Delhi Business Review ✍ Vol. 1, No. 2, July - December 2000

PERFECT COMPETITION: FROM MYTH TO REALITY

Yogesh Upadhyay &
S.K. Singh

IN the last two decades, Information Technology has played a key role in transforming the way business is conducted. With each new wave of technology, it has brought about fundamental changes. In all these, the one technology that has truly been an effective agent in changing the fundamental ways of doing business is none other than ubiquitous thing that everyone knows as Internet (Hindustan Times 1998).

The Perfect Competition

Adam Smith himself recognised that the virtues of market mechanism are fully realised when the checks and balances of perfect competition are present (Samuelson 1992).

Perfect competition refers to a market in which no firm or consumer is effective enough to affect the market price. The firms are usually *price takers*. The buyer is aware of the prevailing prices in the market. The entry and exit of firms have least effect on the market.

Till now, perfect competition was considered to be a myth. But the advent of Internet, has made it a reality. The geographical boundaries are eroding rapidly for the purpose of business with the spread of Internet. The implication is that the sellers or buyers which due to their number or capacity were able to affect the price earlier can not do so now. It is not a single country where buyers and firms are spread. They are spread across the globe. Therefore, the number of such firms and buyers are minuscule in proportion which can have impact on globally prevalent prices. The firms are also free to enter and exit from the market place.

Resultantly, Internet growth has led to a host of new developments, such as decreased margins for companies as consumers turn more and more to the Internet to buy goods and demand the best prices, as observed by C.K. Prahalad, Professor, Business School, University of Michigan. The Internet means that traditional businesses will change because “incumbents (in markets) and large firms do not have the advantage” just by virtue of being there first or by being big, he said. The implication of perfectly competitive market as the world will observe is that markets will produce *an efficient allocation of resources.*

In any market with no entry-barriers – the Net is the biggest of them – the continuous influx of competition will, automatically, drive down prices. Add to that the unique economics of Net-based products and services, where the incremental cost of creating additional units is zero and prices also tend to gravitate towards the zero-mark. In such a case, in long term all firms could only earn normal profits.

Rohan Bulchandani is booking his place in the virtual profit-zone by managing prices. In June, 1998, Annet Communications, the technology solutions company of which he is the CEO, set up India's first on-line bookstore, IndiaBookShop (www.india bookshop.com). Although it has subsequently expanded has become a part of Indishop (www.indishop.com), which e-retails music, gifts, flowers etc. alongside books. India Book Shop remains the engine of this e-biz. Its discount of at least 20 per cent on the cover price of the books that it sells. IndiaBookShop does it by positioning itself as wholesaler and not as a retailer in the book-trade. This brings us trade discounts which we pass on to buyer. Also, we own our delivery as well as procurement networks." In other words, its the cost-structure that counts. However, its never-say-no-to-an-order strategy frequently raises sourcing and delivery costs. But Bulchandani's real focus is on increasing the conversion rate, which, at present, stands at 1.20 per cent-or, about 60 sales out of the daily average of 5,000 hits – amounting to an annual turnover of Rs 73 lakh. After all, he'd love to be India's Amazon et.al. (1999).

What is Internet Commerce?

According to the US based Aberdeen Group: *Internet Commerce* is a term used to describe the automation, the full range of interactions across corporate borders between companies and people – from marketing to sales, order placement to invoicing and payment, product distribution and customer service – by establishing computer-to-computer service by establishing computer-to-computer communication, utilising the infrastructure and standards of the Internet (Data Quest 1998).

Business over the NET comprises different types of commerce. The first is *business-to-business* commerce, which replaces the classic way of doing business – using telephone calls, purchase orders, faxes, mail messages and so on – with real-time interfacing over the NET. This is expected to be the dominant form of business transaction as we move forward. The second is, perhaps, glamorous and so, gets greater publicity in the press: *home-to-business* or *individual consumer-to-business transactions* – where the individual end-user can buy flowers, books, real estate and automobiles over the Net. The interesting fact about this forecast – which suggests that by 2002, $ 500 billion of business will be transacted on the Net – is that each time this forecast is updated, the figure tends to increase by 30 per cent. IBM transacts business worth approximately $ 5 billion over the NET (Craig Radford Barrett 1998).

The greatest payoff for corporate IT investments shall come from actually conducting trade on Internet, i.e. selling goods and services over the net. Companies all over the world are only now coming to terms with what it actually means. Among other things, it actually represents the opportunity for companies to reach beyond the boundaries of its limited reach, be it within its country or outside. Clearly, it promises of possibilities that would have been once considered utopian by practical business heads.

