Talking shop: Wal-Mart bets on China's online growth with Yihaodian

By: Petah Marian | 19 May 2011

Wal-Mart Stores' acquisition of a minority stake in China's leading e-commerce retailer Yihaodian emphasises the growing importance of the online channel in developing markets.

Last week, the world's largest retailer took a stake in China's largest online player. With a logistics network in the major Chinese cities of Shanghai, Beijing and Guangzhou, local market research firm DDMA describes Yihaodian as the country's only national online grocer.

Yihaodian, whose name means No.1 Store in Chinese, has a strong lead on the competition, as the first online supermarket to launch in the country, opening in Shanghai during July 2008.

Its closest competitor, Taobao Supermarket, did not begin offering groceries online until January this year, and is still only available in Shanghai. However, online grocery retail in Shanghai is not a two-horse race, with Yihaodian facing competition from a number of other major players including Lianhua Ok Blemall, French retailer Auchan, Dahouzhan and Binggo.
The acquisition will be a highly complementary for Wal-Mart. The deal gives it an interest in China's leading online retailer and will provide it with an understanding of the challenges faced by online operators in developing markets, giving it a model to take into other emerging markets. And, of course, its minority stake in Yihaodian does position Wal-Mart for a full takeover of the business in the future.

Yihaodian's co-founders Gang Yu and Junling Liu, who have extensive experience in multinational companies including Dell and Amazon, will be an asset to Wal-Mart, particularly in helping the US retailer understand the idiosyncracies of the Chinese market.

Wal-Mart vice chairman and CEO of Walmart e-commerce and global sourcing Eduardo Castro-Wright says that online sales in China are "growing rapidly and are projected to match US online sales in the next few years".

While that comment may raise eyebrows, according to recent research by McKinsey, the number of people with online access in China is set to almost double between 2010 and 2015. In 2010, China had 457m online. By 2015, McKinsey says that will grow to 750m.

China's online population are very willing to shop online, with Internet sales in Shanghai accounting for 10.1% of retail sales. (In the UK, the figure is 10.5%). China as a whole does not fare badly, with the Internet accounting for 3.3% of retail sales in the whole of the country. In the EU, 5.9% of retail sales are made online, while in the US, it is 4.5%.

However, for all the opportunity presented by gaining access to China's fledgling but growing online retail channel, there are, of course, challenges.

Outside of Shanghai, however, the online channel is developing at a slower rate. DDMA attributed the slower rate of growth to online supermarkets only covering first- and second-tier cities, greater access to the Internet in Shanghai, as well as a greater willingness to accept new trends in the major cities.

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According to DDMA's research, China's consumers tend to focus their online purchasing on less perishable categories, with confectionery and snacks being the most popular categories bought online in Shanghai.

According to a study conducted by the group, 39% of survey respondents had bought candy or chocolates online, 34% bought crackers, 33% bought potato chips, 23% bought noodles, while 22% bought nuts or dried fruit. This reflects the unique shopping behaviours exhibited by Chinese consumers, with a high focus on freshness. They tend to shop at physical stores more frequently (four to five times per week on average) than their international counterparts.

Furthermore, Wal-Mart's high focus on value may ill-suit Chinese consumers' preference for well-known and more expensive brands. According to McKinsey's research, Chinese consumers have a strong preference for brands that are well known and they show higher trust in brands that are more expensive, which the research group claims has, intriguingly, led to "reverse price wars in some cases".

Another problem faced by the retail segment in China, and which would only be heightened for online operators is the highly fragmented nature of distribution networks in the country. According to McKinsey research, there are some 30,000 distributors in China.

In an interview with the Wharton Business School in April, Yihaodian chairman Gang Yu said that other companies in China had struggled with their supply chain management, which he had worked on for over a decade with both Dell and Amazon.

When Yihaodian started, Yu says the company had some 3,000 SKUs and hundreds of suppliers. Now it has 70,000 SKUs and 2,000 suppliers. "Managing the products, including quality control, inventory, online marketing and pricing, were all challenges," he says.

Nevertheless, the acquisition by Wal-Mart put forward the retailer's aspirations of becoming the world's leading global multi-channel retailer and is only one of a number of announcements it has made around its online operations in recent months.

Speaking alongside the retailer's results on Tuesday (17 May), Wal-Mart president and CEO Mike Duke said that the growth potential of e-commerce is "especially significant in markets like China" and that it is "committed to being at the forefront of this growth".

While China may arguably be the most important of the emerging markets, it is unlikely that Wal-Mart's online ambitions will end there.

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