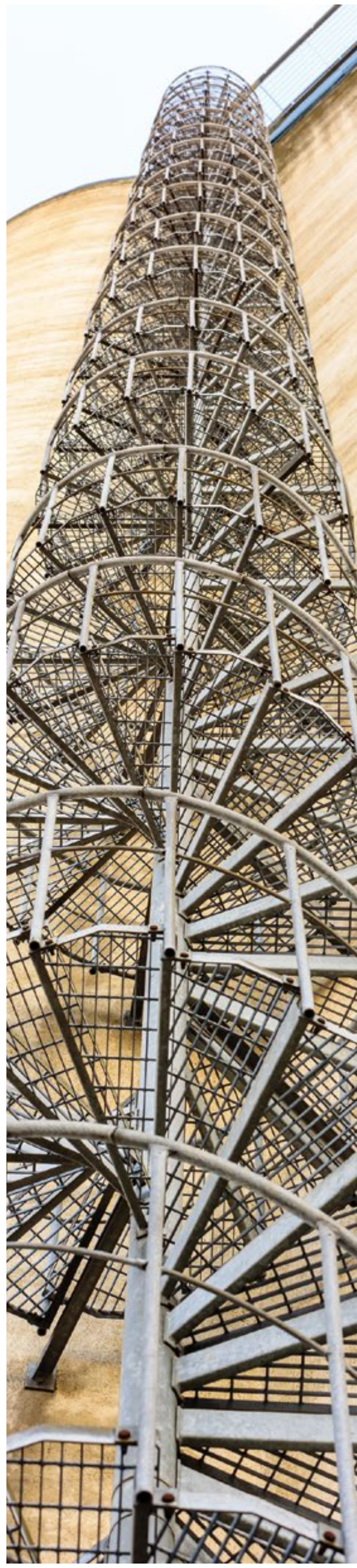
• As a result, private equity funds and other investors are approached for meeting funding requirements.

• With every round of additional funding, the shareholding of the initial shareholders (founders) would be diluted.

• If their shareholding falls below 51%, business losses incurred by the company in the initial years would lapse, whereas, the change in shareholding is only due to compelling needs of the business.

Likely ineffectiveness of proposed tax incentive to start-ups:

The tax incentives proposed in Finance Bill, 2016 with regards to tax holiday for start-ups may not prove useful to e-Commerce companies since they generally report loss in their initial years.



Indirect Tax – Challenges faced by e-Commerce companies

Challenges in characterisation of e-Commerce models by State VAT authorities

• Broadly, there are two types of business models adopted by an e-Commerce company:
a) Stock and sale model
b) Platform for market place

• Under the market place model, an e-Commerce company generally acts as a facilitator for providing platform for buyer and seller to interact and execute the sale transaction. The e-Commerce company only gets a fees/commission for providing the said facilitation services to the sellers on which service tax is paid. VAT on sale of goods is paid by the actual seller registered on such e-Commerce companies.

• Many e-Commerce companies also provide fulfilment services to these sellers, under which goods belonging to the sellers are stored in the warehouses owned by the e-Commerce companies and are delivered from these warehouses to the buyers. Under this model, the e-Commerce companies do not hold any ownership of the goods belonging to the seller stored at their warehouse. However, several state VAT authorities, being unable to appreciate the essence of the arrangement and, hence, direct e-Commerce companies to obtain registration and comply with VAT regulations treating such e-Commerce companies as consignment agent or C&F agent within the state with respect to goods stored/ sold in the warehouse of e-Commerce companies.

Characterization as intra-state or inter-state supply of goods

• In case of inter-state sales, CST is levied in the state from which goods commence/originate their movement. Given the pan-India presence of e-Commerce companies, sometimes the goods are delivered in a state different from the originating state. The states where the e-Commerce consignments are delivered often have been off-late seeking tax on that sale, alleging that the appropriation has happened in the destination state.

• VAT authorities are scrutinising the logistic model followed for final distribution of goods and are making a case that the activity should be treated as stock transfer and not CST sales.

• Such uncertainty with respect to actual treatment of sales as inter-state or intra-state is a significant business risk.

Taxability of digital content and other activities

• Currently, there is a clear demarcation between taxation of goods and services. VAT is applicable on sale of goods, while service tax applies to provision of services. However, in the context of e-Commerce, which deals in sale of digitised products also, there is a greater challenge in defining these digital articles into 'goods' or 'services'.

• This situation worsens in the case of digital downloads like music, e-books etc. wherein it becomes challenging to determine whether the transaction is for sale of goods or a provision of service. This sometimes leads to double taxation in order to avoid disputes from either of the authorities.

• The aforesaid ambiguity has created a significant challenge in classifying the material sold as 'goods' or 'services', especially for electronic downloads like e-books, wallpaper, ringtones, music, movie clips etc.

• If the material sold are classified as goods, then same shall be subject to VAT, and if these are classified as services, then service tax is applicable.

• Such ambiguity related to goods versus services has not reached finality, and this raises potential risks from the tax authorities, which is also a significant business risk.

Registration of multiple vendors at marketplace warehouse/fulfilment centre

• Under the marketplace model, the e-Commerce companies are also engaged in fulfilment services, and goods belonging to multiple vendors are stocked in order to deliver the same to customers in minimum possible time. It is to be noted that these fulfilment services are provided by the e-Commerce companies mainly to save the time and logistics cost and is developed based on the customer preferences and market demand.

• The goods belonging to multiple vendors are stored based on the category of goods rather than vendor. However, with the help of advanced storage technology, the e-Commerce companies are able to recognise and differentiate the goods belonging to different vendor.

• Presently, storage of goods based on their category, and not vendor-wise, is not appreciated by most state VAT laws. Often the state VAT authorities insist on physical demarcation of warehouse space, creating a significant logistics challenge for the e-Commerce companies.

Compliance and Reporting

• Due to its wide reach across the country, the Indian e-Commerce industry is faced with challenging and burdensome compliance requirements.

• In addition to the requirements like obtaining various registrations and filing periodical VAT and other statistical returns, there are several considerations that are peculiar to this industry.

Statutory declarations, way bills and road permits for inter-state sale of goods

• As stated, the e-Commerce companies operate on a pan-India basis, involving inter-state movement of goods. Such inter-state movement of goods from one state to another has been challenging for the e-Commerce companies that are required to produce statutory declarations forms, way-bills, road-permits, transit forms etc. and quite often check-post interceptions at state borders.

