Online-Shopping Market in China -

Adventurous Kingdom for Foreign SME

by

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Table of Contents

List of Figures

List of Tables

List of Abbreviations

B2C online shopping website	B2C online shopping websites are platforms which sell goods or services directly to final customers. Major B2C online shopping websites are Dangdang, Amazon and 360Buy. B2C online shopping customers are customers who purchased from B2C online shopping websites in the past 6 months (CNNIC, June 2008, p.6).
CNNIC	China Internet Network Information Center (CNNIC) is the governmental network information center of China. Established in 1997, the main responsibility of CNNIC includes domain name registry, IP address and autonomous system number allocation service, catalogue database service, technical researches on Internet addressing, Internet survey and relevant information services (CNNIC 2009).
COD	Cash on delivery
CRM	Customer relationship management
C2C online shopping website	C2C online shopping websites are online platforms like EBay for transactions between individuals (CNNIC, June 2008, p.6).
Electronic business and online shopping	Electronic business include any purchase of goods and services via online communication, including business to business (B2B), business to consumer (B2C), consumer to consumer (C2C) and government to business (G2B) (CNNIC, June 2008, p.6). In the report, online shopping will be mainly focused on online B2C market.
Junior college	Junior college is usually known as higher vocational school where students attend after the graduation from senior high schools. The focus of the lectures in junior colleges is on practical skills rather than theoretical knowledge in university education.

Kbps	Kilobits per second
Mbit/s	Megabit per second
MNC	Multinational company
Municipality and sub-provincial city	Municipality refers to cities directly under the jurisdiction of the central government. Chinese municipalities include Beijing, Shanghai, Chongqing and Tianjin. Sub-provincial city refers to Harbin, Changchun, Shenyang, Dalian, Nanjing, Hangzhou, Ningbo, Xiamen, Jinan, Qingdao, Wuhan, Guangzhou, Shenzhen Chengdu and Xian (CNNIC, June 2008, p.7).
Netizen	According to CNNIC (June 2008, p.6), netizen is defined as the Chinese populations who have accessed to Internet in the past 6 months.
ODM	Original design manufacturer
Online customer	According to CNNIC (June 2008, p.6), online customers are defined as the Chinese population who has purchased online in the past 6 months.
Online shopping penetration rate	Online shopping penetration rate refers to the percentage of online shopping customers relative to the total number of netizens for the past 6 months (CNNIC, June 2008, p.6).
Online shopping penetration rate of a website	Online shopping penetration rate of a website refers to the percentage of the customers of a specific online shopping website relative to the total number of online shopping customers in the past 6 months (CNNIC, June 2008, p.6).
SEO	Search engine optimization
SME	Small and medium-sized enterprise

1. Introduction

The Chinese economic miracle has been regarded as a key factor influencing the speed of world's recovery during current economic downturn. In this circumstance, a great number of companies shift their focus to the continuously growing Chinese economy. Online retailing in China is going through a period of exceptional boom. The market is immune to weak economic condition and has experienced an explosive growth. Customers appreciate online price advantages over offline stores and increase their online spending.

In the current financial crisis, Chinese online shopping market provides an attainable opportunity for small and medium enterprises. According to Anderson (April 2009, pp.71-76), online platforms decrease the distribution costs including reduced spending on physical stores, rents and shelf spaces. Number of items sold online can be further extended. SMEs with unique niche products can reach target customers online more cost efficiently. With improved online searching capabilities and communication applications like blogs and product recommendations, consumers' search costs for desired products is largely reduced through online channel. Online buyers can select best suited products at ease. Personalized demands can be satisfied more effectively. SMEs with direct online sales have more opportunities to compete with large conventional players by providing unique and individualized offers.

Mixed with high technology, tremendous growth and distinct culture, Chinese online shopping market shows its promising appeals. Meanwhile, geographical diversity, cultural barrier and lack of understanding make this market less accessible from outside world. Within 10 years, the online market has experienced a dramatic change. One remarkable change in this industry was Taobao's victory, a Chinese local online shopping platform founded in 2003 championed eBay who previously held 85% of market share in 2003 (So/Westland, August 9, 2009). Amazon acquired a Chinese firm Jojo in 2004, still in fierce competition with local opponent Dangdang and has not achieved profitability. Witness a tremendous market potential, Baidu, the Chinese leading search engine who beats Google and controls 76.9% of the Chinese online search market, has moved into the online C2C shopping market in October 2008 and glares at the tempting B2C market (Baidu 2009). In this prosperous market of high competitive intensity and low entry barrier, only the

companies who are able to understand and satisfy local customers can capture the opportunity. Renowned international companies with outstanding technology can easily collapse if consumers are approached in wrong ways.

To understand the roaring potential of this market, especially in the perspective of foreign-based SMEs, major evaluations on Chinese online B2C shopping market are divided into four categories: online shopping market analysis, strategies of online retailers and manufacturers with direct online channels, potential obstacles in the industry and advice on the market entry for foreign SMEs.

Major findings show that this rigorous market will continue its progressive growth. Foreign-based firms with a set of competitive advantages such as product uniqueness, premium service quality or branding knowhow have greater potentials to win over rivals. Disadvantages in the lack of market knowledge can be compensated by collaboration with well established local partners. Complementary services including logistics and online payments should be planned in a comprehensive way and tailored to customers' purchasing habits. For example, online payment through local online third party payment tools and cash on delivery are preferred. Cultural difference has significant influences on marketing techniques, online communication and interaction, payment and delivery terms. For instance, Chinese online shoppers usually contact sellers for product information or price negotiation before their purchases through online instant messengers. It signifies that adequate number of customer service personnel should serve online during working hours and during peak buying time to respond to customers' requests. To conclude, localization in all aspects is the key element for the success. Foreign SMEs should be prepared for an intense and rigorous competition in this environment, but also not to forget the continuous innovation and improvement. In this way, a small scaled company has chances to win over big MNCs in this kingdom of adventure.

2.   Online Shopping Market in China

2.1.   Macroeconomic Environment in China

China' GDP went through an average increase by 9.6% per year from 1979 to 2008 (Men et al., August 2008). The economic crisis has slowed down the Chinese economic growth. Figure 1 below shows the declined GDP growth rate from double digits in 2003-2007 to 9% in 2008. The demand of Chinese export has shrunk due to the global economic downturn and has badly hurt export-oriented manufacturers. Chinese government's current priority is to drive up domestic demands. Stimulus measures have been carried on to re-establish the economy (Chinese government's official web portal, September 11, 2009).

Figure 1: China's GDP and Year-On-Year GDP Growth Rates
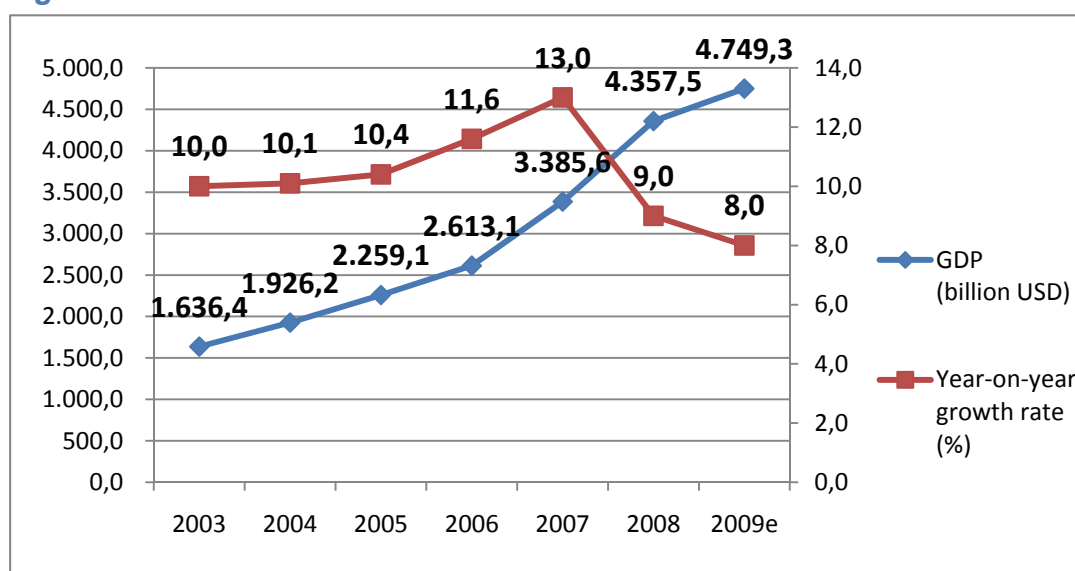
Source: Taiwan bureau of foreign trade, August 19, 2009

The Chinese government offered a fiscal stimulus package of RMB 4 trillion [USD 585.8 billion] to stabilize the economic growth through 2010 (Xinhua, November 14, 2008). The investment is assumed to push up 1 % growth rate of GDP in 2009. IT industry receives around 0.5% to 1% of the cash injection, ranging from RMB 20 billion [USD 2.9 billion] to RMB 40 billion [USD 5.9 billion]. The governmental investment is expected to boost a higher growth in IT industry relative to other countries (IDC, January 20, 2009, p.1). Figure 2 in the next page shows the growth rate of China's IT market and GDP forecast in 2009.

Figure 2: China's IT Market Growth Rate and GDP Growth Rate Forecast, 2009

%	Global	Asia Pacific	US	Japan	India	China
■ GDP growth rate	1,8	3,7	0,0	0,7	6,8	8,0
■ IT market growth rate	2,6	4,0	0,9	1,0	10,0	9,1
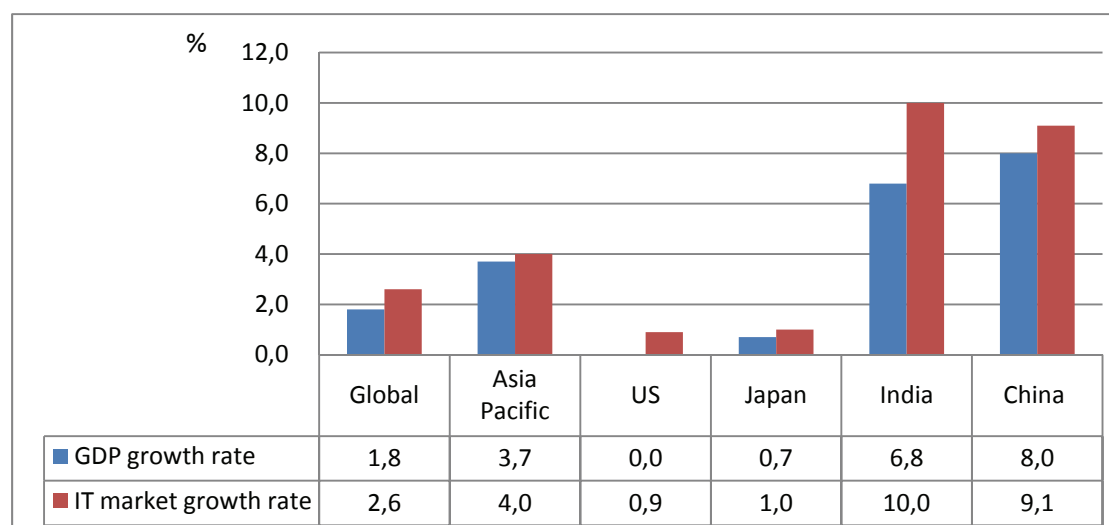
Source: IDC, January 20, 2009, p.1

The Chinese stimulus measure raised the GDP growth rate to 7.1% by June 2009 (Taiwan Bureau of foreign trade, August 19, 2009). The rescue package approved by the State Council includes a plan to revitalize top 10 industries for a faster economic recovery. Electronics and information industry is chosen as one prioritized industry for governmental assistance (Xinhua, April 25, 2009). Even though the growth rate is reduced, Chinese economy is still in a rapid development compared to other countries. World Bank estimates the Chinese GDP growth rate will reach 7.2 and 7.7 in 2009 and 2010 respectively (Xinhua, June 18, 2009).

2.2.   Internet Access Condition in China

2.2.1.   Netizen Scales and Internet Penetration Rates

China has the world's largest online population. The size of web surfers reached 338 million by June 30, 2009 (CNNIC, July 2009, p.4). Figure 3 in the next page shows the increasing size of netizens and the Internet penetration rates in China from 2000 to 2009.

Figure 3: Size of Netizens and Internet Penetration Rates in China
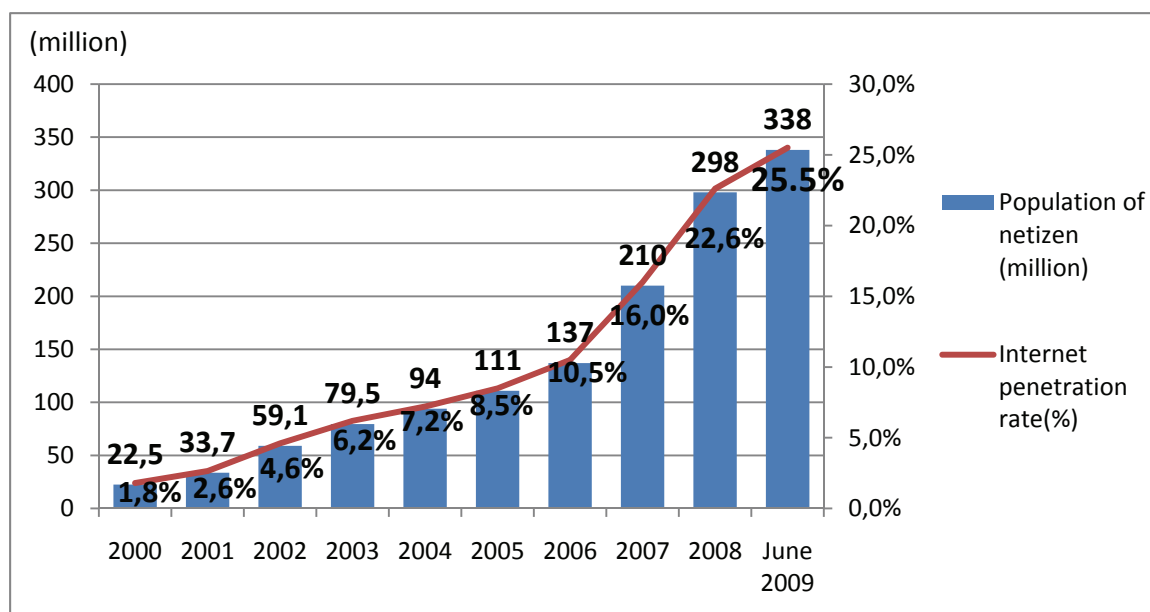
Source: CNNIC, January 2003, pp.35-36,p.38; CNNIC, January 2004, p.38, p.40; CNNIC, January 2005, p.44; CNNIC, January 2009a, p.12; CNNIC, July 2009, p.11; National bureau of statistics of China 2002

The accelerated growth of netizens can be contributed to the elements below:

- Growing disposable income

The rapid economic development raises the level of dispensable income. This has led to an increasing share of expenditures on information and communication products and services relative to the spending on daily necessities. This change in spending patterns has enhanced the adoption of Internet. Moreover, the economic crisis brings a large amount of unemployed workforce from industrial cities back to rural villages of origin. As those jobless return to rural regions, they disseminate knowledge of Internet and Internet usage behavior via their social network and personal contacts (CNNIC, July 2009, p.12) .

