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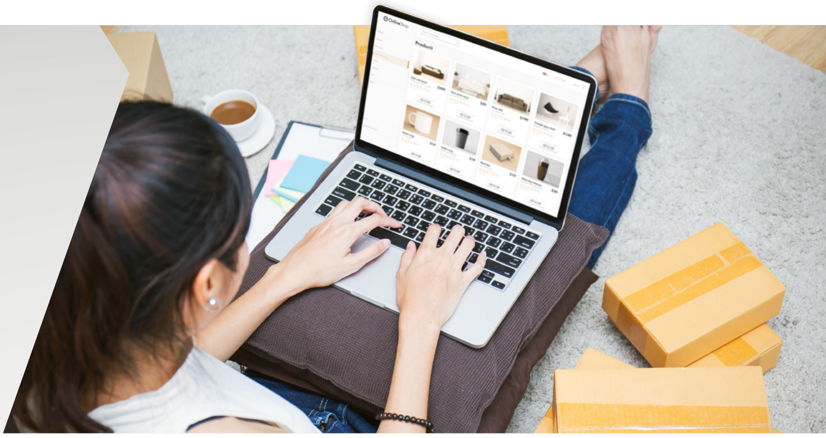
E-commerce: Driving Asia's next leg of growth



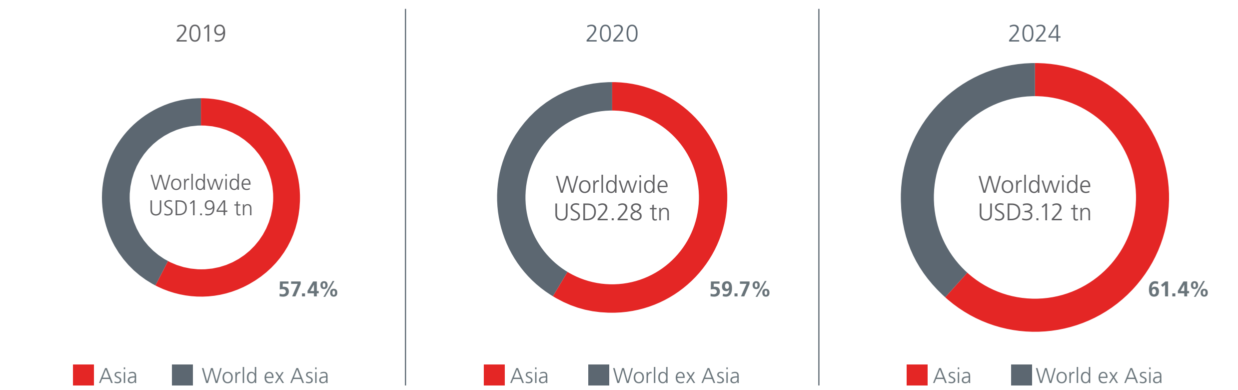
E-commerce

Although Asia already accounts for 57.4% of the global e-commerce market in 2019, its share will only get bigger. Robust logistics networks, a rising middle class, improving financial infrastructure and rapid innovation will fuel Asia's e-commerce revenues, which will in turn drive GDP growth, productivity and economic inclusion in the region.

The world has seen exceptional growth in e-commerce transactions in recent years. Asia, with its growing middle class and increasing internet penetration, is at the forefront of global e-commerce dynamism. The region accounted for 57.4% of global e-commerce sales (business-to-consumer) in 2019. According to Statista[1], Asia's e-commerce revenues are predicted to grow by 22.4% to USD1.36 trillion in 2020 and reach USD 1.92 trillion by 2024. By then, Asian economies will account for 61.4% of the global e-commerce market. See Fig. 1.

While China is a market leader in terms of size, the e-commerce markets in India and Indonesia

Fig 1: Asia is the world's largest e-commerce (B2C) market



Source: Statista, data extracted on 30 May 2020.

Source: [1]Statista: Digital Market Outlook, data extracted on 31 May 2020.

Fig. 2: Rapid growth in Asia's ecommerce (B2C) markets

(USD' million)	2019	2020	CAGR	2024
China	862,239	1,057,967	8.6%	1,474,102
India	33,198	43,489	13.1%	71,049
Indonesia	20,339	28,597	15.4%	50,662
Thailand	5,104	6,921	13.0%	11,266
Vietnam	4,428	5,770	9.0%	8,158

Source: Statista, data extracted on 30 May 2020. Emerging countries. B2C refers to business to customers.