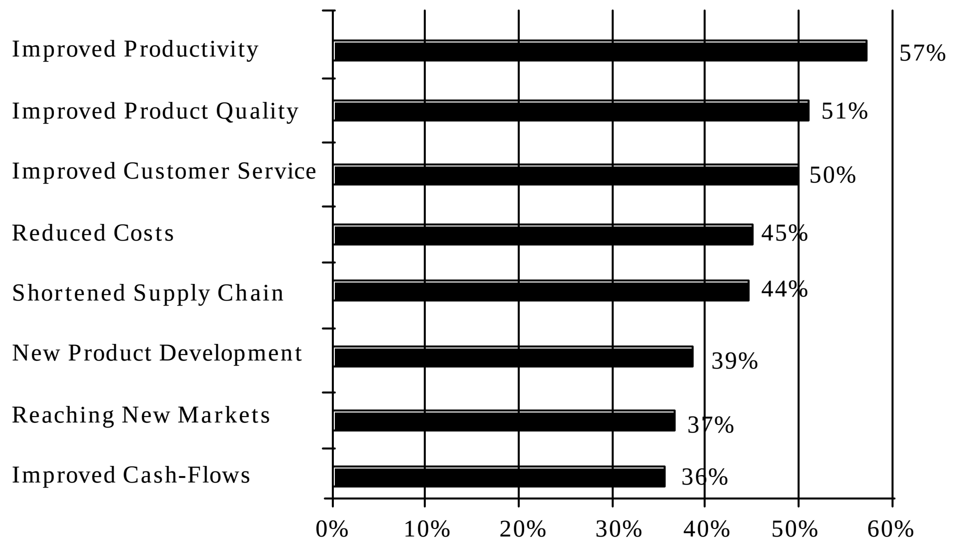
There are several estimates floating around about the potential of this medium as a means of facilitating trade. Going by IDC figures, in 1997 alone more than $ 10 billion in transactions were executed over the Internet. Given the size of conventional trade, perhaps the figure is small indeed, as it amounts to a mere 0.05% of the global trade.

But again, it would be indeed shortsighted to ignore its impact. IDC forecasts that by year 2001, Internet commerce will surge over $ 220 billion. Another research study by Forester predicts that by 2002, the value of goods and services traded between companies over the Internet will reach $ 327 billion, just under 1% of global trade (Craig Radford Barrette 1998).

Benefits of E-Commerce

A survey on the status of E-Commerce has been conducted by KPMG, covering a sample of 116 companies operating in the country more than two-thirds of which have a turnover of over Rs 100 crore. The survey evaluates the perceptions, status and triggers of the use of E-commerce in Indian companies. The results of survey done by *KPMG India Electronic Commerce Survey* regarding the benefits the corporates are observing by conducting business through Internet are summarised below:

What Benefits are your getting from E-commerce?



Source: *KPMG India Electronic Commerce Survey Report, 1998-99 adapted form Business Today, March, 22, 1999, p. 80-83.*

It is clear from the above chart that largest benefit to the corporates transacting business through Internet is improved productivity. It is followed by improved product quality, improved customer service, reduced costs, shortened supply chain etc. It can well be concluded from the array of data that the greatest beneficiary of Internet is consumer. He is going to gain by improved products quality, service, reduced costs etc. In other words, greater the business transacted on Internet, the more consumer satisfaction shall follow.

Net Profits

Drawn irresistibly by the digital economy, where 100 million shoppers will spend an estimated $ 15 billion in 1999, a host of entrepreneurs around the world have planted their start-ups in the marketspace, capitalising on the fact that it only needs a computer and a phone-line to get going so have corporates with deep roots in the physical marketplace, whose entry has been parked off more by the fear of mission out on an opportunity than by the profit motive et.al. (1999).

Most of them have proved that economics of E-commerce isn't easy to master. Most, but not all, for, a small, but select, set of Net-millionaries are demonstrating that the Net can, indeed, be a theatre for profitable business.

- Bill Gross is millionaire many times over after an e-biz, *shopping.com*, funded by his company, ideala!, was acquired by Compaq Computer for $ 220 million.
- The 39 per cent equity held by Jeff Bezos in *Amazon.com*, which he founded, is worth $ 2.50 million with the company's stock priced at $ 133.
- Brothers Andrew and Thomas Parkinson's stake in America's No. 1 online-retailer, Peapod, is worth $ 64 million.
- Timothy A. Koogle, the CEO of Yahoo!, can value his stock at $ 625 million, with the company being priced by the stockmarkets at $ 2 billion.
- By selling, Junglee to Amazon.com, founders Venky Harinarayan, Rakesh Mathur, Anand Rajaram and Ashish Gupta raked in $ 180 million.

Several genres of such media have emerged: the portal – Yahoo!, MSN, Lycos or Excite are classic examples – in its most generalised form acts as an entry-point to the vast reaches of the Net for surfers, offering them links to the subject of their choice. A more specialised version, the so-called affinity portal, acts as a broad window to a narrow theme – such as ESPN Sportzone to sports, or C-Net to technology. And, in its most focused form, the portal is devoted to specific events – the Academy Awards, for instance.

