

# Subscription-Based Model: The model of 21<sup>st</sup> Century

Pranjal Jha

*Student, Birla Institute of Technology, Mesra*

Submitted: 20-01-2021

Revised: 31-01-2021

Accepted: 03-02-2021

**ABSTRACT:** In the age of digital economy, subscription-based business model is the bread and butter of many of the technological companies, it helps many of these companies retain customers, build better and up-to date products, increase the revenue of the firm and make sure of cash flow for the time of subscription. We have seen many famous subscription business models like Spotify, Netflix, MS Office, Amazon Prime to name a few. But the subscription-based business model is limited to e-commerce, SaaS and streaming services and since we have seen these businesses give their customers value for money. So, instead of limiting this kind of business model to online players if brick and mortar stores and other kinds of offline firms start their subscription services then they could decrease the cost of the product offered by creating a group of loyal customers hence decreasing any wastage of products if they crossed their expiry date and by going public help the capital markets to grow enormously. And since Indians' investment habits do not give them a high rate of return on their investment, these subscription-based firms may help them save more money through subscription benefits, and then generate more through investment. It will even increase consumer spending and thus drive the economy for a better future. It would decrease the chances of companies filing for Bankruptcy as it would provide a surety of Cash Flow hence decreasing the chances of a NPA and would allow companies to make more risks for larger profits. A subscription-based business model would allow business to grow exponentially and even expand to different countries and markets in a faster way, if implemented perfectly, it can help India achieve \$5 Trillion Mark and would even help some of our domestic companies to give a good competition to not just foreign firms locally but also in their home market.

**KEYWORDS:** subscription-based, Capital Markets, Cash Flow, NPA, consumer spending, investments, Derivatives, Hedging

## I. INTRODUCTION:

There are many styles of business models, such as Barter Model, Razor and Blade business models, Reverse Razor and Blade business models, Hidden Revenue Business models, Peer to Peer business models, a Cash Machine business model, subscription-based model and many more. In this paper, we will concentrate on the business model focused on subscription and how it can benefit both consumers and businesses.<sup>[1]</sup>

The subscription-based business model is a model in which the consumer is expected to pay a recurring fee for access to a product or service at periodic intervals. That form of service helps to boost loyalty to the company, only one-time product sales will build a lifelong customer. A contract may be extended periodically and automatically triggered in such a way that the cost of a new term is automatically charged by a pre-authorized payment to a credit card or debit card, thereby keeping the customer stuck even if they do not wish to do so.

The Freemium model (Free Premium model) is one of the common variations of this business model, which means that customers do not pay for content at first, they then have to pay for better services / premium content.

In subscription models, there are two types of payment structure:

1. Pre-payment: You pay the product in this kind of payment, or simply pay in advance for the product or the service.
2. Post-payment: in this case, you use the facilities, and, like a news account, you pay them afterwards.

Customers pay for the service at the outset of the process with the pre-paid pricing model and only use their service over the payment period. The companies benefit from this type of payment service since they are sufficiently liquid to operate and have a certain number of customers during the duration of the subscriber agreement. This greatly decreases the company's vulnerability and risk.<sup>[1]</sup>

The subscription price mechanism is made for software systems to greatly improve the income

from annual transactions relative to the income from single one-time sales. It also raises revenue of many subscription services (like magazines), by not offering consumers the opportunity to approve or deny any specific issue. This reduces the costs of obtaining consumers and makes for targeted campaigns. However, the requirement for this system is that the company must manage and track subscriptions accurately and efficiently.

This has the vendor's additional advantage, understanding the precise number of users actually participating as a membership usually requires a binding arrangement. This environment massively promotes customer experience management, as the organization has reliable knowledge from Active and In-Active stakeholders.<sup>[1]</sup>

Many benefits include a higher Average Customer Life Value (ACLV) than non-recurring market models, lower consumer apathy and a larger client base, since it has the ability to up-sell and cross-sell many goods or services.<sup>[1]</sup>

Some IT firms have moved from a contractual model of licensing to a subscription model, known as "software as a service" OR SaaS model. This move has important implications for organizations providing sales and customer support.<sup>[1]</sup>

Consumers may find subscriptions useful because they plan to buy a product on a regular basis which may save them money. The consumer often saves time with regular usage of the product or service.

