

# THE LATEST BUZZ AROUND E-COMMERCE

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Foreign Capital, Foreign Trade & BOP

*The new clarification issued by the government regarding FDI in e-commerce has created a furore among firms in the sector and their vendors alike. Here is a lowdown on the new rules:*

## What happened?

The Department of Industrial Policy & Promotion on Wednesday issued a clarification to the existing rules pertaining to Foreign Direct Investment in e-commerce companies. The main features of the clarification include the provision that vendors that have any stake owned by an e-commerce company cannot sell their products on that e-commerce company's portal.

Another provision says any vendor who purchases 25% or more of its inventory from an e-commerce group company will be considered to be controlled by that e-commerce company, and thereby barred from selling on its portal. This provision aims to ensure that vendors in which marketplaces, such as Amazon, have a stake do not sell the bulk of their items to a third-party vendor who then goes on to sell those items on the e-commerce marketplace.

In other words, the provision seeks to deny control by the marketplace entity over vendors. The third major provision says the e-commerce firm will not be allowed to influence the price of a product sold on its portal by giving incentives to particular vendors.

## What is the context for these changes?

E-commerce companies can operate under two different models in India. The first is the marketplace model where the e-commerce firm simply acts as a platform that connects buyers and sellers. FDI is allowed in e-commerce companies in this model. The second model is inventory-based where the inventory of goods sold on the portal is owned or controlled by the e-commerce company. FDI is not allowed under this model.

What has been happening is that large e-commerce companies such as Amazon and Flipkart, while not owning inventory themselves, have been providing a platform for their group companies such as CloudTail and WS Retail respectively.

Some see this as skewing the playing field, especially if these vendors enjoyed special incentives from the e-commerce firm, over others. These controlled or owned vendors may then be able to offer discounts to customers that competitors may not be able to match.

## Who benefits?

The thrust of the DIPP policy is directed at protecting small vendors on e-commerce websites. It seeks to ensure small players selling on the portals are not discriminated against in favour of vendors in which e-commerce companies have a stake. The Confederation of All India Traders welcomed this move as it feels the new set up will ensure a level playing field for all vendors looking to sell on the e-commerce portals. Smaller marketplaces that do not have stake in any vendors will also be able to now compete with the big daddies.

## Who else will be affected?

The main players to be affected will be group companies and affiliates of the biggest e-commerce platforms, Amazon and Flipkart. These include CloudTail, WS Retail, Myntra and private label brands such as Amazon Basics and Flipkart's MarQ and to some extent the private label business of online marketplace operator ShopClues.

The provision that bars companies — in which e-commerce firms have a stake — from selling on their portals will hurt start-ups as well, since many of these will be barred from selling due to minor equity stakes being held by the e-commerce companies. L. Badrinarayanan of Lakshmikumaran & Sridharan Attorneys says small vendors will not be as affected because most of them, anyway, do not purchase more than 25% of their inventory from a single source and so they will be allowed to sell their items on the e-commerce platforms.

### **Where will Amazon now sell its own products such as Kindle and Amazon Echo?**

The verdict on this is unclear. FDI in single-brand retail is allowed in India, so if Amazon has a licence for single-brand retail, it can sell its own products on its portal. Or vendors like Tata Croma, for example, may buy these products from Amazon and sell them on its portal.

### **Is it the end of discounts?**

Discounts will not go away, said Satish Meena, senior forecast analyst, Forrester Research. Earlier, Amazon used to give discounts through CloudTail, but now it would have to give discounts through other sellers as well, he said. That is, e-commerce firms will have to ensure a level playing-field among their vendors. They can still promote their own portals by offering cashback offers and vouchers, but these will have to apply to purchases from all vendors.

### **Will a vendor be unable to sell on a marketplace, if the latter holds any stake in the vendor?**

Experts agree that this provision will likely be amended, with a benchmark equity percentage being set. That is, the rules may be changed such that a vendor with more than a certain stake owned by an e-commerce firm cannot sell on that portal, rather than the current wording that says 'any stake'.

### **Will the business model or shareholding in a vendor such as CloudTail change?**

This is difficult to say, Mr Meena said, as it is difficult to imagine CloudTail selling via Amazon's competitors. It would be difficult for Amazon to go on with the current structure. CloudTail must change ownership if it has to sell on Amazon, which means Amazon has to sell its CloudTail holding, he said.

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