• Besides, the recent requirement of separate local VAT/CST registration, filing of separate returns and declarations required by certain states under the VAT/ CST legislations for entry or sale of goods into the state have been hindering the free flow of goods as well as adding challenges in terms of managing compliances. Also, in many states, e-Commerce companies are made liable to furnish the details of sales made through their portal and also required to furnish periodic returns.

• Further, if the sales tax authorities contest that the e-Commerce company, which provides platform, is required to obtain VAT registration and pay VAT, it will not only handicap the functioning of the e-Commerce companies (usually operating in multiple states), but also paralyse the innovative and ever expanding medium by which the sellers are able to access and cater the needs of the unserved buyers spread across the country.

Imposition of entry tax on inter-state supply of goods is regressive

• Emergence of e-Commerce companies in India has resulted in centralisation of logistics and increase in end-user transaction on an inter-state basis. One of the key commitment of the e-Commerce company is to deliver the customer orders within committed timelines.

• This has resulted into loss of revenue for the destination states. Thus, the states have started to impose entry tax on goods bought online via e-Commerce companies. Further, entry tax laws, coupled with entry tax regulations such as check post etc., are resulting in delayed delivery of goods.

Place of supply rules for taxation of facilitation fees in GST

• The e-Commerce companies generally operate in a marketplace model wherein they earn income in the form of marketing fee, facilitation charges, etc. It is possible that income from marketing fee and facilitation charges are billed from separate premises. Such incomes, presently, are taxable under service tax. Under the GST regime, services are to be taxed by both centre and state authorities. The e-Commerce industry is apprehensive that multiple authorities taxing the same transaction could increase the complexities. Hence, the e-Commerce industry is expecting clarity/clear guidelines on this front.

Forensic – Challenges faced by e-Commerce companies

Based on discussions with various stakeholders in the e-Commerce industry, the significant fraud and governance concerns threatening the growth of the e-Commerce industry in India include counterfeiting, inadequate governance measures, and data security.

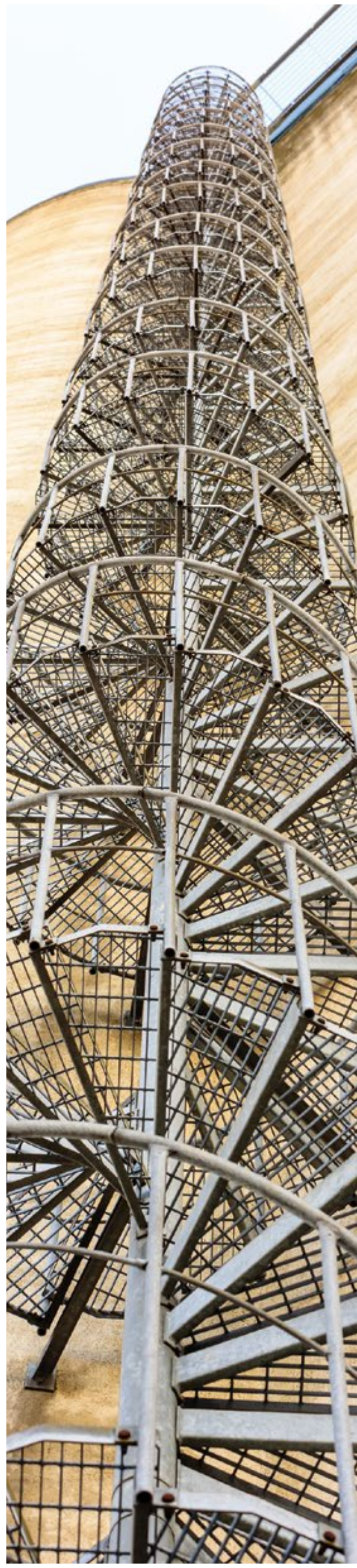
Counterfeiting

Significant dependence on sellers

• The e-Commerce platforms are increasingly being used for the distribution of banned and counterfeit goods, as observed by media reports in the last few years. This can typically happen when certain suppliers/distributors introduce counterfeit products in the supply chain alongside genuine products, making it difficult for the e-Commerce companies to detect counterfeits. Further, since the onus of ensuring product quality, authenticity and packaging compliance rests on the seller (having procured the goods), the e-Commerce companies, which act primarily as aggregators, are often unable to proactively detect counterfeits or inferior/faulty products that may be sold to customers via their networks.

Lack of a robust due diligence mechanism

• While some of the leading e-Commerce marketplaces may have already instituted Know Your Sellers (KYS) procedures to help identify unscrupulous sellers, it has been observed that the data sought from sellers as part of these procedures can be quite rudimentary. For instance, while PAN numbers may be sought from sellers, there is no process to ensure that duplicate PAN numbers do not exist in the seller database. Also, little information is collected (or due diligence carried out) pertaining to the credentials of the seller, such as market reputation, physical verification of the seller's premises, track record in ensuring product quality, litigation history, adverse media history, relationship check to indicate conflict of interest, political interests etc.



Lack of a mechanism to identify unscrupulous sellers

- There is currently absence of a trustworthy mechanism for a customer to authenticate sellers or the products sold by them on e-Commerce sites, since no independent offline verification of these aspects is carried out by the e-Commerce companies. Customers, therefore, are left to make a choice based on the seller ratings given by fellow customers (or in many cases fake reviewers).

Lack of a comprehensive law to address counterfeiting and associated enforcement actions

- It has been felt that one of the major issues leading to counterfeiting in the e-Commerce industry is lack of comprehensive law against counterfeiting, coupled with inadequate enforcement by regulators.

Inadequate governance measures

The limited fraud risk governance frameworks in the e-Commerce industry have resulted in the prevalence of well-known traditional fraud schemes such as procurement fraud, supply chain fraud, bribery and corruption. The industry stakeholders have observed the enumerated risks arising from inadequate governance measures:

- Misreporting/theft of inventory
- Failure to report damaged/expired inventory
- Unauthorised sale of products
- Kickback received from distributor/wholesaler for favourable contractual terms and annuity business
- Packaging frauds
- Unauthorised sale of free products/gifts

Data security

The volume of customer information present with e-Commerce companies, including purchasing patterns and other customer profiling information, can be a goldmine for fraudsters and competitors. Since some of this information tends to get shared with third parties, such as logistics providers who may be making home deliveries, it is difficult to exercise controls on how such data must be used and safeguarded. In such a scenario, it is easy for individuals (employees and third parties) to feel tempted to leak such information in return for money, goods or better job prospects. Additionally, lack of a specific data privacy law, along with Information Technology Act (IT Act) in its current form being broad in nature, does not provide clarity on what data is to be secured.

