India's Mobile Market

Just as Xiaomi fervor has swept China, Micromax fervor is sweeping India. With affordable prices and simple functions, Micromax products are tailored to Indian customers' needs. India's smartphone market, which has been dominated by foreign handsets, is undergoing a rapid transformation. India's mobile services market is one of the world's fastest growing markets. This Special Report delves deeply into the characteristics and ecosystem of the Indian mobile services market.

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With a 22% Market Share, Micromax Dethrones Samsung as the Top Handset Seller in India

As Chinese smartphone maker Xiaomi has dominated the Chinese market, Micromax, India's homegrown smartphone manufacturer, is dominating the Indian Market. Micromax beat South Korea's Samsung Electronics to become the largest smartphone supplier in India for the first time. According to a report by British research company Canalys, Micromax accounted for 22% of smartphone sales in the fourth quarter of 2014, overtaking Samsung, which had a 20% share.

Micromax has made great strides mainly because it appeals to India's lower to middle income consumers with a variety of affordable models. Price is still the most important determinant in India, which has a small high-end market. Based on the Canalys report, more than 20% of smartphones sold in India in the fourth quarter of 2014 were priced under USD 100. With a view to expanding its product recognition in international markets, Micromax is implementing aggressive marketing strategies. The Indian handset maker has run TV commercials starring Hollywood actor Hugh Jack-

A sales clerk taking a picture with a Micromax smartphone. Micromax dethroned Samsung as the number one supplier in India in the fourth quarter of 2014 [Bloomberg]

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man and sponsored the Indian cricket team, raising both its brand awareness and market share.

From IT software to mobile phones

Micromax, one of countless Indian IT software companies, was founded in 2000 with its headquarters in Gurgaon, Haryana. As an IT service company for Nokia, Micromax accumulated knowhow in the distribution of mobile phones. Based on this knowhow, the company distributed data cards from 2007, and started selling its own low-cost mobile phones in 2008, beginning a period of rapid growth. After 2010, Micromax quickly moved into the smartphone market, further propelling its growth. By the fourth quarter of 2014, the company had surpassed all global multinational corporations, topping the Indian smartphone market.

Micromax was quick to expand from the Indian market to the markets of its South Asian neighbors. It emerged as the world's tenth largest handset supplier in 2013. The company is rapidly increasing its market share in Russia by adopting localized, innovative business models. It is reportedly seeking entry into the East European market. Micromax is an unlisted company and does not release annual reports disclosing its sales and revenue. However, its revenue in fiscal year 2013-14 is estimated at INR 75 billion, a ten-fold increase in the five years from 2008.

Three success factors for Micromax

Micromax's success story in India's mobile phone market is inspiring. In 2013, just five years after its entry into the market, Micromax was India's largest and the world's tenth largest mobile phone maker. The factors of the company's success merit attention.

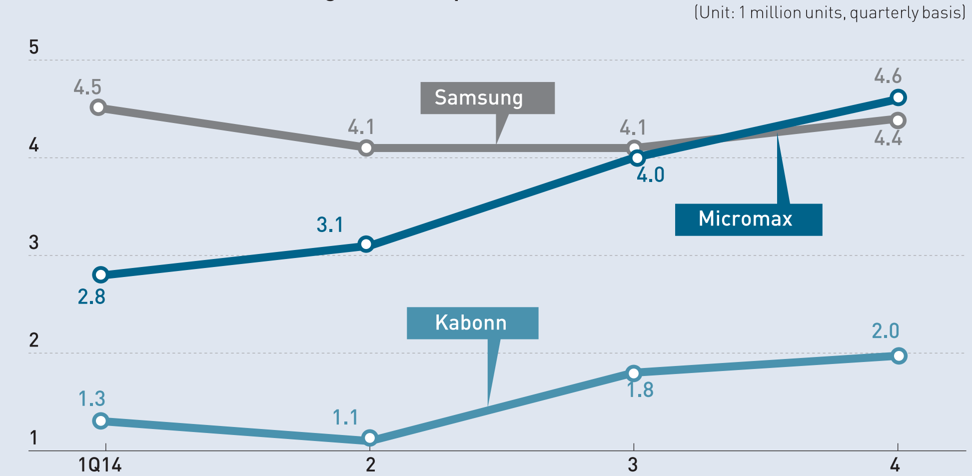
The first factor of success is that Micromax adopted a business model comparable to Apple's in India's low-end mobile phone market. Products are manufactured through Chinese OEMs, while the company focuses on localization and design that increase the convenience of users, as well as software development and local marketing. By doing so, Micromax reduces costs profoundly and passes on the savings to its customers. The Indian handset maker has effectively responded to customers' needs through continuous innovation.