- Increasing availability of affordable offers

Increasing level of competitions between telecom carriers and activities of merging and acquisition among Internet service providers enhance the quality level of both software and hardware. The competition makes Internet connection more affordable. Mobile phones will become a more convenient device for Internet connection as 3G gains more prevalence. These factors lower the barrier to Internet use among populations (CNNIC, July 2009, pp.11-12).

- Governmental supports and investments

The governmental policies have contributed to the rising Internet penetration rate. The Chinese government promotes Internet development mainly through the Eleventh Five-Year Plan and the 2006-2020 National Informatization Development Strategy. These policies include investment in infrastructures for more prevalent Internet connections (CNNIC, July 2009, p.11). The project of rural informationalization was launched to establish phones and Internet access in every village by 2010. With the aims to urbanize countryside and bridge the gap between cities and villages, improving telecommunications infrastructures and providing online access to rural populations are regarded as priorities (CNNIC, January 2009a, pp.11-12).

2.2.2. World Internet Penetration Rates

The Internet penetration rate in China reached 25.5%, which has exceeded the world average rate of 24.7%. Figure 4 below illustrates the Internet penetration rate in major countries.

Figure 4: World Internet Penetration Rates, 2009
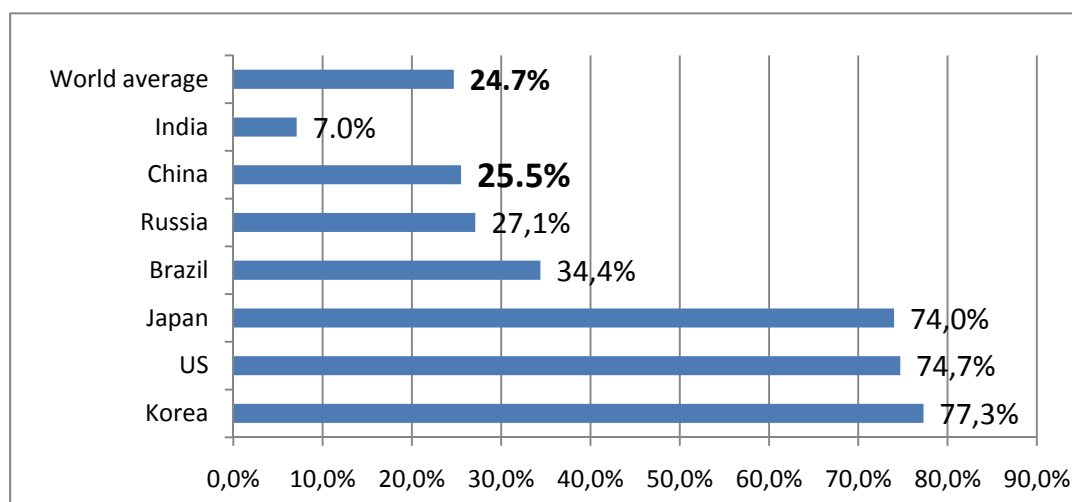
Source: CNNIC, July 2009, p.12, Internet World Stats 2009a, Internet World Stats 2009b.

2.2.3. Methods of Internet Access

- Broadband

Broadband Internet access has been used by 94.3% of Chinese netizens, which is equivalent to 320 million, by June 2009 (CNNIC, July 2009, p.12). Though broadband Internet access gains a wide popularity in China, download speed remains less than 4 Mbit/s, lower than the average of OECD major countries, which is 17.4 Mbit/s, and far behind that in Japan and in Korea, where the download speeds reach 90 Mbit/s and 80 Mbit/s respectively

(CNNIC, July 2009, p.13; Wang July 28, 2009). Because broadband width is shared, the data transfer rate further slows down during peak hours. The country still has a great deal of catching up to provide high-speed Internet service (CNNIC, July 2009, p.13). Figure 5 below shows the comparison of download speeds in major OECD countries.

Figure 5: Download Speeds in Major OECD Countries
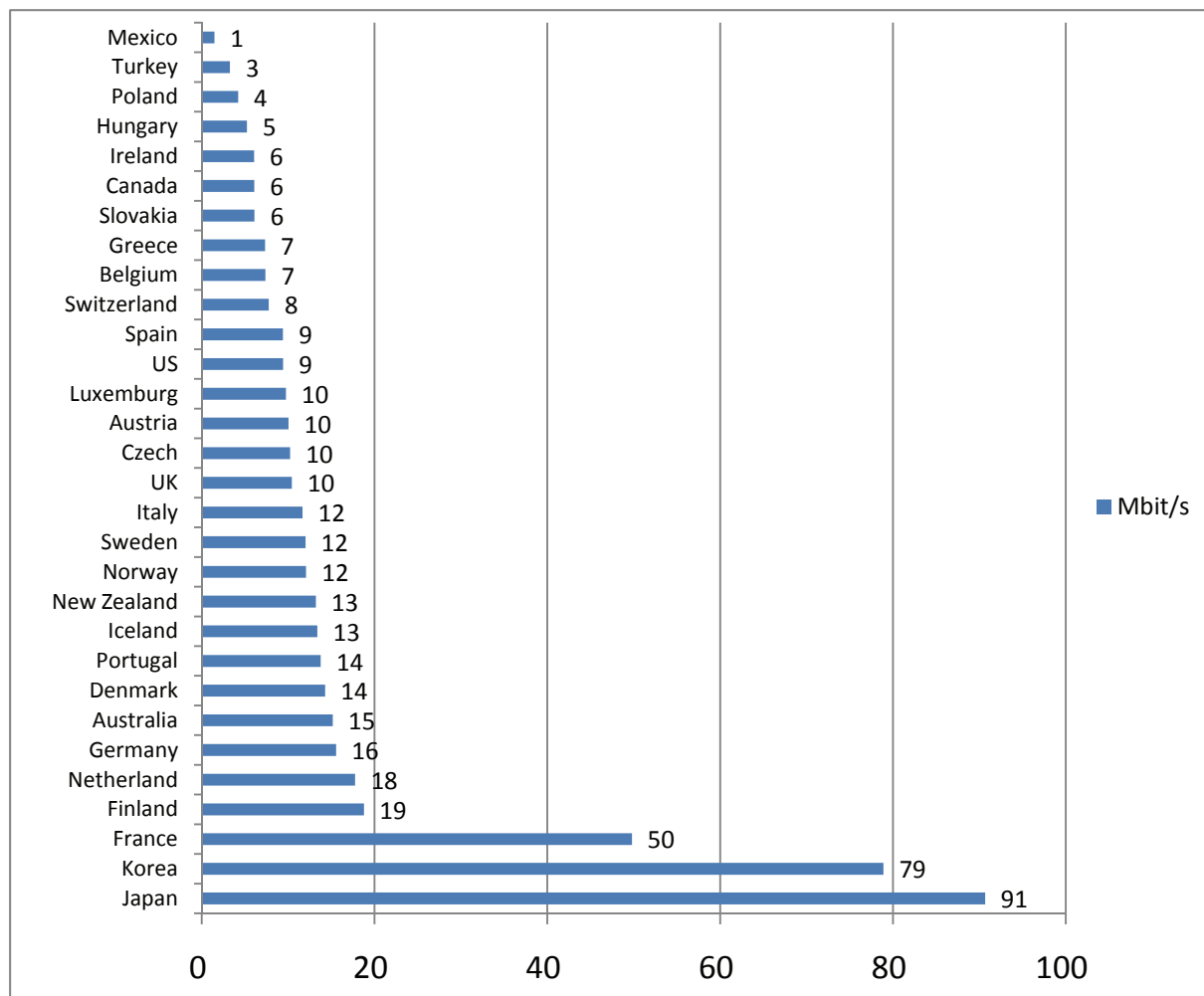
Source: CNNIC, July 2009, p.14

- Mobile Internet

The number of netizens who are connected to the Internet via mobile phones reached 155 million (CNNIC, July 2009, pp.14-15). The usage rate of mobile Internet is related to the reduced monthly tariffs and the increasing applications developed for mobile Internet. The most used mobile Internet applications are entertainment-oriented, such as online music, television and blogs. Online music has 6.6 million active users. Meanwhile, the use of mobile commerce has not been widely penetrated but is also fast growing. In particular, the application of mobile WAP email has 4.8 million of active users (CNNIC,

January 2009b, p.5). The security of payment system and the number of mobile applications play important roles in the adoption of mobile commerce (IResearch, August 5, 2009).

Users of mobile Internet and traditional Internet access overlap to a high degree. 94.5% of mobile Internet users use also PC for Internet access. Users use both channels for the same online applications. These two channels are complements for each other (CNNIC, January 2009b, p.6).

2.3. Demographic Structure of Netizens

2.3.1 Gender

By June 2009 the gender distribution of male and female netizens is 53% versus 47% (CNNIC, July 2009, p.16). As Internet penetrates more widely, the gender structure of netizen has become more balanced (CNNIC, January 2009a, p.18). This means the male and female ratio among netizens will become more similar to Chinese citizens' gender ratio, which is 51.5% and 48.5% in the year 2007 (National bureau of statistics of China 2008). The proportion of female netizens increased rapidly from 30.4% in 2000 to 47% in June 2009. Figure 6 below shows netizens' gender distribution from 2000 to 2009.

Figure 6: Netizens' Gender Distribution
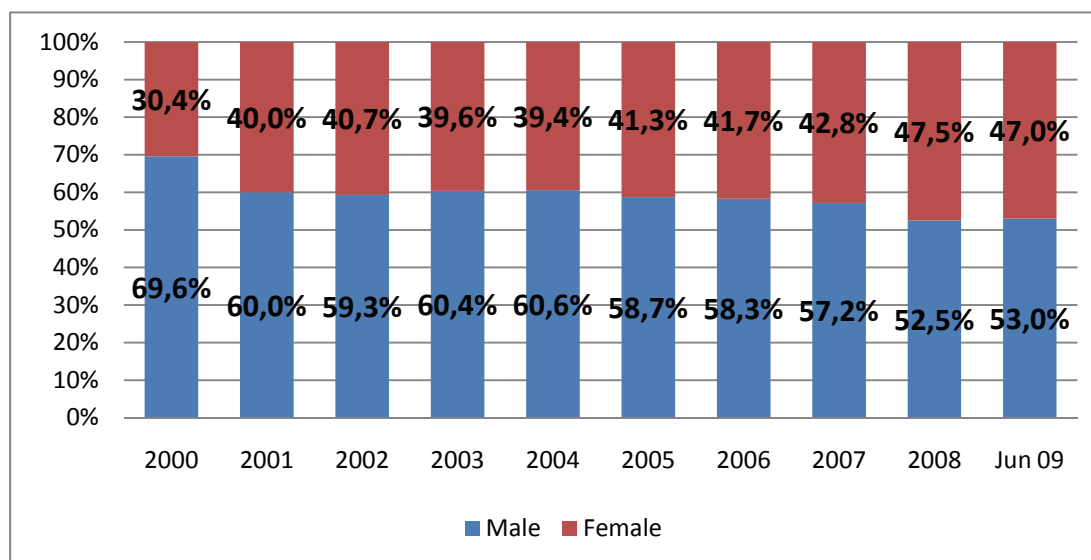
Source: CNNIC, January 2007, p.45; CNNIC, January 2009a, p.18; CNNIC, July 2009, p.16

2.3.2 Age

Chinese netizens' age structure is concentrated in the young age range,

especially from 10 to 29. The number of netizens aged from 10 to 29 accounts for more than 60% of total netizens (CNNIC, July 2009, p.16). According to IResearch (2009b, p.17), the concentration among young population is because online entertaining applications such as online shopping and socialization tools are more appealing to young generations. Moreover, young adults are relatively more technologically competent which facilitates the adoption of Internet. Figure 7 below shows netizens' age distribution in 2008 and June 2009.