Most subscriptions to newspapers and magazines are paid in advance, and this might prevent a certain client from paying the fixed price, which would benefit consumers frequently using these services. It may, however, be a drawback for a customer who plans to consistently use the service but then drops out. The decision to pay for a kit may have been more costly than would have been a single order. Furthermore, subscription structures raise the risk of product lock-in, which can have seriously commercial-critical effects for a company

because its business depends on the quality of a program.<sup>[1]</sup>

Subscription structures frequently allow or authorize businesses to obtain large volumes of consumer information (such as magazine mailing lists), increasing privacy concerns.<sup>[1]</sup>

A subscription model may be of benefit to the consumer of the software if it encourages the manufacturer to improve its product. Therefore, if a customer renews a subscription which may not occur during a single deal, a psychological phenomenon may occur: if a buyer is not satisfied with the service, we can leave the subscription or cancel a subscription simply, get the money back and find another seller.<sup>[1]</sup>

This contrasts with many one-time transactions, when customers are forced by high software prices to make significant commitments. Historically, some feel that the "one-time-buying" model does not give sellers incentives to maintain relationships with their customers. Some who favour a software subscription model do so because it could perhaps change that situation.<sup>[1]</sup>

The subscription model is meant to match buyers and sellers with similar interests, since both will thrive if the subscription gives the buyer value. The user who gets interest is most likely to renew the service and maybe at a better cost.<sup>[1]</sup>

So if we actually apply this kind of model that already operates in the media and SaaS field across all sorts of entertainment, food, clothes and other kinds of businesses, then we will save our consumers a lot of time, help them get the right product for their cash and also boost the profits of all these kinds of businesses, building a fairly nice competition.

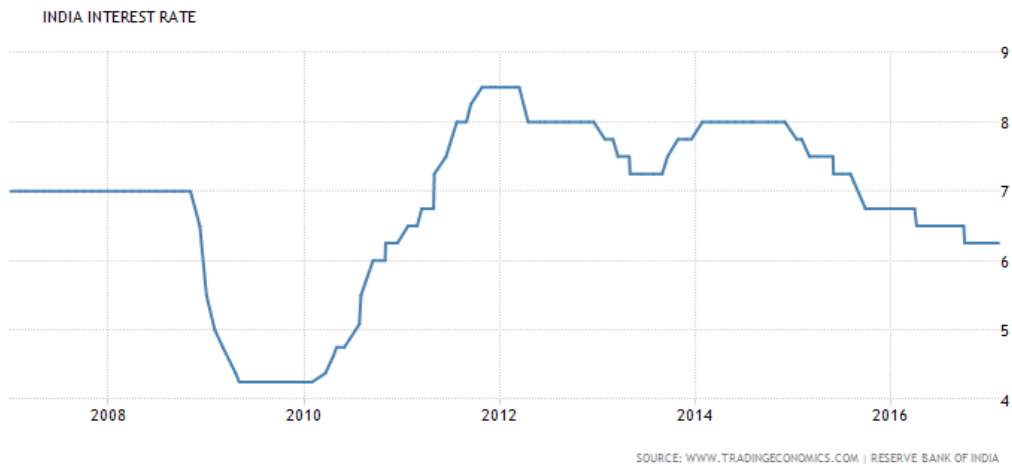
## II. RESEARCH METHODOLOGY:

The GDP of the country stands at **\$2.94 Trillion<sup>[4]</sup>** with a population of over **1.37 Billion<sup>[5]</sup>** taking the GDP per capita of the country to around **\$2146** and the GDP(PPP) of the country is around **\$10.51 trillion<sup>[4]</sup>** and per capita income (PPP) of around **\$7672**.