Rahul Sharma, co-founder of the company, once said, "The strategy is simple: create high volumes, reach the customer base through effective distribution, give them products that are innovative and cost-effective. Finally, create a strong brand."

As its manufacturing is highly dependent on China, Micromax is threatened by increasing manufacturing costs due to rising labor costs in China.

Sales of India's Three Largest Smartphone Makers

(Unit: 1 million units, quarterly basis)

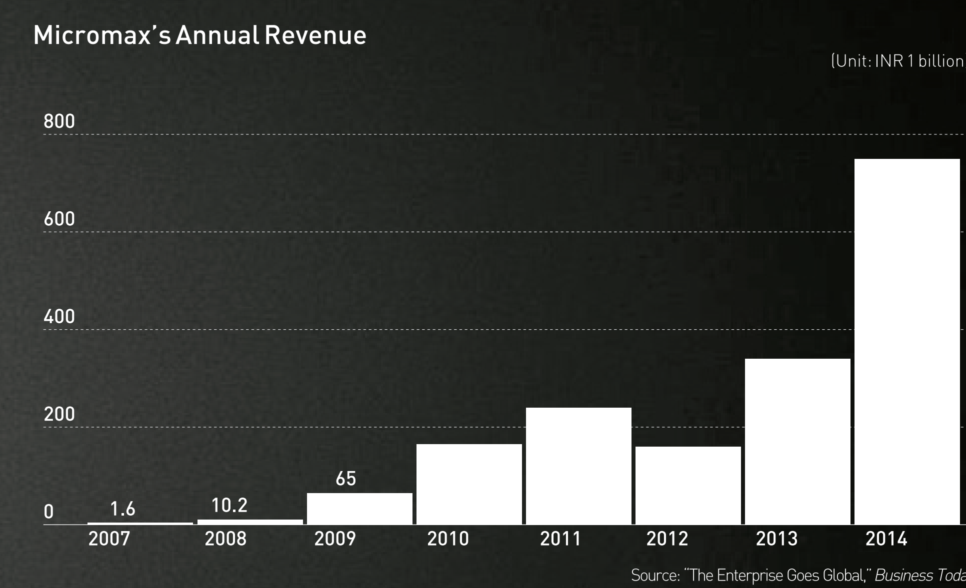


Source: Dazeinfo, Inc (Originally from Canalys, January 2015)

The second factor is the convergence of Micromax's bold brand strategy, frugal innovation strategy, and localized strategies tailored to customers' needs. Micromax adopted the "own-brand strategy," whereby it attaches its label to existing products for sale through its distribution networks in India. In this simple business model, imported Chinese handsets are sold in the Indian market under the Micromax brand. This business model greatly reduces product development and manufacturing costs. Micromax has integrated its own-brand strategy with frugal innovation, delivering low-cost products with minimal innovation to match consumers' needs. For example, for a certain segment of consumers that is not interested in high-resolution cameras, Micromax offers mobile phones with five megapixel cameras at a lower cost than phones with eight megapixel cameras.

Forgoing independent research and development and extraneous functions, Micromax slims down its products and saves costs. Micromax has won the hearts of consumers by conducting thorough needs analysis and adopting strategies to match consumers' needs.

For example, Micromax has released a phone with a battery that can last for up to a month in super power-saving mode, in consideration of the inconvenience of charging mobile phones due to



disrupted power supplies in India.

