Economic Of Food Delivery Business

Zomato calculates the contribution per order and looks at the overall financials for a month. Since the business has its peak and non peak duration the orders during peak hours will make good profits while the orders during non peak periods will be less profitable. But it is important for the business to make sure that overall order economics is profitable for the entire month considering the peak and non peak periods.

The below table shows the sample data for about 7,50,000 orders processed and fulfilled in a month by Zomato. There are two types of order a) The ones which are delivered by restaurant on their own, called Type A order and b) The ones which are delivered by Zomato through their delivery and logistics partners, called Type B orders. Of the overall orders, Type B contributes to about 20% of the orders in a month.

Average Order Value / Ticket Size / Basket Size

Average order value represents the average value of the both Type A and Type B orders during a given period of time. This average order value is arrived at after deducting the discounts given to the consumers. Order can be discounted both by Zomato and the restaurants. Orders discounting by Zomato is less than 2% of the overall orders while 27% of the orders are discounted by the restaurants. Discounting by the restaurants is known as pricing and not the discounting.

Take-rate/Commission/Gross Margin

Commission or Gross Margn represents the money paid by restaurants to the Zomato for getting the food delivery orders through Zomato Platform. This is usually fixed as a percentage of the order value. This percentage would bet higher in the case of Type B orders as it would include the charges for delivery of food orders to be be paid to Zomato. As per the sample data, average commission for Type A order is 8.2%and for Type B order is 18.2%. Type B order commission would include charges for order delivery.

Delivery Cost

Applicable only for Type B orders, this is the cost incurred to deliver a single order. This is a loaded cost, which means it includes salaries for delivery staff, the equipment and vehicles they use, as well as training and administrative costs. Zomato pay Rs 50 to our delivery partners per order on an average, while it costs them Rs. 62/- per delivery. Because of the spiky nature of the business, the delivery cost would work out to ~Rs 105 per delivery. Of course, in some dense areas, during peak times, this can be much lower. But over a month, over all the markets you serve, it makes no sense at all, and you will lose more money than you can ever imagine recovering in any way possible.

Processing and Support Cost

Processing cost includes the telecom data fee they incur when they automatically transmit a new order over to the restaurant. However, sometimes the device at the restaurant's end has a bad signal, and we have to then make an SOS call to them to get the order processed. The network is designed to have 95% automation, but it ends at 80% automation because of data/battery issues at the restaurant's premises. Obviously, automation is way cheaper, easier, and quicker than making a call to relay an order. Then there's the support cost, which is what they incur when something goes wrong, and the customer raises an issue with our support team. For Type A orders, they only have a two-way conversation to handle – between the customer and the restaurant. For Type B orders, they have a three-way conversation to work with – the customer, the restaurant, and the delivery partner's person who is on the road.

The total processing and support cost as per sample data for Type A orders adds up to Rs 18.4 per order. For Type B orders, it adds up to Rs 27.4 (primarily because of the three-way calling, which adds more support agent time, and tariff to the cost stack). Three-ways aren't always a good thing.

Six months ago, our support cost was about Rs 50 per order – Zomato has managed to bring this down to current levels with automation, and by making hundreds of micro improvements

Net Contribution Margin

Net contribution margin = (AOV * Take Rate – Delivery Cost – Processing Cost)

this is what contributes towards the overall profitability of the business, and has to over time offset the fixed cost of the business.

Customer Acquisition Cost

This is in the nature of marketing cost for business. This is beyond per unit margin for the order and is fixed in nature. How much CAC you incur, depends upon the quantum of discounts or money require to be spend to acquire each customers.. Most e-commerce/transaction businesses have a traffic problem. Unless customers visit the platform for something else (e.g. content, reviews, photos, and sharing) and then naturally move into the transaction flow, it is very hard to drive high re-engagement rates for commerce platforms. And that's exactly what makes it easy for us at Zomato – the classifieds business, where they have 8.5 million monthly unique in India alone. And so far, less than 3% of them are ordering from us. There's massive room to grow without incurring too much customer acquisition costs.

About the Authors

Sanjeev Kumar is from the organisation of the defence forces and has got a wide variety of experience in managing men and material in trying circumstances. In an eighteen years span of his illustrious career the author had the privilege of tenanting various command, staff and instructional appointments. He has served in the most difficult of terrains of the country to include lofty peaks of Kargil and Kashmir valley to thick jungles of Assam.

