



Uncovering the emerging players in China's
e-commerce - Issue 3

Group-buying platform – Pinduoduo

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While Alibaba and JD.com continue to dominate the e-commerce scene in China with 58.2% and 16.3% market share according to eMarketer, a number of relatively smaller specialist players have caught increasingly attention in China's e-commerce market recently. In today's rapidly evolving and highly competitive online marketplace, these fast-growing companies provide another option for businesses to market and sell their products. Fung Business Intelligence has identified some of these emerging players, each focusing on a specific area such as group-buying, O2O lifestyle services, social commerce, vertical online platforms and short videos. In this series of articles, we provide an overview of the key business and developments of these emerging player; we also identify their strengths, weaknesses, opportunities and threats.

In this issue, we look at the business model and latest developments of Pinduoduo – a popular group-buying platform which targets consumers in the lower-tier cities and rural markets. Customers can buy products at a cheaper price on Pinduoduo, while retailers can clear inventory on the platform. Pinduoduo is seen as a major rival to Alibaba. Pinduoduo made its debut on the NASDAQ Stock Exchange on 26 July, 2018. Since then, the company has faced a series of accusations that products on its platform are fake or substandard.

Company background

Founded in September 2015, Pinduoduo was set up by former Google engineer Colin Huang (Zheng Huang) in Shanghai. Pinduoduo is a third-party social commerce platform, mainly offering low price group buying products (or “team purchase”). It covers major product categories including apparel, shoes, bags, mother and childcare products, food and beverage, fresh produce, electronic appliances, furniture and household goods, cosmetics and other personal care items, sports and fitness items as well as auto accessories. Currently, all products offered on Pinduoduo are supplied by individual merchants, who are responsible for sourcing their own products. According to Pinduoduo, it focuses on selling off-season products of brands and retailers, unbranded products with flexible pricing, as well as a few popular products which can gather large amount of orders in a short period of time.

It is noteworthy that Tencent has been a principal shareholder of Pinduoduo since February 2017. It led Pinduoduo's Series C financing round in February 2017 and invested again in the company in April 2018 (Exhibit 1).

Exhibit 1. Major funding rounds of Pinduoduo, 2015 – 2018

Date	Funding rounds	Money raised (USD million)	Lead investors
11 April, 2018	D	1,400	Tencent Holdings, Sequoia Capital China
1 February, 2017	C	213.7	Tencent Holdings, Sequoia Capital China
20 July, 2016	B	110	Sequoia Capital China
1 September, 2015	A	8	Gaorong Capital

**Note: Tencent first invested in Pinduoduo's Series B funding round in 2016.*

Source: Various Internet sources, compiled by Fung Business Intelligence

Pinduoduo made its debut on the NASDAQ Stock Exchange on 26 July, 2018, raising US\$1.63 billion. The deal is one of the largest Chinese tech IPOs of the year in the U.S. According to Pinduoduo, the fund raised will be used mainly to expand the company's business operation, promote research and development, and enhance its technology infrastructure. It is reported that Tencent will hold 17.0% of the total shares of Pinduoduo after the IPO.