The third factor is that Micromax has guaranteed greater margins for vendors to expand their distribution channels rapidly. With lower brand awareness than Nokia, Micromax had few customers in the early stage of mobile phone sales. In an effort to boost its brand awareness, Micromax decided to give radical commissions to vendors.

At a time when Nokia was giving 1-2% commission to vendors, Micromax decided to offer 5% commission. In return, vendors had to complete an online bank transfer to Micromax before receiving products. Vendors willingly paid Micromax in advance for a desired number of handsets, and strove to sell them.

Venturing into other markets and increasing manufacturing capability

Building on its accumulated brand power in the smart phone sector and its strong user platform, Micromax is venturing into other sectors of the electronics industry, including TVs and tablet PCs. Just as it did in the smart phone market, Micromax is implementing a strategy of providing consumers with options and setting lower prices than global brands, under the motto of "frugal innovation."

Micromax is expected to rapidly increase its market share in the smart TV sector based on high compatibility with its existing mobile phones. This means that South Korean companies with a strong presence in India, namely Samsung Electronics and LG Electronics, will likely lose share to Micromax. South Korean companies are in urgent need of a response strategy.

As its manufacturing is highly dependent on China, Micromax is threatened by increasing manufacturing costs due to rising labor costs in China. In response to this threat, Micromax is trying to secure manufacturing capabilities, as exemplified by the construction of its own plant in India for the production of TVs and tablet PCs. However, it will likely be difficult for Micromax to secure low-cost manufacturing capabilities due to disrupted power supplies and other problems in India. These problems will threaten Micromax's low-end market strategy.

Korean companies should note how Micromax has secured manufacturing capabilities, because there are potential opportunities to cooperate with Micromax. In October 2014, Micromax discussed the supply of parts and materials with LG Group. The Indian company also expressed interest in buying a stake in the South Korean company Pantech, which is in receivership.

Considering the massive potential of India's domestic market and possible synergy between Korean and Indian companies, South Korea's government and companies should make the utmost effort to cooperate with native Indian companies like Micromax.

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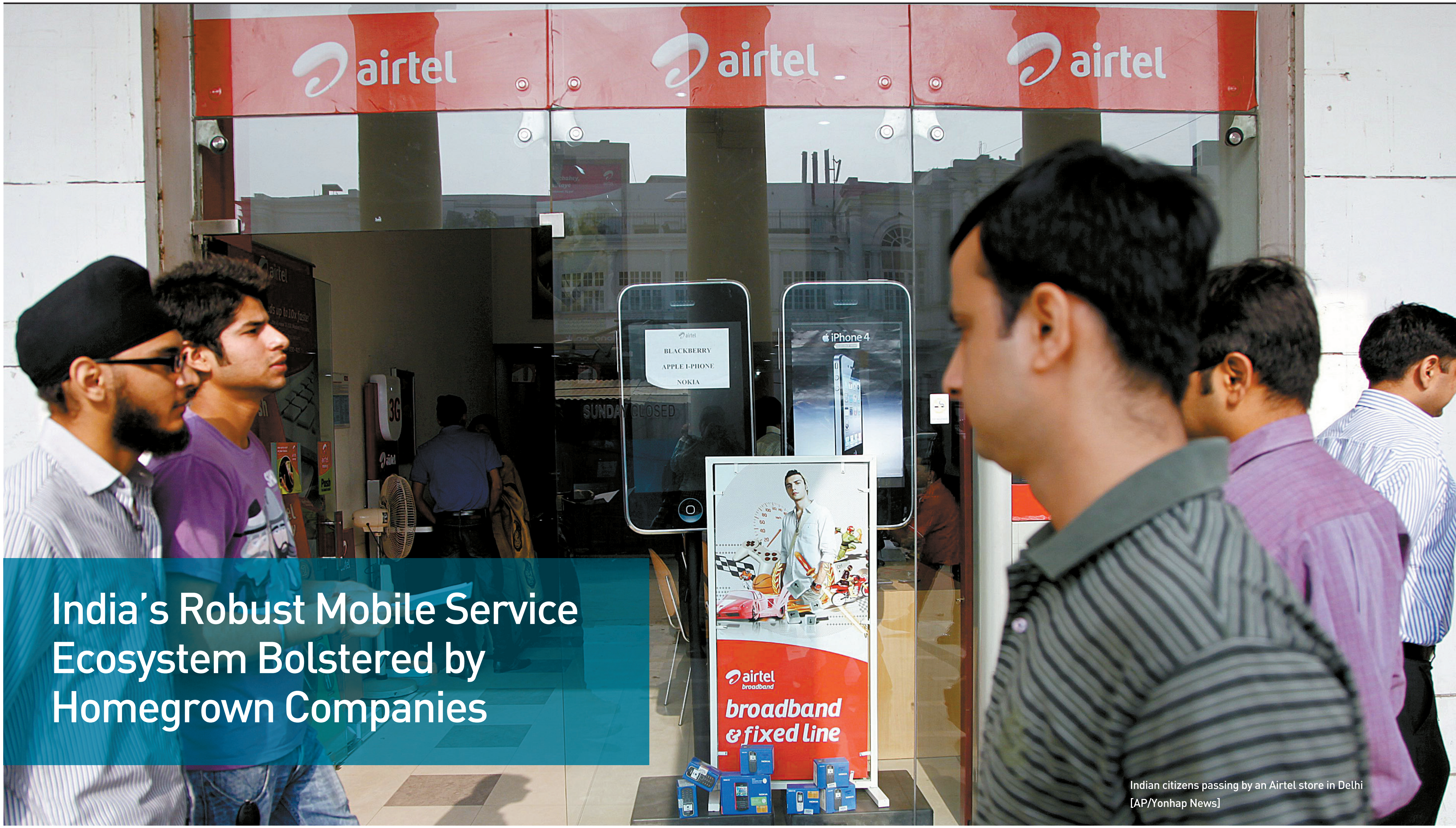
India's Robust Mobile Service Ecosystem Bolstered by Homegrown Companies