SOURCE: TRADINGECONOMICS.COM | MINISTRY OF STATISTICS AND PROGRAMME IMPLEMENTATION (MOSPI)

**Graph 1: Inflation Rates of India<sup>[2]</sup>**



SOURCE: WWW.TRADINGECONOMICS.COM | RESERVE BANK OF INDIA

**Graph 2: FD rates of India<sup>[3]</sup>**

The first graph is the inflation rate for the period 2014-2018 and the second graph is the FD figure for the period 2008-2017.

If you can see, the difference between the rate of inflation and the rate of FD returned by the

banks is about 2%, and the actual rate of return is just 2%-3%.

Therefore, if you invest in FDs, the actual rise in your assets (only taking inflation into account) will be just 2-3 percent.

Scheme	AUM (Rs in cr)	Ratings	5-year returns (%)	Returns since Inception (%)
SBI Small Cap Fund-Direct (Growth)	1604	5-star	29.5%	26.5%
Mirae Asset Emerging Bluechip-Direct (Growth)	6,444	5-star	26.6	24.9
L&T Midcap-Direct (Growth)	3,733	5-star	23.4	21.2
Aditya Birla SL Equity – Direct (Growth)	10,027	5-star	19.2	17.7
ICICI Prudential Bluechip fund – Direct (Growth)	20,101	5-star	15.4	15

Scheme	AUM	Rating	5-year return (%)	Return since inception (%)
Axis Long term (ELSS)	17,426	5-star	19.3	20.1%
Birla Tax Saving 96- Direct (Growth)	7,561	5-star	19.4	17.9
Invesco India Tax-Direct (Growth)	712	4-star	19.4	18.3

### 5 Year Mutual fund Returns<sup>[7]</sup>

These are the data on the rate of return for some of the best mutual funds in the country, as we all know that mutual funds are subject to market risks, so it does not always infer profits if we carefully consider that some years would have been losses, while others would have been profitable, but on average mutual funds would have a rate of

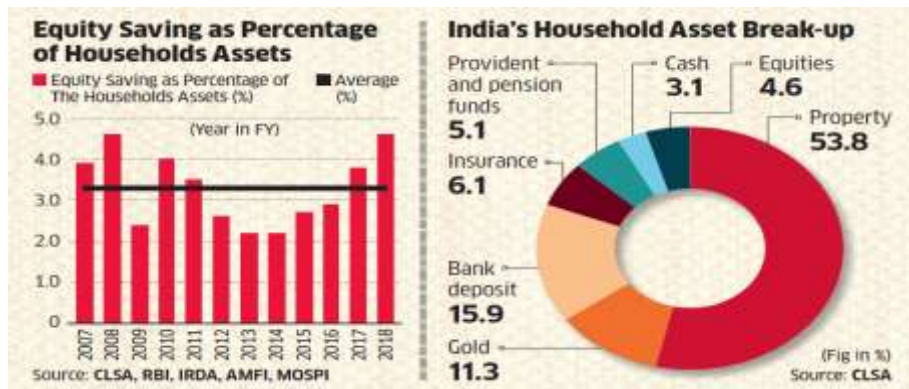
return of 8.5-21% per year if they had been invested for an average of 5 years.

Investing in mutual funds is one of the ways people tend to increase their assets, but because of its nature of high price fluctuations, it doesn't garnish most of the wealth people invest to increase their money.