Figure 7: Netizens' Age Distribution
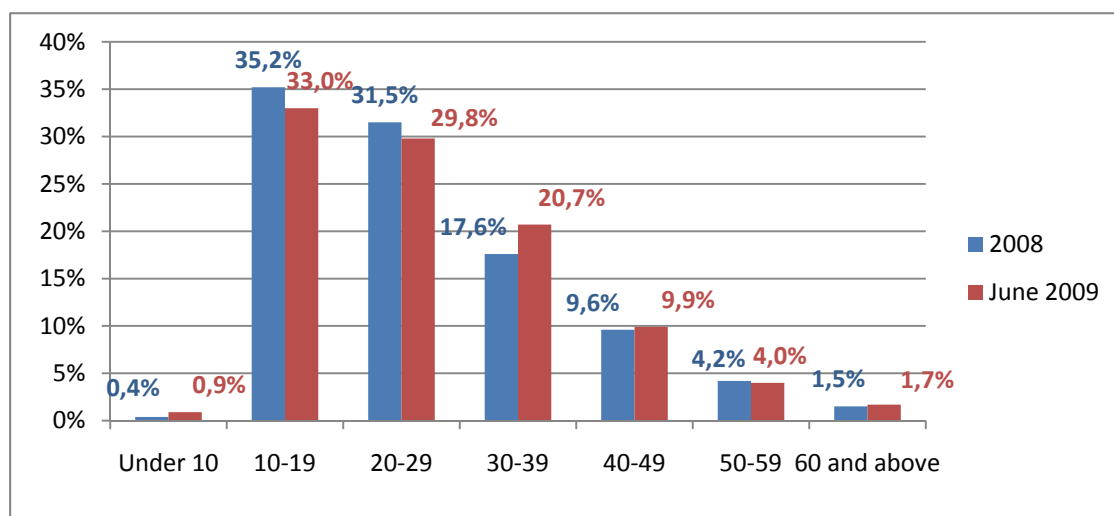
Source: CNNIC, July 2009, p.16

Chinese netizens are largely composed of young populations unlike other markets such as Macao, Hong Kong, Taiwan and Korea. Chinese netizens aged from 15-24 account for 44.5% of total netizen, largely surpassing these four markets mentioned above. Figure 8 in the next page examines the age distribution of netizens in Mainland China, Korea, Taiwan, Hong Kong, and Macao.

Figure 8: Netizens' Age Distribution in China, Korea, Taiwan, Hong Kong, and Macao
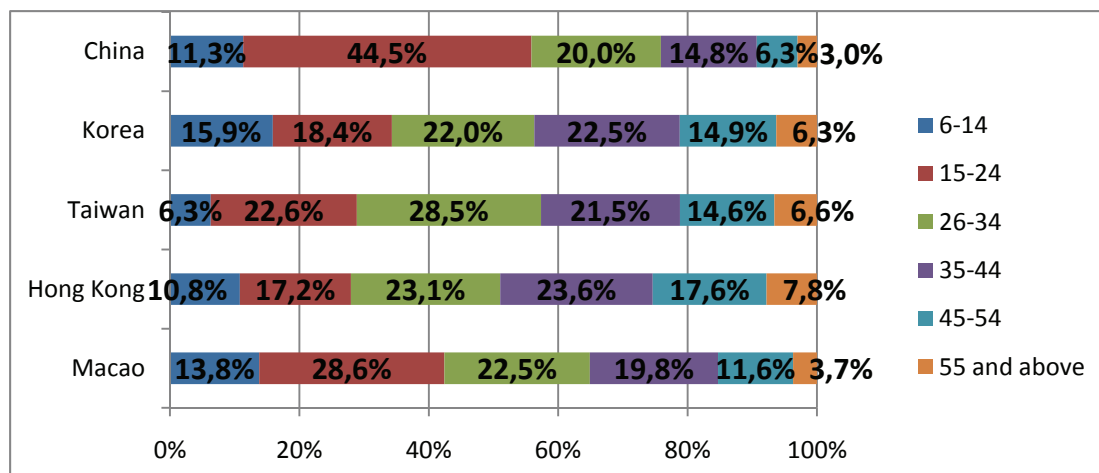
Source: Wang, August 26, 2009

As Figure 9 shows below, the relatively high percentage of young web users group illustrates the concentration of netizen in the young segments. Nevertheless, this concentration appears to decrease. The age group of 18-24 has gradually decreased its importance from 41.2% in 2000 to 31.8% in 2007. As Internet develops more prevalently, netizen's age structure will become more proportionally distributed as the structure of whole population (Wang, August 26, 2009). Figure 9 below shows the netizens' age structure from 2000 to 2007.

Figure 9: Development of Netizens' Age Structure from 2000-2007
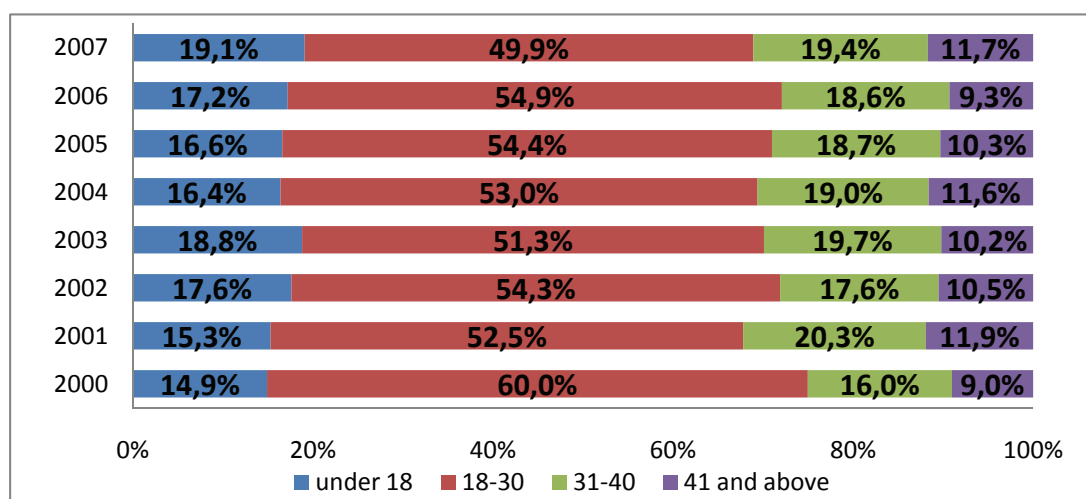
Source: CNNIC, January 2002, p.7; CNNIC, January 2003, p.3, p.9; CNNIC, January 2004, p.11; CNNIC, January 2005, p.12; CNNIC, January 2006, p.14; CNNIC, January 2007, p.11; CNNIC, January 2008, p.17; CNNIC, January 2009a, p.18; CNNIC, July 2009, p.17

2.3.3   Income

More than 70% of netizens have an income level of less than RMB 2000 [USD 292.9] per month. Figure 10 below shows the evolvement of netizens' income level from 2000 to 2009.

Figure 10: Development of Netizens' Income Structure from 2000 to June 2009
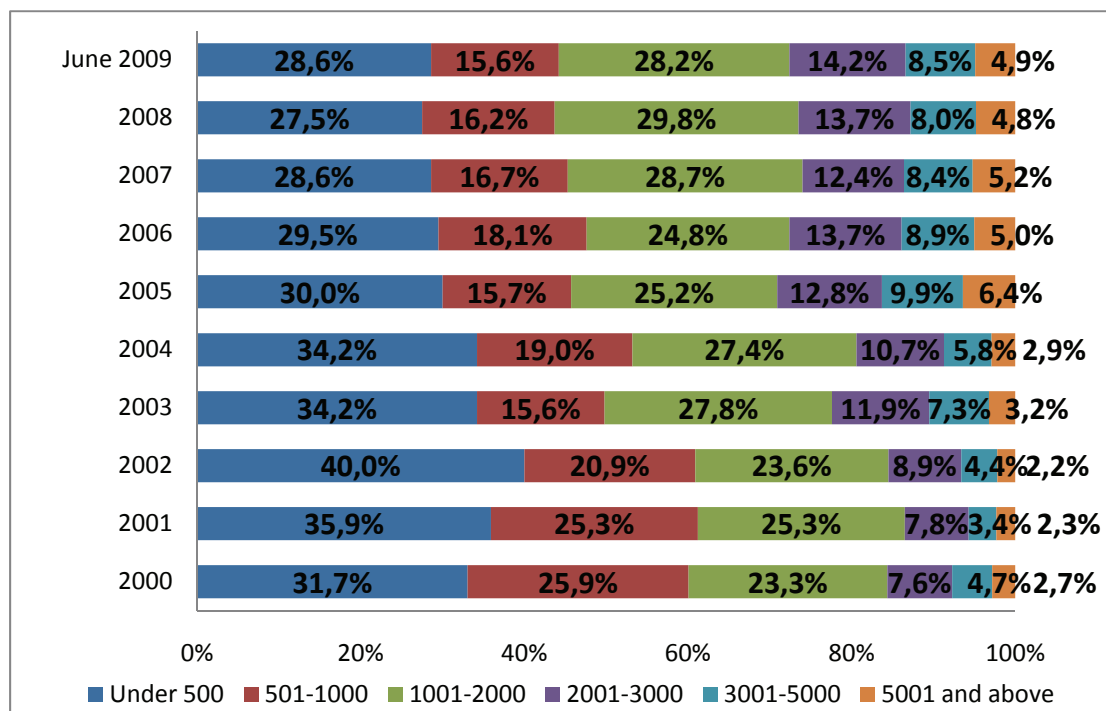
Source: CNNIC, January 2002, p.9; CNNIC, January 2003, p.5, pp.11-12; CNNIC, January 2004, pp.12-13; CNNIC, January 2005, p.14; CNNIC, January 2006, p.17; CNNIC, January 2007, p.13; CNNIC, January 2008, p.20; CNNIC, January 2009a, p.19; CNNIC, July 2009, p.18

2.3.4   Educational Structure

The educational level of netizen develops toward a lower degree of education (IResearch, 2009b, p.17). 74.9% of netizens have the educational level at senior high school or lower in June 2009, increasing from 29.9% in 2000. This development demonstrates that Internet is no longer limited to high education groups as it penetrates more widely. Figure 11 in the next page shows netizens' educational structure from 2000 to 2009.

Figure 11: Netizens' Educational Structure

Year	junior high school and below	senior high school	junior college	bachelor and above
Jun 09	33,9%	41,0%	12,7%	12,4%
2008	33,4%	39,4%	13,9%	13,2%
2007	27,8%	36,0%	18,7%	17,5%
2006	17,1%	31,1%	23,3%	28,5%
2005	16,2%	30,2%	24,4%	29,2%
2004	13,0%	29,3%	27,1%	30,7%
2003	13,5%	29,3%	27,4%	29,8%
2002	12,9%	30,6%	26,1%	30,4%
2001	10,2%	30,0%	26,9%	32,9%
2000	6,4%	23,5%	29,0%	41,1%
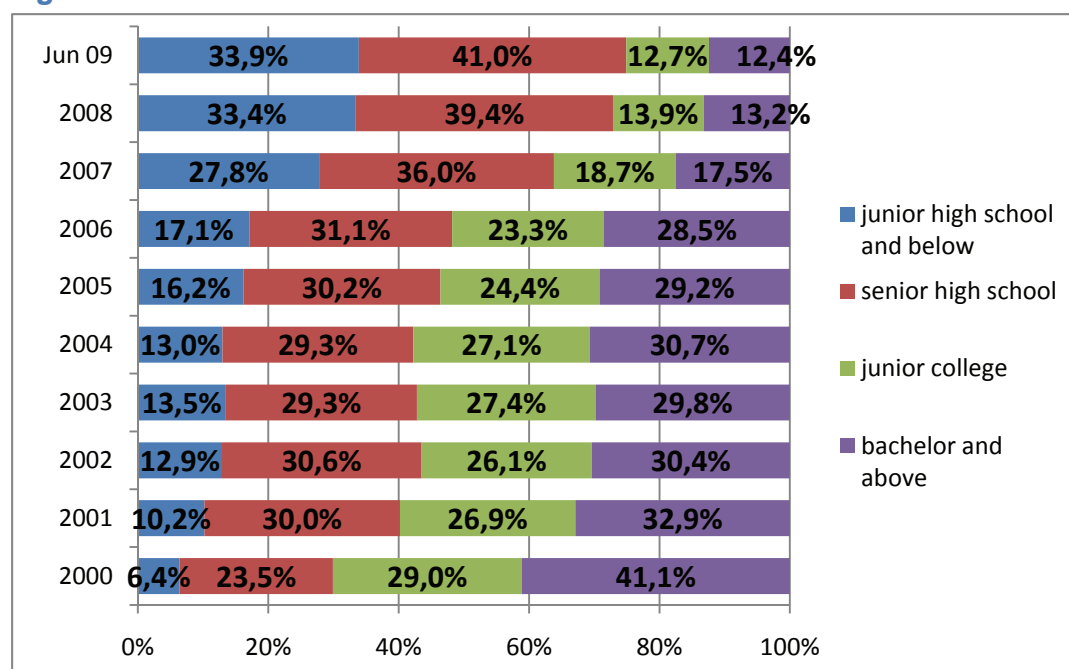
Source: CNNIC, January 2002, p.8; CNNIC, January 2003, p.4, p.10; CNNIC, January 2004, p.12; CNNIC, January 2005, p.13; CNNIC, January 2006, p.15; CNNIC, January 2007, p.12; CNNIC, January 2009a, p.20; CNNIC, July 2009, p.17

2.4. Trends in the Internet Development in China

Internet connection is expected to be more prevalent in China due to continuous improvement in infrastructures, governmental promotion, and increasing mobile access. The continuous economic growth in the following years will lead to a constant increase in GDP per capital. Chinese population will enjoy more dispensable income, which generates more informative and recreational demands. Internet will penetrate more deeply in existing user groups in all aspects of life and become more widely accessible across the country.

2.5. Current Development of the Chinese Online Shopping Market

2.5.1. Market Potential

The number of online buyers reached 87.9 million by June 2009, increasing from 74 million in 2008 and 46 million in 2007. The online shopping penetration rate achieved 24.8% by June 2009, meaning 1 out of 4 netizens has purchased online in the past 6 months (CNNIC, July 2009, p.31; CNNIC, May 2009, p.31). The market value reached RMB 128.2 billion [USD 18.8 billion] in 2008 with a robust growth rate of 128.5% compared to 2007 (IResearch,

2009a, p.14). Figure 12 in the next page shows the sales revenue and the growth rate of online shopping market from 2007 to 2012.