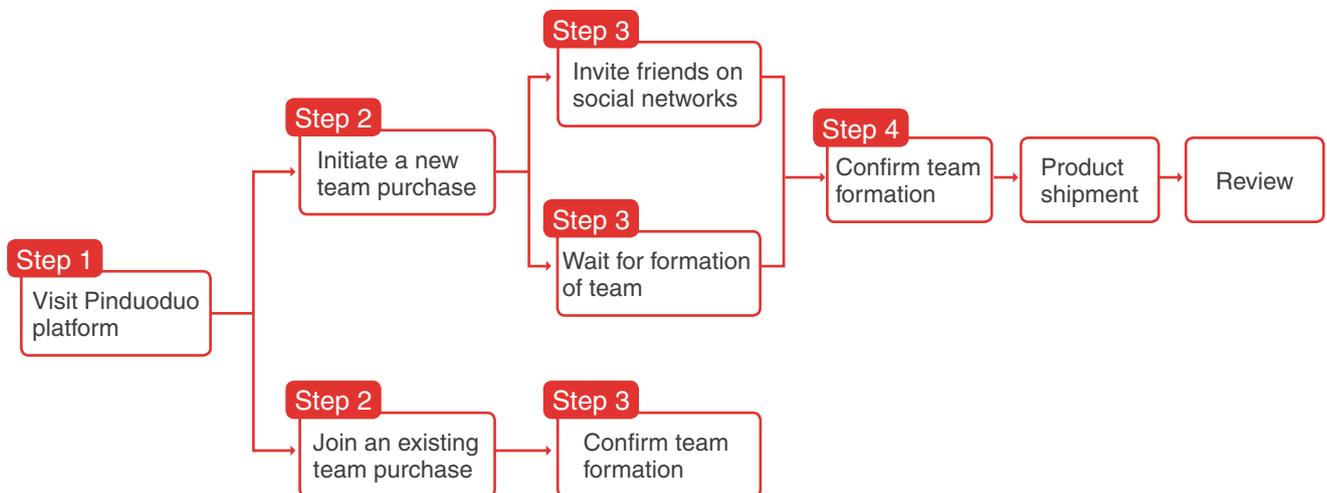
The business

Pinduoduo is a third-party social commerce platform, mainly providing group buying offers at reduced prices. Pinduoduo has an app and a WeChat Mini Program. For each product on Pinduoduo platform, shoppers can choose to buy the product individually, or initiate or join a team purchase.

Team purchases typically allow customers to enjoy lower prices but a team purchase order will only be confirmed once a team is formed. To successfully create a team purchase order, the shopper can kickstart the whole process by placing his order with an initial payment. The shopper can share relevant product information among his friends on WeChat. The order is considered successful if there are enough number of friends (other buyers) showing their interests in buying the product; otherwise, the platform will refund the initial payment to the shopper if the order cannot proceed further.

Meanwhile, instead of paying the initial fee, the shopper can send out a price reduction post to his circle of friends on WeChat; the shopper and his friends can enjoy a discount if there are more number of potential buyers in the pool; and eventually the shopper may get the product for free if the pool of buyers is big enough. Exhibit 2 illustrates the steps to complete a team purchase on Pinduoduo and Exhibit 3 shows the interface of Pinduoduo app.

Exhibit 2: Steps to complete a team purchase on Pinduoduo



Source: Pinduoduo

Exhibit 3: Interface of Pinduoduo app

Invite friends on social networks

Quantity sold, requisite number of buyers to form a shopping team

Join an existing team purchase

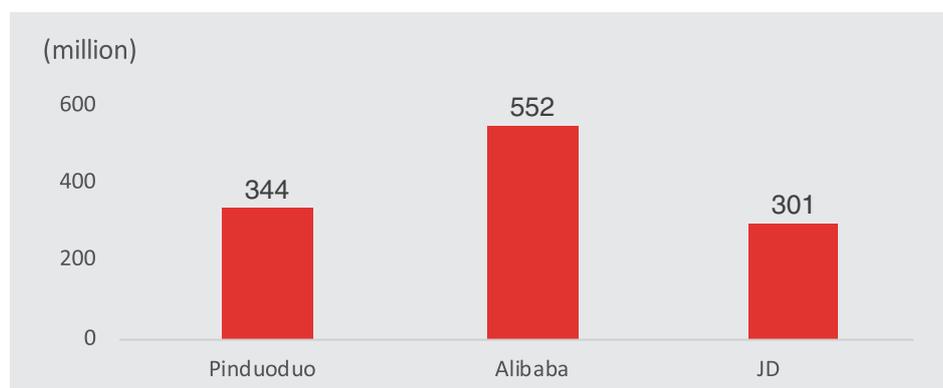
Initiate a new team purchase

Source: Pinduoduo

Financials and other key facts

Pinduoduo's total revenues amounted to about 1.7 billion yuan in 2017, with a net loss of 525 million yuan. As of 30 June, 2018, the number of active buyers on Pinduoduo platform reached 344 million (Exhibit 4). Pinduoduo's gross merchandise value (GMV) in 2017 and in the twelve-month period ended 30 June, 2018 was 141.2 billion yuan and 262.1 billion yuan respectively. In the twelve-month period ended 31 March, 2018, Pinduoduo has over one million active merchants on its platform.