Regulatory – Challenges faced by e-Commerce companies

FDI in retail trading and particularly in e-Commerce has been a matter of great debate across the country. Different organisations and trade bodies/governments have had differing views on the subject.

The sector has largely been restricted to protect the numerous small companies who may not receive funding through FDI. However, there are views that FDI in e-Commerce for retail will also benefit MSMEs, who can receive funding from abroad.

The e-Commerce companies have largely been pressing for 100% FDI in retail trade (whether single brand or multi-brand), with no special restriction on transacting through e-Commerce. Through the recently released press note, the Government has taken a step in this direction by allowing FDI in e-Commerce for single brand retail trading in certain circumstances.

Further, some organisations are of the view that retail trade should be categorised by the item sold and not based on single/multi brand for the purpose of regulating FDI.

As the FDI policy did not explicitly refer to the marketplace model, there were concerns whether the same is recognised and FDI permitted for entities engaged in such models. This issue has recently been resolved by clarification through the press note.

Further, the press note has also defined the terms 'e-Commerce' and 'marketplace-based model of e-Commerce'. These definitions could bring up new questions for the e-Commerce companies on account of their potential interplay with definition/provisions under other laws.

There have also been concerns that the e-Commerce organisations functioning as online marketplaces are actively involved in activities closely linked to retailing and also in predatory pricing/offering discounts. However, the recent press note has clarified that the online marketplace companies with FDI can also engage in support activities such as warehousing, logistics, etc., however, they cannot influence pricing. The e-Commerce companies will have to analyse their existing operations to ensure conformity of their business model with the guidelines issued and evaluate the impact, if any.

VIII. Key digital imperatives for e-Commerce companies: Deloitte's Point of View

Continual innovation will help e-Commerce companies to remain disruptive towards building Exponential Organisations

To build sustainable and innovative legacy firms, e-Commerce companies need to aim to effuse a strong vision to build Exponential Organisations whose impact / output is disproportionately large -10 X larger- compared to their peers. Exponential Organizations are led by innovative imperatives and enablers such as digitisation, technology enablement, analytics, cloud-based solutions and mobilisation of services. They are characterized by 6 Ds: Digitised, Deceptive, Disruptive, Dematerialise, Demonetise and Democratise.

Exponential Organization's journey for an e-Commerce company to create disproportionate impact

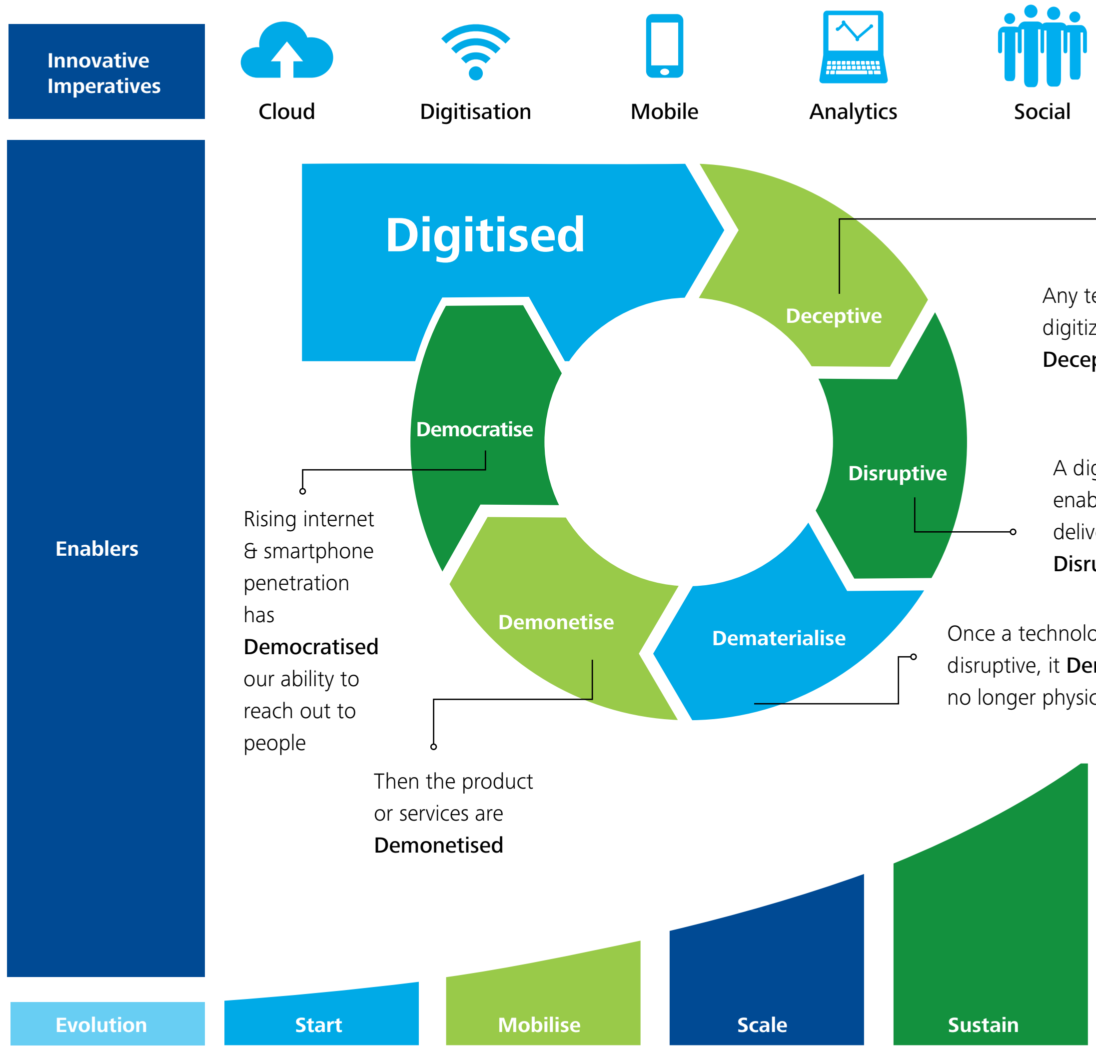


Figure 17. Journey of an Exponential Organization

Source: A Singularity University* book on "Exponential Organizations" by Salim Ismail, Michael S. Malone
Relationship: Deloitte is a thought leadership partner with Singularity University

In order to keep up with the pace that is set by the 6 Ds, e-Commerce companies need to be 'Exponential' in their thought process and thus need to be continually innovative, scalable, adaptive and technologically smart.