Indian citizens passing by an Airtel store in Delhi
[AP/Yonhap News]

Due to strict government regulations, local companies have been leading India's mobile telecommunications industry. Excluding Vodafone, there are no notable foreign mobile telecom companies. Indian companies have a stronghold on the market. Unlike in China, independent telecom tower companies are leading the Indian market. As for smartphone hardware, foreign companies, including Samsung and LG, led the market until recently, but these days, Micromax and other Indian companies are quickly gaining ground. The IT venture companies that are shining in the smartphone application sector are also homegrown companies.


AP/Yonhap News

Intense competition among the top three mobile telecom operators

The Indian mobile service market can be divided by wireless technology into GSM and CDMA. India had 794 million GSM subscribers and 74 million CDMA subscribers as of March 2013. The number of CDMA subscribers is only about one-tenth of the number of GSM subscribers. Reliance Communications is the leading CDMA service provider in India, with an 11.3% market share as of December 2014. Its share was 17.7% in 2008, but it lost market share to GSM service providers over the last six years.

Looking at regional distribution of wireless service providers in India, Bharti Airtel, Vodafone India, and IDEA Cellular cover the entire country. Mahanagar Telephone Nigam Limited (MTNL) offers service only in Delhi and Mumbai, while Bharat Sanchar Nigam Limited (BSNL) covers all of India except Delhi and Mumbai.

Unlike in the hardware sector, Indian firms stand out in the service sector. Government regulations have been a factor, but Indian IT venture companies have played a major role, as in the example of app development.

With a view to expanding wireless service networks, India's telecom operators have competitively expanded their networks. As a result, eight to ten providers are competing for one region.

Despite fierce competition, the total market share of three major Indian companies—Bharti Airtel, Vodafone, and IDEA—reached 58% at the end of 2014, up 5%p from 53% at the end of 2008. The number of companies with more than 10% market share declined from five in 2008 to four in 2014, because the combined market share of state-owned BSNL and MTNL dropped to 9%.