Figure 12: Value of Transactions and the Market Growth Rates in the Chinese Online Shopping Market
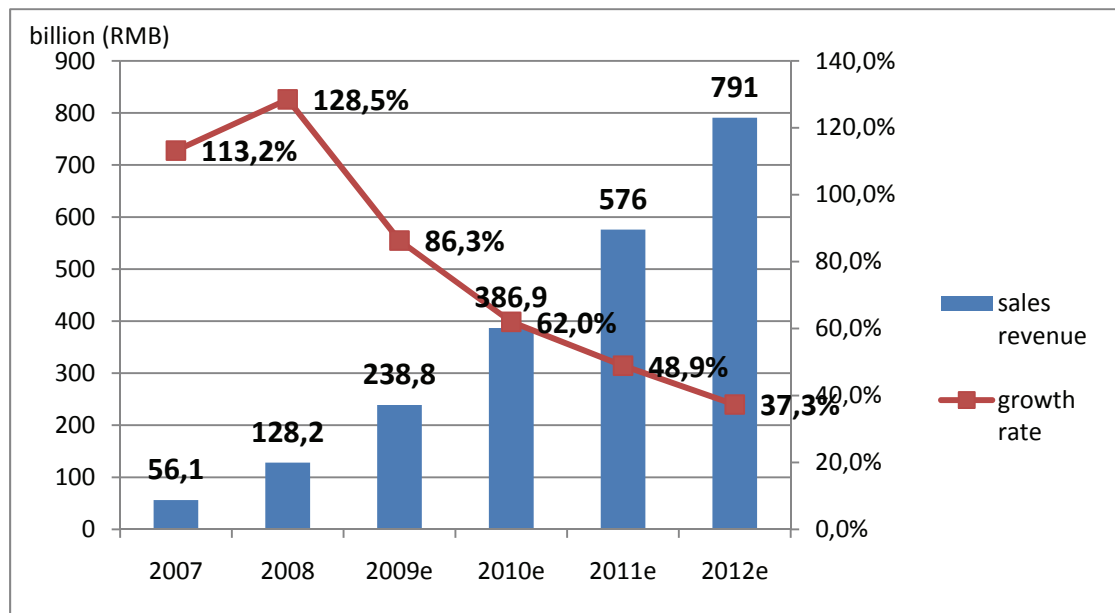
Source: IResearch, 2009a, p.14

Online sales accounted for 1.2% of retail sales in 2008 as Figure 13 shown below. Relative to the US where online sales accounted for 6% of retailing sales in 2008, Chinese online shopping market still has a large room to grow in the future (IResearch, 2009a, p.16).

Figure 13: Percentage of the Online Retail Sales in the Total Retail Sales in the Chinese Market
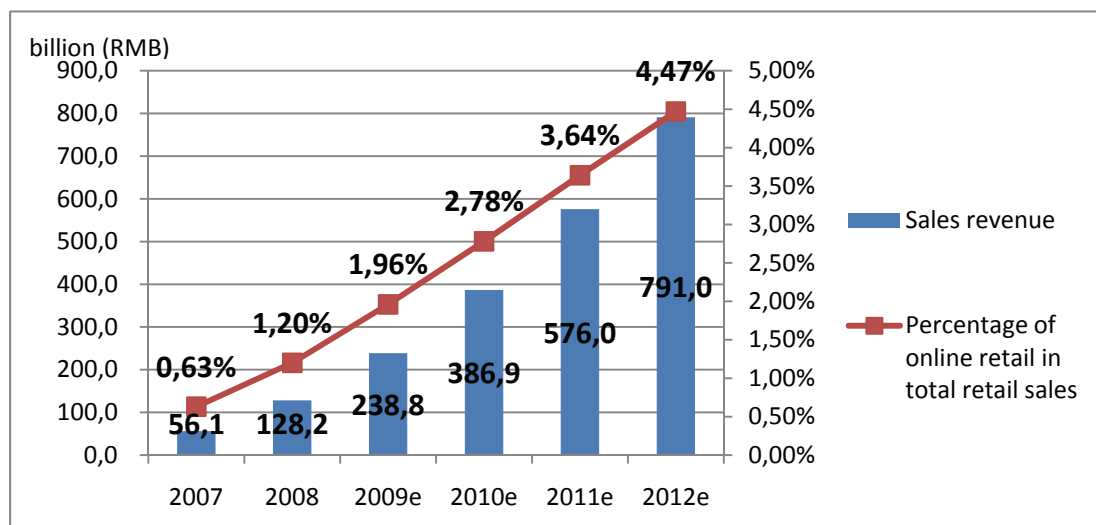
Source: IResearch 2009a, p.17

Chinese online shopping market is largely composed of the sales in C2C marketplace, covering 93.2% of total online sales in 2008. Online B2C sales accounts for 6.8% of total online sales in 2008 and has been increased rapidly. Online B2C sales doubled in 2008 compared to 2007. As more enterprises start to enter into the online B2C market, the sales is expected to expand further (IResearch 2009a, p.19). Figure 14 below shows the composition of online shopping sales of B2C and C2C sectors.

Figure 14: Value of Transactions in the Chinese Online B2C and C2C Market
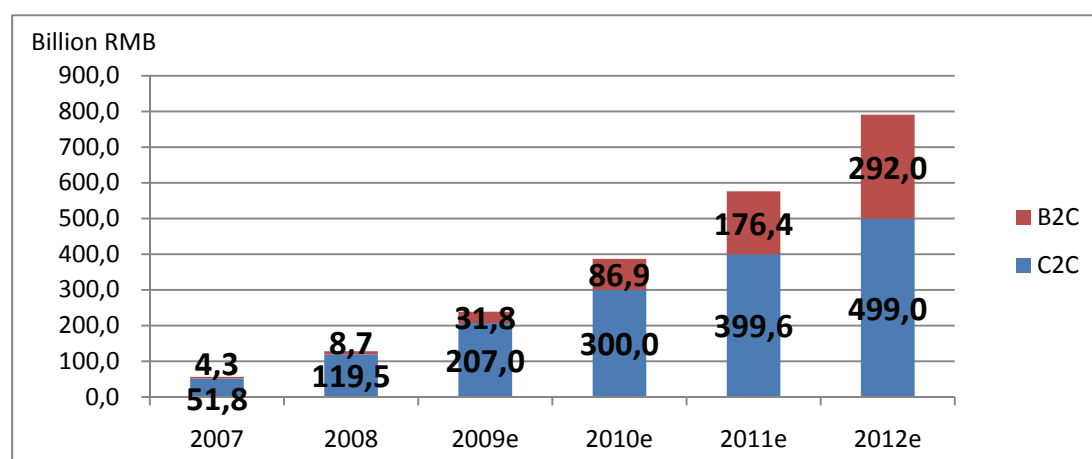
Source: IResearch 2009a, p.19

In 2008, the purchasing amount per person achieved RMB 1,600 [USD 234.3], with an increase of RMB 582 [USD 85.2] compared to the year 2007 (IResearch, February 12, 2009). Figure 15 below shows the constant growing spending of online customers from 2003 to 2008.

Figure 15: Average Online Purchasing Amounts per User per Year
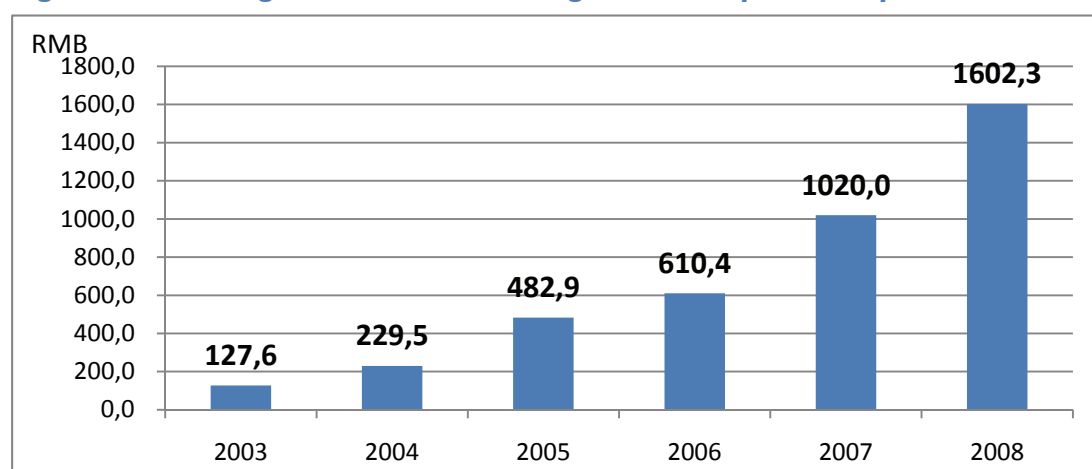
Source: IResearch, February 12, 2009

2.5.2.   Best Selling Product Categories

The most popular products sold online are fashionable goods, books, audio and video products. The combined sales of apparels, fashionable accessories, footwear and cosmetics reached RMB 27.46 billion [USD 4 billion] in 2008, with a 136.8% growth compared to 2007. This product segment accounted for 21.4% of the total online sales in 2008 (IResearch, March 13, 2009). Table 1 below ranks the best sold items over Internet.

Table 1: Ranking of Best Sold Items over Internet, 2008

	Items	Purchased by % of Online Buyers
1	Apparel, accessories and footwear	57.1%
2	Books, CDs and DVDs	46.0%
3	Cosmetics	40.6%
4	Electronics (Cameras, MP3)	35.4%
5	Rechargeable cards for games and cell phones	32.1%
6	Home decorations	29.2%
7	Cell phones and electronic accessories	27.4%
8	Gifts and toys	24.7%
9	Computer, laptops and hardware	23.0%
10	Home appliances	22.1%
11	Jewelries, watches, accessories, glasses	20.3%
12	Foods	19.7%
13	Maternity and baby products	11.5%
14	White goods (fridges, washing machines, air conditionings)	2.9%
15	Others	2.0%

Source: IResearch, March 13, 2009

Fashion products top the online shopping can be explained by three reasons. First, online channels provide many cost advantages in offering wide collections in this fast moving industry. Compared to physical stores, online stores are not confined to limited shelf space. Changing customer requirements and short product life cycles can be addressed rapidly. Second, fashionable products are mainly high value-to-weight without major difficulties in delivery concerning product defect during transport and expiration dates. Third, the market demand for apparels is inherently strong. This industry occupies a substantial share in the offline retailing business, ranking at the second place after food products with RMB 2,400 billion sales revenue in 2006 (CNNIC, June 2008, p.30).

According to IResearch (2009b, p.24), high standardized products, like books and CDs, have been one of the most sold products online. As online customers gain more experience with online transactions and its convenience, online purchases will not be limited to standardized products, but will contain a broader product range for personalized needs.

2.6. Online Buyer Analysis

2.6.1. Gender

The ratio of male and female buyers is 45.6% and 54.4% in 2008 (IResearch 2009a, p.84). Figure 16 below compares the gender composition among netizens and the online shopping customers in 2008.

Figure 16: Netizens and Online Customers' Gender Distribution, 2008
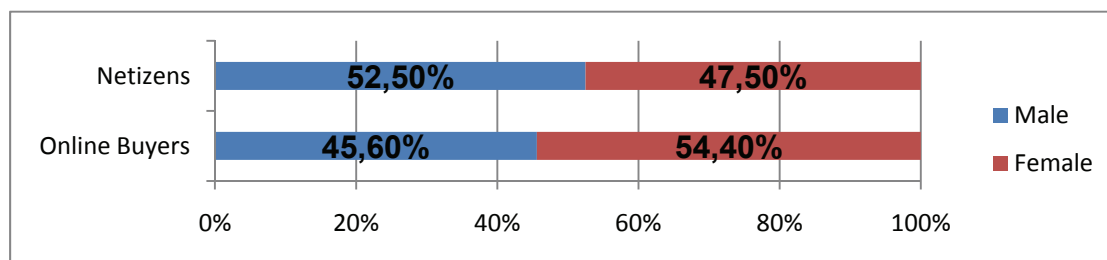
Source: IResearch 2009a, p.84

2.6.2. Age

Major online shopping buyers are aged from 18 to 30, accounting for more than 57.4% of total online customers (IResearch 2009a, p.84). According to IResearch (2009a, p.84) and CNNIC (January 2009a, p.18), 69.5% of online customers and 67.1% of netizens are aged less than 30 in 2008. Figure 17 below shows the age structure of online shopping customers.

Figure 17: Online Customers' Age Distribution, 2008
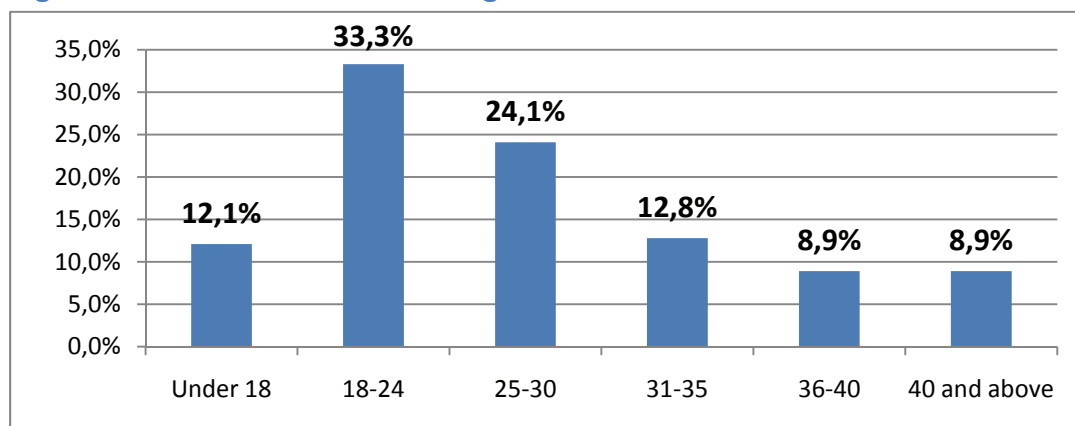
Source: IResearch 2009a, p.84

2.6.3.   Income

The average income of online customers is higher than that of netizens. Compare netizens' income level with that of online shoppers, 27.6% of netizens and 51.1% of online customers have the salary over RMB 2,000 [USD 292.9] respectively (CNNIC, July 2009, p.19, CNNIC, June 2008, pp.44-45). Table 2 below shows the income per month of online customers in June 2008

Table 2: Monthly Incomes of Online Customers, June 2008

	Monthly income of online buyers
No income	6.8%
Under 500	6.6%
501-1000	18.0%
1001-2000	17.6%
2001-3000	17.0%
3001-5000	17.9%
5001-8000	8.6%
8001-10000	2.7%
Above 10000	4.9%
Total	100.0%

51.1%

Source: CNNIC, June 2008, p.51

Income level has a positive influence toward online purchasing amounts. The higher the income level, the more purchasing amounts. As Figure 18 indicates in the next page, 25.4% of online buyers whose monthly income exceeded RMB 5,000 [USD 732.3] spent more than RMB 5,000 online in the whole year 2008. In contrast, 59% of online buyers with income less than RMB 1,000 [USD 146.5] purchased less than RMB 1,000 online in 2008. This is because high income customers have far less time and higher opportunity costs for offline shopping. Online shopping provide time saving benefits for their purchasing needs (IResearch 2009b, p.31).

