

Case example

Alibaba: the Yangtze River Crocodile

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Jack Ma, founder of Alibaba.

Source: Eugenio Loreto/EPA-EFE/Shutterstock

In late 2018, Jack Ma, founder of China's largest e-commerce company Alibaba, announced shock news: in the coming year, he would step aside as company Chairman in favour of the Chief Executive, Daniel Zhang. Jack Ma had been Alibaba's charismatic leader for two decades. But Ma made it clear that he was not disappearing altogether: he remained a major shareholder and would be a permanent member of the 36 strong 'partnership' that nominated the majority of the company's board of directors. A senior banking analyst observed of Ma: 'He has been the spiritual leader of the company since he founded it, and everyone looks up to him. People call him Teacher Ma. That means people are not looking at him as manager or chief executive or chairman – they are looking to him for guidance.'

The new Chairman and Chief Executive Daniel Zhang was more of a professional manager than the entrepreneurial Ma. Educated in China, he had begun his career in the accounting firms Arthur Andersen and PwC before joining Alibaba in 2007. One of Zhang's great successes at Alibaba had been the idea of making Singles' Day in November a national festival of shopping, all served by Alibaba's online commerce businesses of course. Recently Zhang has rolled out Singles' Day internationally, backed by his experience in international firms. During a company-wide strategy session soon after becoming Chief Executive in 2015, he said: 'We must absolutely globalize. We will organize a global team and adopt global thinking to manage the business and achieve the goal of *global buy and global sell*.'

Jack Ma and colleagues had launched Alibaba in 1999 as China's first business-to-business portal connecting domestic manufacturers with overseas buyers. Since then, the Group has grown in many directions. 1688.com was founded for business-to-business trade within China. Alibaba's Taobao Marketplace serves small businesses and individuals. Tmall.com provides electronic shop fronts to help overseas companies such as Nike, Burberry and Decathlon to reach Chinese consumers. Juhuasuan offers daily deals on everything from toys to laptops. Behind all this are Alibaba's enormous server farms, which form the basis for another market-leading business, cloud computing. There is also Alipay, effectively under Ma's personal control but functioning as the Group's equivalent to PayPal, which processes most Group transactions. One way or another, it is possible for Alibaba's customers to trade almost anything: the American security services have even set up a sting operation on Alibaba to catch traders selling uranium to Iran. In 2018, Alibaba had approaching 58 per cent of the e-commerce market in China, the largest e-commerce market in the world. In 2015, Alibaba had invested in the Indian e-commerce business Snapdeal and the following year it bought a majority stake in the Singapore e-commerce business, Lazada. The company also had strong positions in Brazil and Russia. International e-commerce represented nearly 7 per cent of the company's sales in the last quarter of 2018 (about \$1,247m out of total quarterly sales of \$17,057m: see also Table 1).

Alibaba had always had an international bent. Jack Ma had started his career as an English language teacher in the city of Hangzhou, capital of the prosperous province of Zhejiang and not very far from Shanghai. Ma had discovered the Internet on his trips to the United States in the mid-1990s. As early as 2000, Ma had persuaded both the leading American investment bank Goldman Sachs and the Japanese internet giant Softbank to invest. The then ascendant American internet company Yahoo had bought nearly a quarter of the Group in 2005. Even after Alibaba went public in 2015, SoftBank still held 32.4 per cent of the shares and Yahoo 15 per cent. The Alibaba Group board counted as members Yahoo's founder Jerry Yang, Softbank's founder Masayoshi Son and Michael Evans, former vice-chairman of Goldman Sachs. Even so, Jack Ma was ambivalent about Western investors: 'Let the Wall Street investors curse us if they wish!', Ma had

Table 1 Key statistics

	2010	2012	2014	2015	2016	2017	2018
Alibaba Group Sales Yuan bn	6.7	20.0	52.5	76.2	101.1	158.3	250.3
Chinese GDP Yuan Tr.	40.4	53.4	64.4	68.9	74.4	82.7	90.0
Chinese online retail sales Yuan Tr.	0.5	1.3	2.8	3.9	5.2	7.2	n.a.
Per cent of Chinese using Internet	34.3	41.0	46.0	50.3	52.2	55.8	n.a.