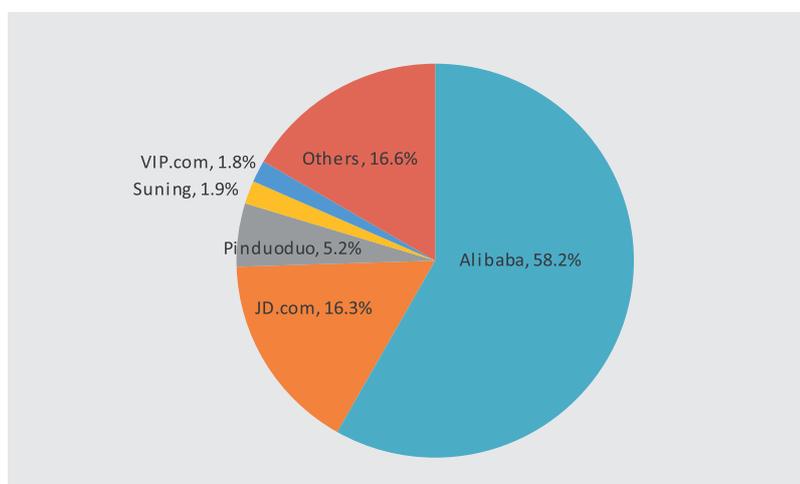
Exhibit 4: Number of annual active customers of Pinduoduo, Alibaba and JD.com, as of 31 March, 2018



Source: Pinduoduo, Alibaba, JD.com, compiled by Fung Business Intelligence

According to market research consulting company eMarketer, Pinduoduo is the third largest e-commerce player in China, holding 5.2% of market share, following Alibaba and JD.com, which hold 58.2% and 16.3% of market share respectively (Exhibit 5). Pinduoduo achieved a mere 0.1% of market share when it first entered the market¹.

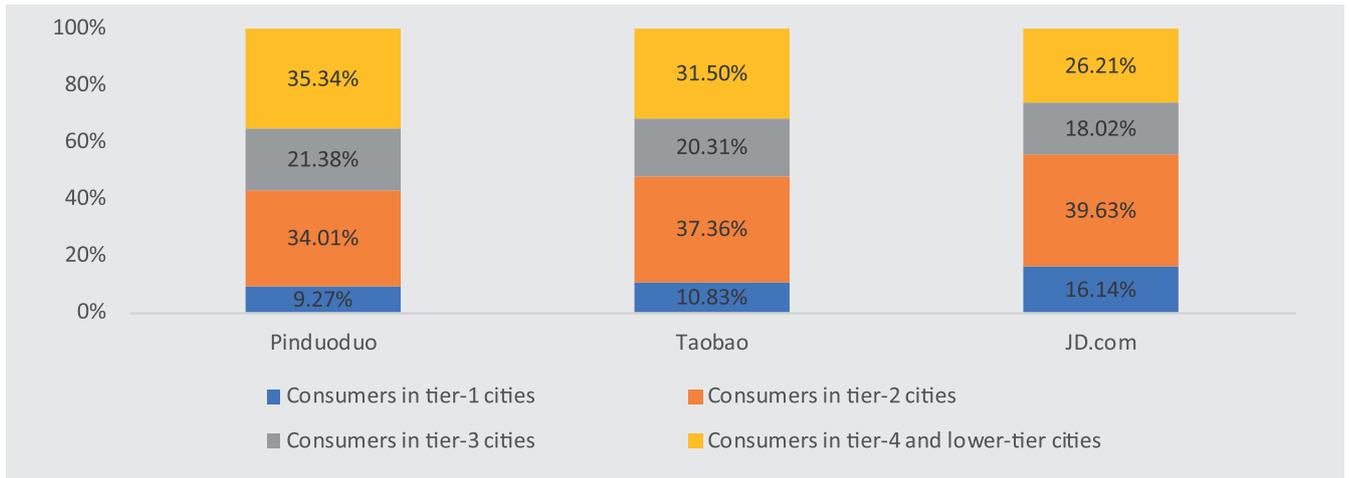
Exhibit 5: Market shares of e-commerce platforms, April 2018