This will help the e-Commerce companies to build legacy firms with the aim to add value to the overall customer e-buying experience

Supply Chain Analytics

e-Commerce companies are dealing with multiple products moving across states and simultaneously are also managing a large number of merchants, delivery personnel and customers. The large volume of transactions, multiple moving parts coupled with a Pan India footprint makes the e-Commerce supply chain operations significantly complex keeping the Infrastructure and Regulatory constraints in perspective.

To drive cost optimal efficiency in the Supply Chain, e-Commerce companies need to leverage supply chain analytics to facilitate decision making across all levels of supply chain and use visualization and optimization tools to control, measure, and respond to supply chain events in real-time. These can result in improvements in both, the Profit & Loss and the Balance Sheet performance for an e-Commerce company.

Key features of a supply chain analytics framework:

- Supports live visibility of day-to-day operations through exception management and triggers actions to respond to supply chain events
- Enables performance tracking through KPIs (Key Performance Indicators) and helps in understanding performance trend
- Supports root cause analysis and facilitates a deep dive into the key drivers of a problem
- Enables scenario planning to understand the impact of any improvement across supply chain

Merchant Life-cycle Management

Merchants are key partners in an e-Commerce business and the brand reputation of an e-Commerce company rests on its merchants as much as on its employees. Thus, merchant on-boarding and life-cycle management is critical, given the large number of merchants associated with any online platform. Quality and delivery standards have to be maintained consistently across merchants, else an e-Commerce company runs the risk of brand dilution in a fiercely competitive market.

However, managing such a large number of merchants manually can become a challenge. Digitisation holds the key to navigate these challenges as also to enhance customer experience, brand loyalty, and cost optimization.

Benefits of merchant life-cycle management:

- Combines basic forensic and supply chain skills, technology and analytics to not only build a robust supply chain but to also nurture all partner relationships
- Enables a comprehensive merchant due-diligence process
- Makes the on-boarding process smoother and faster
- Helps evaluate best practices followed by merchants
- Ensures performance tracking against Service Level Agreements (SLAs)
- Merchant Scoring Analytics Platform (MSAP) tool tracks and provides information on a merchant's likely credit risk through ongoing monitoring, back testing, stress testing, benchmarking and statistical analysis

Recommendation Engine

A customer's experience can either make or break an e-Commerce platform (website or apps). In addition to providing a visual appeal and convenience, these platforms attempt to provide value-add to a customer through product recommendations.

To deliver a sophisticated e-Commerce service model, a powerful analytics solution that integrates and analyses portal-generated data is required. This integration enables a recommendation engine to provide smart, real-time and relevant recommendations to customers. Along with recommendations for products, sophisticated algorithms that change prices in response to delivery time, weather and market conditions are required. These have the potential to fundamentally change the way businesses work and also what customers pay. They bring in price transparency, boost supply during peak hours and also ensure standardised policies for pricing.

Key features of recommendation engine analytics:

- Provides customer-specific personalized recommendations based on web behavioural analysis
- Recommends customised complementary and alternative products, as the customer browses the site
- Sends targeted promotions and offers to the customer offline
- Helps in keeping customers on the website for a longer time thus increasing the likelihood of a purchase and thus supporting the growth in sales