In addition to fierce competition, Indian telecom operators now face many challenges. One challenge is high tax rates. Operators are subject to a license fee (8% of adjusted gross revenue), service tax (12.36%), and spectrum usage charges (3-5% of AGR). They are also burdened with the cost of 3G and 4G spectrum auctions.

Market Share Change of India's Mobile Operators in terms of Subscriber Base

Company	Market Share (%) Dec.2008	Market Share (%) Dec.2014
Bharti Airtel (GSM)	24.7	23.0
Government Expenditures (CDMA)	17.7	11.3
Vodafone (GSM)	17.6	18.9
BSNL/MTNL (GSM, CDMA)	14.5	9.0
Idea+Spice (GSM)	11.0	15.9
Tata Teleservices (Gsm, CDMA)	9.2	7.0
Aircel (GSM)	4.6	8.3
Telewings/Uninor (GSM)	-	4.6

Source: Statistics Indonesia, 2013

Telecom tower companies going independent

Currently, there are about 650,000 telecom towers in India. This number is growing by 40% each year, mainly because of massive investment in rural areas for effective wireless services. About 1 million telecom towers will be installed by 2017. India's telecom tower industry had revenue of INR 485 billion in 2012.

About 72% of India's telecom towers are owned by wireless telecom operators, and the remaining 28% are owned by independent telecom tower companies. In Europe, telecom towers are owned by wireless telecom operators, but they generally share telecom towers, while independent tower companies are just emerging. In the USA, the telecom business and the telecom tower business are two different businesses. The two largest telecom tower companies jointly hold more than 30% share in the U.S. market, and the number of tower companies continues to rise. India's telecom tower business falls somewhere in between the USA's and Europe's: as in the USA, India's telecom tower sector is independent from the telecom sector, but the share of Indian telecom operators is not as high as in the USA.

The reasons for the rising number of independent tower companies are as follows. Threatened by declining profitability due to fierce competition over the building of networks, wireless telecom operators over-expanded their businesses to increase market share and became burdened with massive loans. Under pressure to save costs, some telecom operators began sharing telecom towers, and even spun off subsidiaries to operate telecom towers. In this way, India's major telecom tower operators have separated from their parent companies.

Exceptional performance of Indian companies in the smartphone app sector

According to India's representative portal, YourStory, Indian smartphone users are increasingly using made-in India applications. As India's smartphone market is led by Android smartphones, most apps operate on the Android platform.

The most popular Indian app is Hike, a messenger app, followed by mobile commerce app Paytm and online store Flipkart. Hike messenger gained popularity with functions tailored to Indian users, and hit 35 million users within only one year of its launch. Despite an offensive by foreign messenger apps such as Facebook and Telegram, Hike is rapidly increasing its user base.

The following are some popular apps on the market by service category. In the travel sector, redBus offers online bus ticketing services. As of 2014, this app had more than 1 million users. MakeMyTrip, which was already a popular online site for flight, bus, and hotel booking, also has more than 1 million app users. In the entertainment sector, BookMyShow is the best-known app. BookMyShow is a movie ticket booking application that has more than five million users. In the news sector, Cricbuzz, an app for the latest cricket news, and Newshunt, have five million users each. In the online shopping sector, Paytm is the best-known app. FreeCharge, which provides pre-paid mobile recharge service, has one million users. In the gaming sector, poker app Teen Patti and Parking Frenzy, a driving and parking simulation, are popular. These apps are generally developed and serviced by Indian IT companies. Eyeing the growth of these companies, investors are seeking them out.

Unlike in the hardware sector, Indian firms stand out in the service sector. Government regulations have been a factor, but Indian IT venture companies have played a major role, as in the example of app development. Indian app developers are inferior to global app developers in terms of company size and product quality. Considering their software development ability and global sense, however, it will not be long before smartphone applications made in India become popular overseas.

Affiliation of Wireless Telecom Operators and Telecom Tower Companies

Wireless Telecom Operator	Telecom Tower Company
Bharti Airtel (GSM)	Bharti Infratel Ltd. Indus Tower Ltd.
Reliance	Reliance Infratel Ltd.
Vodafone	Indus Tower Ltd.
BSNL	MTNL, BSNL, etc.
Idea	Indus Tower Ltd.
Tata	Viom
MTNL	BSNL, MTNL, etc.