Figure 18: Online Buyers' Yearly Purchasing Amounts by Income, 2008
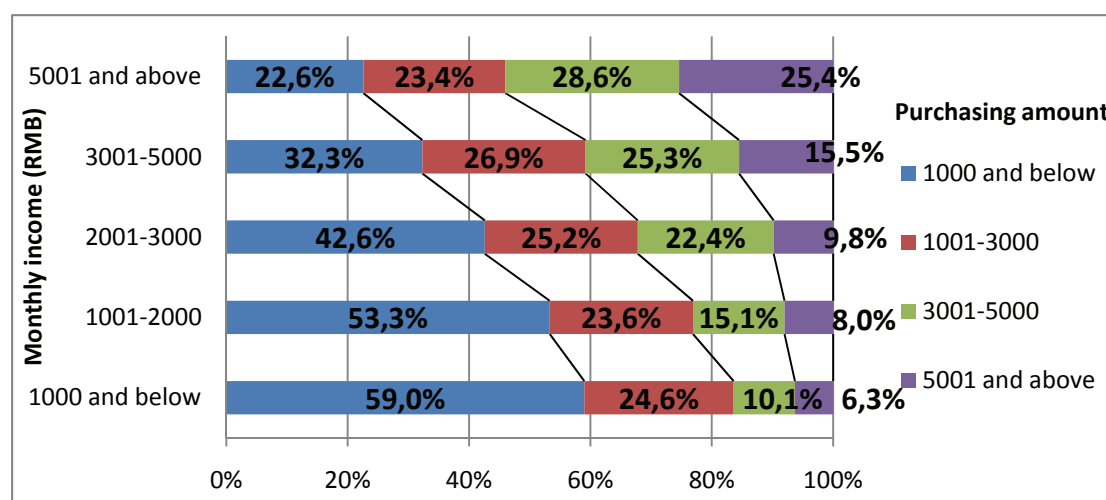
Source: IResearch 2009b, p.31

Income level of online customers differs by regions. The online customers in Shanghai have higher income level than the customers in other sub-provincial cities. Table 3 below shows online customers' income structure by cities.

Table 3: Online Customers' Income Structure by Cities, June 2008

	Under 500	501-2000	2001-5000	Above 5000	Total
Beijing	11.2%	28.2%	42.7%	17.9%	100%
Shanghai	10.7%	25.5%	38.1%	25.8%	100%
Guangzhou	13.5%	29.2%	37.5%	19.8%	100%
Other sub-provincial cities	14.7%	42.4%	31.1%	11.8%	100%

Source: CNNIC, June 2008, p.51

2.6.4. Educational Structure

Online buyers have average higher educational level compared to netizens. In June 2008, 84.9% of online customers have the educational level of junior college or above. Among netizens, only 36.2% have the educational degree of junior college and above in June 2008 (CNNIC, June 2008, p.48). Table 4 in the next page shows the educational level of online buyers.

Table 4: Online Customers' Educational Level, June 2008

	% of online buyers
Junior high school and below	3.6%
Senior high school	11.5%
Junior college	25.4%
Bachelor	50.3%
Master and above	9.2%
Total	100.0%

84.9%

Source: CNNIC, June 2008, p.48

2.6.5.   Length of Prior Internet Experience

Netizens who have been using Internet for a longer period of time have more opportunities to experience online applications more frequently and have more tendencies to become online customers. According to IResearch (2009b, p.16), 2 to 3 years are generally required for Internet beginners to understand online shopping and become online customers. Afterwards, new online buyers will be converted into either active online customers with repeat purchases, less involved buyers or buyers who discontinue subsequent purchases. As Table 5 below shows, more than 80% of online shopping customers have used Internet for more than 5 years. This indicates that the number of online customers is expected to increase as more new Internet users become more familiar with Internet and other online applications (CNNIC, June 2008, p.47).

Table 5: Length of Prior Internet Experience among Online Customers in Different Cities

	2003 and before	2004	2005	2006	2007	2008	Total
Beijing	**84.5%**	5.5%	3.5%	3.8%	2.0%	0.8%	100%
Shanghai	**84.0%**	7.0%	4.0%	1.5%	2.0%	1.5%	100%
Guangzhou	**82.5%**	5.8%	5.8%	2.5%	3.5%	0.0%	100%
Other sub-provincial cities	**81.6%**	7.6%	4.4%	2.9%	3.2%	0.2%	100%

Source: CNNIC, June 2008, p.47

2.6.6.   Region

Online customers are concentrated in top tier cities[1] including municipalities and sub-provincial cities. In 2008, the online customers in Beijing, Shanghai

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[1] Due to the lack of a unified definition on tiers of cities, the administrative divisions defined by Ministry of Civil Affairs of the PRC will be applied here. First tier cities refer to municipalities and sub-provincial cities. Second tier cities refer to prefecture-level cities.

and Guangzhou accounted for 28.8% of total online buyers. The customers in these three cities alone covered 33.1% of total online shopping sales. According to IResearch, the penetration rate of online shopping in Shanghai and Beijing reached 67.2% and 65.3% respectively (IResearch 2009a, p.26). Table 6 below exhibits the detailed penetration rates in each region.

Table 6: Online Customers' Scale and Penetration Rates by Region, 2008

Region	Number of Online Customers (million)	Number of Netizens (million)	Online Shopping Penetration Rate*
Whole China	87.88	338.00	26.8%
Shanghai	7.46	11.10	**67.2%**
Beijing	6.40	9.80	**65.3%**
Guangdong	**9.18**	**45.54**	20.1%
Zhejiang	7.29	21.08	34.6%
Jiangsu	7.06	20.84	33.9%
Shandong	4.10	19.83	20.7%
Hubei	3.15	10.50	30.0%
Sichuan	3.15	11.03	28.5%
Fujian	3.08	13.79	22.4%
Hunan	2.52	9.99	25.2%
*Online shopping penetration rate in this section is defined as online customers who have purchased online within the whole year 2008			

Source: IResearch 2009a, pp.26-27; CNNIC, July 2009, p.11, p.32

In this section, a different methodology is used to define the penetration rate of online shopping. The online shopping penetration here is calculated by the number of customers who have purchased online within the whole year 2008 divided by the number of netizens within the region. This is different from the definition of CNNIC where the online shopping penetration rate refers to the proportion of customers who have online purchase experience within 6 months rather than within a whole year.

Compared with the country-wide penetration rate of online shopping 26.8%, the penetration rate in Zhejiang, Jiangsu, relatively wealthy provinces of Yangtze River delta, achieved more than 30%. The penetration rates in Hubei and Sichuan also surpassed the country's average. In terms of online sales

value, Zhejiang, Jiangsu, Shandong, Fujian, Sichuan, Liaoning and Hubei have increased their importance within the country and demonstrate their growth potentials (IResearch 2009a, pp.26-27). Figure 19 below shows the online sales by region in 2008.

Figure 19: Value of Online Shopping Transactions by Region, 2008
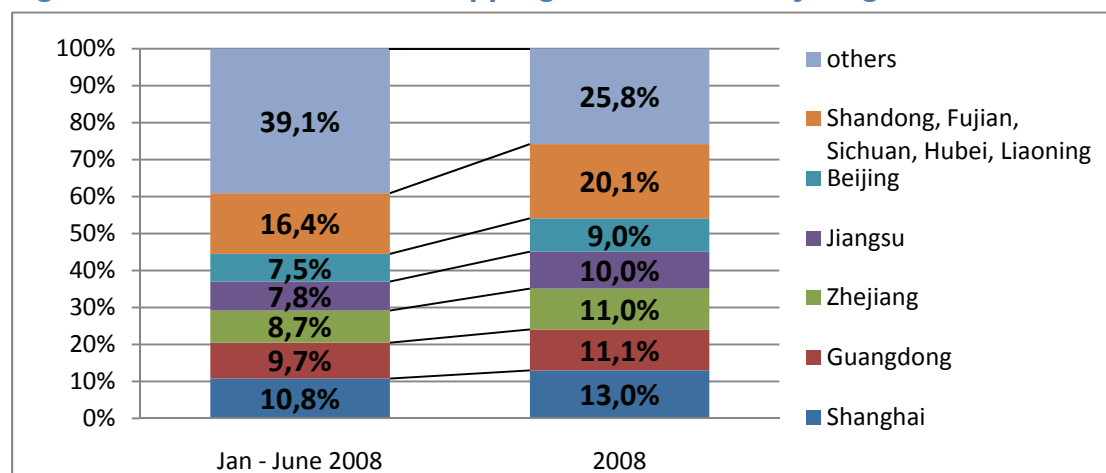
Source: IResearch 2009a, p.27

2.6.7.   Payment Methods

The number of online payment users reached 75.7 million. Among all netizens, the online payment penetration rate reached 22.4%. 86.2% of online buyers have used online payment by June 2009 (CNNIC, July 2009, p.32). Other than online payments, fund transfer can be done via cash on delivery, bank or post transfer. Despite the fact that online payment is prevalent; cash on delivery is still one of the preferred payment methods offered by major online retailers. Table 7 below shows the most used payment tools for online transactions in 2008.

Table 7: Most Used Payments Methods by Online Customers, 2008

	% of Most Used Payment Methods
Online third-party payment platform	50.4%
Online banking	21.4%
Cash on delivery	16.8%
Bank transfer	3.8%
Post transfer	3.1%
Card on delivery	2.3%
Cash and carry	0.9%
Mobile payment	0.7%
Telephonic payment	0.4%

Source: IResearch 2009a, p.100

In terms of online payments, major service providers are Alipay, Tenpay, and UnionPay. These three operators occupying 78.1% of online payment market share (IResearch, July 28, 2009). The rest of market is divided by more than 50 smaller service providers (Shi, June 2009, p.155). Providing services similar to PayPal, Alipay and Tenpay belong to Alibaba and Tencent group respectively. UnionPay is the government-owned online payment system which connects major Chinese banks. Figure 20 below shows the market share of major online payment providers.

Figure 20: Market Share of Online Payment Providers in China, 2008
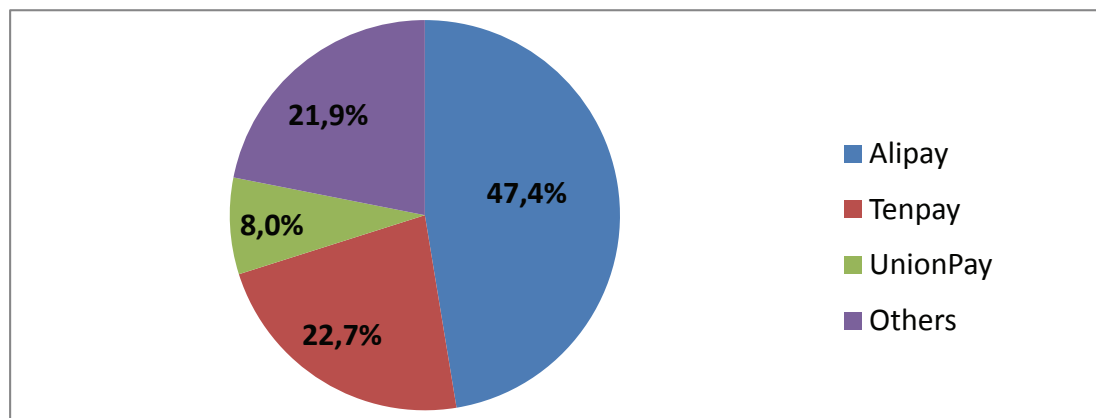
Source: IResearch, July 28, 2009

2.6.8.   Determinants of Online Purchase Decisions

Major factors affecting online purchasing decisions include reputation of sellers, after sales services, other buyers' feedbacks, delivery timing and quality, price, brand recognition, web surfing speed, promotions, advertisements and user interface of websites (IResearch 2009b, p.28).

From customers perspectives, sellers' reputation, other users' feedbacks and after sales services are three underlying factors which determine the level of reliability and security of online purchases. These are areas where online sellers could enhance performance by reducing buyers' perceived risk and gaining trustworthyness from customers (IResearch 2009b, p.23).

As Figure 21 and 22 shown in the next page, male and female online customers express similarities and differences for online shopping decision making. Reputation of sellers is one of the most influential factors for both male and female customers in their online purchase considerations. Other users' feedbacks are regarded as slightly more important for female customers than for males. Male buyers consider more on price and after sales service. According to IResearch (2009b, p.28), the difference are resulted from

psychological reasons and product characteristics. Male customers are more likely to act rationally and seek more measurable hard product information. Products purchased by females tend to be relatively less standardized. In this case, soliciting advice from other users may facilitate decision making (IResearch 2009b, p.28).