Sources: Statistical Report on Internet Development in China; InternetLiveStats.com; Statista.com. One Yuan = €0.13; \$0.15; £0.11.

proclaimed at a staff rally. 'We will still follow the principle of customers first, employees second and investors third!'

Strictly, overseas investors do not directly own stakes in the Alibaba Group, instead owning shares in a shell company – a so-called variable interest entity (VIE) – that has a contractual claim on Alibaba's profits. This VIE structure is a common way for Western-listed Chinese firms to get around Beijing's foreign-ownership rules. But the Chinese government could close the loophole at any time, and it gives foreign shareholders limited recourse against abuses by Chinese companies' managers. Ironically, the most notorious VIE controversy so far involved Alibaba's Jack Ma, who in 2011 separated Alipay from the rest of the Group without board approval. Ma said new Chinese regulations forced him to make the move. Yahoo was only told about the spin-off five weeks after it had happened. A fundraising round for Alipay's new parent company valued Alipay at nearly \$50bn.

Jack Ma cultivated important relationships within China as well as abroad. Early on he socialised with a group of businessmen known as the Zhejiang Gang, because of their common roots in the province whose capital was Ma's home city of Hangzhou. Prominent members of this group included some of China's most successful entrepreneurs: for example, Guo Guangchang of the huge diversified Fosun Group; Shen Guojun of China Yintai Holdings, a retail property developer; and Shi Yuzhu, of the online gaming company Giant Interactive.

Alibaba's relationship with the Chinese government is hard to read. Jack Ma insists that he has never taken loans or investment from the Chinese government or its banks: he had gone to overseas investors instead. However, given that a third of Chinese business activity is carried out within state-owned enterprises, the government is bound to be in close liaison with the dominant national player in e-commerce. Ma explained his philosophy as: 'Always try to stay in love with the government, but don't marry them.' The Alibaba Group has built up its political connections. Tung Chee-hwa, Hong Kong's first chief executive after its return to China, served on its board of directors. Alibaba

has also allied with several so-called 'princelings', children of important political leaders. Princeling investors include Winston Wen, son of a former Chinese premier; Alvin Jiang, grandson of a former Chinese President; He Jinlei, son of a former Politburo member and a senior manager of the state Chinese Development Bank; and Jeffrey Zang, son of a former vice premier and a senior manager at China's state sovereign wealth fund, Citic Capital.

Given Chinese President Xi Jinping's sweeping political and economic reform campaign, there are no guarantees of Alibaba's position domestically. In 2015, princeling investor He Jinlei's older brother was placed under house arrest because of accusations of corruption. 2015 had also seen the publication of an investigation by China's State Administration for Industry and Commerce into counterfeit goods and fake listings on the Group's Taobao site, leading to a 10 per cent fall in Alibaba's share price. Jack Ma commented on his relations with Chinese regulators: 'Over the past two years, not only was I a very controversial figure, but also these days, the disputes are bigger and bigger.' He continued, 'I, too, felt puzzled, sometimes wronged – how did things become this way?' Nonetheless, Ma promised to clean up the site. In 2018, in an apparent reproof, Chinese state media let out the news, previously withheld, that Jack Ma was a longstanding member of the Chinese Communist Party.

