



The Spending Tap – A Look at China’s Booming E-commerce Sector

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“When you realize nothing is lacking, the whole world belongs to you,” was penned by the ancient Chinese philosopher Lao Tzu and intended as a message of wellbeing. Fast forward to 2020, and his words could be reinterpreted as a slogan for the always-in-stock global e-commerce industry. This is particularly so in China, where consumers have quickly discovered they can buy whatever they want from anywhere in the world at the tap of a smartphone screen.

Certainly, the Chinese e-commerce market is the biggest globally in terms of sales. And if we look at levels of market penetration, then the country is currently vying with South Korea for the world’s number-one spot.

That said, e-commerce penetration in China is still hovering around the 20% mark, so the industry has plenty of room to expand in the coming years.

Rather than dwell on these numbers, we want to take a closer look at some of the competitive dynamics that are driving the market’s growth and assess how it will develop as we move through this year and beyond.

TOP 10 COUNTRIES, RANKED BY RETAIL ECOMMERCE SALES, 2018 & 2019

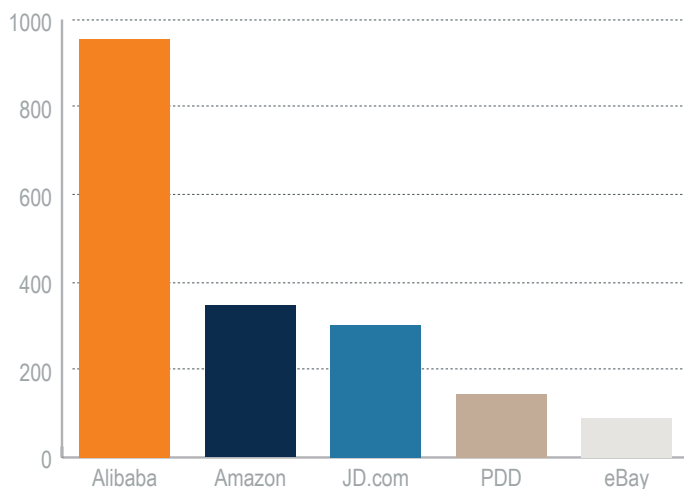
BILLIONS AND % CHANGE	2018	2019	% CHANGE
1. China*	\$1,520.10	\$1,934.78	27.3%
2. US	\$514.84	\$586.92	14.0%
3. UK	\$127.98	\$141.93	10.9%
4. Japan	\$110.96	\$115.40	4.0%
5. South Korea	\$87.60	\$103.48	18.1%
6. Germany	\$75.93	\$81.85	7.8%
7. France	\$62.27	\$69.43	11.5%
8. Canada	\$41.12	\$49.80	21.1%
9. India	\$34.91	\$46.05	31.9%
10. Russia	\$22.68	\$26.92	18.7%

Note: includes products or services ordered using the internet via any device, regardless of the method of payment or fulfillment; excludes travel and event tickets, payments such as bill pay, taxes or money transfers, food services and drinking place sales, gambling and other vice good sales; *excludes Hong Kong
Source: eMarketer, May2019

CHINA'S LEADING PLAYERS

If we take the five most significant global players in the e-commerce space, then three of these are Chinese businesses. And of this trio, two domestic platforms dominate – Alibaba and JD, which hold approximately 80% of the market share.

GMV OF RETAILERS WITH AN E-COMMERCE MARKETPLACE: 2019



Source: Bernstein Estimates/Company Disclosure/eMarketer

Alibaba operates two leading brands, Tmall and Taobao, with Taobao adopting a consumer-to-consumer (C2C) approach that provides space for sellers, often small businesses, to connect with customers who, in turn, benefit from low prices (a broadly similar concept to eBay). The company's range of products and services runs into hundreds of millions.

Taobao's partner platform is Tmall, which trades as a business-to-customer (B2C) concern and was established to satisfy a need among consumers for quality goods sold by established businesses rather than a sole trader or small firms. With a brand-first approach and a strong presence in the luxury goods space, Tmall has been Alibaba's key growth driver in recent years, with leading retail names often creating bespoke stores within the Tmall site.

In direct competition to Tmall is JD, which is also a B2C operator with a similar focus on high-quality (read: genuine) goods that are often purchased in bulk from suppliers. Also, it underlines its service with a bespoke distribution system that is now the most advanced in the country. However, the company has been under competitive strain with pressure coming from the more dominant Tmall and newcomer Pinduoduo.

Founded in 2015, it has taken Pinduoduo only four years to reach US\$100 billion in gross merchandising value (GMV)¹, an amount JD took 13 years to achieve. It has done this by fusing two critical 21st-century lifestyle elements – social media and shopping – to pioneer a bulk-purchase strategy, whereby groups of friends, families or work colleagues join forces to buy its goods. The discount on offer rises in line with the size of the purchasing group.

Moreover, with Alibaba having focused more on Tmall over Taobao, there was perhaps space for Pinduoduo to slip through the gaps and establish a presence in the low-priced-goods market.