Source: ICRA Research

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On the Brink of 1 Billion Mobile Service Subscribers, Entry of Major Global Companies Turns India into a Battlefield

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India has the world's second largest telecom subscriber base after China. In 2013, India had 890 million mobile service subscribers. This figure reached 970 million at the end of 2014. India's mobile phone market continues to expand. As a result of continuous economic growth and an increasing number of rural mobile service subscribers, India is projected to have 1.1 billion subscribers by 2019, becoming the second country to eclipse 1 billion mobile service subscribers. India's mobile service subscription rate is 62.5%, far lower than the global average of 93.5%. Compared to China's mobile services market, which has a mobile service subscription rate of 92.3%, India's mobile services market has room to grow.

A massive emerging smartphone market

Notably, India's mobile services market is transitioning rapidly from feature phones to smartphones. The market is also changing in terms of growth method, from quantitative growth to qualitative growth. In 2013, feature phones accounted for 90% of India's mobile services market, while smartphones accounted for the remaining 10%. Smartphone sales increased by more than 20% each quarter. The share of smartphones surged to 65% in the fourth quarter of 2014, while the share of feature

Female students looking at their mobiles phones in Kolkata, India
[AP / Yonhap News]

phones dipped to 35%. If this trend continues, India, currently the world's sixth largest smartphone market, will surpass the United Kingdom, Japan, and Brazil by 2017, and emerge as the world's third largest market after China and the USA.

The reason for the jump in smartphone sales and the share of smartphones in total phone sales is a large supply of budget smartphones. Indian consumers no longer have to spend over USD 300 on smartphones, because domestic and Chinese smartphone makers have rushed to offer affordable smartphones priced between USD 100-200. New products such as Xiaomi's Redmi Note and Micromax's Canvas Nitro and Canvas Hue fulfill consumers' desires for faster speeds and wider screens.

Small but fast-growing m-commerce

India's m-commerce (mobile commerce) is growing rapidly in the Asia Pacific region. According to Forrester Research's online retail forecast, India will have 125 million online buyers by the end of 2019. Forrester expects the number of people using mobile phones for purchases to overtake the number of people using PCs for purchases in 2016, and mobile phone purchases to reach USD 19 billion by 2019.

About one-third of Indian people live in urban areas, but only 8% of them live in first-tier cities with good e-commerce infrastructure, such as Delhi, Mumbai, and Chennai. Other cities have lower PC and broadband penetration rates, making e-commerce difficult, and have fewer offline stores than first-tier cities. These cities will serve as fertile ground for the development of m-commerce.

India's mobile shopping application developers are increasing investment to seize opportunities in m-commerce. One of the country's major online shopping sites, Paytm, currently processes an average of 320,000 orders made on mobile devices per day. Paytm is looking to raise USD 200 million to increase its capacity to 1 million orders by 2016. In order to boost m-commerce, India should refurbish logistics and delivery systems. To this end, Indian companies are working to utilize the networks of India Post and petrol outlets to increase their coverage.

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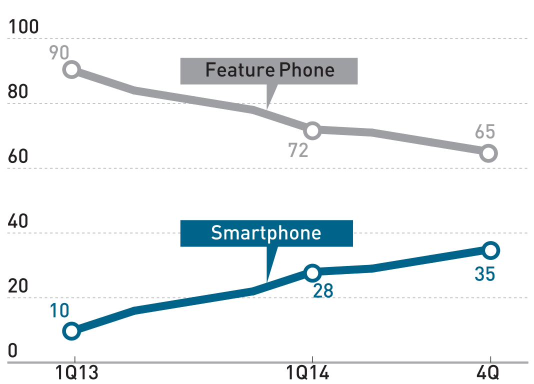
Feature Phone to Smartphone Transition in India

(Unit: %)