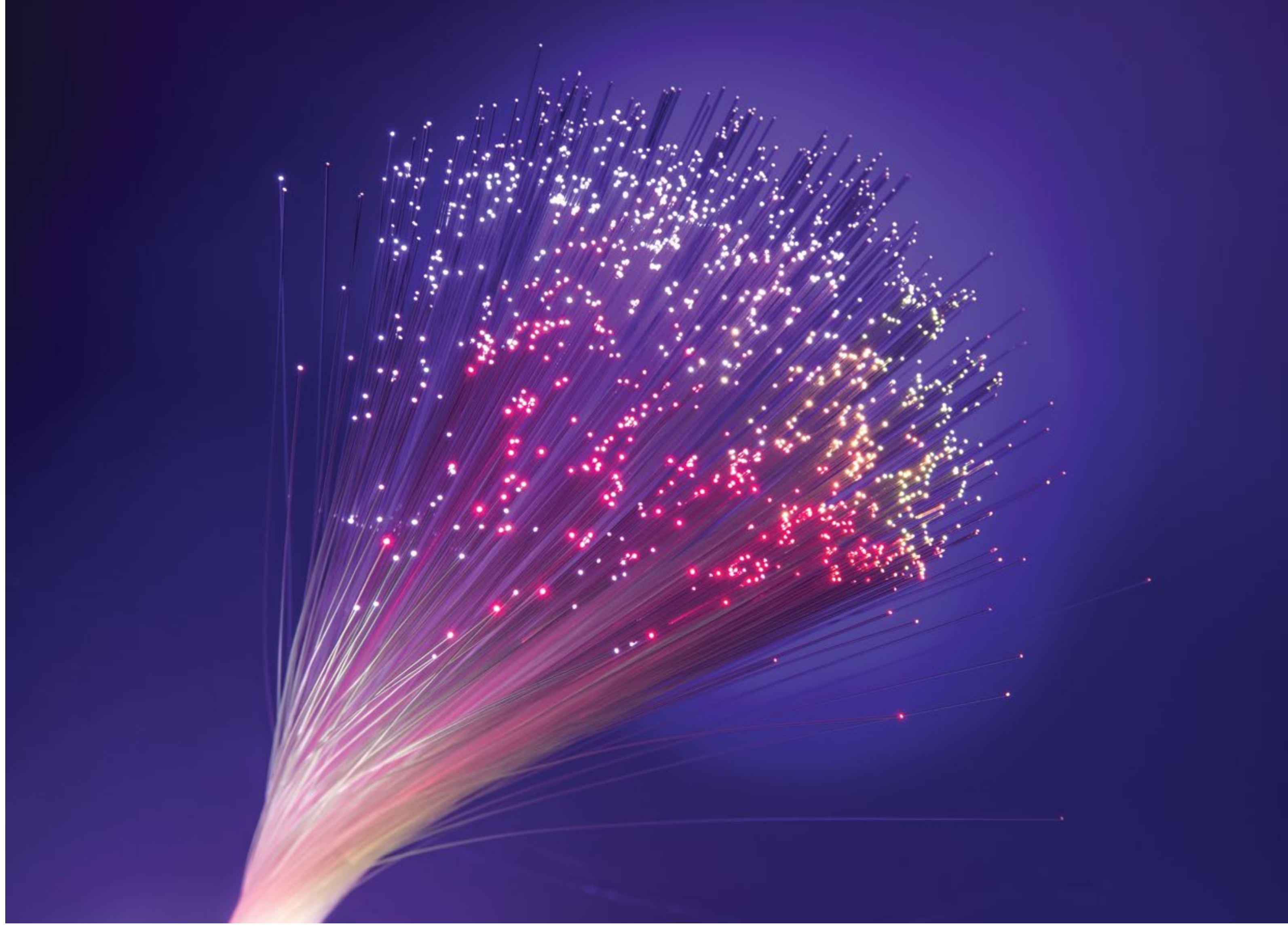
Integrated Business Planning

With focus for e-Commerce companies moving to profitability, optimization of business processes is becoming imperative. There are several challenges such as lack of intra business unit coordination, high logistics costs, complex inventory issues, etc. which surface in this ever-evolving industry.

To stitch together the different operations and decision making elements within an e-Commerce organisation, an integrated business and financial plan is required. Integrated Business Planning enhances a traditional Sales & Operating Plan by focusing on end-to-end decision making and drive a unified go-to-market plan.

Key features of Integrated Business Planning:

- Provides Executive Reviews and Financial Planning (FP&A) for one integrated review and decision making process
- Integrates forecasts, product launches, promotions, and market sensing in development of consensus demand
- Includes optimal inventory positioning as a key de-coupler between production and demand



Digital HR

e-Commerce is changing the talent ecosystem in the country, which in turn has impacted the human resource function. Considerable time and effort has to be invested to hire and train young dynamic talent, manage high turnaround due to fierce competition, and frequent leadership level movements.

The Digital HR solution will enable e-Commerce companies to drive innovation, process efficiency and take care of their most important asset i.e. their people. It will reduce redundancies within the human resource function and help reallocate resources to more strategic initiatives within an organization. The solution will reimagine the role of HR, simplify life of the Overwhelmed Employee and reduce cost.

Key benefits of Digital HR management:

- Manage and control the dynamic changes or adopting new ways of working
- Aligning culture between parent organization and its subsidiary
- Expanding operations across multiple business units or growing rapidly with the desire of maintaining its cultural DNA
- Undertaking M&A, divestures and amalgamation and ascertain its implication to the organization
- Assist and support embarking on large digital / technology transformation
- Manage the talent challenges around quality of talent, leadership and retention

IX. Key Recommendations

Government's Role and Participation

Increase internet penetration

At the heart of the e-Commerce lies the ability to not just stay connected online but also to do so at a fast speed. India ranks relatively lower when compared to its Asian counterparts, the U.S. and China in respect to Internet speed. Additionally, many parts of rural India are yet to receive broadband connection. While efforts have been made in this direction, the Government plans to facilitate Internet connectivity for over two lakh Gram Panchayats. PPP (Public Private Partnership) projects in this space would become instrumental in enhancing the reach of the Internet to rural parts of India.

Seamless integration between Government departments and agencies

An integrated and coordinated approach is much needed between different government agencies, such as Policy-makers, Income Tax, Sales Tax, Direct Tax, Excise, and Registrar of Companies, to ensure faster turnaround, efficiency and transparency for all stakeholders in the e-Commerce ecosystem.

With instances where one state is levying a flat entry tax on all e-Commerce consignments and another state barring taxi-hailing companies from dynamic surge pricing, the Government is likely to limit the business models of e-Commerce players. The Government should ensure a uniform regulatory and tax structure across the states to prevent such instances from dampening the growth of e-Commerce in India.

Faster implementation of initiatives

The Government has already launched several initiatives such as Digital India, Skill India, Innovation Fund, and Start-up India. However, the success of these initiatives lies in speedy and result-oriented implementation. Thus, faster implementation of these initiatives would have a positive impact on the e-Commerce industry.

Build a conducive environment

A consultative approach with periodic interactions with all stakeholders, Trade Bodies and industry associations such as CII, will help in building a uniform and favourable e-Commerce ecosystem. Government should provide a level-playing field for Public and Private Sector Enterprises as well as all models of e-Commerce platforms.

Training and Skill development

e-Commerce has already become an attractive destination for budding entrepreneurs and MSMEs. This has generated both, blue-collar and white-collar employment opportunities in India. Further, functions such as logistics, analytics, pricing, inventory management, transportation, last-mile delivery etc. are unique and highly specialized. Lack of skilled manpower in these areas is one of the bottlenecks faced by the e-Commerce industry. To address this challenge, joint programmes by the private and government sector would be instrumental to ensure a steady flow of trained talent who have the ability to quickly adapt to the dynamic growth phases experienced by this industry.

Towards institutionalizing this recommendation, strategic alignment between the Central and State government is imperative to strengthen this talent development initiative. For example, e-Commerce private players could feed into the Skill India initiative of the Government to make it more industry relevant while the State governments identify potential talent pockets in their area of influence to feed the raw potential into this programme.

Follow a procurement process to appoint Public Sector Enterprises (PSEs)

A process whereby PSEs and Private Sectors Companies are selected using bids or tenders to ensure that the Public Sector and the Public Exchequers get the best service possible should be enforced. This will benefit the B2B e-Commerce companies.

Create customer and sellers scoring database

A consultative approach with participation from all stakeholders in the e-Commerce industry should be encouraged to come up with a scoring database of customers and sellers. Stakeholders should determine key scoring parameters based on previous online shopping behaviour for buyers. Similarly, scoring can be assigned to merchants based on their quality of products delivered, etc. The scoring mechanism will discourage the abuse and fraud instances from both buyers and sellers.