On-line Shopping Yet to Take Off in India

According to a survey done by Capital Images (Chatterjee, 1999) with a sample of 470 individuals across the four metros of Mumbai, Delhi, Pune and Bangalore only 29 per cent of the respondents have shopped on the Internet. And an overwhelmingly 71 per cent of the respondents have not done so-ever.

This is interesting on two counts. First, considering the fact that 94 per cent of the respondents are users of Internet, the fact that they are 'passive' would come in the way of companies launching E-commerce business.

Second, since the survey was conducted among respondents aged between 25 and 45 years and comprised of corporate executives and professionals (middle-to-high-income-groups), it also proves that the cost of the product is not a hindrance. It is simply the mindset of the respondents.

According to the survey, buying movie tickets on the Net is the most preferred option. Thirty-four per cent of the respondents have bought movie tickets on-line, while 27 per cent have bought audio cassettes/CDs. Another 25 per cent respondents have bought books, while 12 per cent have bought items like flowers and chocolates. The remaining 2 per cent have bought items like cosmetics, garments or booked train tickets.

Bottomline: Low-cost purchases dominate E-commerce in India today, with high-end products yet to make any impact.

There were some other interesting findings in the survey. As 33 per cent of the respondents surf the Net 'very often' and another 25 per cent 'often' surf, Internet surfing in urban India is clearly beginning to emerge as a regular habit, with approximately 58 per cent of the respondents logging on fairly often. However, around 42 per cent of the respondents are infrequent users.

Among the favourite sites and search engines, Yahoo.com emerged as the most widely-used search engine with 49 per cent of the respondents giving it the first choice, followed by Netsape.com with 3 per cent respondents choosing it as the second most preferred search engine.

Excite.com and AOL.com are not very popular, with only 5 per cent and 4 per cent of the respondents using them respectively. Significantly, the most widely used sites are Indiatimes.com, Indiajobs.com, Khoj.com, Khel.com, Infoseek.com and Askjeeves.com.

In terms of users' buying patterns for consumer durables involving a higher budget outlay, consumers would prefer to physically examine product specifications prior to purchase. This refers to computers, TV, properties and cars. Buyers of consumer durables also look at value discount, freebies and financing options.

Interestingly, a significant 52 per cent of the respondents are flexible on buying branded clothes on the Net. The respondents were confident of the consistency of brand value and also the fact that they could choose from a colour range wherein many have a prior disposition.

Moreover, in the readywear market there seems to be a trend to buy instantly on the 'known size'. However, 48 per cent of the respondents are not keen to buy apparel on the Net, as they would like to 'try them on first'.

E-commerce essentially relies on electronic transfer of money involving instruments like credit cards. In India, it could be difficult. Sixty-seven per cent of the respondents do not want to give their credit card details over the Net. This, in fact, is one of the main reasons they are averse to shopping on the Net. The remaining 33 per cent do not mind giving their credit card details, subject to the authenticity and brand perception of the site.

As regards choice of payments, surprisingly 35 per cent of the respondents would still prefer to make their payments via cheques, 34 per cent through credit cards, 24 per cent in cash, while the remaining 7 per cent would prefer to make their payments through VPP.

Convenience in shopping, guarantees on product quality and discounts were some of the main reasons that prompted a Net user to buy goods and services over the Net.

While the potential of E-commerce in India is phenomenal, the fact of the matter is that India is way behind developed nations in terms of the Internet and its allied services. Consider this: 72 per cent of the Web sites are still based in the US and 92 per cent of the total volume of E-commerce business is generated through US-based Web sites.

Conclusion

It can fairly be concluded that the advent of Internet at last could turn the myth of perfect competition into reality. Though it is the best form of competition but it eluded so far due to imperfections prevailing in the real world. But the introduction of Internet could remove the imperfections from the market. The biggest beneficiary in such a case is the consumer. It will be in the interest of consumers that the Internet be used as a means of transacting business at the earliest. But the scenario in India presently is not very encouraging. It will still take time for the Internet to become a full-fledged tool for transacting business due to low per capita incomes and poor infrastructure.

References

Chandrashekar, S., Dobhal Shailesh & Sukumar R. (1999). Net Profits or how (finally) to make money on the net", Business Today, March 22, p.77.

Chandrashekar, S., Dobhal Shailesh & Sukumar R. (1999). Net Profits or how (finally) to make money on the net", Business Today, March 22, p.68-79.

Chatterjee, Aditya (1999). The Times of India, September 20, p.12.

Data Quest (1998). Internet Commerce-Leveraging the Net for Profit, Internet Commerce Supplement. September 30. p.6.

Excepts from Intel's Business Strategy by its CEO Craig Radford Barrette, (1998). Inside New Millennium Computing, Business Today, November 22-December 6, p.102.

Ibid., p.7.

Hindustan Times, 18 June, 1998, p.12.

KPMG India Electronic Commerce Survey Report, 1998-99 adapted form Business Today, March 22, 1999, p.80-83.

Samuelson, A. Paul, & Nordhaus, D. Williams (1992). Economics, McGraw-Hill International Ed., p.40.