President Xi Jinping's reform campaigns were partly in response to changing economic conditions in China. After three decades of double-digit growth, China's growth rate has slowed to around 7 per cent a year more recently (see Table 1). Such growth is very respectable by world standards. Besides, faced with rising domestic concern about the environment, President Xi was happy to restrain the expansion of high polluting industries such as cement, coal and steel. At the same time, the Chinese government was promoting e-commerce as a key area for future economic growth. However, there were causes for concern. Many local authorities and firms had borrowed heavily on expectations of higher growth, and there

were fears that financial institutions had over-lent. Some warned of a consequent crash. Moreover, it was hard to see China's growth rate picking up again, on account of an aging population and the drying up of the traditional supply of young labour from rural villages: the Chinese labour force participation rate has dropped from a high of 79 per cent in 1990 to 69 per cent by 2017. Although the government relaxed the famous one-child per family rule in 2013, Chinese parents are still reluctant to have more children because of the cost of housing and good education in the main urban centres. It is predicted that by the early 2030s, about a quarter of China's population will be over 65 (against 17 per cent in the United Kingdom). Slower economic growth in China overall is being matched by a slowing in the rate of growth of the Chinese e-commerce market (see Table 1).

At the same time, Alibaba faces greater competition in its home market. A decade ago, Alibaba had seen off an attack by American rival eBay in the Chinese market with a fierce price-war. Jack Ma had proclaimed: 'eBay is a shark in the ocean; we are a crocodile in the Yangtze River. If we fight in the ocean, we will lose, but if we fight in the river, we will win.' A combination of cultural, linguistic and government policy factors kept Western internet companies at arm's length in the Chinese market: Google has been reduced to a market share of about 1 per cent, while Amazon eventually chose to list on Alibaba's Tmall site after a decade pushing its own venture in China.

But now Alibaba's home-market dominance is facing a local challenge from the aggressive JD.com. JD.com's founder and chief executive Richard Liu has declared a goal of beating Alibaba to the top position: 'The competition makes the two companies stronger. I'm actually enjoying competing.' While Alibaba depended for a long time on China's unreliable postal service to get its goods to customers' doors, JD.com has been more like Amazon in investing heavily in its own distribution centres and delivery services. By 2018, JD.com had 16.3 per cent of China's e-commerce market. Tencent, China's largest social networking and online games company, has taken a 15 per cent stake in JD.com, giving the challenger access to more than 890 million users of its WeChat phone messaging app. WeChat allows users to scan product bar

codes with their smartphone cameras to make instant purchases through JD.com. Mobile commerce is increasingly important in China, with 788 million people being mobile users, 98 per cent of the country's total user base in 2017. Mobile has been a challenge for Alibaba's traditional PC-based retail model, but the company has been catching up with about 80 per cent of its e-commerce business on mobile devices by 2017.

In a context of slower Chinese growth and increased domestic competition, the internationalisation strategy of Alibaba's new Chairman Daniel Zhang seemed to make sense. However, Zhang faced one major challenge: resistance in the world's second largest e-commerce market, the United States. In January 2017, the first month of the new American Presidency, Jack Ma had met Donald Trump in New York and promised that Alibaba's investment in the United States would bring one million new jobs to America. Alibaba invested in two large data centres for its expanding cloud computing business. However, the United States was the home of Amazon, Microsoft and Google, all with vast cloud businesses of their own. Besides, nationalist Donald Trump was imposing boycotts on Chinese technology companies and threatening tariffs. At the end of 2018, Alibaba announced the winding down of its cloud computing operations in the United States. For the Yangtze River crocodile, attacking the ocean sharks in their home seas may have been a step too far.

Main case sources: *China Daily*, 8 and 13 May 2015; *Financial Times*, 9 September 2014 and 14 September 2018; *South China Morning Post*, 12 February 2015; *Washington Post*, 23 November 2014; *Wall Street Journal*, 4 December 2018.

Questions

- 1 Carry out a PESTEL analysis of Alibaba at the time of the case. Evaluate the balance of opportunities and threats, using the same kind of figure as in Illustration 2.1.
- 2 Draw a basic sociogram of Alibaba's network (see Section 2.2.3 and Figure 2.5): some simplification may be necessary. Explain why Alibaba's network might be useful.