Source: IDC Asia Pacific Quarterly Mobile Phone Tracker

Strict government policies

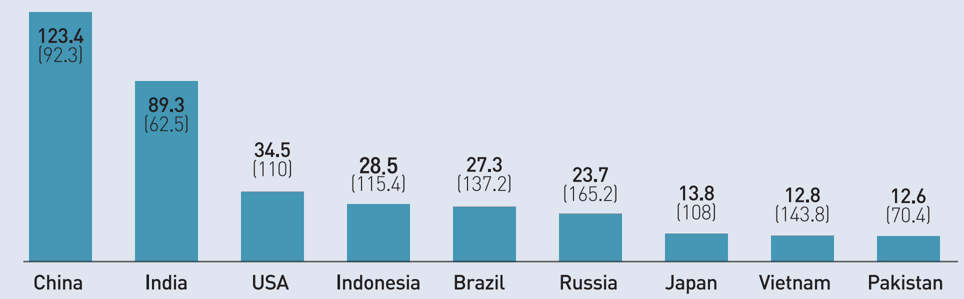
Competition for 3G spectrum is fierce in India's mobile services market. In 2010, a 3G spectrum auction opened the door to foreign players in India. The floor price for the auction of 3G wireless licenses set by the Indian government was roughly USD 6 billion. However, the auction failed several times as the bidding price climbed higher than expected and economic slowdown continued. The Indian government aims to finalize the auction by August 2015.

As of 2015, top national carriers Bharti Airtel, Vodafone, and Reliance Communications are competing in the 3G spectrum auction, and the bidding price has reached USD 13 billion. With fiercer competition than ever before, the price will increase to a record high. In India's mobile services market, where insufficient spectrum and infrastructure are major hindrances, mobile service providers cannot help but buy more spectrum to respond to the growing market. In the future, competitive prices for 3G spectrum will be a major determinant of the development of corporations.

India's taxation policy is also a major hindrance to market growth. There is an increasing number of cases wherein tax authorities set taxation goals and impose taxes on multinational corporations accordingly. India did not impose a capital gains tax on Vodafone for its purchase of an Indian firm in 2007, but it later reversed its decision and imposed a retroactive tax of more than USD 2 billion on the deal. In 2012, India's Supreme Court ruled that Vodafone was not obligated to pay the tax, but the Indian government passed retroactive legislation and imposed the tax again. Later, under the Modi administration, the Supreme Court again ruled in favor of Vodafone, thus opening the way for foreign investors.

No. of Mobile Phone Subscribers by Country in 2013

(Unit: 10 million people)



Note: The numbers inside the parentheses denote share of mobile subscription (%)
The share of mobile subscription is the ratio of mobile service subscribers to total population.
Source: Paul Lambert, Informa (Q2 2013); national telecoms regulators

In 2013, the Indian government removed the 74% foreign direct investment cap for telecom firms and opened the door wide for foreign investors. This allowed foreign companies, which used to enter India through joint ventures, to independently establish subsidiaries in the country. Since then, foreign telecom companies have entered India one after another. Japan's IT conglomerate NTT Communications hopes to be the first Japanese company to acquire a telecom license, and to begin providing domestic network services in India by the middle of 2015. South Korea's Samsung Electronics has inked a deal with Reliance Jio Inforcomm (RJIL) to bring a 4G LTE network to India. South Korea's mobile equipment manufacturer S-TECH entered India's LTE base station antenna business, together with Reliance Communications, to bring LTE services to 700 cities. China's TCL is planning to expand its smartphone business in India. Xiaomi has entered India's 4G market in partnership with Airtel.

Currently, 15 companies are involved in cutthroat competition in India's mobile services market, which is under strict government regulation. They have to obtain licenses separately for 20 regional service areas. Moreover, new players in the market are risking huge losses by undercutting the mobile calling charges of existing operators by more than 20% to attract customers. India's mobile service industry, the fastest growing in the world, will grow into a major industry in the future. However, competition is fierce and government policies are inadequate to support the market's rapid growth. Companies hoping to succeed in the Indian mobile services market should consider these conditions carefully.