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TIER 2 AND TIER 3 CITIES: THE GROWTH ENGINES OF INDIA

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ABSTRACT

As services sector started growing over manufacturing and agriculture, lack of employment opportunities, career growth and crumbling infrastructure in India's smaller cities and towns drove country's youth and labour to tier 1 cities. However, latest trends indicate economic revival and better growth opportunities as tier 2 and 3 cities in recent years making them next big markets for companies. In the 2010s, the overcrowding, pollution and high cost of living in tier 1 cities was compelling retiring people to move out to tier2 and 3 cities which offered better life. However, with increased public investment and better telecom services availability, these cities have become lucrative with higher captive consumption forcing more people to stay back and even return from tier 1 cities. People are investing in retirement properties in the tier 2 and 3 cities. Start-ups find these cities attractive as the initial costs are much lower, skilled personnel and their retention are affordable, and local authorities a lot friendlier than tier 1 cities. The co-working companies have expanded into smaller towns making it easier for start-ups to start functioning without heavy initial investment. Internet penetration in India helped in rising trend of smaller cities, improvement in connectivity has made these smaller cities more attractive. Growing consumerism also attracted retail and supermarket chains to open modern retail stores. Opening of malls and multiplexes, pubs and fast food restaurants made people never feel like missing on big city charms. Launching of delivery services by ecommerce players and cab hailing apps narrowed the service facilities enjoyed so far only by big city residents. The consumption boom led by these cities in all spheres make them next growth engines of India.

Keywords: *Tier 2, Tier 3, E-Commerce, Internet Penetration, Consumerism.*

Introduction

Objective

- To understand the factors helping tier 2 and tier 3 cities to grow.
- To understand the changing role of tier2 and tier3 cities in the economic development.
- To explore shopping and consumption pattern of consumers and suppliers in tier2 and 3 cities in India.

Introduction

The real measure of economic growth of a country like India is rise in income of poor families specially outside the metro cities. In the vast geographical area of the country, tier 2 and 3 cities present a huge potential opportunity for local population in terms of various services like education, healthcare, tourism, telecom, logistics, IT/BPO, Financial services etc.

While the number of metro cities in India doubled from 4 to 8 in last decade, several tier 2 and 3 cities with population ranging from 5 lakhs to up to 25 lakhs emerged in presenting alternative destinations for growth of business.

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As the economic growth saturated, cost of living went up and living standards were compromised in the major metros of India. High property prices, overburdened infrastructure in metro cities made some people start shifting to smaller cities. Covid -19 pandemic and lockdown made a large number of labour and executives move back to their home towns from metros. Tier 2 cities like Ahmadabad, Chandigarh, Dehradun, Kanpur, Patna, Jaipur, Cochin, Pondicherry, etc have a population of one million plus, whereas cities with population less than one million like Guwahati, Amritsar, Surat, Vadodara, Nashik and Trichy are termed as Tier 3 cities. These cities are promising great potential to investors and businesses because of ample availability of lowcost land, skilled labour and availability of basic amenities. The growth of tier 2 and tier 3 cities will also reduce the pressure on metro cities along with providing opportunities for growth in these areas. Jawaharlal Nehru National Urban Renewal Mission (JNNURM), a government scheme launched in 2005 helped many of these cities undertake modernisation of infrastructure thereby attracting real estate companies to multiply the effect of such improvements by building better offices, malls and residential houses.

With several state governments improving public infrastructure in the state capitals and increasing public spending and real estate companies riding the bandwagon, companies and skilled manpower have made a beeline for these cities thereby brining along a host of other economic opportunities. State of the art office spaces at affordable prices and equally good network connectivity has narrowed the difference between metros and other towns. Skilled engineers and manpower who was once moving to metros are now returning along with another class of population buying retirement homes in these places. A surge of reverse migration, of executives who lost the employment in Covid-19 pandemic or moved back as WFH (work from home) became the norm has been a strong factor in taking many young professionals back to their homes due to relocation.

Recent announcements over last 2 -3 years by the government on upgrading the urban infrastructure have ensured that the trend is irreversible. The government announced that by 2025, 15 more cities will have metro train networks, all of which are tier 2 cities. Further, 100 additional airports will be built in India by the year 2024 and spending of Rs. 1.7 trillion has been allotted for boosting the transportation infrastructure in the country. The new airports will be a boon under government's UDAN blueprint. Regional air connectivity will ensure easier access to air travel for citizens, particularly in tier-2 and tier-3 cities. IT companies have been successfully operating their software development and BPO centres from several tier 2 cities for past several years due to affordable and sticky manpower, government incentives and low cost of office spaces.