– the world's second and fourth most populous countries, respectively – are expected to enjoy double-digit growth rates in the coming years (see Fig. 2).

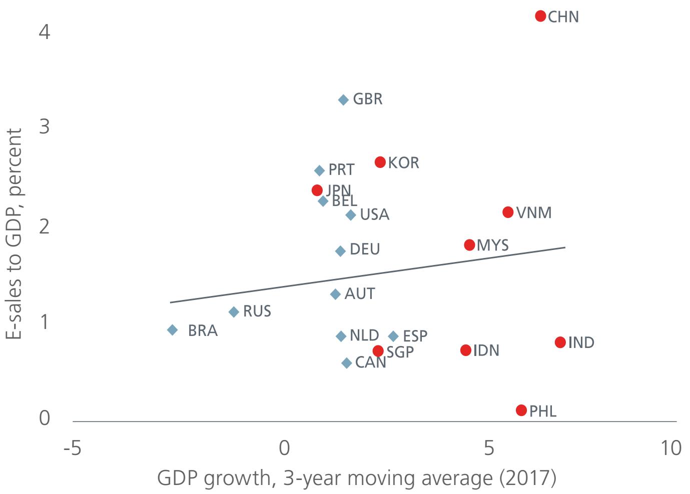
A POWERFUL ENGINE FOR ECONOMIC GROWTH

The economic benefits of e-commerce are stark. IMF Senior Economist, Tidiane Kinda, noted in his research paper that historically, Asian countries with higher e-commerce penetration (as measured by % of e-commerce sales to GDP) are more likely to experience higher GDP growth (see Fig. 3).

This is because businesses that engage in e-commerce tend to require a more knowledgeable and innovative workforce. This in turn lifts productivity and profitability. Fig. 4. puts this in perspective by showing that participation in e-commerce lifts global total factor productivity by 14%. The impact is even greater in Asia.

As economies gradually emerge from their lockdowns, we believe that Asia is uniquely positioned to ride on the e-commerce wave and enjoy higher growth on the back of the following key success factors:

Fig. 3: Correlation between e-sales and GDP growth (2017)



Source: Adapted by Eastspring from IMF, World Economic Outlook; and IMF staff estimates. China (CNH), Vietnam (VNM), Malaysia (MYS), India (IND), Indonesia (IDN), Korea (KOR), The Philippines (PHL), Singapore (SGP).

1 ROBUST LOGISTICS NETWORKS

Efficient logistics services are vital in order to fulfil deliveries of online purchases to end-consumers – be it domestically or internationally. While there is still room for improvement, Asia's logistics performance has advanced considerably in the past decade. According to the World Bank's logistics performance index[2], Asia accounts for

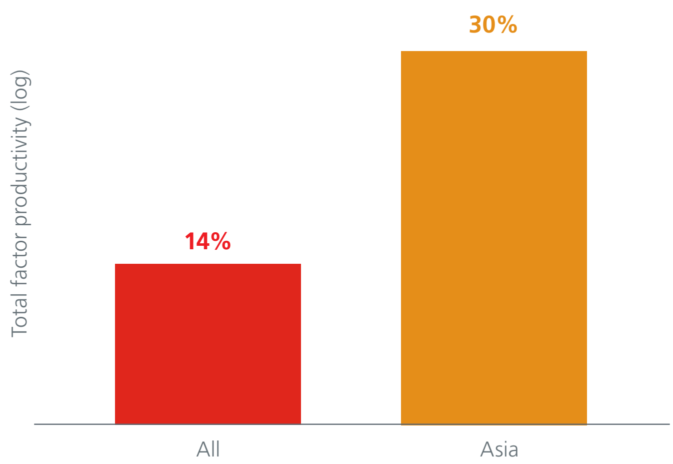
Source: [2]The World Bank's Aggregate logistics performance index (LPI), 2018. Asian (developed and emerging) countries: 16 (Japan, Singapore, China, South Korea, etc), Non-Asian developed countries: 34 (Germany, Sweden, Belgium, Austria, etc), non-Asian emerging countries: 4 (Chile, Panama).

17 of the world's top 50 performers. Within Asia, Japan and Singapore are the two top-performing countries, followed by United Arab Emirates, Hong Kong, Australia, South Korea and China. China's logistics performance is advancing rapidly. Logistics operators in China can now fulfil urgent deliveries within 12 hours in select city clusters and within 24 hours nationwide[3], making online shopping ubiquitous in urban areas.