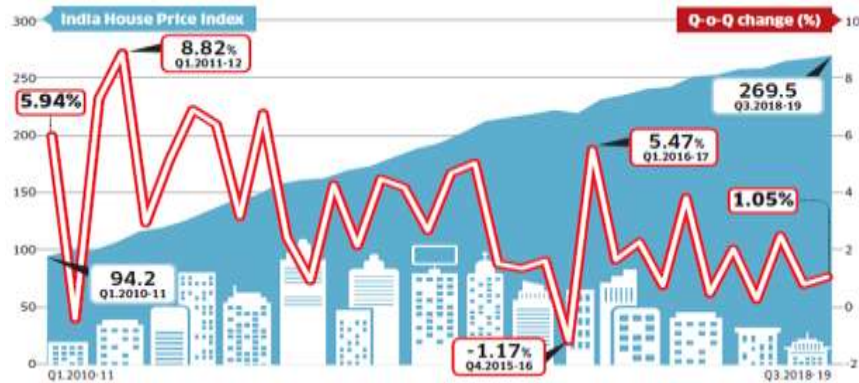
Till now, most of the investments in India is done in gold, property, PFs and FDs.



Graph 3: 5-year Gold Price Chart<sup>[12]</sup>



Indian household Asset Breakup<sup>[14]</sup>



Graph 4: India Property rate<sup>[13]</sup>



**EPF rate in the past 5 years<sup>[6]</sup>**

If Rs.1 million was the asset at the start of 2014, then average asset after 5 years is:

Asset type	Percent retained	y-o-y return% (past 5 yrs.)	Asset increment (Rs.)
Property	57.3	8.1	845831
Gold	12	3.7	143904
Bank deposit*	16.9	7.5	242621
Equities**	4.9	12.87	89761
E Provident Fund	5.5	8.68	83389
Cash	3.4	0	34000
		<b>TOTAL:</b>	<b>1439506</b>

Since, the information given was incomplete \*Bank Deposits is thought to be FDs and \*\*Equities are thought to be Mutual funds.

So, the increase in the assets for an average Indian during the period 2014-2019 is around 43.95% (8.26% year-on-year).

Percentage of increase in cost of a product due to inflation in the period of 2014-2019 is around 29.16%.

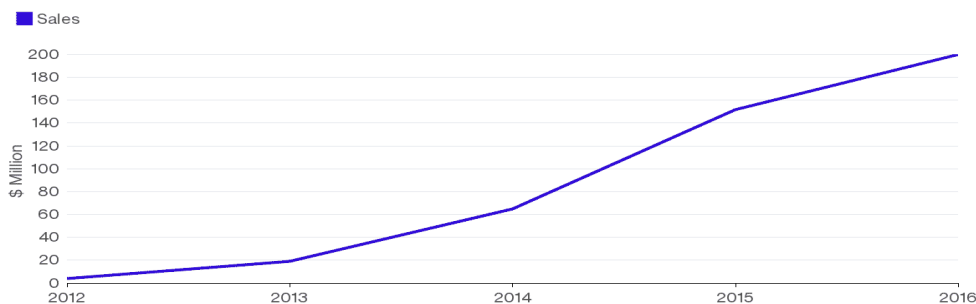
So, the real increase in buying power from 2014-19 is: **14.79%**.

Thus, the real increase in GDP year-on-year from 2014-19 is: **2.8%**.

**With not a very high returns on investments, the Indian economy can afford to see a change in the way of doing business as the GDP is also not increasing fast, neither the NPA rate, nor the BOND rating of Indian government.**