Growth in Tier 2 and 3 cities

A study of Top 10 emerging business destinations in India, conducted by Cushman & Wakefield, a global real estate solution provider, mentions the growth in Tier 2 and 3 cities is aided by the increasing disposable income of the people that has created immense opportunities for companies looking out for new markets to grow. The study also mentions that companies are being attracted to these cities because of 'availability of talent pool at a lower cost, reasonable real estate prices and a 'conducive business environment' created by State and local governments in these cities. Further, because of 'outstanding performance' in skill-based manufacturing industries such as automotive, consumer andcapital goods, engineering, textiles, IT and pharmaceuticals sectors, tier2 &tier3 cities have witnessed industrial growth, providing route for rapid urbanisation. The study identifies the cities of Ahmedabad, Bhubaneswar, Chandigarh, Coimbatore, Jaipur, Kochi, Indore, Nagpur, Vadodara and Visakhapatnam as the top 10 emerging cities of India. Whereas Coimbatore has more than 25,000 small and medium enterprises (SMEs), Vishakhapatnam has been found to be suitable for industries such as mining, heavy manufacturing etc. Jaipur has been counted as a significant service sector investment destination while Ahmedabad has been hailed as an attractive investment in the manufacturing sector. In recent years, tier 2 cities like Jaipur, Patna, Indore and Surat have recorded an economic growth rate of over 40%, making them attractive options for larger firms.

Real estate trends, whether residential or commercial, are noticing a shift and have seen a major growth in these sectors. Businesses find these locations attractive to expand their operations, for back offices and technology centres as they provided rental cost advantages, manpower is sticky and has lesser salary expectations. The local governments are creating clusters and providing incentives, which results optimum development of a specific location, aiding the businesses to further reduce costs. With an increase in employment opportunities provided by above mentioned factors, home buyers are increasingly becoming more interested in the residential properties in these areas making real estate companies launch modern housing projects. Viewed as excellent investment options, these places are more cost-effective than metros which have escalating land and property prices. Many people have been investing in these cities for their second homes for themselves or for ageing parents for whom the pollution and rising costs of living in a metrois a deterrent.

Many move to these cities as they find it better to live closer to their families while some feel that their chances of promotions are better in smaller towns. There is obviously a financial advantage as the cost of living in a tier 2 or tier 3 city is considerably lower than in a metro. Those moving back in with their families can save on rent, which is a huge economic benefit large families.

Many hotel chains are now expanding their presence by launching hotels in tier2 cities.More flights are being added in international airports in cities like Chandigarh, Amritsar, Jaipur, Cochin etc. Also tier 2 and 3 cities mitigate the disadvantages that are associated with metros - of a reduced quality of life, high cost of living, expensive transportation, high pollution level, huge traffic and travel time, expensive house rent and education. Whereas metros are suffering various drawbacks in projects like delay in execution, overall slowdown in demand and a dip in the supply, smaller cities like Pune are experiencing increased demands for mid-segment housing.

E-Commerce Penetration in Tier 2 and Tier 3 Cities

Covid-19 pandemic restricted consumers to shop from their homes and had a major effect on their consumption pattern. Malls and markets were closed and customers had to wait for over 30 minutes to purchase regular groceries in neighbourhood shops due to covid restrictions. This forced them to move to online shopping and home delivery apps. Ecommerce websites witnessed a sharp rise in orders and rising number of new users opting for online shopping for safety and convenience from tier 2 and 3 cities as well.

E-commerce companies already had identified tier 2 and 3 cities as next growth markets and Covid induced lockdown accelerated the adoption of ecommerce. In earlier years, a small user base with a limited smartphone and internet penetration, and a low internet speed made it extremely challenging for e retailers to attract buyers and expand in Tier 2 and Tier 3 cities. When 84% of the total urban population had access to the internet in 2018, the internet penetration was only 16.41% in rural India. However, initiatives by major telecom players in last couple of years created the next revolution making 227 million people in rural India active internet users. According to the latest report, rural India has 10% more internet users than the urban population as of 2019. E-commerce players witnessed a sharp increase in sales of branded products and appliances across multiple categories when shoppers in Tier 2 and tier 3 went online. The key reason for the steep growth of online consumers in Tier 2 and tier 3 cities is the cheap data and mobile recharge plan. The digital adoption in Tier 2 cities in India, strategic surge in mobile internet usage has boosted the expansion of E-commerce to all areas of India to tap a new segment of shoppers who prefer internet content in local languages.