OPENING THE COUNTRY

Another reason behind Pinduoduo's rapid rise has been its decision to steer clear of first-tier cities, such as Shanghai and Beijing, and target lower-tier cities and rural areas. This move was canny, as China's secondary cities are traditionally more value-conscious and less likely to be swayed by brand attachment, so the bulk-purchase approach struck a chord.

However, Alibaba will be acutely aware of the opportunities that exist in the country as a whole. In the nation's lower-tier cities and rural communities, the percentage of the population actively using the company's services is still only 40% (the equivalent figure for the country's leading population centers is 85%).

And now that it has established a strong position with Tmall, Alibaba has turned its sights toward penetrating the broader Chinese market through its various apps and businesses – in other words, the entire Alibaba ecosystem.

How will this translate into business activity? We could see Alibaba take the community aspects of bulk purchase and create consumer-to-manufacturer (C2M) platforms, which allow groups of consumers to deal directly with manufacturers. C2M can be an incredibly efficient method of production because it guarantees that the goods are sold. In other developments, we expect to see same-day and next-day delivery rolled out in a growing number of cities thanks to advances in distribution-related technology.

Another recent driver of the market's expansion has been the concept of live streaming. This approach often features a media personality who promotes a product during a real-time broadcast that is tailored for mobile consumption. Crucially, viewers can interact by posting comments or asking questions. It is this immersive blend of sales and entertainment that is helping businesses to break into new areas of the country. People feel included – this matters a lot if you feel distant from the main metropolitan centers.

In terms of the competition, we think that JD and Pinduoduo will remain essential players in the market. But with advantages that are underpinned by the scope and scale of its operations, plus the ease with which merchants can become part of its ecosystem, Alibaba will maintain its status as China's dominant player.

EATING IN

Food delivery in North America and Europe still has something of an image problem. People see it as either unhealthy or indulgent, which isn't surprising given the leading names tend to be fast-food firms, and delivery costs are considered high. Exacerbating this image problem is the logistical difficulties created by relatively low population centers in these areas of the world.

Not so in China, where some estimates claim that a quarter of the population uses a food-delivery app. At a high level, this is explained quite easily – population density, convenience, and cost. There are eight times more people per square kilometer in China than in the US,¹ which means more potential customers within a smaller delivery radius.

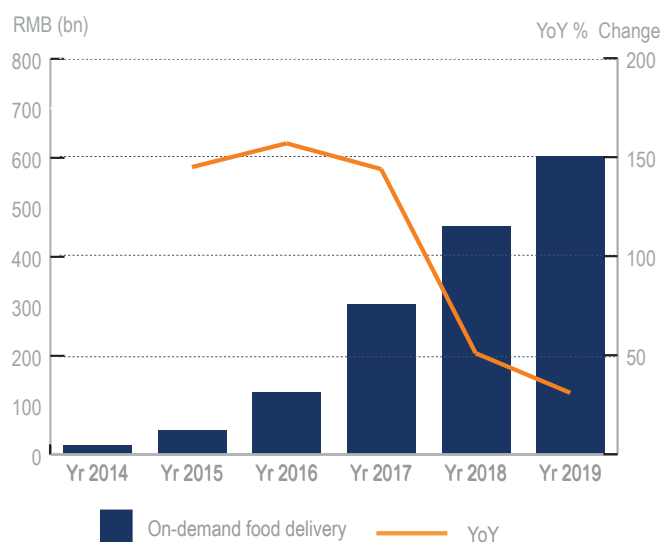
There is another reason why food e-commerce is booming and that is cost, with customers benefiting from two factors that are keeping prices down.

Firstly, there is intense competition between the two players who currently dominate the food-delivery market: Ele.me and Meituan. Both offer broadly the same service, with customer choice driven by discounts or promotions, often in the form of coupons – which is excellent news for diners.

Secondly, both firms have their sights firmly set on market expansion, and this means accepting weak numbers on the balance sheet. As with retail e-commerce, the lower-tier market remains underpenetrated, so lacklustre short-term profits (or even losses) are being willingly absorbed given the enormous opportunities that could come from expanding the entire market.

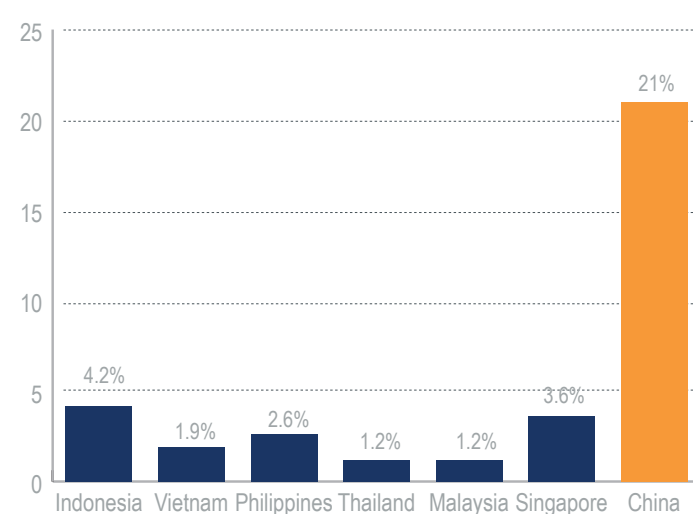
In the case of Ele.me, it is also an integral part of the Alibaba ecosystem, so its parent can glean a considerable amount of customer data and leverage it toward other opportunities within the group. Therefore, weak numbers are even more tolerated.