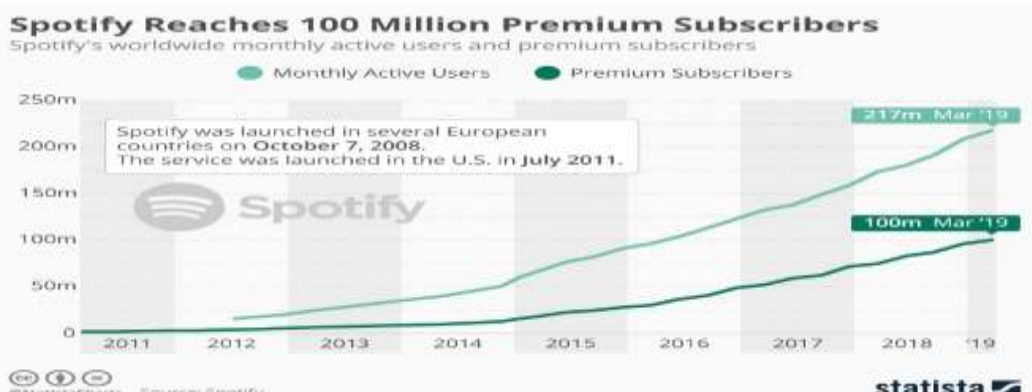
**Blade Runners**

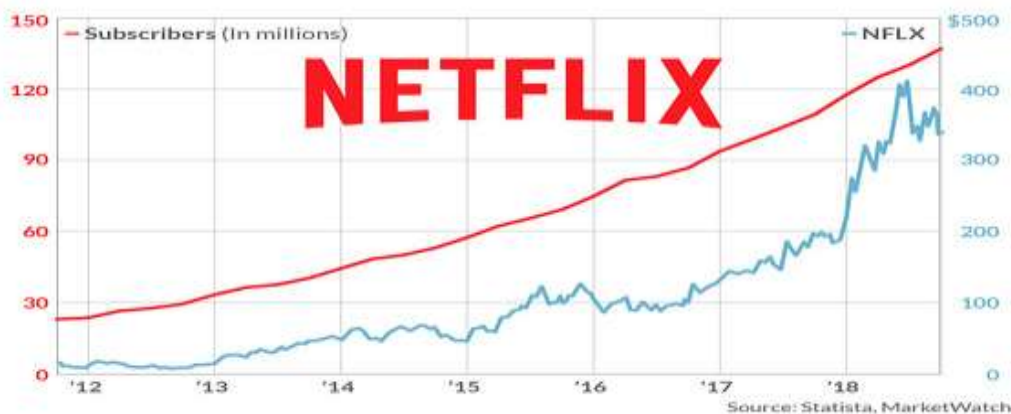
Dollar Shave Club's sales have soared since its 2012 founding, yet competitors now loom



SOURCE: Dollar Shave Club, Unilever

Bloomberg





### Subscription services stats<sup>[9][10][11]</sup>

The two graphs above illustrate how these companies challenged conventional market models by adopting subscription-based business models and providing value for their money to consumers. They were able to offer small costs to their clients and make lots of profits only because they used a subscription-based business model because they did not have such rapid growth in their sales as well as valuation.

This is because, as I have shown in the above pages, a man increases his assets by an average of 44 percent in 5 years, whereas if we use this type of business model he would be able to save more money and get better return rates for his assets.

### Let me explain the above paragraph with an Imaginary Case using the above Data,

Let us have a man with a Rs.40k / month in-hand salary, and let his monthly expenses be around Rs30k and Rs.10k savings. So, he will usually spend his money in the manner seen above and get an 8.3 per cent y-o-y return.

But now suppose the same man bought a year's subscription of groceries instead of saving Rs.10k. Therefore, he would not have much money in the immediate present, but he would not have to buy a few food items in the future.

Now, the main problem is how much monetary value such subscription companies offer their clients?

For example, let's assume that you bought an annual subscription of 5 kg of corn every month, the average price of corn is now Rs.50 / kg, take inflation, and it will be Rs.52 / kg by the end of 12 months (4 percent real inflation).

So, buying 60 kg of rice a year would cost us about Rs.3060.

Profit gained by not taking a subscription and saving is around Rs.139.45 for 60 kg of corn a year costing around Rs.3060, which is a return rate of around 4.55 percent.

So, the company must give the benefit of Rs.139.45/4.55% which we would lose by taking the subscription.

The company would have to price it at the current price or at a lower price, if priced at the current price, then some benefits would also have to be given or else customers won't be loyal for a long term.

The company could even hedge its positions by buying the Corn Futures for throughout the year before hand, and hence they could even pay less than quoted to the customer. As, the futures market is completely unpredictable it allows people to buy products at a very nominal price.