Source: eMarketer, compiled by Fung Business Intelligence

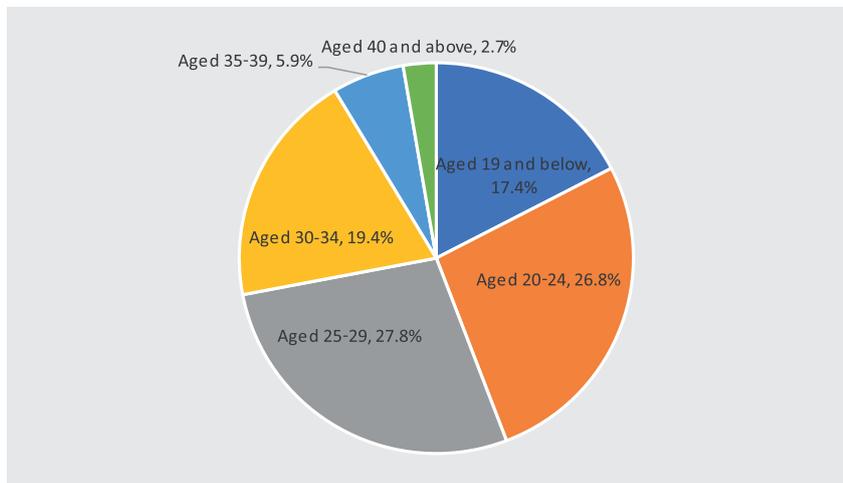
According to big data service provider Jiguang², over half of Pinduoduo’s customers live in tier-3 and tier-4 cities; over half of Pinduoduo’s customers are aged 20-29 (Exhibit 6 and 7).

Exhibit 6: Types of Pinduoduo’s customers, by city tier, February 2018



Source: Jiguang, Changjiang Securities, compiled by Fung Business Intelligence

Exhibit 7: Age distribution of Pinduoduo’s customers, March 2018



Source: Jiguang, compiled by Fung Business Intelligence

Recent developments

Pinduoduo signs strategic cooperation framework agreement with Tencent

In February 2018, Pinduoduo entered into a strategic cooperation framework agreement with Tencent, Tencent would offer Pinduoduo access points on the interface of its WeChat Pay, enabling Pinduoduo to utilize traffic from WeChat Pay. In addition, Pinduoduo and Tencent would cooperate in a number of areas including payment solutions, cloud services and user engagement, and explore and pursue additional opportunities for potential cooperation. The agreement has a term of five years.

China's market regulators probe Pinduoduo for sale of counterfeit and imitation goods

After Pinduoduo filed for an IPO in the U.S. in July 2018, growing accusations of Pinduoduo selling counterfeits and imitation goods have prompted the government to rein in by investigating the company. On 1 August, 2018, the State Administration for Market Regulation (SAMR) said it called for the Shanghai Municipal Administration of Industry and Commerce (SHAIC), as well as other relevant market regulators, to investigate Pinduoduo, which is headquartered in Shanghai. The regulators reportedly would look into issues related to the sale of imitation products and counterfeits³.

Pinduoduo removes 4 million listings following concerns over fake goods

In response to the counterfeit accusations, on 22 August 2018, Pinduoduo issued an open letter stating that between 2 August and 9 August, it closed 1,128 stores and removed nearly 4.3 million listings from its platform. According to the letter, Pinduoduo has already reported 36 businesses that infringe on copyrights to the Changning District Market Supervision Administration in Shanghai. Pinduoduo said it will continue to report suspected illegal companies to the relevant local market supervisor. It will also upgrade its merchant verification system in the future⁴.