ON-DEMAND FOOD DELIVERY (RMB BN)



Source: iResearch, Bernstein

E-COMMERCE SALES PENETRATION 2018



Source: eMarketer and Bernstein Analysis.

¹ Bloomberg, as of 28 March 2019.

CURRENTLY, LAZADA AND SHOPEE ARE TWO MAJOR PLAYERS ACROSS THE REGION, THOUGH THEY ARE FACING FIERCE LOCAL COMPETITION IN SOME MARKETS SUCH AS INDONESIA, VIETNAM, AND SINGAPORE

Combined iPhone and Android Phone Average Monthly Active Users, 2019Q1

	INDONESIA	VIETNAM	PHILIPPINES	THAILAND	MALAYSIA	SINGAPORE
1.	Tokopedia	Shopee	Lazada	Lazada	Lazada	Lazada
2.	Shopee	Lazada	Shopee	Shopee	Shopee	Qoo10
3.	Bukalapak	Tiki.vn	Zalora	AliExpress	Taobao	Shopee
4.	Lazada	Sendo	Amazon	JD Central	11street	Taobao
5.	JD.id	Adayroi	AliExpress	Amazon	AliExpress	ezbuy

Total Average Visits on Desktop and Mobile Web, 2019Q1

	INDONESIA	VIETNAM	PHILIPPINES	THAILAND	MALAYSIA	SINGAPORE
1.	Tokopedia	Shopee	Lazada	Lazada	Lazada	Qoo10
2.	Bukalapak	Tiki	Shopee	Shopee	Shopee	Lazada
3.	Shopee	Lazada	Zalora	Chilindo	Lelong.my	Shopee
4.	Lazada	The Gioi Di Dong	argom all	NBS	11street	Straberrynet
5.	blibli.com	Sendo.vn	ebay	Advice	Zalora	ezbuy
		Alibaba camp	Tencent camp	JD	Amazon	eBay

Source: iPrice and Bernstein Analysis.

In case of Meituan, although having Tencent as a major shareholder, operates as a standalone firm. However, the company can compensate for marginal food-delivery numbers through its hotel division and other business activities.

From a restaurant's perspective, having this clear pathway to the customer can be vital, given the life span in China's highly competitive food business can be as short as six months. Moreover, once we emerge into a post-Covid world, the delivery firms may see further growth with the addition of previously successful but subsequently struggling businesses that now realise the value of this channel.

DATA-DRIVEN

Indeed, if we step back and look at the e-commerce market as a whole, then the next few years will see e-commerce players utilize big data to drive sales. The audience is already captive; in other words, there is no need to persuade people to leave their comfortable homes to visit crowded malls. The mall is at their fingertips. E-commerce firms know so much more about us than traditional retailers and can, therefore, act quickly to tailor-make suggestions or nudge us towards other services or subsidiaries. Targeted recommendations make for an improved customer experience, which drives further engagement and spending and, in turn, leads to better data acquisition and even more customer-specific recommendations – a positive feedback loop.

By way of an example, let's look at the concept of online-offline (O2O) integration. In other words, this is where the online world meets traditional bricks and mortar stores. E-commerce companies will identify and attract customers via online activity, such as strategic advertising or email campaigns. The customer is then nudged towards a local physical shop (which has built a relationship with the e-commerce platform) to purchase the item or buyers can have the item delivered from the local establishment.

A good example of this is Alibaba's Singles Day shopping experience, whereby the firm teams up with hundreds of thousands of neighborhood shops, which acted as delivery centers. Data also show that Hema, which is Alibaba's retail store chain, boasts levels of operational efficiency that are notably stronger than offline-only equivalents.

From a broader geographic perspective, e-commerce still has to make deeper inroads into South East Asia. However, Alibaba and Tencent are still the biggest operators in the region. If we take dominant local names, such as Lazada and Shopee, the former is owned by Alibaba, while the latter has Tencent as a leading shareholder.

E-commerce is the most exciting chapter in Asia's consumption growth story. It is a microcosm of the fundamental change that is happening in the region, as the economic structures continue to shift from investment and production toward consumer activity.

This process of change is expected to accelerate, as Covid-19-related events trigger a spike in e-commerce activity. People confined to their homes are adapting their spending habits, which, in turn, is helping to reduce some of the uncertainty surrounding the digital experience. Now that consumers are crossing the line, there is a good chance that many will embrace the concept and adopt it as the new normal.

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For more information, please visit our website or contact our sales representatives.

¹ eMarketer, as of Dec 2019.

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