Over in Indonesia, as **Ari Pitoyo, Chief Investment Officer of Eastspring Indonesia,** noted in his paper **Indonesia's infrastructure reforms have helped reduced its logistics costs**[4] from 27% of GDP in 2015 to 22% in 2020. In fact, the government has an ambitious target of lowering logistics costs to 19% of GDP by 2024 and to eventually match the standards of Japan and Singapore, where logistics costs represent just a single-digit percentage of total GDP.

It is this robust logistics performance, especially when compared against non-Asian emerging markets, that provides the stage for Asian e-commerce companies to capitalise on the region's growing middle class.

Fig. 4: Estimated impact of e-commerce participation on total factor productivity[7]



Source: Tidiane Kinda 2019, citing World Bank Enterprises Survey and IMF staff estimates.

2 GROWING MIDDLE CLASS

Since 2015, Asia's middle class has overtaken those of Europe and North America. According to the Brookings Institute[5], as urbanisation continues, Asia's middle-class population will increase from 2.02 billion in 2020 to 3.49 billion in 2030. By that time, the region will account for 57% of global middle-class consumption. The growth of the middle class is particularly noticeable in China and India, followed by Southeast Asia. According to Bain & Company[6], 50 million new consumers are expected to join the middle class in Southeast Asia by 2022, contributing to the region's USD300 billion middle-class disposable income. With Asia accounting for 50.3% of global internet users[8], this new generation of middle-class consumers is comfortable with digital marketplaces and purchasing products from social media sites. This change in consumer behaviour will in turn push traditional retailers to integrate more technology into their businesses.

3 IMPROVING FINANCIAL INFRASTRUCTURE

Fintech is a key enabler of e-commerce. In this aspect, China leads the way. In 2019, Chinese consumers were comfortable with digital payments, with 86% of consumers using mobile (digital) payments for purchases. This is significantly higher than other Asian economies. See Fig. 5. Today, Alipay is the world's largest mobile payment platform, with 900 million users

Source: [3]Morgan Stanley Research: The Rise of China's Supercities: New Era of Urbanization, P. 83. [4]www.eastspring.com/insights/emerging-opportunities-in-southeast-asia-s-largest-logistics-market. [5]Brookings Institute: The Unprecedented Expansion of the Global Middle Class – An Update, by Homi Kharas, February 2017. P. 14. Middle class = households with income between USD11 and USD110 per person perday in 2011 purchasing power parity (PPP) terms. [6]Bain & Company and facebook IQ: Understanding Southeast Asia's Emerging Middle Class, 18 March 2019. [7]These figures illustrate coefficients and confidence intervals from two firm-level estimations: (a) the impact of e-commerce participation on total factor productivity controlling for firms' age, size, foreign ownership, export status, and human capital; and (b) the impact of e-commerce participation on the share of exports in total sales controlling of firms' age, size, foreign ownership, and human capital. The error bars refer to the 95% confidence intervals around the estimated coefficients. For Asia, the estimated coefficients imply that participation in e-commerce is associated with a 30% increase in total factor productivity and an increase in the share of exports to total sales by close to 2 units, corresponding to a 50% rise. [8]Learnbonds.com: Asia Accounts for over 50% of All Internet Users Worldwide, 3 April 2020.

in China (and 300 million users outside China)[9]. Its more than 200 financial partners offer users a multitude of financial services, such as bank account management, peer-to-peer money transfers, digital payments, and more.

Across the region, Covid-19 has also expedited the use of digital payments. In India, more shops and e-commerce platforms are reportedly urging consumers to pay via digital wallets to avoid the spread of the infectious disease. A survey conducted in April 2020[10] shows that with the growth of India's United Payments Interface (UPI) scheme, digital wallets were preferred by 53% of consumers. Over in South East Asia, the same research shows that during the pandemic lockdown, Indonesia, Singapore and Malaysia saw varying degrees of increase in the use of digital wallets and online payments. That said, while individual countries have their own regulations to protect customer's personal data and financial information, regional payment regulations will go a long way to boost Asia's e-commerce eco-system.

