Live streaming e-commerce?

China update

In May, global equity markets continued their declines from April before, recovering most of the losses in the second half of the month.

Inflation and tapering expectations remained the dominant factors for creating market volatility.

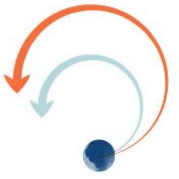
Chinese equities showed signs of stabilising and bottoming out on the back of easing lockdowns and marginal improvement in economic data. For the month, the MSCI China and MSCI China A Onshore indices were up 1.2% and 2.8% respectively, with both the offshore and onshore markets receiving positive inflows from overseas investors.

The month of May reversed the trend of Chinese stocks underperforming developed markets. We expect this trend to continue as developed markets deal with the risk of stagflation and high valuations in the USA. China, on the other hand, is recovering from a cyclical low and does not face the same inflationary pressures. At the time of writing, Chinese markets in June outperformed the MSCI World Index by more than 16% and MSCI China is ahead of the World by more than 10% year to date.

Chinese economic indicators showed improvement off a low base with the gradual resumption of work and production in the regions affected by recent COVID-19 lockdowns.

Restrictions have largely been lifted in Shanghai and life is returning to normal with restaurants, schools and amusement parks reopening.

Most recently, China has reduced the quarantine times for overseas travellers by half, the biggest shift in COVID-19 policy since the pandemic started. This will certainly help restore business and investor confidence. At the same time, policy reflation is still underway. New measures were announced, such as extending tax breaks, increasing loan support for SMEs, boosting consumption in specific sectors such as automobiles and easing housing policies.



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Economic growth has become the priority of the Chinese government now.

During times of turbulence and economic volatility, it is very easy to forget the main reason for investing in China. It is the single largest digital-savvy population globally presenting excellent opportunities for innovative entrepreneurs to exploit. The emergence of live streaming e-commerce in China is one such example of this innovation. It has now become a rapidly growing area of the online retail market in China.

Live streaming e-commerce: an emerging sales channel

China is already the world's largest e-commerce market, thanks to the immense size of its economy and internet user base. According to eMarketer, China accounts for 52% of all e-commerce transactions worldwide, with total online sales of over $2 trillion (about three times the US market) in 2021.

It also has the highest penetration rate (online sales as a per cent of total retail sales) globally, at nearly 30%.

Despite recent setback due to temporary COVID-19-related measures, Chinese e-commerce is likely to grow for many years, driven not only by continuous consumption growth and increasing penetration, but also the invention of new technology and business models that make online shopping a better experience for consumers. Community group buying and live streaming e-commerce are examples of models that emerged in China.

Live streaming e-commerce is a digital and more advanced version of infomercials (television channels dedicated to selling products).

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The live streaming feature allows shoppers to interact with the host (usually a celebrity or a key opinion leader), the brand and other shoppers in real-time, blending entertainment with instant purchasing. The host demonstrates and critiques the products, answers call-in questions, and urges viewers to take action with time-limited tactics such as one-off coupons. Thousands of items can sell out in seconds.

During the "Double 11" online shopping festival in 2021, the top two hosts recorded total sales of nearly $3 billion in a single day, a number that tops the annual sales of 90% of listed companies in the China A-share market.

To illustrate the concept, the following are screenshots of hosts selling cosmetic products on Alibaba's Taobao Live:

As an emerging sales channel, live streaming e-commerce creates value for both shoppers and brands. Products are selected and bulk-purchased by the host, offering shoppers ease and assurance with deep discounts to the normal retail prices. It is also entertaining to watch and participate in the show. If done well, brands find it an effective way to gain awareness and generate sales. Some companies report conversion rates of up to 30%, which is about ten times higher than in conventional e-commerce.

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In pursuing live streaming e-commerce, China is far ahead of the West.

Early movers have benefited greatly from it and set themselves apart from their competitors that are behind in this channel.

This new way of promoting and selling goods and services online has reinvigorated the industry landscape and experienced explosive growth since its debut about five years ago. Its market value grew a hundredfold between 2017 and 2021 to reach an estimated $315billion in 2021, representing roughly 16% of the online retail market in China.

Traditional players like Alibaba, JD.com and Pinduoduo, as well as social platforms like Douyin (the Chinese TikTok), Kuaishou (another short-video platform), Little Red Book (a crowd-sourced review and social shopping site) and Tencent's WeChat, are all taking advantage of this rapidly growing segment of the market.

Even New Oriental, previously known as a leading private tutoring firm until last year's regulatory crackdown, is now thriving in this business having, reinvented itself with former teachers selling agricultural products on the internet.

In pursuing live streaming e-commerce, China is far ahead of the West. Only a few retailers, such as M&S and Ted Baker, have recently launched livestream initiatives in the UK. It is unsurprising to see this, given the Chinese population is tech-savvy, as seen in their fast adoption of digital payments and the government heavily expanding the 5G network. The domestic popularity of live commerce has grown from lower-tier to higher-tier cities, from Gen-Z and Millennials to seniors, from small to large brands, and from apparel and beauty products to electronics and many other categories.

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Regulation is necessary and playing catch-up

There has been minimal regulatory oversight of this sector until recently.

Like any new sector, the government has allowed it to develop with few restrictions but now needs to catch up with regulations.

This is not without good cause. According to the China Consumers Association, a surge of complaints was reported by online shoppers about misinformation, product quality and lack of after-sales service. It is also causing legal and tax problems given the complicated business arrangement between the involved parties (i.e. host, brand, multi-channel network and platform). Regulation is, therefore, necessary. The latest guidance issued just a week ago states that the hosts must have the relevant professional qualifications for broadcasts related to healthcare, finance, law and education. The platforms need to verify this and keep appropriate records.

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e-commerce until recently.

As we have seen in the past, regulation can bring headwinds and tailwinds. For example, it can help accelerate consolidation in the industry, benefitting the larger or more compliant players. Our managers' job is to understand the opportunities and risks that result from regulation and make the right investment decisions.

We do not doubt that live streaming e-commerce in China will continue its rapid growth in the years ahead via expansion into new niches, a broader demographic of users and a combination with new technology such as virtual reality. We are very excited to see that many growth opportunities like this still exist in the Chinese market today. We will examine these in future letters.

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