Figure 21: Key Influencing Factors on Online Purchasing Decisions of Male Customers, 2008

Source: IResearch 2009b, p.28

Figure 22: Key Influencing Factors on Online Purchasing Decisions of Female Customers, 2008
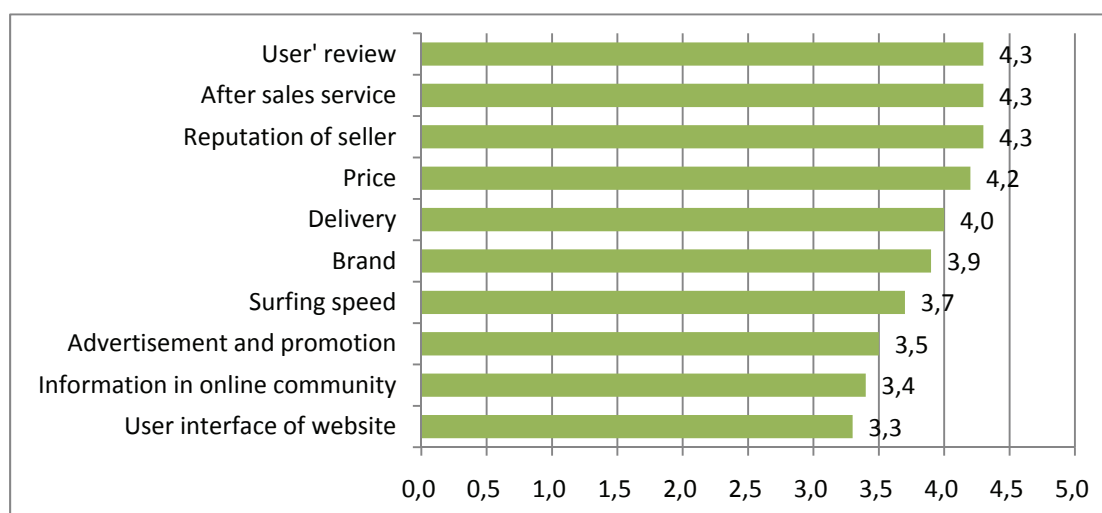
Source: IResearch 2009b, p.28

2.6.9. Information Channels Among Netizens

Among netizens, Internet, friends and families are major sources of information for online shopping websites. These channels have outpaced the

traditional offline advertisements (CNNIC, June 2008, p.29). Figure 23 below shows netizens' information channel to acquire information of online shopping websites.

Figure 23: Netizens' Media Channels for Information of Online Shopping Websites, June 2008
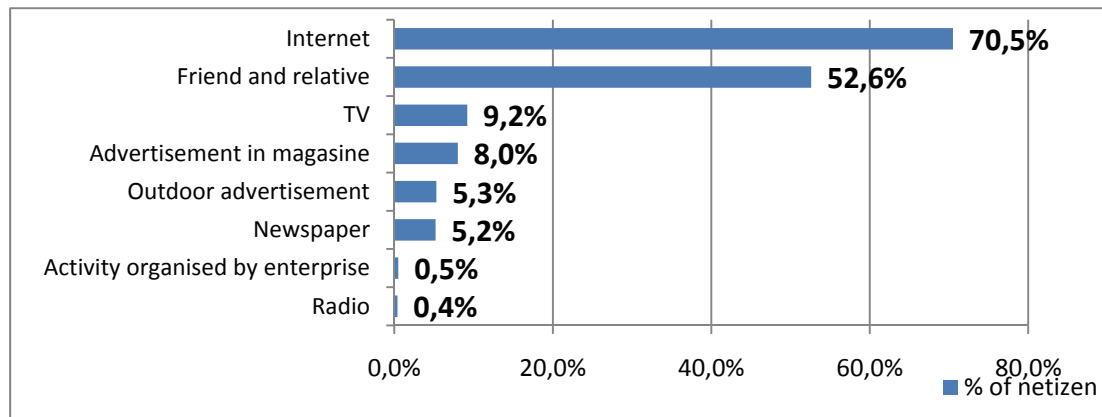
Source: CNNIC, June 2008, p.29

Among online advertising tools, important components are search engines advertisements and links exchange with other websites targeting similar group of audiences (CNNIC, June 2008, p.31). Blogs has gained rising importance as well. 53.8% of the netizens own a blog or a web space. 35.3% of total netizens update their blogs within 6 months (CNNIC, July 2009, p.30).

2.6.10. Future Development of Online Shopping Customers
Changing customer behaviors can cause significant impact on any company's operations and strategies, notably in the dynamic online shopping industry. Some potential changes in Chinese online customers are identified as below:

• Wider and deeper penetration of online shopping

Online shopping will penetrate more widely and deeply in the daily lives. As netizens use Internet for a longer time, shoppers will gain more familiarity toward online technology. More interactions will be generated between customers and online applications (CNNIC, June 2008, p.47). While web browsers become more accustomed to online applications, they will have more opportunities to acquire online shopping information and to be engaged in online purchases.

Though metropolitan cities account for the main part of online shopping sales, the sales contribution from second tier cities has shown a steady increase. The

penetration rates in Beijing and Shanghai will become more saturated in the future as 65.3% and 67.2% of netizen already had online purchase experience in 2008[2]. In the future, second tier cities will provide opportunities for the continuous growth in this market (IResearch 2009a, pp.26-27).

- More focus on convenience and personalized needs

Price has been one major concern for Chinese online shopping customers. Customers purchase online mainly for better prices in the beginning. As online customers gain more knowledge about online shopping, price will not necessarily be the dominant deciding factor anymore. Convenience will become one of the core values, especially for those time-starved white collars and middle class who appreciate efficiency and flexibility in their tight schedules.

Customers will develop more confidence in online shopping and purchase wider product categories online due to the improvements of product varieties and complementary services. Online sellers will learn to understand customers' needs and provide more specialized products and services. Moreover, logistic providers have enhanced their service coverage. Online retailers have also become more skilled in marketing techniques. The enhancing service level will lead to more customer satisfaction and positive growths in the industry.

To sum up, online customers are expected to be more aware of the value and advantages of online shopping in the coming years. More personalized needs and offers will emerge. As online shopping gets more involved in customers' lifestyle, more unique personal styles will arise. Furthermore, as regulations of online shopping market have become more comprehensive, perceived risk of online shopping can be further reduced. This indicates positive outlook to the market growth in the future.

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[2] The online shopping penetration rate mentioned here is defined as the percentage of netizens who purchased online among number of netizens within the whole year 2008

3.   Market Participants in the Online Retailing Market and their Business Models

3.1.   Overview of the Online Retailing Market

In the Chinese online B2C market, Taobao platform is the market leader with 20.2% of market share, followed by 360Buy, Amazon and Dangdang with 16.1%, 12.1% and 11.3% of the market share respectively in 2008. Details of the online retailing market share and the sales revenues of major retailers can be found in Figure 24 and Figure 25 below.

Figure 24: Market Share of Online Retailers in China, 2008
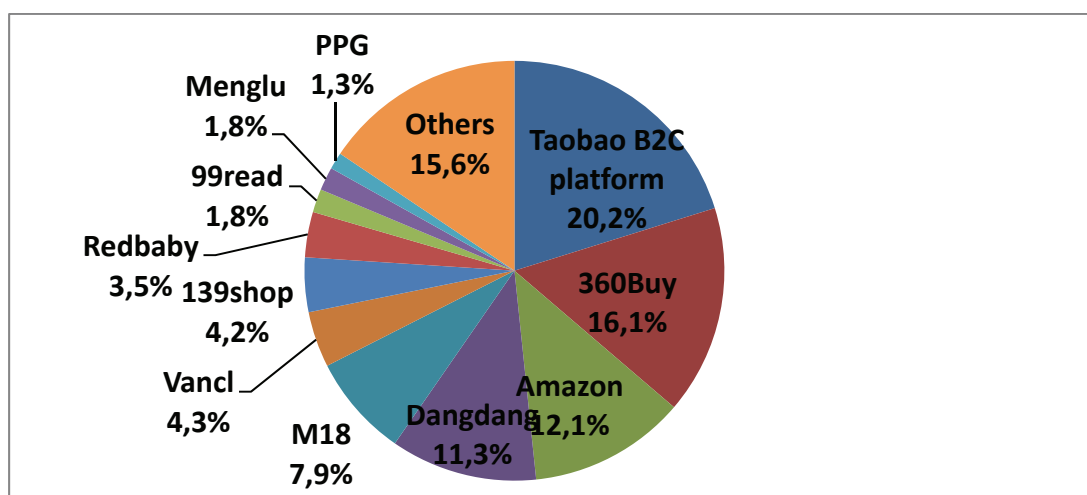
Source: IResearch 2009a, p.35

Figure 25: Value of Transactions of Major Online Retailers, 2008
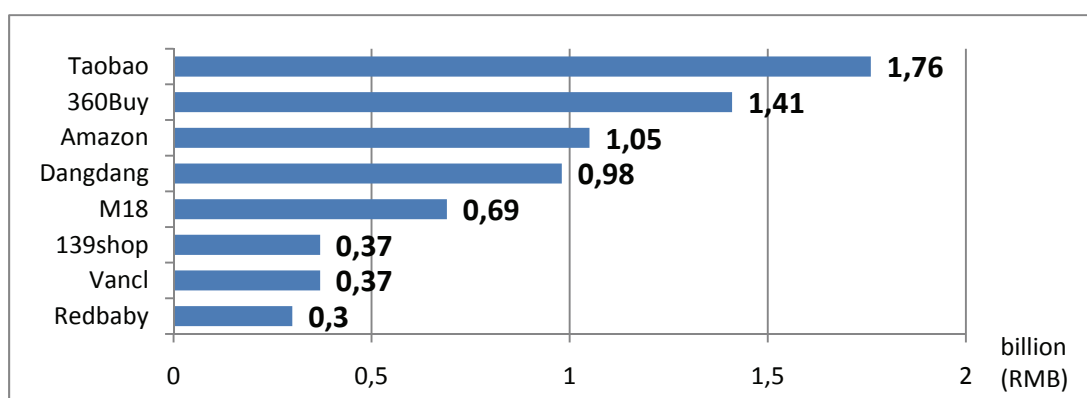
Source: IResearch 2009a, p.37

The general characteristics of the Chinese online shopping market are

discussed below.

- High competition intensity in the online retailing market

The online shopping industry is going through a period of fast growth and turbulence with fierce competition. Major players compete to gain a controlling share of the market in all aspects (Analysys International, June 15, 2009). Common promotional activities including price discounts and shipping cost reductions are widely used to gain customers. As one online shopping mall takes initiatives on sales promotion, competing firms follow very shortly (Economic Observer, August 16, 2009). Automatic price comparison system is adopted by top players to offer best prices among competitors and modify automatically online price to a comparable level if rivalry companies' reduce their prices. Due to the intense price competition, online buyers are swayed by lower prices with relatively low brand loyalty (Economic Observer, August 16, 2009)

One difference between offline and online shopping is that physical supermarket in the neighborhood without price advantages or product differentiation can still survive by its convenience. However, online retailers are easily neglected if product distinction or further values are not provided. Moreover, purchasing online involves less opportunity costs relative to offline shopping because price comparison between several online malls can be realized within a second (Liu, May 15, 2009). This aggravates the price competition and lead to squeezed profits in the market.

Online retailers compete with all means for winner-takes-all markets in the long run (Economic Observer, August 16, 2009). Most large scaled online B2C retailers still struggle to become profitable due to lack of scale economies; therefore, inability to achieved reduced costs per unit (Analysys International, June 15, 2009). Meanwhile, new comers backed by venture capitalists enter this market to a great extend. A number of young established specialist retailers emerge by offering specific product categories, like online specialists in food, clothes, and shoes (IResearch, April 28, 2009).

- Wholly-owned logistic service

To increase customers' online shopping experience, major large online retailers, like 360Buy and Amazon invest in their own logistics systems. Different from other online business operations in developed markets, online retailers in China are not purely electronic companies dealing with information flow but bear more responsibilities in complementary services. In Chinese

market, there are two major reasons that several online retailers handle logistics in house. First, delivery time and shipping quality have been obstacles undermining the online shopping development, especially in rural areas. Local logistic providers' service level cannot be guaranteed at a high standard. Controlling logistic partners' delivery timing and service level on each transaction requires substantial monitoring and is difficult to fully achieve. Second, because international logistic providers' services are too pricy for online business where price counts the most, wholly-owned delivery teams are set up to support wider coverage at speedy delivery. Both online retailers and customers are able to monitor the delivery progress. In the perspective of customers, high quality dispatches lower perceived risk and encourage online purchases. It also signifies that online retailers bear huge investments and are in a high stake battle.

- Critical inventory management

Major online retailers satisfy wide market segmentations by extending to millions of items in an attempt to stay ahead of competitors. Most large players develop toward online shopping malls, like Dangdang and Amazon. The cost of increasing items sold for online stores is much lower than in physical stores because online space is unlimited. However, inventory level is bounded by warehouse sizing and financial fluidity. To well manage extensive stocks, online retailers focus on increasing turnover rates. Stock is usually kept at a low level to minimize inventory costs. Major online retailers work with frequent on-time deliveries with small lot size. Accurate sales forecasts are in strict control to anticipate precise demands and avoid stock-out. For example, Amazon and 360Buy all have strictly accurate sales forecasts. Amazon has its automatic ordering systems to process orders and forecast order quantity. Unsold goods for one to four months stored in retailers' warehouses will be returned to suppliers, depending on different online retailers. The way to manage stocks efficiently and effectively becomes a top issue for all big players.

3.2.   Major Retailers in the Online Shopping Market

3.2.1. Company Overview

- Taobao

Taobao is the largest online shopping marketplace in China. It operates under the same business model as EBay, providing an online marketplace, payment solutions and technological infrastructures to match buyers and sellers (EBay 2008, p.1). Created by the parent Alibaba group as a C2C online retailing

platform in 2003, Taobao controlled 82.2% of online C2C market share in 2008 (IResearch 2009a, p.28). In 2006, the company had set up its B2C platform catered to business sellers. The new platform was released in April 2008 to enrich its product and services offers (Market Intelligence and Consulting Institute, May 2009, p.5).

Combining the C2C marketplace with the B2C platform, Taobao online platform allows buyers to surf from C2C bazaars to B2C branded stores. The large user base on C2C marketplace can be guided to B2C stores. B2C online store in turn attracts additional consumers who have needs for quality branded goods. The number of registered online stores on B2C platform reached 7,000 in August 2009. International brands such as P&G, Motorola, Adidas, and Lenovo are all participants. The number of registered stores expects to reach 10,000 stores by the end of 2009.

- 360buy

Established in 1998, 360Buy is the largest online retailer for consumer electronics in China, focus on price quality. The company has gradually enhanced its positioning as an online department store, with widened product ranges since 2008. (Le, June 8, 2009).