Comments from Fung Business Intelligence

Fung Business Intelligence believes Pinduoduo's unique social approach to e-commerce underpins its rapid growth, especially in lower-tier cities. Over half of Pinduoduo's customers live in tier-3 and tier-4 cities. Compared to consumers in tier-1 and tier-2 cities in China, consumers in lower-tier cities generally demand products with lower price-points. Since Pinduoduo focuses on offering selected popular goods at a bargain price, through its team purchase model, it can generate substantial revenue within a short period of time. In other words, it can combat low margins through large number of team purchase orders.

Driven by the higher penetration of mobile devices, social-commerce platforms, as well as better logistics infrastructures in lower-tier cities in recent years, Pinduoduo has been growing very rapidly. Thanks to strong backing from Tencent, users can easily share deals on WeChat platform and easily bring others into the fold. Hence, it can gain high traffic at relatively lower costs than other e-commerce platforms.

Product prices on Pinduoduo are generally much lower than other e-commerce platforms as well as offline retail stores. For merchants, Pinduoduo may be a good channel to sell their off-season products and get rid of excess inventories, but it is not suitable for brand building as it emphasizes on price rather than brand stories and product quality.

We believe Tencent's investment in Pinduoduo is one of its strategic moves to tap the highly competitive e-commerce market and better compete with Alibaba, especially in lower-tier cities and rural areas. Tencent has a strong hold on Pinduoduo — Pinduoduo users can leverage WeChat and WeChat Mini Programs to spread the deals and pay by WeChat Pay. In response to Tencent's move to tap the lower tier cities, Alibaba launched a new low-end shopping app "Taobao Tejiaban" (Taobao Special/Bargain Edition) in March 2018. The app targets shoppers in lower-tier cities and rural markets, selling products with similar price points as Pinduoduo. Alipay also launched a group-buying function on Alipay's homepage in August. It offers group-buying deals within limited time, and the deals will be changed regularly. Meanwhile, JD.com's group-buying platform "JD Pingou" is now open to individuals for store opening. Starting from 1 June, individuals with valid ID cards can register and open their store on the platform under the category of "unbranded product".

Exhibit 8: SWOT analysis of Pinduoduo

Strengths	Weaknesses
<ul style="list-style-type: none"> • Offers bargain sales; customers can buy products at a cheaper price, while retailers can clear inventory. • Backed by Tencent, users can easily share deals on WeChat platform and easily bring others into the fold; it can gain high traffic with relatively lower costs. • Pinduoduo has a clear target market - customers who desire products in low price and do not care about quality and brands. 	<ul style="list-style-type: none"> • Difficult to control the quality of products on the platform; counterfeit goods and knockoff products remain a huge concern. • Depends too much on WeChat to spread the deals and generate new orders. • Difficult for merchants on Pinduoduo to build brand awareness and increase brand stickiness as the platform focuses on low-cost products. • Generates revenue mostly from advertisement but not from products; its business model may not be sustainable in the long run. • Adopts a “push strategy” when selling products; may not be able to provide good shopping experience to customers.
Opportunities	Threats
<ul style="list-style-type: none"> • Rising consumption power of lower-tier cities and rural markets provides huge opportunities for Pinduoduo. • High Internet penetration and large numbers of social media users allow Pinduoduo to build its customer base quickly. 	<ul style="list-style-type: none"> • Faces increasing market competition - Alibaba and JD.com have tapped the group-buying market. The former has launched “Taobao Tejiaban” app targeting the lower-tier cities and rural market, and launched a group-buying function on Alipay’s homepage, while the latter has opened a group-buying platform “JD Pinguo”. • Pinduoduo’s business model is not in line with the consumption upgrading trend in China.

Source: Fung Business Intelligence

References

¹“Alibaba and JD facing keen new rivals, says eMarketer”, 11 July 2018. Inside Retail Hong Kong.
<https://insideretail.hk/2018/07/11/alibaba-and-jd-facing-keen-new-rivals-says-emarketer>

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<https://www.jiemian.com/article/2007379.html>

³“China’s market regulators probe Pinduoduo for sale of counterfeit, imitation goods”, 1 August 2018. South China Morning Post.
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⁴“Pinduoduo shuts 1,128 stores and removes 4 million listings following concerns over fake goods”, 23 August 2018. Technode.
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