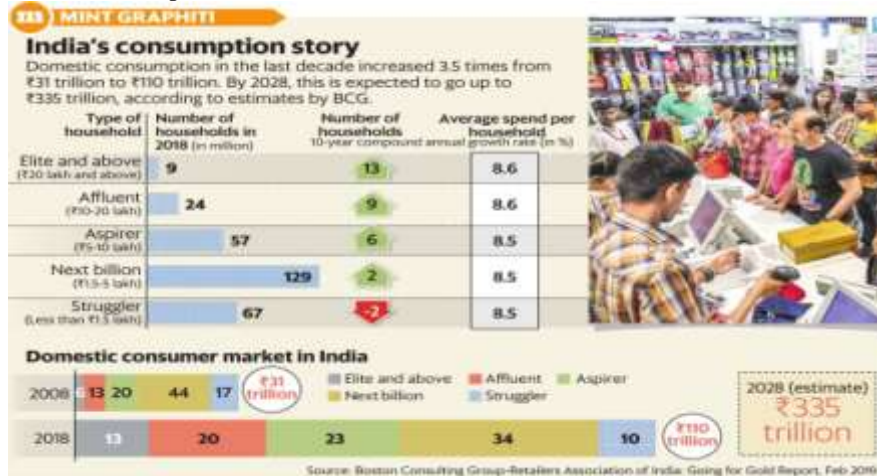


**5-year US Corn Futures/bushel<sup>[16]</sup>**

As, we have seen the graph of Netflix, Spotify and Dollar shave club, on an average Netflix stock increased at 41% y-o-y from 2014-2019 whereas the net sales of dollar shave club increased by 115% y-o-y from 2013-2016 and the paid subscribers of Spotify increased by 53.5% y-o-y from 2015-2019. And, as of June 2019 Amazon Prime had a 59% subscriber growth in India from Q1 2018-Q2 2019. As you can see in the above data the subscription companies if they spend the extra money on themselves to expand and deal with

derivatives in the commodity market so they can attract a lot of customers to raise their valuation exponentially, giving them leverage to give the customers strong discounts to aim to keep them successfully.

This trend is to continue for about 5-6 years when the subscription companies are exponentially growing and thus rapidly increasing their valuation. Therefore, I do not think there's any reason during this amount of time that the service providers would have a difficulty offering their clients big discounts.