Empowerment of Logistics Ecosystem

Develop a robust infrastructure

India needs a deeper and wider network through efficiencies in road, rail, sea and air transportation. Better road connectivity, shorter turnaround time at sea ports; and a resilient railway service ecosystem will enhance fulfilment and last-mile deliveries for e-Commerce.

Enable sharing of railway containers

To strengthen logistics in India and to reap cost benefits in the railway freight system, sharing of freight containers should be allowed. This would enable e-Commerce companies to find a collaborative approach to use the current railway freight network.

Promote digital modes of payment

CoD is a major portion of e-Commerce transactions today. This results in risks of carrying cash and inefficiencies in cash lifecycle management, thus digital payment though credit/debit cards, net banking, wallets etc. should be promoted. Customers could be incentivized to promote payments via digital mode. Launch of the Unified Payments Interface (UPI) is likely to address CoD challenges.

Optimize Reverse Logistics

Technology-enabled efficient solutions need to be developed to manage the complex framework of reverse logistics. E-Commerce players should consider differential pricing for online shopping to minimize instances of returned good.

Facilitate easy movement of goods across States

To ensure faster delivery of goods across the country, there needs to be an efficient mechanism in place at border check posts and railway cargo centres, which allows for a thorough yet speedy clearance of e-Commerce consignments.

Adopt smart technology

Technology-enabled solutions such as apps, low-cost hardware devices, e-signature of customers could be leveraged to reduce dependencies on paper-based fulfilment. Also, technology-enabled solutions across the logistics supply chain could reduce turnaround time and enhance traceability of goods-in-transit.

Direct Tax

Withholding Tax Matters

As a Payer	As a Payee
To alleviate the difficulty being faced by the Indian payers who are required to bear tax cost on transactions: • Higher rate of withholding tax for non-availability of Permanent Account Number (PAN) of the payee should not apply • Documentation requirements to be simplified for applying tax treaty provisions (such as declaration by the payee, as opposed to tax residency certificate)	• Simplified mechanism to obtain lower / nil withholding tax certificates for e-Commerce companies, without requiring payer details • Mechanism to apply the rate for the preceding financial year in a certificate till such time that the certificate for the current financial year is issued, provided an application is made at the start of the financial year in question
For other transactions: • Higher rate of withholding tax for non-availability of PAN of the payee 17 should not apply in cases where the relevant tax treaty provides for a lower withholding tax rate • Simplicity of documentation requirements for applying tax treaty provisions (such as declaration by the payee, as opposed to tax residency certificate)	
Other key aspects: • Requirement of obtaining PAN should be restricted. In the Finance Bill, 2016, an exemption from requirement of furnishing PAN has been proposed for certain non-residents, subject to such conditions that may be prescribed. The Hon'ble Finance Minister in his Budget Speech referred to furnishing of alternate documents in place of PAN. • Limited compliance requirements in case of non-resident payees (as opposed to full-fledged tax returns and transfer pricing filings)	

Other Matters:

• Unutilised business losses of e-Commerce companies should not be lost even if the shareholding of the company changes by more than 49%

• Increasing the number of years within which the tax holiday can be availed by start-ups in the e-Commerce industry

Indirect Tax

The Indirect tax environment in terms of policy as well as administration would also be key towards unleashing the potential of e-Commerce industry in India. The Indirect tax laws needs to be evolved and re-designed to consider the changing business dynamics of e-Commerce since the activities involve high volume and low-value supplies.

On the basis of interactions with various stakeholders, the following recommendations, including expectations under the GST regime, were proposed in order to resolve the challenges faced by the e-Commerce industry:

Institution of Central Committee for tax policy recommendations and implementation

- A Central Committee to be constituted to oversee the implementation of a conducive environment for the e-Commerce industry in India; it can also provide recommendations on the proposed GST legislation
- State and local bodies across administrations to cooperate and an integrated approach to be adopted in conjunction with Central Government.
- States and local bodies to ensure that a comprehensive tax is uniformly interpreted, and implemented for facilitating the growth of e-Commerce in the country.

Need for clarity on characterisation of tax liability

- GST laws should take into consideration the actual nature of the transaction to determine tax liability of the sellers and e-Commerce companies
- Taxes under the proposed GST legislation should be based on the actual scope and obligation of each parties such that there is no deemed taxation in the hands of e-Commerce companies

Need for clarity on supply of digitised products and place of supply rule

- Supply of digitised products sold over the internet to be considered as 'services'
- In the GST regime, there should be clarity and certainty to reduce double taxation and any efforts to manipulate the classification

Registration of multiple vendors at marketplace warehouse or fulfilment centre

- Sellers should be allowed to register market place warehouses or fulfilment centres as an additional place of business under applicable state VAT as well as the proposed GST laws
- The Central and the State governments should extend the required relaxation under the proposed GST laws to enable multiple vendors to register at a marketplace warehouse/ fulfilment centre

E-invoicing and tax credits

- State VAT legislations should also allow issuance of digitally signed electronic invoices
- Electronic invoices should be treated as valid documents for claiming tax credit of VAT

Facilitate free movement of goods

- Entry and exit of e-Commerce consignments across multiple states should be eased with uniform legislative structure
- Instead of filling forms on entry into each state, the truck carrying the consignment can be given a number that will give the check post all the details of the consignment

Uniform tax rates on supply of goods across states

- A single common GST rate is proposed on all inter-state supplies so that businesses are not constrained to apply multiple rates

Need for specific place of supply rules for e-Commerce transactions in GST

- The place of supply rules under the proposed GST regime should effectively address the concerns that are likely to arise such as: determination of place of supply in the context of contractual recipient vis-a-vis actual provision/ consumption of the services, excess accumulation of credits in one state and liability in another state and no provision to set off the same

GST implementation holds the key

- A consultative approach is adopted to implement GST and roll-out is in accordance with all the e-Commerce ecosystem
- GST is introduced uniformly across all States, to ensure uniform tax structure
- Ensure faster and efficient integration of technology systems and processes

Key Recommendations

- Central Committee for Tax Policy
- Clarity on Tax Liability
- Clarity on Supply of digitised products
- Registration of vendors
- E-invoicing and tax credits
- Free movement of goods
- Uniform tax rates
- Specific place of supply rules
- GST implementation

