Retail Week
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WHITE PAPER

In association with channeladvisor

Understanding China's online marketplaces

How to establish a presence in the world's fastest-growing ecommerce market

INTRODUCTION

On November 11, 2015, Alibaba sold goods worth £9.9bn. The £3bn mark was hit in just under 90 minutes. That Singles' Day sales performance didn't break the internet – à la Kim Kardashian – but it was just the latest in a growing list of ecommerce records that China is smashing with increasing frequency. And, despite the economy slowing down, forecasters suggest there's plenty of fire left in the dragon yet.

China bypassed US ecommerce sales three years ago and accounts for 40% of the global online retail market. In three years' time (2018) it will have 50%. By then, it could even be the largest retail market in the world, surpassing the US. The rocket fuel behind this growth will be digital.

Online penetration has already hit 40% in five major categories – casualwear, casual shoes, handbags, snacks, and smartphones – but 10 more will be added by the end of the decade, predicts Alibaba. This is a population that has come of age in a digital environment. Around 65% have a smartphone (most of them 4G enabled) and 90% of internet users access the web using their mobiles. People here have "skipped" desktops entirely, says James Huang, managing director for Greater China at ChannelAdvisor.

Some of the numbers can be hard to comprehend. After listening to Alibaba's UK managing director, Amee Chande, speak at Retail Week Live this year, Nectar managing director Will Shuckburgh said the scale consistently amazes him. "The numbers are unbelievable…even in the worst case scenario."

Chande believes that international retailers do "get" just how big the Chinese market is. "What I don't think they understand is how easy it [now] is to access this market."

A fear of red tape, counterfeit goods and limited understanding of the Chinese consumer has meant only a few have dipped their toes in the water. This white paper, produced by *Retail Week* in association with ChannelAdvisor, explores the challenges of setting up an online marketplace in order to launch a presence in China, as well as the opportunities that exist in major online marketplaces such as Tmall and JD.com. Find out the critical ways to capitalise on the extensive opportunities China's lucrative etail sector offers those retailers brave enough to take the plunge.

CHAPTER 1: CHINA'S ONLINE SHOPPER

On January 22 this year, the China Internet Network Information Centre released its 37th report on internet development. It showed that China now has 688 million internet users, which is about half the country. Just 10 years ago internet penetration stood at 8.5%.

This was good news for ecommerce – especially amid an economic slowdown that has given a few investors the jitters. "Make no mistake: although the pace [of economic growth] is slower and the course is bumpier, consumption growth is still tracing a staggering trajectory," noted the Boston Consulting Group in its December 2015 *New China Playbook* report.

Retailers should have no fear, with "three great forces" ushering in a transformation, the researchers noted: a new generation of freer-spending, sophisticated consumers; the rise of upper-middle-class and affluent households as the drivers of consumption growth; and the increasingly powerful role of ecommerce.

Last year was a breakthrough year for young spenders: the post-1985 generation that has grown up with the internet are reaching their 30s and, as CNN reported, are now set to become the "mainstream consumption power". They have money to spend, rely heavily on research and are incredibly brand conscious.

HOW DO CHINESE SHOPPERS MAKE THEIR PURCHASING DECISIONS?

63% look at what **friends** are doing, wearing or using

58% rely on **online product reviews** by other shoppers

38% use **official reviews** in newspapers, magazines and blogs

Source: Demandware's Future Ready Research

Members of this group also have an insatiable appetite for Western brands, but their motivations have changed: a decade ago status motivated the purchase of international brands; today it's more about provenance, reputation and, critically, value. "They're very aware of value," says Chande. "The whole idea of finding a deal is like a sport."

PRICE-CONSCIOUS SHOPPERS

The perception of value and the higher degree of price sensitivity is something non-domestic retailers must understand. Today, 66% of the purchasing decisions made by millennials in China are driven by cost.