- Amazon and Dangdang

In 2004, Amazon entered the Chinese online shopping market by acquiring Joyo, a Chinese local online retailer established in 2000. China is the market where the 7th website of Amazon.com is launched and is Amazon's first establishment among emerging markets (Market Intelligence and Consulting Institute, May 2009, p.18). Amazon aims to provide wide variety of products at best price and provide a convenient online shopping experience (Amazon 2009).

Being Amazon's top competitor in China, the local player Dangdang started its business by selling books, audio video products in 1999. The company extends the product offers to home appliances, decorations and cosmetics (Dangdang 2009b). The company attempts to develop toward an online mall with wide-ranging brands to satisfy all needs (CNET, July 29, 2008). Table 8 in the next page shows the product and services of 360Buy, Dangdang and Amazon.

Table 8: Comparison of Products and Services of 360Buy, Dangdang and Amazon

	360Buy	Dangdang	Amazon
Main Products	• Electronics • Extend to online shopping mall since 2008	• Books and audio video products • Extend to online shopping mall since 2008[6]	• Books and audio video products • Extend to online shopping mall since 2006 [2]
Market Positioning	• Every day low price • Focus on electronics gradually extend to related product categories	• Every day low price • Wide product categories	• Every day low price • Wide product categories
Price	• Heavy discount compared to physical electronics retailers	• Automatic price comparison with other major online retailers [5]	• Automatic price comparison with other major online retailers [5]
Payment	• Cash on delivery (certain regions) • Credit card • Alipay • Tenpay • 99Bill • IPS • Fund transfer through banks and post • Installment payment, collect by customer[3]	• Cash on delivery (certain regions) • Credit card • Tenpay • 99Bill • Yeepay • Fund transfer through banks and post	• Cash on delivery (to 600 cities) • Credit card • Alipay • PayEase • Fund transfer through banks and post
Refund policy	• 7-Day refund policy • 15-Day replacement	• 7-Day refund policy • 15-Day replacement [4]	• 15-Day refund policy
Additional service offer	• After sales service • Service at home for electronics (not limited to goods purchased from 360Buy) • Warranty extension	• Personalized recommendations of products • Online book preview	• Personalized recommendations of products • Online book preview
Logistics	• Combine the wholly-owned logistic department and third party partners	• Alliance with third party logistic partners [2]	• Combine the wholly-owned logistic service and third party partners[1]
Year of establishment	2004	1999	Jojo established in 2000. Amazon acquired Jojo in 2004.
Major online competitor	Newegg	Amazon	Dangdang

Source: [1]Sun, November 28, 2008; [2]Sun, August 8, 2007; [3]360Buy 2009 [4]Dangdang

3.2.2.   Operating Modes with Major Online Retailers

- Amazon, Dangdang and 360Buy

A common collaboration mode with most online retailers and sellers is similar to consignment, in which manufacturers provide goods to retailers and receive payments until the items are actually sold, usually one month after the sales instead of being paid upfront. The online retailers hold the right to return any unsold product in a given time period or to exchange new items. Different from common cases of consignment, it is the retailers, rather than consignors, who have the decision making on final retail prices.

Before the contract, online retailers evaluate products and order the quantity according to their sales forecasts. Initial ordered quantity depends on both the strength of brands and the pricing strategies. The first order for new stock items are usually on small quantities. In terms of shipments, manufacturers are required to deliver goods to one of the three Amazon's warehouses in Shanghai, Beijing or Guangzhou. 360Buy's major fulfillment centers locate in Shanghai, Beijing, Guangzhou and Chengdu. Advertising and product promotions can be jointly developed by online retailers and manufacturers.

Upon the sales of consigned products, online retailers charge a percentage of the sale price as their commissions. For example, approximate 6% of the sales revenues are charged by 360Buy and Amazon. It is important to note that the above operating modes and payment terms vary by companies, brands and product types and could be negotiated.

- Taobao
- Payment and logistics collaboration with Taobao

Being a pure online marketplace provider as EBay, Taobao does not have the ownership of any goods sold on its platform. Major operational tasks such as deliveries, payment, marketing activities and customer services belong to sellers' responsibility. Taobao charges 3-7% of the revenue on each transaction, varying according to product categories (Wu, July 20, 2009). In addition, sellers are obliged to give an extra rebate of 0.5% of the selling price to reward the buyers based on Taobao's selling policy.

Regarding the payment mode, Taobao's sister company, Alipay, is the most widely used online payment system created by Alibaba group for Taobao platform (Alipay 2009). Sellers can provide other payment alternatives like

credit cards, bank and post transfer, online banking, cash on delivery to facilitate payments.

Taobao does not offer delivery services but proposes several logistic companies where their service is supervised by Taobao. Logistic companies usually have different delivery networks and service points. Online sellers on Taobao usually cooperate with several logistic partners to fulfill wide coverage. On Taobao platform, delivery costs are normally handled by buyers except special promotions on shipping costs reduction are provided.

For remote areas where no suitable logistic companies can deliver, postal EMS service is widely used. The EMS service cost is higher and delivery time might takes longer in countryside. To prevent misunderstanding between buyers and sellers concerning delivery time, when buyers make the purchases, sellers can view shipping addresses. If sellers do not have cooperative logistic company for a quick delivery, sellers can inform buyers in advance.

- Advertisement on Taobao Platform

Taobao provides paid advertising solutions with customization. The advertising costs range widely depending on sellers' budgets, desired goals and existing brand familiarity among customers. Some companies purchase specific locations of advertisement to obtain preferred places on the frontpage at the beginning of the year. Free promotions are organized periodically by Taobao for sellers who offer suitable products with large price discounts.

Taobao's most popular online advertisement tools are pay per clicks and solutions for web design and creation. First, the pay per click advertisement operates like Google AdWords and allows sellers to bid on relevant keywords that target audiences use to find their desired products. Pay per click advertisements will be shown on the right up side of the frontpage. Second, the website design supports include images and software to enhance visual appeals for more enjoyable online experience. Third, Taobao offers the service of website creation and back office integration, which aims to integrate manufacturers' online shops on Taobao marketplace and their external online stores outside of Taobao to simplify data management system (Taobao 2009b). Additional paid CRM services have been work in progress, including features like daily sales, data analysis and analysis of advertising effect.

3.3.   Key Considerations in the Choice of Online Retailers

The decision on how and where to sell online contain the evaluations on operation modes, type of online retailers and customer bases. These three issues are interlinked and will affect the options of one another and should be considered concurrently. The detailed considerations on these three aspects are discussed below.

- Operating mode - online retailer / shop-in-shop / independent website

The operation modes can be distinguished into three categories, which include collaborations with online retailers, through shop-in-shop systems and establishment of independent websites.

- In the collaboration with online retailers, the online retailers like 360Buy, Amazon and Dangdang handle overall website maintenance, delivery, payment, after sales service.

- Under online shop-in-shop system, the platform provides only places online and a collective payment system. Manufacturers have control on pricing and manage their own delivery and customer service. Online store design can be partly adapted to each company to a certain level but under an overall framework. Manufacturers' online stores on Taobao platform are examples in this category.

- The third approach to establish companies' own websites. It is suggested for products or services with existing brand awareness or high uniqueness. Because this operation requires considerable domain name promotions and advertisements to attract traffic to sites; therefore, it is not suitable for nameless and non-distinguishable products.

While choosing online shopping platform providers, companies need to decide the operating mode intended to use and amount of available resources. For online shop-in-shop system, higher investment is needed relative to selling through online retailers because companies need to engage personnel and manage independently in various functions like online store design, IT infrastructure, deliveries, marketing campaigns and customer services. Nevertheless, hard work is rewarded by advantages of own decision making on product, pricing, marketing, and direct contacts with customers. The collaborations with online retailers and online shopping platforms contain different tasks and advantages. The tasks for manufacturers and the costs

benefits of this operating mode are summarized in table 9 and table 10 below.

Table 9: Tasks for Manufacturers to Sell through Online Retailers

	Tasks for Manufacturers
Manufacturers Sell to Online Retailers	• Shipments to online retailers' warehouses • Payments for retailers include sales commission, listing fee and promotional fee • Follow online retailers' repair and refund policy
Manufacturers adopt Online Shop- in-Shop System	• More liberty in deciding which products to sell, pricing and promotional activities • Deliveries to final customers • Customer services including collection of products for refund/replacement • Online platform design (to a degree)

Table 10: Advantages and Disadvantages of the Collaboration with Online Retailers

Advantage	Disadvantage
• Only shipment to retailers' warehouses is needed. • Retailers handle payment, delivery, repair and refund with final customers. • Delivery to remote villages will be handled by retailers. • Comprehensive E-commerce knowledge is less obligatory. • Online retailers are specialized in logistics and customer services and may work more efficiently. • Online retailers have online market knowledge.	• No full decision power on the items to sell because online retailers evaluate products sales periodically; hard-to-sale items will be removed from online store. • No full control over pricing • No direct contact with customers; Customer information may not be accessible. • No full control over advertisement and promotional activities • Rules such as repair and refund are set by online retailers.

• Online Retailers with Different Product Ranges

Besides operation mode, a company needs to choose which platform to sell. Location undoubtedly matters and will affect future growth. The major online retailers currently develop toward two directions, which are online department stores and online specialist retailers. The two business models are explained below:

- Online department stores

Online department stores provide various product categories and aim to reach

the greatest possible number of consumers. Major large scaled online retailing companies such as Amazon, Taobao, and Dangdang fall into this group.

- Online specialist stores

Online specialist stores are online retailers specialized in certain product categories, offering narrow variety with deep assortment. Examples are online retailers specialized in electronics, organic products, garments, cosmetics retailers and so on. These online specialized stores have made fast growth recently due to the rapid increase in number of netizens which creates a large user base with various demands. Online specialist stores serve specialized customer segments with specific product offers, professional services with flexible approaches (Dong, September 9, 2009).

• Customer Bases on Different Online Platforms

The scale of customer base plays an important role in the platform selection. A well-operated online retailer can attract more traffic flow. Running online stores on traffic frequented platforms increases the potential exposure of product offers. The more online stores establish on a platform, the more potential buyers are attracted and in turn more new online sellers will join, creating a positive self-reinforced cycle for a busy traffic website.

Furthermore, different platforms have different user base concerning age, gender, income level, customer locations and users' habits. Companies need to decide which platform fit their product categories. Table 11 in the next page compares user characteristics by major online platforms.

Table 11: Composition of Users by Types of Online Retailers

		Book, Audio/Video Product	Electronics	Garment
		Dangdang/Amazon	360Buy/Newegg	Vancl/Olomo
Gender	Male	94	**118**	107
	Female	**108**	76	91
Age	18 and below	96	83	72
	19-24	**110**	**105**	**107**
	25-30	100	**104**	**107**
	31-35	98	100	**107**
	36-40	98	93	102
	41 and above	85	103	91
Income	No income	**111**	96	97
	Under 1000	**113**	99	95
	1000-2000	90	85	98
	2001-3000	97	106	104
	3001-5000	105	**114**	102
	5001 and above	95	**119**	105
User Concentration Index = (% of target users in total user of a specific online shopping site : total users of the specific online shopping sites divided by total netizens)*100				

Source: IResearch, June 29, 2009

- Customers' Age structure on Taobao, Dangdang and Amazon

Dangdang has more mature customers. 39.2% of customers on Dangdang are aged 31 or more, higher than 24.8% and 27.7% on Taobao and Amazon respectively. Taobao has younger customer groups, with 72.3% of customers aged from 18 to 30, followed by Amazon and Dangdang whose 18-30 customers account for 69.4% and 57% respectively (CNNIC, June 2008, p.50). Table 12 below shows age of customers by online shopping platforms.

Table 12: Users' Age Structure by Online Shopping Platforms, June 2008

	Under 18	18-24	25-30	31-35	36-40	40 and above	Total
Taobao	2.8%	39.8%	32.5%	13.3%	6.7%	4.8%	100%
Dangdang	3.8%	27.4%	29.6%	16.3%	13.9%	9.0%	100%
Amazon	2.9%	42.3%	27.1%	12.9%	7.1%	7.7%	100%

Source: CNNIC, June 2008, p.50

- Customers' Income structure on Taobao, Dangdang and Amazon

Different platforms attract users of different income levels. As Table 13 below shows, Dangdang's customers have higher income level with 23.5% of customers with monthly income exceeding RMB 5,000 [USD 732.3] (CNNIC, June 2008, p.51).

Table 13: Online Customers' Income Levels by Online Shopping Platforms, June 2008

	Under 500	501-2000	2001-5000	5001 and above	Total
Taobao	12.1%	36.8%	35.3%	15.8%	100%
Dangdang	16.3%	26.9%	33.2%	23.5%	100%
Amazon	16.0%	33.1%	35.2%	15.7%	100%

Source: CNNIC, June 2008, p.51

3.4.   Manufacturers with Online Sales

The success of online companies is relevant to the choice of business model. To demonstrate online firms' business models and their operating experience in the Chinese market, eight companies from various industries are presented in the table 14 below. Key issues of online operation for these companies are further discussed in chapter 4.

Table 14: Types of Online Business Models

Online Business Model	Explanation	Corresponding Interview Companies
Manufacturers' Direct Online Sales	• Manufacturers sell through their direct online channels to final customers without intermediaries in between. • Producers can understand and fulfill customers' wishes directly. • Product designs are originated from customers' needs. • Intermediary added-up costs can be eliminated. • Online channels facilitate the change from mass production to customization.	• JXSZZ • Markfairwhale • Uniqlo • PGMall • Gadozi
Distributors	• Wholesalers or resellers use online channels to distribute goods or services.	• Hadou
Subscription	• Products are sold under freemium and premium pricing models. • Premium products contain more specialized features with charges.	• Praxis Language
Agent	• Provide an interface between buyers and sellers • Commission fees are collected based on transactions	• Ctrip • Taobao

Source: adapted from Deng et al., September 2008, pp.62-65

- Profiles of Interview Companies

- Hadou – Food Distributor

Hadou is a food retailer created in 2006, originally as a pure online business established on Taobao platform. Until 2009, Hadou has expanded to three physical stores in heavily frequented areas in Shanghai. With around 100 items, sales revenues reached RMB 3 million [USD 0.43 million] in 2008. The growth rate of online sales doubled each year. Hadou sells mid-priced Chinese snacks such as dried fish chips and enhances the product range to dried prune and meat, frozen dumpling and frozen cheese cake. Major customers are middle income buyers. High income earners also recognize the price quality and make purchases from time to time. Low income customers purchase special treats from Hadou during festivals as well. 80% of customers are aged from 20-40. White collars and university students are main customer groups. 85% of total sales are generated from Shanghai and Jiangsu and Zhejiang provinces. The rest 15% of sales comes from Beijing and Guangzhou regions.