While basic warehousing and delivery infrastructure was already created by the major players, they invested heavily to ensure a great experience for the new online shoppers. Special schemes to attract customers from these areas were also launched. The privilege of a superior lifestyle, whether it be branded clothes and accessories, electronics, gadgets, imported foods etc. enjoyed so far by metro city residents only were now just a click away for all shoppers in tier 2 and 3 cities. Due to covid-19 pandemic, the e-commerce orders in tier 3 cities saw fastest growth at 53% while the top 5 Tier 3 cities contribute 22% of total volume. Taking cues from tremendous growth in this medium, most of the top brands have either launched or overhauled their own websites. According to a report, 65% for the brands have upgraded their own ecommerce website, which led to an increase in orders.

Another problem faced by online retailers was large volume of returns from tier 2 and 3 areas as compared to tier 1 cities. However, during lockdown period, the return rate has seen a significant dip indicating serious purchases. Tier 2 and beyond cities have seen a significant reduction of 23% in overall returns as last mile delivery improved. The return percentage on cash-on-delivery (COD) orders has reduced from 27% in 2019 to 20% in 2020 and for prepaid orders, the total return has decreased from 12% in 2019 to 11% in 2020.

The consumer consumption behaviour and preferences have also changed significantly during covid period with categories like groceries, FMCG, medicines etc seeing a surge and exponential growth with a rise in the number of first-time users (FTUs). Beauty & wellness is another sector that has witnessed an unprecedented order volume growth of around 130%. These are emerging sectors with potential to accelerate e-commerce growth in India.The number of consumers shopping directly from the brand’s websites have witnessed 88% order volume growth as compared to 32% order volume growth on marketplaces. The sales of non-essential products is more in tier 2 and 3 cities while shoppers in metros are buying more essential goods during the covid period. Further, expensive smartphones and appliances do well in the metros, while shoppers in tier 2 and 3 cities are more value and price conscious due to their limited spending capacity. They buy lower priced mobile phones and are ready to spend money on personal care products, garments, ethnic wear and branded shoes.COD is still the preferred mode of paying in tier2 and 3 cities as customers still prefer to pay only after getting the product in their hands.

All leading horizontal and vertical e-commerce companies are focusing on cities beyond the metros. Currently, Tier 2 and 3 combined with rural areas contribute around 66% of the total online consumer demand in India. Tier 3 and beyond cities witnessed 53% growth, making it the fastest-growing region. Flipkart's Big Billion Day sale witnessed a whopping 52% visits from Tier 3 and beyond cities, out of a total of 666 Mn visits during their festival sales. Paytm Mall also saw a 2X increase in the number of users from tier 2 and 3 cities. Myntra reported a 180% increase in new shoppers from the tier 3 cities.

Food delivery apps have also witnessed a surge in orders from tier2 and 3 cities.Both Zomato and Swiggy reported 100% traffic increase for dinnertime, however with tier 2 and 3 cities like Jaipur and Vizag, the numbers increased by almost 200%. Swiggy reported tier 3 and 4 cities such as Berhampur, Rourkela and Karimnagar also saw a 150-200% growth, which was higher than what it observed in the metros.

Conclusion

Better road and air connectivity, improved infrastructure, spacious homes, walk to work options with the rise of service sector and local industries and better logistic options have contributed in the growth of cities beyond metros. It is also evident from reports, data and studies that Indian E-Commerce industry has reached next level with all major players focussing on tier2 and 3 city shoppers as rising disposable income, consumerism and a desire to access better products drives new shoppers to ecommerce. The growth potential of tier2 and 3 cities in India has increased drastically with better logistics and telecom infrastructure. The benefit of smart planning in creating more liveable cities have transformed the scenario of small cities.

Research Methodology

Secondary data was collected from various reports, newspaper articles, conference proceedings, articles from peer reviewed journals published journals, magazines, press releases and online articles published in 2020, which help the researcher to write and give a proper shape to this paper.

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