If the price is right, then other factors such as quality and availability will drop down the priority list, says Jamie Merrick, head of industry insights at Demandware.

This price sensitivity explains why 90% of all Chinese-based ecommerce transactions are completed through marketplaces. The lion's share take place on the big two – JD.com and Tmall.com, run by Tencent and Alibaba respectively. "Chinese shoppers like the one-stop shopping place idea," says Ivan Zhou, managing director at Sociomantic China. The marketplaces have the variety of products, the brands and the transparency they are looking for, he adds.

Comparison is key for even the most brand loyal consumer – even if it takes more effort. Indeed, Chinese shoppers are heavy researchers. Typically they have 15 to 20 touchpoints on their journey to purchase – far more than in the UK. The major marketplaces are the final step in converting, which means there's a lot of legwork to do before that.

SOCIAL MEDIA

Many multinationals have been led to believe that ecommerce will level the playing field for expansion into China, allowing them to leapfrog establishing a bricks-and-mortar presence and jump straight into the fray. To a certain extent, that's still true, says Jason Spencer, managing director at Incite, but he warns "you also need to build salience, relevance, aspiration and engagement". "The ways in which this is achieved are quite different," he adds.

Chinese shoppers not only look for recommendations, but when they buy something they're keen to share the news – 40% say doing so brings a sense of achievement, according to Mintel.

In a nutshell, brands need to focus on enabling others to tell and sell through being brand ambassadors, says Andrew Robinson, senior strategist at TMW Unlimited.

"The Chinese shopper is mobile first," he explains. "They are light years ahead of how we in the West use mobile to engage with brands and transact because they have a much more integrated and developed app system." (see chapter 3: Taking the plunge).

> "Make no mistake: although the pace [of economic growth] is slower and the course is bumpier, consumption growth is still tracing a staggering trajectory"
>
> *New China Playbook* report, Boston Consulting Group

YOUNG AT HEART

Consumption within the under-35s is growing at 14% a year – double that of their elders. Members of the younger generation also outspend their parents and grandparents – by as much as 40% in many product categories, according to Alibaba. Over the next five years, their share of total consumption will reach 53% from its current level of 45%.

CHAPTER 2: THE MAJOR MARKETPLACES

China's shoppers are risk averse and price conscious, so it's perhaps not surprising that 90% of Chinese-based ecommerce transactions are completed through marketplaces. In the UK it's roughly a third. China has become a "fertile ground" for marketplaces, and the massive growth of the country's ecommerce sales volume reflects the surge of the big players such as Alibaba and Tencent, according to ChannelAdvisor.

Taobao is the C2C arm of Alibaba's vast online operation – it has 8 million sellers, most of them individuals. British retailers will be more familiar with the group's B2C platform Tmall – or more specifically Tmall Global, which sells only imported goods. Asos.com, Burberry, Uniqlo and Reebok have all established 'storefronts' on Tmall to help launch their Chinese online presence.

The attractions of Tmall are clear – it ranks in the top 10 most visited sites in China and allows companies to create their own stores to reflect their branding. Uniqlo has certainly benefited: on Singles' Day (see box, below) last year the retailer recorded sales of $100m (£69.5m) – double the previous year. Some heavy investment in social media has helped too: it has built an army of 2 million followers on the mobile messaging service WeChat.

Uniqlo also had a dalliance with Tmall's big rival in the B2C market, JD.com. It didn't last long, though it's not quite clear why. Sales were good, according to JD.com. There's no question it was a setback for a company that's very much the David to Alibaba's Tmall Goliath. But, although it has less than half Tmall's share of the B2C market (22.8% versus 58.6%), it is expected to gain further ground by investing in logistics and its growing consumer base.

CAT-AND-DOG BATTLE

A survey by *China Confidential* in the first quarter of 2015 showed that 45% of Chinese shoppers regularly use JD.com. Two years prior it was 30%. JD.com's partnership with Tencent has also given it access to the 1 billion people on the WeChat and QQ mobile apps.