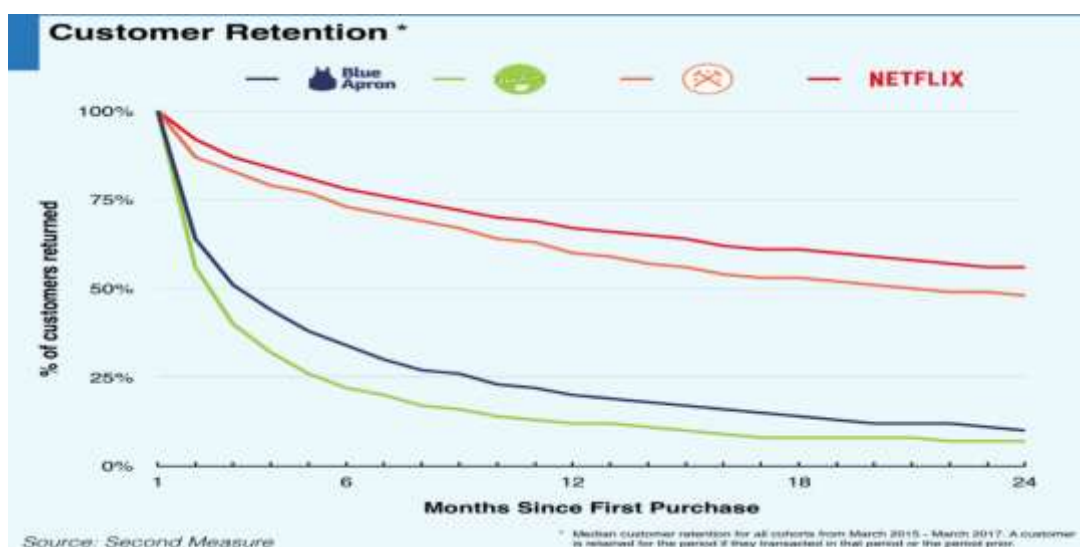




### Consumer spending in India<sup>[8]</sup>

With increase in the consumption appetite of India, it is poised to be a very big economy and a good market opportunity for companies, this is the right moment to start and change the way people do business in India as the government aims for a \$5 Trillion economy by 2024, I believe this change in the system will play a major role in making the economy big and more reasons for the markets to touch new heights.

The Increase in subscription-based model would mean that the companies have the required funds required to run the company before then expected hence it will allow the companies to take less loan, less riskier loans as if they are not subscribed enough, they and the lender can be assured that loaning to them is like buying a “faulty CDO”, hence the lenders can lend less risky loans and decrease net NPAs.



### Customer Retention graph<sup>[15]</sup>

This report is not indicative of real customer satisfaction for Blue Apron, Hello Fresh, Dollar Shave Club, and Hulu, because it is based on a demographic sample of U.S. customers. Yet it gives one a taste of what real retention feels like. Monthly retention shall be measured as a mean percentage for all categories on the basis of the customer's purchases in a given month or month.<sup>[15]</sup>

One of the disadvantages that strikes everybody's mind when they hear this idea is that this will kill the start-up sector of the country, no new businesses will be able to flourish in this kind of business model and the famous companies whose subscriptions are most subscribed will become monopoly-like. No organization will become a monopoly in the world today because if they are one, both we and the government have legislation to deal with these types of circumstances.

I thought about the issue of starter culture perished, but the client retention chart tells another story: Even Netflix, which for 5 years has not been able to retain more than a third of its customers with an annual stock increase of 41 percent.

With technology rising, customer tastes evolving and creativity, start-ups can still develop and expand. Many start-ups will certainly suffer from these types of business models, but the ones that consumers are not fond of will still survive those start-ups whose products are not suited for the market. But those with both a superb product and a good business model, would always compete with the big players and would always prosper. Let us not forget the examples above, all start-ups have formed or changed their business model around 2010 or later.

But still there will be a big problem for fishes to live in a pool with sharks and with subscriptions in place, it would help a few of those sharks to become the great white shark.

### III. CONCLUSION:

I conclude that subscription and a subscription business model are the future of business and an ideal business model to be pursued, as it was written and proven in the above methodology. When companies change to a subscription business model, they create value in the form of loyal, more customer inertia, greater potentiality for cross-selling and upselling goods,

whereas the customer gets a good value for his money, no strain in daily goods buying, better products and services.

As, discussed earlier that a subscription provider should compensate for the loss we 'd make by taking a subscription and overcoming the people's mindset of not paying high for tomorrow even after they know they 'd pay higher than requested tomorrow.

Therefore, a subscription service has to benefit customers, as we have seen that Amazon Prime and Netflix had the highest rates of growth as well as income, respectively 59% and 41%. A high per cent of the benefits must therefore cut competition as well as save on potential infrastructure and services growth, so that the provider can seek to hedge its losses by derivatives trading or some other process.

To both consumers and vendors, suscription-based programs and goods are a Win-Win scenario.