Figure 18. Key recommendations for Indirect Tax

Forensic

Enumerated are the top three areas to improve the fraud risk management structure in e-Commerce companies:

Reduce Counterfeiting risks

- Institute a robust Know Your Seller (KYS) procedure for merchant on-boarding – Often, in a bid to improve their valuations, e-Commerce companies may be in a rush to empanel a large number of vendors and sellers, without ascertaining their background in detail. Given the past boom and bust phases in e-Commerce in overseas markets, it is recommended that Indian e-Commerce companies should institute a robust due diligence mechanism before on-boarding sellers. This will help to establish genuineness, credibility and reputation of sellers. Additionally, once the GSTN portal is active, it can be leveraged to check the status (active/inactive) and other statutory information about sellers.
- Increased collaboration between companies in the sector to identify unscrupulous sellers –The e-Commerce companies should collaborate to undertake a comprehensive exercise to this effect and share the findings amongst themselves. This can help organisations blacklist and take appropriate action against these sellers. Since the same set of vendors tend to be empanelled on multiple e-Commerce websites, the knowledge of malpractice identified on one website and shared amongst the larger e-Commerce community can be a significant deterrent for these unscrupulous sellers from conning other companies
- Push for a more comprehensive law to address counterfeiting and associated enforcement action
  - o Industries such as FMCG have long expressed concerns about the need to strengthen the current anti-counterfeiting laws in India backed by stringent enforcement action. The e-Commerce industry is increasingly finding itself in the same boat. The US, for example, has specific laws outlining several categories of counterfeits and copyright infringements, including images and packaging, and states penalties starting at USD 500,000
  - o There is a need for collaboration between enforcement agencies, consumers and associated stakeholders to reduce the risk of counterfeiting in e-Commerce

Improve Governance Measures

- Setting up an ethical culture – Educating employees and third parties about larger implications of fraud can help deter such incidents significantly. The e-Commerce companies should put in place specific policies pertaining to bribery and corruption, conflict of interest and ethical practices, followed by training programmes for employees and third parties. Organisations should also set-up whistleblowing hotlines to encourage the reporting of malpractice and fraud by employees and third parties
- Fraud risk monitoring of transactions – e-Commerce companies are intrinsically technology driven and tend to rely on sophisticated data analytics tools to help them with business decisions. However, industry stakeholders state that organisations have to gain larger ground to leverage analytics for fraud prevention, detection and response. For this, e-Commerce companies need to work with forensic experts who can help customise prevailing data analytics tools by including rules, routines and algorithms that can effectively identify red flags pertaining to fraudulent behaviour
- Segregation of roles and responsibilities – A segregation of roles and responsibilities, followed by annual rotation of team members within roles, can help prevent conflict of interests and kick-back scenarios

Enhance Data security

- Effective configuration of data leakage prevention tool to closely monitor data travelling outside the organisation's domain
- Information security controls on electronic devices, which not only restrict unauthorised usage but also restrict usage of external storage devices or block cloud storage
- Clearly defined employee contracts that mandate disclosure of potential conflicts of interest and penalties for violation of the contract with regard to IT security and conflicts of interest.
- Once a potential data breach is suspected within the company, attempts should be made to immediately identify the data breach source (department, team, individual) and the nature of information leaked through. A comprehensive forensic investigation (involving logs analysis, usage behaviour, email review, exception testing etc.) should be conducted to identify the veracity of the suspected breach and root causes of such incident, if any

X. Key Future Trends

e-Commerce industry is driven largely by continuous innovation and technology-led solutions and these are expected to continue in the future. Enumerated are a few key future trends:

Innovation in Payments

The ever increasing use of digital wallets together with the newly launched UPI platform, will foster innovation in payments. The UPI platform will be leveraged to offer innovative payment modes to customers and also make CoD seamless by cashless fulfilment at the time of delivery. This would make payments even more seamless and will hopefully reduce goods return.

New Delivery models

Keeping in perspective the "choked traffic" situation in India's metros leading to late deliveries or increasing the biker count to meet the delivery timelines, e-Commerce and Logistics service providers are exploring moving from synchronous hand delivered parcel system to an asynchronous model, where parcels are delivered to a locker secured by a code sent as a text to the recipient. This experiment, if successful, is likely to help e-Commerce companies to enhance customer experience.

Collaboration of e-Commerce and offline entities

There will be a collaborative approach between e-Commerce companies and offline entities such as retailers, banking business correspondents, micro-finance companies, etc. for order fulfilment in tier 2 & 3 cities. Likewise, the extensive distribution network of entities who have secured small bank and payments bank licenses (For e.g. Telecom operators, India Post) will be leveraged by e-Commerce logistics service providers for enhancing and optimising the last-mile delivery to the new markets in the rural hinterland.

Technology and Wearables

The launch of wearables, such as Google Glass, Apple Watch and other Smart Watches, opens new opportunities for reaching out to customers. e-tailers would keep an eye on developments in this arena, although this might only be an urban phenomenon at the moment.

Efficiencies attained by Artificial Intelligence and the use of Drones

Anticipating the seasonal surge especially during festive seasons is a challenge for e-Commerce companies in terms of managing the supply chain logistics to provide on-time deliveries to all customers. Therefore, Artificial Intelligence technologies will be leveraged in the future to anticipate demand, manage price fluctuations and to overcome challenges of last-mile deliveries.

Automated Guided Vehicles (AGV) could solve many logistics problems of the e-tailers and result in highly successful product deliveries. For example, Amazon Prime Air is working on drone-based delivery of its products. Local knowledge of the delivery person complemented by GPS-based device could lead to efficient delivery of products.