The, at times terse, competition between the two major players – actually nicknamed 'the great cat-and-dog battle' – will only intensify as China's economy cools. Both believe the Western market is a huge opportunity; and both are on a charm offensive to attract the biggest brands.

In a recent interview, Chande explained how

SINGLES' DAY 2015 IN NUMBERS

11.11 光棍节

1.7m delivery staff

200 aeroplanes

400k vehicles

£9.9bn Alibaba sales versus **£1bn** Black Friday UK sales

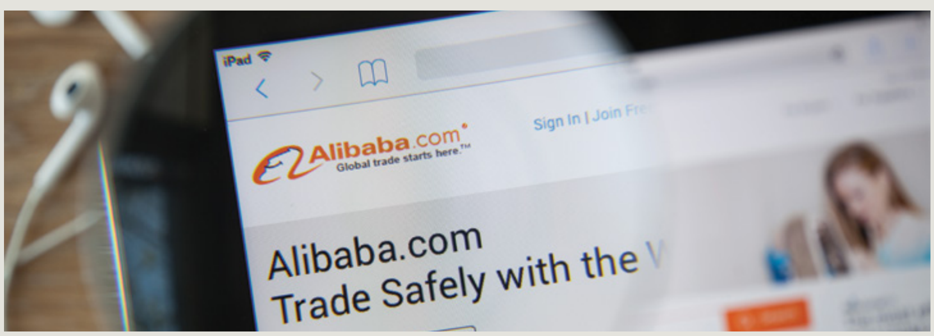
£181 average planned spend per consumer

BEST-SELLING ITEMS INCLUDE:
Nike trainers; Levi's jeans; baby products; nutritional products

FOCUS ON: SINGLES' DAY

Dreamt up in the 1990s, Singles' Day started as an occasion for single people to spend time with single friends. But in 2009, Alibaba spotted a commercial opportunity to boost sales between the national holiday in October (Golden Week) and Christmas. Just £5m was spent in the first year. Last year Alibaba's sales hit £9.9bn.

November 11 has actually become the perfect microcosm for the scope and energy that define the opportunities in Asia for global retailers. Alibaba has even trademarked the term '11.11'. "It creates a new spending opportunity based around a desire to belong and be involved in a community rather than on bagging massive discounts," noted Cheil president Simon Hathaway in a *Retail Week* blog recently. For this reason "it will become even bigger", he added.



Topshop, Marks & Spencer and the Cambridge Satchel Company are among the retailers that are embracing the anti-Valentine's Day – and the sales boosts that go hand in hand with it. In all, there were 5,000 international brands signed up in 2015.

However, returns are thought to be as high as 30%, while margins are also below other times of the year. "It might be more of a marketing investment than a genuine margin generator," says Incite managing director Jason Spencer.

> "There's a premium label put on a lot of international brands thanks to reputation, quality and trust"
> James Huang, ChannelAdvisor

Alibaba has built the infrastructure of ecommerce and now it wants "businesses around the world to have access to this structure".

JD.com is wooing businesses in a similar fashion. After signing a deal with Gap, JD Mall chief executive Shen Haoyu said: "A clothing company can set up stores in 200 cities, or they can open a store on JD.com and immediately access tens of millions of consumers. The math is easy."

CROSS-BORDER B2C

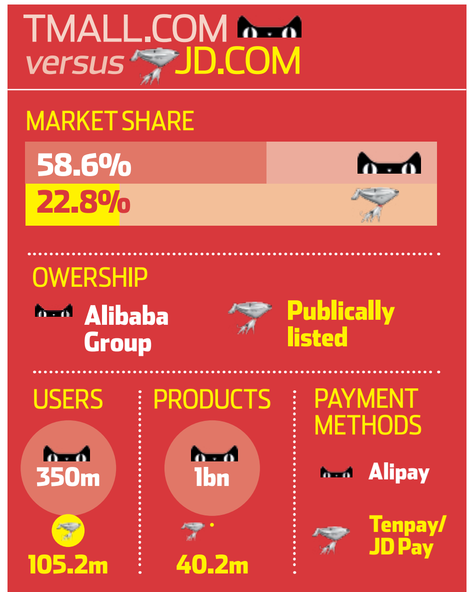
Once again, the numbers being churned out are already impressive. Research just published by Mintel shows that 58% of Chinese consumers bought foreign products from a domestic shopping website between June and November 2015.