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This case study is being prepared under the guidance of Dr Monica Singhania, Professor, Faculty of Management Studies (FMS), University of Delhi. She is a graduate from Shri Ram College of Commerce, post-graduate from Delhi School of Economics and a Fellow Member (FCA) of the Institute of Chartered Accountants of India. She has the distinction of being placed in the merit list of the examinations conducted by both the University as well as the Institute. She has been awarded a PhD in the area of corporate taxation from the University of Delhi. She is the author of five books on direct tax laws and has had many research papers published in leading journals. She teaches management accounting, management control systems, project management and corporate taxation to MBA students at FMS

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Teaching Notes

Monica Singhania

The purpose of this case study is to do an analysis of the way Zomato has scaled up its operations, expanded its business into various countries and then course corrected the operations to reduce the cash burns. We will also be looking the details of the order unit economics of the Food order delivery business and how the detailed cost benefit analysis has helped them take various decisions / evaluate options enabling them to optimise their contribution per order to recover fixed costs. We will also be evaluating how their relentless focus on costs take out has helped identify opportunities and deliver on cost reduction. We will study how the Zomato has constantly innovated to drive new products and offering resulting into new revenue streams. We also plan to find out the strengths, weaknesses, future opportunities and threats of their business model, Porters Five forces model and financial modelling to understand the financial decisions taken by the Zomato to drive business growth, break-even and valuation.

The case can be used in the following courses:

- Post-graduate program in entrepreneurship. Students can be introduced to different cost concepts to be considered in cost benefit analysis while undertaking managerial decision making.
- Executive training program for middle and senior level employees to highlight the concept of looking at various cost and revenue factors that influence the decision making process and can be applied to new projects as well as projects not performing as per the objectives of the organization.
- MBA/post-graduate program in management in strategic management. It can be used to introduce the concept of SWOT analysis, competitor analysis, and Porter’s five forces model. In addition, students learn the technique of marketing, innovation, cost benefit analysis, collection of relevant cost data, forecasting revenues and using them to arrive at a decision aimed at meeting the company’s objectives.

Zomato is an online ecommerce business which has the information on food joints, restaurants and cafes. It is also in the business of online food ordering, delivery and providing options for table booking in various restaurants. In 2008, it was started by Pankaj Chaddah and Deepinder Goyal (both of them were from IIT Delhi). The initial name of the website was Foodiebay.com and this was renamed to Zomato in November 2010. The key idea behind the name Zomato was that it resembled with Tomato. Zomato has now operations spanned across 24 countries including India. The other key countries include Dubai, United Kingdom, Australia/ New Zealand, Turkey and Canada. Zomato has been recognised as the "25 most promising internet "companies in India by SmartTechie Magazine.

The revenues of the company have grown exponentially from Rs 11 Cr in 2012-13 to Rs ~450 cr in 2017-18 and it has achieved an EBIDTA breakeven globally in the year 2017-18. It has also been able to attract continuous attention investors and has got investments more than $ 400Mn till June2018. In this case, we will evaluate the decision taken by company over the years to drive growth and improve unit economies to help them achieve breakeven.

Expected Learning Outcomes (limit 250 words)

Use of SWOT analysis to identify the strengths, weaknesses, opportunities and threats

Highlighting the importance of strategic tools such as Porter model and evaluating the impact of competition and new start-ups in this area

Understand the variable cost and Marginal contribution with respect to the unit economies of food delivery in India.

Understand the sources of revenue, marketing and innovation techniques, elements of fixed and variable costs in the business. Capture the various cost optimisation scenarios, backward integration / acquisition to develop capabilities and their implications on the unit economics / business.

Capture Pros and Cons of certain business decisions from a sustainability and long term perspective

Most of the information and data used in this case study will be based on information available in public domain, company website and views of the founders as expressed through various interviews. There is a limitation on the availability of the financial data as the company is not a public listed company.

In a short span of just ten years, Zomato has become India's favourite online Food Order/ Delivery and Restaurant selection platform. It has influenced and changed the way people have their meals, both in house and outside in hotels or restaurant. Zomato's mission of being able to deliver nutrition rich, hygienic meal for under Rs 50/- will have significant life style implications mass consumers in India. The real challenge would lie in replacing the home-cooked food with a restaurant and outside food. Zomato's launch of Cloud Kitchen, an innovative concept will really change the way we order food today. The ambition is to serve 2-3 billion orders a month. This will also lead to significant employment generation in the country as these orders needs to be delivered.

Its new initiatives like Table reservations and Zomato Gold aims to provide differentiated services to specific section of consumer. User engagement is the biggest social factor of Zomato. User Reviews and User Ratings make the website very engaging and ensures a high level of customer participation. The latest concept of Food Hygiene Rating for restaurants listed on the Zomato addressed the user’s care for hygiene. Zomato’s founder Deepinder Goyal now has laid down the long term vision for Zomato – “The biggest farm to table Food Company in the world”.