XI. Acknowledgements

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We would also like to thank *Shamal Patel, Shivali Valecha, Hardik Gandhi* and *Rahul Murarka* for their valuable inputs and contribution

XII. Appendix

Approach

Primary Research was conducted with key companies in each category of stakeholders in the e-Commerce ecosystem of India. In order to get comprehensive and deep insights, standardised questionnaires were prepared for each category of stakeholders. The questionnaires were based on the enumerated aspects:

- Analysis of growth and trends in the Indian e-Commerce industry (B2B and B2C)
- Current regulatory landscape for the e-Commerce companies
- Challenges for new age entrepreneurs / SMEs / MSMEs and probable imperatives in digitising multiple business aspects within the e-Commerce eco-system
- Evaluation of how SMEs, MSMEs and new age entrepreneurs can leverage government initiatives like Digital India, Make in India and Start-up India to leapfrog and advance their growth
- Recommendations to the Government of India regarding, the major initiatives it needs to trigger in order to provide direction for a sustainable and robust e-Commerce eco-system

Respondents' specification

A mixed methodological approach was used to capture as broad a range of ecosystem respondents as possible. This comprised:

- A telephone, interviewer-led approach or
- A face-to-face meeting with Deloitte's team

Responses were evaluated and synthesised by our Subject Matter Experts using a framework developed by the team.

The respondents comprised leading companies from the enumerated categories of the e-Commerce ecosystem

S. No.	Primary Research Category
1	e-Commerce and e-tailers (B2C)
2	e-Commerce and e-tailers (B2B)
3	MSME / Sellers
4	Government of India/Ministries
5	Trade Bodies
6	Logistics Service Providers
7	Subject Matter Experts

In the preparation of this report, we have also referred to Deloitte's repository and knowledge resources for secondary research, wherever required.

XII. Glossary

Term	Definition
1. Aggregator	A type of e-Commerce entity which aggregates information on goods and services and then designs a system which allows easy matching of prices and specifications
2. Angel Investor	An investor who provides financial backing at the initial stage to small start-ups or entrepreneurs
3. B2B	Business-to-Business (B2B) refers to commercial transactions between businesses i.e. both buyer and seller are businesses
4. B2C	Business-to-Consumer (B2C) refers to commercial transactions in which one business sells directly to the consumer i.e. buyer is a consumer and seller is a business
5. CAGR	Compound Annual Growth Rate (CAGR) is the growth rate that gets from the initial investment value to the ending investment value if we assume that the investment has been compounding over the time period
6. CoD	Cash-on-Delivery (CoD) is a type of transaction in which payment for a good is made at the time of delivery
7. CST	Central Sales Tax (CST) is a form of indirect tax imposed only on goods sold from one state to another state, which particularly takes into account that the buyer and the seller needs to be in two different states
8. CRM	Customer relationship management (CRM) is a term that refers to practices, strategies and technologies that companies use to manage and analyze customer interactions and data throughout the customer lifecycle, with the goal of improving business relationships with customers
9. CGST	Central Goods and Services Tax (CGST) is a form of indirect tax levied and collected by the Centre on goods and services
10. C2C	Consumer-to-Consumer (C2C) refers to commercial transactions which take place between customers i.e. both buyer and seller are consumers
11. e-Commerce	Purchase and sale of goods and services, or transmitting funds over an electronic network, primarily the Internet
12. EDI	Electronic Data Interchange (EDI) is the transfer of data from one computer system to another by standardized message formatting, without the need for human intervention. EDI permits multiple companies, possibly in different countries, to exchange documents electronically
13. e-tailing	Short for "electronic retailing". Refers to sale of retail goods on the Internet
14. FDI	Foreign Direct Investment (FDI) is a controlling ownership in a business enterprise in one country by an entity based in another country

Term	Definition
15. GMV	Gross Merchandise Value (GMV) is a total sales dollar value for merchandise sold through a particular marketplace over a certain time frame. For the purpose of this report, e-Commerce value refers to B2C only e-tailing and does not include online travel and classifieds
16. GDP	Gross Domestic Product (GDP) represents the monetary value of all goods and services produced within a nation's geographic borders over a specified period of time
17. GST	Goods and Services Tax (GST) levied on goods and services sold for domestic consumption. It is perceived as the most radical taxation reform that could alter India's economic prospects if implemented
18. Hyper-local delivery	Hyper-local delivery mechanisms include neighborhood focused new sources for products and services
19. Inventory Led Model	A type of e-Commerce entity which sources products directly from brands and/ or sellers and stock these. There are no multiple sellers selling one product, unlike marketplaces where buyers get to choose from several merchants
20. IGST	Integrated Goods and Services Tax (IGST) is a form of indirect tax levied by the Central Government on inter-state supply of goods and services
21. KYS	Know your sellers (KYS) is the process of a business verifying the identity of its sellers and merchants
22. LSP	Logistics Service Provider (LSP) is a company that provides management over the flow of goods and materials between points of origin to end destination
23. Marketplace Model	A type of e-Commerce entity in which product or service information is provided by multiple third parties, whereas transactions are processed by the marketplace operator
24. MSME	Micro, Small & Medium Enterprises (MSME) are defined based on (i) on the investment in plant and machinery for those engaged in manufacturing or production, processing or preservation of goods and (ii) on the investment in equipment for enterprises engaged in providing or rendering of Services
25. NOFN	National Optical Fibre Network (NOFN) is a project initiated in 2011. It is funded by Universal Service Obligation Fund to provide broadband connectivity to over two lakh (200,000) Gram panchayats of India at a cost of Rs.20,000 crore ($3 Billion)
26. NSIC	National Small Industries Corporation (NSIC) is a Public Sector Union established by the Government of India and falls under the Ministry of Micro, Small & Medium Enterprises

Term	Definition
27. Omni-channel	A multi-channel approach to sales that seeks to provide the customer with a seamless shopping experience. It means providing multiple shopping touch points, whether the customer is shopping online through a desktop or mobile device or a telephone or a bricks and mortar store
28. PE	Private Equity (PE) consists of investors and funds that make investments directly into private companies or conduct buyouts of public companies that result in a delisting of public equity
29. SGST	State Goods and Services Tax (SGST) is a form of indirect tax levied and collected by the respective States on goods and services
30. SLA	Service-Level Agreement (SLA) is a part of a standardized service contract where a service is formally defined. Particular aspects of the service – scope, quality, responsibilities – are agreed between the service provider and the service user
31. UPI	Unified Payments Interface (UPI) is a new process in electronic funds transfer which will allow customers to transfer money and make payments instantly and very easily
32. VAT	Value Added Tax (VAT) is a form of indirect tax imposed only on goods sold within a particular state, which essentially means that the buyer and the seller needs to be in the same state., VAT can be imposed only on the sale of tangible goods and products
33. VC	Venture Capital (VC) consists of investors and funds that make investments directly into start-ups with strong growth potential

Source – Media Reports, Investopedia

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