Pricing was one of the drivers (38%), but it wasn't the main one – quality was (63%). "There's a premium label put on a lot of international brands thanks to reputation, quality and trust," says ChannelAdvisor's Huang. "Cross-border is currently the fastest growing segment of ecommerce in China."

The value of this so-called "haitao shopping" (buying overseas) grew at a compound annual growth rate (CAGR) of 63.3% in 2015, compared with the 48.8% mustered by ecommerce overall.

Between now and the end of the decade, cross-border will achieve 18% CAGR, according to Mintel.

The future "looks good", says Mintel research director Matthew Crabbe. That's an understatement, suggests Chande, who points out that on Singles' Day last year a third of shoppers on Alibaba bought foreign brands. "The appetite is astounding," she says.



Source: China Briefing; Dezan Shira & Associates

CHAPTER 3: TAKING THE PLUNGE

The stuttering economy may have given some cold feet but China remains a hotbed of opportunity for Western retailers. But there's still all that red tape to cut through, right? Wrong.

The government has actually made it much easier for overseas brands to sell online having relaxed its rules on cross-border ecommerce. This has prompted the major etailers to ramp up their efforts to romance the Western brands. Alibaba, JD.com and Amazon China have all created special sections of their sites featuring imported goods.

But it's not just the marketplaces that are benefiting: consumers are also becoming more comfortable making purchases on standalone brand websites. Research by PayPal in 2014, for example, showed that 25% of cross-border consumers buying from the UK are from China. They are also seeking out brands directly, bypassing the marketplaces, in a bid to find trustworthy goods at lower prices.

FAKES AND IP

Trust is a key issue in China currently. The government has led a crackdown on corruption and tens of thousands of officials have already faced punishment. President Xi Jinping wants 2016 to be a year when "nobody dares to be corrupt".

Some of China's big marketplaces – in particular Alibaba's C2C platform – are also battling against fraud, but they don't seem to be winning. As one of the region's business commentators put it recently: neither the big brands, the Chinese government nor the pressure from the US can do much about the torrent of counterfeit and sham goods.

China does have a functioning intellectual property registration system to help protect brands, but companies need to engage with the system early, advises Michael Conway, a trademark attorney at Haseltine Lake. "Failing to register a brand in China at an early stage may mean that another company applies to register it, which means you can lose control of your own brand."

NetNames, which helps companies fight back against the fraudsters, says even more worrying than the levels of fake goods available is the fact that some marketplace sites in China advertise their services on how to avoid takedowns. But consumers are cottoning on, and ecommerce is already beginning to pivot away from the counterfeit-flooded C2C marketplaces and towards the more trustworthy B2C ones.

According to iResearch data, B2C's share of ecommerce will be 64% come 2018; in 2011 it was just 25%. Within the next five years, the transaction volume of imported goods bought online by Chinese shoppers will hit £173m, making China the largest cross-border B2C market in the world. As PwC's Michael Cheng puts it, the country is "irresistible" to global retail chains.

SMART OPPORTUNITY

Much of the available ecommerce pie will be accessed through mobile and social media. The highest performing brands all have a strong mobile presence, not simply as purveyors of products and services, but to make consumers' lives easier, and better. This is the message that Alibaba et al are pushing, and it's one that UK retailers could buy into: Sainsbury's digital and technology director Jon Rudoe has said that retailers must no longer define themselves by what they sell but the customer problem they are solving.