#### REFERENCES:

- [1]. Bhasin H, June 12, 2020, 23 Types of Business Models Examples <https://www.marketing91.com/23-types-of-business-models/>
- [2]. <https://tradingeconomics.com/india/inflation-cpi>
- [3]. <https://tradingeconomics.com/india/interest-rate>
- [4]. <https://www.investopedia.com/insights/worlds-top-economies/>
- [5]. <http://statisticstimes.com/demographics/population-of-india.php><https://www.priceintelligently.com/blog/subscription-business-model>
- [6]. [https://www-livemint-com.cdn.ampproject.org/v/s/www.livemint.com/money/personal-finance/epf-interest-rate-hiked-to-8-65-ahead-of-elections-2019/amp-1550747234936.html?usqp=mq331AQA&amp\\_js\\_v=0.1#referrer=https%3A%2F%2Fwww.google.com&amp\\_tf=From%20%251%24s&ampshare=https%3A%2F%2Fwww.livemint.com%2Fmoney%2Fpersonal-finance%2Fepf-interest-rate-hiked-to-8-65-ahead-of-elections-2019-1550747234936.html](https://www-livemint-com.cdn.ampproject.org/v/s/www.livemint.com/money/personal-finance/epf-interest-rate-hiked-to-8-65-ahead-of-elections-2019/amp-1550747234936.html?usqp=mq331AQA&amp_js_v=0.1#referrer=https%3A%2F%2Fwww.google.com&amp_tf=From%20%251%24s&ampshare=https%3A%2F%2Fwww.livemint.com%2Fmoney%2Fpersonal-finance%2Fepf-interest-rate-hiked-to-8-65-ahead-of-elections-2019-1550747234936.html)
- [7]. <https://www.financialexpress.com/money/mutual-funds/10-best-performing-mutual-funds-over-the-last-5-years/1554892/>
- [8]. [https://www-livemint-com.cdn.ampproject.org/v/s/www.livemint.com/news/india/aspiring-affluent-households-driving-india-consumption-growth-bcg-report/amp-1551222553295.html?usqp=mq331AQA&amp\\_js\\_v=0.1#aoh=15640473679518&amp\\_ct=1564047382389&referrer=https%3A%2F%2Fwww.google.com&amp\\_tf=From%20%251%24s&ampshare=https%3A%2F%2Fwww.livemint.com%2Fnews%2Findia%2Faspiring-affluent-households-driving-india-consumption-growth-bcg-report-1551222553295.html](https://www-livemint-com.cdn.ampproject.org/v/s/www.livemint.com/news/india/aspiring-affluent-households-driving-india-consumption-growth-bcg-report/amp-1551222553295.html?usqp=mq331AQA&amp_js_v=0.1#aoh=15640473679518&amp_ct=1564047382389&referrer=https%3A%2F%2Fwww.google.com&amp_tf=From%20%251%24s&ampshare=https%3A%2F%2Fwww.livemint.com%2Fnews%2Findia%2Faspiring-affluent-households-driving-india-consumption-growth-bcg-report-1551222553295.html)
- [9]. <https://www-statista-com/chart/15697/spotify-user-growth/>
- [10]. <https://www.feedough.com/dollar-shave-club-business-model-case-study/>
- [11]. <https://www.marketwatch.com/story/netflix-is-ditching-freeloaders-from-subscriber-forecasts-after-volatile-stock-moves-2018-10-16>
- [12]. <https://goldprice.org/gold-price-history.html>
- [13]. <https://economictimes.indiatimes.com/wealth/real-estate/which-indian-city-saw-the-highest-increase-in-property-prices-over-the-last-5-years-find-out/articleshow/69608962.cms?from=mdr>
- [14]. <https://economictimes.indiatimes.com/markets/stocks/news/indian-households-increase-equity-play-via-the-sip-route/articleshow/67465398.cms?from=mdr>
- [15]. <https://medium.com/@nbt/how-blue-apron-compares-to-other-subscriptions-in-one-graph-6404a74ccf2d>
- [16]. <https://www.macrotrends.net/2532/corn-prices-historical-chart-data>



**International Journal of Advances in  
Engineering and Management**

**ISSN: 2395-5252**



# IJAEM

**Volume: 03**

**Issue: 01**

**DOI: 10.35629/5252**

**[www.ijaem.net](http://www.ijaem.net)**

**Email id: [ijaem.paper@gmail.com](mailto:ijaem.paper@gmail.com)**