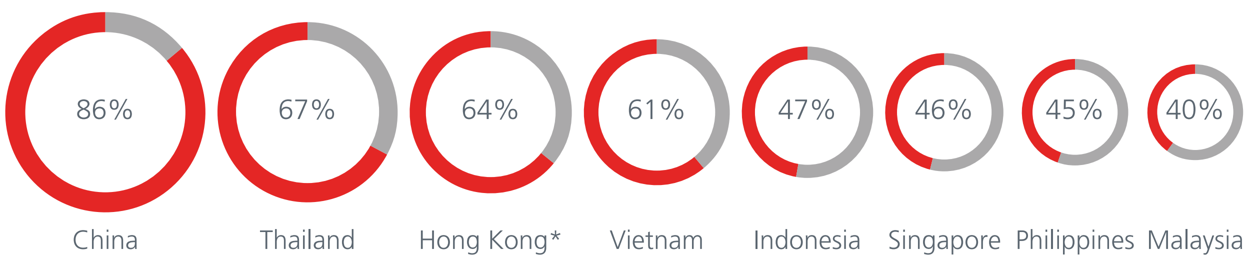
4 RAPID INNOVATION

Despite Asia's rapid e-commerce growth, its retail market is still dominated by small physical retailers with insufficient digitalisation and online retail expertise. According to Bank of America Global Research[11], brick-and-mortar still accounts for 75% of retail sales in China, 90% in India and 61% in Indonesia. This gives innovative e-commerce players an opportunity to tap the potential in these 'fragmented' markets.

China's rural live-streaming is a prime example. In the early weeks of the Covid-19 outbreak, many farmers had to scrap tonnes of rotting produce – even as household demand for fruits and vegetables surged. Coming to the rescue of these farmers, e-commerce giants JD.com and Alibaba-owned Taobao quickly launched rural live-streaming initiatives to help them set up online stores and transport their produce directly from farm to home.

As of March 2020, more than 60,000 farmers have leveraged Taobao Live to sell their products across the country. According to Xinhua News Agency, the total revenue of agricultural products sold online reached RMB 283 million from January to April 2020, 28% more than last year[12]. In the course of bringing 'fragmented' brick-and-mortar farmers onto the e-commerce platform, **Kieron Poon, Eastspring Singapore's China equity portfolio manager,** believes that live-streaming, together with the last mile on-demand local services ("Daojia" in Mandarin Chinese), will be a new e-commerce format that will experience

Fig. 5: Percentage of consumers using mobile payments in stores 2019



Source: PwC: Global Consumer Insights Survey 2019. Question: Paid for my purchase using mobile payment (summary by territory). *Low base for Hong Kong.

Source: [9]Yahoo Finance: Alibaba spinoff Alipay surged past 1 billion users in 2019. [10]Rapyd: Asia Pacific eCommerce and Payments Guide, June 2020. [11]BofA Global Research: New Retail: A secular theme across EMs: Covid to accelerate adoption, 17 June 2020. P.2. [12]China Daily: From the farm gate to your door, via the net. 13 June 2020.

rapid growth. With a larger base of online buyers and sellers from rural areas, he expects China's online sales penetration (now 24.1% of total consumption[13]) to continue to grow in the coming years.

Of course, such innovations are not limited to China. In India, Reliance Jio's mobile phone app, 'JioMart' helps kiranas (neighbourhood retail stores) with online grocery orders and ensures timely delivery to customers. Its growth potential is widely recognised, and the company has attracted significant private equity investments from global investors. More recently in April 2020, US-based Facebook agreed to buy a 9.99% equity stake in Reliance Jio – a further testament of the growth potential in India's e-commerce market. As visibility and acceptance of e-commerce rise in India, **Krishna Kumar, Eastspring Singapore's India equity portfolio manager,** expects to see more small enterprises adopting technology in their business models, thereby attracting greater investment and capital flows. At the same time, opening up the sector to foreign players will accelerate the development of India's e-commerce market.

UNDERSTANDING THE IMPLICATIONS

Robust logistics networks, a rising middle class, improving financial infrastructure and rapid innovation will fuel Asia's e-commerce revenues, which will in turn drive GDP growth and productivity. At the same time, this asset-light business model can help small entrepreneurs and start-ups access larger markets, which increases competition but also makes Asian economies more inclusive. Meanwhile, consumers benefit from greater choice and better price transparency.

Companies that can harness the massive amount of data generated by e-commerce transactions to interact with customers and improve the consumer experience are likely to be at an advantage. Understanding how all these dynamics play out is key for investors when assessing how current business models or economies will fare in an increasingly digital world. The dynamism of the e-commerce market also means that investors' analytical framework needs to evolve along with the changing competitive landscape.

This is the fourth of six articles in our Asian Expert Series which explores the future of Asia post-covid.

Source: [13]National Bureau of Statistics, 15 May 2020.

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