The mobile experience needs to represent the brand in all its aspects: advertising and marketing, social communication, shopping, purchasing, and payment. This is where UK retailers may find themselves out of their depth and in need of assistance. Mobile payment wallets are already integrated into the app ecosystem, which makes it incredibly easy to transact. As a result, m-commerce is now over half of all ecommerce volume, and increased 85% year on year in 2015. And the big two are, once again, locking horns in the battle for social commerce.

SOCIAL MEDIA INFLUENCE

The power of social media in China's ecommerce market cannot be ignored. According to a survey by DigitasLBI, 53% of Sina Weibo users claim to be influenced by the platform. This is slightly ahead of Facebook (52%) and way ahead of Twitter (36%).

Nearly 40% of those polled had bought things through Sina Weibo in the previous 30 days, around double the number who'd purchased through Facebook (23%) or Twitter (17%).

In 2013, Alibaba bought an 18% stake (£414m) in Sina Weibo, a microblogging website akin to Twitter. Less than 12 months later it announced the integration of Alipay into the microblog platform, allowing users to pay for goods and services more easily. Around the same time, Tencent started allowing small merchants to open stores inside its hugely popular (400 million users) mobile messaging service Weixin (aka WeChat).

It's not just social networks that commerce has brazenly infiltrated either. iQIYI, a content platform similar to Netflix, broadcasts "hot" Korean soaps, offering consumers deals on the products that are used in the show and by the celebrities in real life. This combines an understanding of what turns Chinese consumers on with the instant gratification of making a purchase, says Incite's Spencer.

So what products are the Chinese particularly attracted to buying online? First and foremost, the things they don't trust in the 'normal' retail channels, such as food and cosmetics. Sales of homewares and maternity products are also in rude health. "There's a lot of faith in UK brands, so it's all about finding where the demand lies," says Oban Digital chief executive Greig Holbrook. And where it doesn't: "Promoting snow boots in Guangzhou [in the south] may not be the roaring success that you experience in Beijing [further north]."

The big cites have traditionally been the targets for ecommerce in China, but not any more. "There are no malls and if you want access to brands, online might be the first choice," notes one expert. Unilever, for example, has forged relationships with both Alibaba and JD.com to promote its brands to a "massive" new audience.

DELIVERY DEMANDS

The Fung Business Intelligence Centre estimates that, as the urban ecommerce market nears saturation, the transaction value of the rural ecommerce market will surpass that of local urban areas within the next decade or two. This will also pave the way for growth of last-mile logistics – another big battleground.

In such a vast country, the logistics of delivering outside the big cities will inevitably create headaches, but money is being ploughed into infrastructure. Alibaba has targeted 100,000 ecommerce centres where people can make orders and collect them, while JD.com has spent heavily on its own logistics network with a focus on accuracy and speed.

CONCLUSION

The pace of change in China's ecommerce market shows little sign of abating. The major players are unlikely to take their feet off the gas anytime soon, which will mean ecommerce sales accelerate past the $1trn mark within the next year or so.

Behind the wheel are hundreds of millions of young, mobile-first, value-hunting consumers. Millions more are joining from outside the urban settlements. All are looking for a good deal on quality products, which will lead them to international brands.

With 90% of all Chinese-based ecommerce transactions completed through marketplaces, opportunities abound for those brands brave enough to establish a presence in the world's fastest growing ecommerce market. China's marketplace offers retailers an immediate audience and ease of transaction, not to mention a safe and quick way to expand reach and scale.

Within a couple of years it is almost inevitable that China's retail market will overtake the US for good. The question is: are UK retailers ready to come along for the ride?

LOW TOUCH TO FULL BLOWN: HOW TO ENTER THE MARKET

The first and most important question any foreign retailer must ask is: should I set up a shop in an established marketplace or establish a standalone online shop?

Low touch:

- Put Alipay or Unionpay onto a UK site
- Translate some landing pages (better still some product pages) into Chinese
- Tip: ensure the address field at checkout can accept Chinese characters

Market tester:

- Via the Royal Tmall store (Tmall Global)
- Store handles all shipping, customer service, returns and payments
- Tip: charges are currently "remarkably small" for a few SKUs

Marketplace partner:

- Open a store on Tmall Global or JD Worldwide
- Greater cost and complexity but much better brand awareness
- Look at fulfilment programmes offered by Amazon and eBay, ChannelAdvisor advises

Full online entry:

- A standalone brand website
- Comes with inventory risk; requires significant research and investment
- Tip: the offer must compete with marketplaces on user experience, delivery times and payment options

Tips provided by James Hardy, chief executive of Avenue51 and former EMEA director at Alibaba.com.

PARTNER COMMENT

According to McKinsey & Co, China's cross-border consumer ecommerce amounted to an estimated ¥259bn (£1.65bn) in 2015, more than 6% of its total consumer ecommerce, and it's growing at a rate of more than 50% annually.

These figures highlight that the Chinese market is vast. Previously retailers looked at the region with trepidation, concerned about the restrictions and barriers to entry. But the past few years have overhauled that perception, and UK retailers are now hungry for success in this thriving region.

Marketplaces and their prevalence in China have transformed the opportunity for European retailers. Expanding to China through marketplaces can be one of the most effective ways to scale your ecommerce business. The captive customer base and established infrastructure on channels like Tmall allow you to focus on other important priorities, such as sourcing, pricing, promotion and fulfilment – each of which presents real complexities when selling to China.

The popularity of marketplaces in China has enabled retailers of all sizes to cast their nets into the region. In the past, it may have felt like success in China was limited to larger, well-established brands. But marketplaces and their efforts to attract Western sellers have levelled the playing field. Without requiring large investments to set up in a new region, channels such as Amazon and Tmall are enabling smaller retailers to test the waters of selling to China.

Even if China isn't part of your ecommerce plans just yet, I believe there are still some lessons to be learned from this mammoth market.

First, the remarkable dominance of marketplaces in the region is an interesting trend. From a UK perspective, marketplaces are becoming more popular, and we believe the UK market could adapt to mirror the Chinese model. The result: as a retailer, if marketplaces aren't part of your overall ecommerce strategy, consider ways to include them.

Second, China's relationship with mobile is vastly different to the UK's. In fact, we lag when it comes to messaging, as we are still rooted in legacy text messaging and email. In China, messaging is the primary means of communication – apps like WeChat (which is owned by Tencent) dominate.

WeChat is more of an ecosystem than a messaging app. Critically, it includes a wallet and an open ecosystem that partners can tap into. The result is that in China, people use WeChat to chat, bank, pay, order taxis, buy movie tickets or donate to charity. Arguably it's as much a commerce app as it is a messaging app.

If you sell to China, understanding the mobile model will greatly aid your success. For the UK bystanders it's an interesting trend to analyse, as the intersection of mobile and commerce could very well be a trend we see develop on our shores.

Overall, the Chinese opportunity is rife, and the retailers that approach expansion and embrace the shopping habits and marketplaces of the East have an exciting journey ahead.

• Mike Shapaker, vice-president and managing director, EMEA at ChannelAdvisor

CHANNELADVISOR'S KEY POINTS

- Marketplaces are a great point of entry to China and the most popular ecommerce tools.
- The Chinese mobile landscape is vastly different from the UK. Get to grips with messaging and how you should interact with your Chinese consumers.
- Consider how you will manage fulfilment to China. Amazon's FBA or other fulfilment programmes can be useful.
- Mark Singles' Day in your calendar and plan promotions to capture Chinese consumers.
- Make transactions on your UK website a possibility by accepting AliPay and enabling your forms to accept Chinese characters.

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