- Jiaxing Sanzhenzhai Foodstuff Co., Ltd (JXSZZ) – Food Manufacturer with Direct Online Sales

JXSZZ has been a traditional Chinese food manufacturer established in Chin dynasty 150 years ago. JXSZZ sells traditional foods like cooked meat, fish, rice and moon cakes through supermarkets, with 500 points of sales in China and abroad. The online business was launched in 2006 on Taobao platform. Items sold online are vacuum packed with expiry date within 6 months. The total revenue of the whole firm reached RMB 100 million [USD 14.6 million] (Jiaxing Sanzhenzhai Foodstuff Co. Ltd 2009). Online sales revenue reached RMB 1 million [USD 0.15 million] in 2008, accounting for around 1% of total revenue. The online sales grow at 20% each year.

- Markfairwhale – Clothing Manufacturer with Direct Online Sales

Markfairwhale is a well known Chinese clothing brand founded in 2001. Originally focus on men's ware and extend to female clothing in 2004, the brand has a wide variety of collection and focuses on its Italian style of design. With around 800 of physical stores including both franchised and wholly owned stores in China, Markfairwhale launched its online shop in 2008 on Taobao

platform. Online sales revenue is expected to reach RMB 15 million [USD 2.2 million] in 2009, accounting for around 2.5% to 3% of total sales revenue of the company.

• Uniqlo – Clothing Manufacturer with Direct Online Sales

Uniqlo is the sixth largest apparel retailing group, ranking after GAP, Zara, H&M, Limited Brands and NEXT (Uniqlo 2009). Entering in the Chinese market in 2002, Uniqlo originally positioned itself in the same way as in their Japanese market, delivering good quality clothes to all population at a low price. That means the price of Uniqlo in China was similar to other Chinese clothing manufacturers. However, the low cost strategy did not drive to the success. The company failed to defend itself in fierce price competition among local manufacturers.

In 2006, Uniqlo has switched its strategic direction to target urban middle class, providing apparels which are easy to mix and match with other brands. New strategy led to 6 times growth in sales in the Chinese market from 2006 to 2008. Major customer groups are aged from 20 to 30. (Hangzhou Daily, July 2, 2009). Both online and offline channel experienced a fast growth in 2009. The online shop was opened on Taobao platform in April 2009. The number of physical shops reached 34 in China, and 26 of them are built in 2009. All their physical stores are wholly owned.

• PGMall – Bag Manufacturer with Direct Online Sales

Established in 2003 as an online female bags seller on Yahoo platform in Taiwan, the company has extended its business to mainland China in 2007. The total sales revenue reached RMB 29 million [USD 4.2 million] in 2008 and expects to achieve RMB 41 million [USD 6 million] in 2009. The company has more than 1,000 items on Taobao online stores and sells around 50,000 bags a month (Businessweekly, April 26, 2009). Average price of bags is around RMB 40 to 60 [USD 5.9~8.8] which targets young female students and white collars. With 18 physical stores in Taiwan, online and offline channels adopt identical market positioning, except online shop have larger collections due to unlimited space. PGMall's physical storefront has not set foot in mainland China. The primary goal is to stabilize sales revenues in Chinese market at the beginning.

- Gadozi – Bag Manufacturer with Direct Online Sales

Established in 2004, the company sells female bags on Taobao platform. Main target customers are female white collars aged 20-35. Gadozi aims to deliver fast fashion to its customers with new product release every week. Average price for a bag is from RMB 100-200 [USD 14.6~29.3], targeting urban white collars with income level from RMB 2,000-5,000. Gadozi's products are comparatively more expensive than average low priced bags sold online but with good price quality relative to physical chains. The sales revenue was RMB 3 million [USD 0.44 million] in 2008 and expects to reach RMB 4~5 million [USD 0.59~0.73 million] this year.

- Ctrip – Online Travel Agent

Ctrip is the market leader of online travel agency in China, with 53.7% market share in the second quarter 2009 (Xinhua, August 12, 2009). This Shanghai based company was established in 1999 and listed on NASDAQ in 2003. Product offers include hotel reservation, air ticketing, and packaged tour, accounting for 52%, 44% and 7% of sales revenue respectively in 2008 (Ctrip 2009). As an online travel platform, Ctrip is an intermediary, linking hotels, airlines agents, travel agents and final customers together. The company uses its scalable customer base to ask for cost effective offers from hotels and airline agents.

In Chinese online travel market, 4.1% of netizens, that is around 13 million, use online traveling service in the first half of 2009 (CNNIC, July 2009, p.28). The number of users using online traveling service reached to 13.86 million in June 2009. Ctrip's target customers are business and individual travelers whose income level reaches RMB 60,000 [USD 8,788] per year. Target customers locate mainly in first and second tier cities and some in third tiers.

In spite of being an online firm, only 30% of the sales revenue is concluded online. The remaining 70% of sales revenue comes from call centers. Among foreign customers, 85% and 15% of the sales are conducted via Internet and by phone respectively. Chinese consumers like to hear a real person responding to their requests and prefer booking by phone rather than online. Call centers with 19,000 seats (capacity) are established to provide efficient service. This demonstrates Chinese customers are comparatively more reliant on offline channels and less dependent on Internet booking.

- Praxis – Language Course Provider with Direct Online Sales under Subscription Model

Established in 2005 in Shanghai, the company starts its business by offering online Chinese courses via podcast. Until now, its products extend to online English, French, Italian and Spanish courses. Major paid customers reside in English speaking countries (Liu, May 9, 2008). The number of learner achieved 250,000 in 2007. More than thousands of paid customers receive one-to-one language training.

In Chinese B2C market, ChinesePod and EnglishPod target on a niche market, mainly expatriates working in China, foreign enthusiasts interested in Chinese culture, local business professionals who are willing to improve their English proficiency. The competitiveness of the company's products lies in its rich and up-to-date content, learning with fun feature, friendly user interface, various topics covering all needs, short and efficient course at different levels. The products are designed for busy business people and students focus on time saving and efficiency. Online training creates a learning environment without distance. For example, Praxis offers tailored training for Microsoft in China. Microsoft's employees are scattered in Beijing, Shanghai and Guangzhou areas. With online courses, staffs receive the same set of lecture simultaneously in a cost efficient way.

Praxis's business is operated under freemium pricing system, meaning some contents can be downloaded for free. Additional supports include course transcripts, exercises, study plans and one-to-one conversations are with different charges. Freemium strategy is to attract traffic and enlarge the potential customer base who might become premium service users in the future. To increase the conversion rate from free to paid users, Praxis adapts free trial for seven days where customers can first experience online lectures and all supporting materials at no costs.

4. Major Operational Issues in the Chinese Online Shopping Market

4.1. Multichannel Distribution and Price Competition

The emergence of online business brings different levels of negative and positive impact on multichannel management for companies. Three different situations can be distinguished while analyzing competitive effects resulting from online channels. The three circumstances are explained as below.

- Online companies go offline – symbiotic relationship

When pure online shops expand to physical stores, online and offline channels are in complementary relations if prices are set at identical level. Two channels complement each other to cover wider customer segments. The advantages brought by the establishment of physical stores include creating and reinforcing brand awareness, strengthening customers' confidence on brands and products sold online, enabling direct customer interaction, and accumulating knowledge on physical store management for future expansion. Physical stores can further provide real shopping experience including seeing, smelling, tasting, touching real products to compensate disappointment when buyers consider products to be different in terms of texture, size and color while shopping online. The two channels can further motivate each other for further improvements on customer services and sales techniques. Altogether, physical stores remain a complementary channel for the online shop. In previous interview companies, Hadou, PGMall, Gadozi all belong to this category.

One particularity for small and medium food retailers like Hadou is that the physical stores complement critically the online stores. Different from other manufacturers of fashionable goods, food quality is tremendously influential to health. The correlation between food and health is regarded much stronger than health with other product categories. Besides, Chinese customers are concerned about food security after the incident of poisonous milk. The existence of physical stores generates more confidence among customers. With the establishment of physical stores, customers feel more secure and have less doubt toward a newly established online food company. If any concern about product quality arises, customers know at least a channel, a place, a brand to consult their worries. In a word, a physical address

demonstrates the reliability of an online company.

- Companies with wholly owned physical distribution channels go online

Companies who have wholly owned physical stores extend to online channel will not confront channel conflicts problems if the online and offline prices are uniform to eliminate price difference. As no franchised chains or distributors are involved in the supply chain, potential dissatisfaction of franchisees or resellers toward online shops can be eliminated. Two channels complement each other to cover more customers groups and increase sales revenues. Online shops provide a more convenient shopping experience for customers without time and space limits.

For example, Uniqlo falls into this category and its online sales further bring up sales revenues of physical stores. The online store can reach other provinces where the physical chain has not presence yet. The company's market positioning of online and physical shops is similar, with almost identical prices and products as in their large-sized store. The combination of two channels allows customers trying clothes in physical points of sales and purchase later online. Or the other way round, customers surf Internet for information and purchase in physical stores afterwards. Generally speaking, for companies with full control over distribution channels, online and offline channel do not cause horizontal conflicts and synergy can further be created through a combination of the two approaches.

- Traditional enterprises with complex offline distribution channel go online

Channel conflicts arise seriously when many actors (e.g. wholesaler and reseller) are involved within distribution channels. The more extended a channel, the more price difference between players at each level. Price competition normally occurs in the distribution channels with high complexity. If a manufacturer has franchisees, wholesalers and retailers in the distribution system, settling horizontal channel conflicts requires great efforts. In general, several possibilities to cope with potential channel conflicts are listed below:

- Maintain online and offline price consistency
- Different market positioning for online shops and offline stores
- Differentiate online and offline product offers
- Promote official online shopping websites to avoid customers buying from the online shops which are not recognized by the original manufacturers.
- Create a new brand (not related to the existing brand) to target online market, but building a new brand from scratch is very costly.

In the case of Markfairwhale, a company composed of franchised chains and wholly owned stores, the launch of online channel brings concerns of sales competition between online and offline stores, because a great part of physical stores are franchised. To minimize horizontal conflict, Markfairwhale adopts different positioning for online and offline channels. The online channel aims to attract young and lower-income customers who look for sales promotion and great barging. 90% of the company's online customers are aged from 18 to 29. In contrast, its physicals stores target fashionable shopping lovers with higher income level. Table 15 indicates the different positioning of Markfairwhale's online and offline stores below.

Table 15: Market Positioning of Markfairwhale's Online and Offline Channels

	Online Channel	Offline Channel
Objective	• Sell overstocks • Pipeline for clearance	• Build brand image • Emphasize new product release • Attract new customers
Target customer	• Lower-income level	• Fashionable, higher-income level
Focus of the channel	• Financial result	• Brand awareness and recognition

For Markfairwhale, online store provides a channel to reduce excess stock at heavy discounts. Over stock is common in clothing retail business due to the fast moving characteristics of unpredictable changes in climate, fashion and every public incident. Once an unexpected change in the trend is not under controlled, stocks pile up easily. The company's online store provides an extra channel to liquidate excess merchandises and improve the company's financial structure. On the contrary, offline stores concentrate on maintaining high-end brand image. Therefore, launching fashionable products and attracting new customers are priorities for offline stores.

In the case of JXSZZ, a traditional food producer previously selling through major supermarkets, the company tries to prevent channel conflicts by maintaining the online price at similar level to the offline stores and develop new products mainly for online customers.

Online buyers are different from offline customers in terms of age, preference

and eating habits. Customers who shop online are younger, used to eating out and have less disposable income whereas offline customers are more elderly and prefer traditional tastes. Providing different series of products online help prevent channel conflict and attract more online buyers.

Selling to physical supermarkets encompasses high listing fees for shelf-space and obliged price reductions during sales promotion periods of supermarkets (Mills 2003, p.151). For JXSZZ, selling through its own online channel save all the expenses mentioned above. Compared to the offline operations, the online shop reduces the costs mentioned above and creates higher profit margins. Besides, no delayed account receivable from supermarkets will occur from online sales where manufacturers can collect payments once the sales are completed. Furthermore, online channel serves as a preferred marketplace to test new products before their launch in supermarkets. This is because sales of new items are variable and unpredictable. Without any historical sales record, it is relatively difficult to convince retail chains to accept new items. With a direct online channel, new products can be assessed by online customers prior to the sales in supermarkets. If a product is successfully sold online, the company can further consider its sales potential in the offline stores. The risk of being forced to off-shelve due to the poor sales result in physical channels can be largely reduced.

Online shop can be the frontline to gather feedbacks from customers. If customers are satisfied or dissatisfied with the products, they can express opinions or criticisms on online comment areas. Customer feedbacks are especially valuable for JXSZZ who always had supermarkets in between where direct customer contact could not be achieved. The need for customers' feedback is essential for this traditionally well-established company. The company's potential pitfall lies in its neglect in new product development due to the reliance on its past success and its well established brand image. Experienced employees in the company may not regard new product development as a necessity for the future growth. Therefore, direct customer feedback help provide valuable information on further improvement of the company.

4.2.   Price Competition with Unauthorized Online Stores

The low entry barrier in the online retailing industry creates a great number of online sellers who trade genuine goods produced by the brand companies but

these online sellers are not officially endorsed by the original manufacturers. The merchants who sell the branded goods but are not authorized by the original brand companies are referred to as unauthorized resellers. Many brand companies compete to sell the same products with these unauthorized online stores in difficult price battles.

The price competition with unauthorized online shops happens usually when companies' distribution channels are complex and involve numerous parties. When more parties are involved, more actors will have access to genuine goods, from upstream factories to downstream wholesales, resellers and even final customers. As long as there is a price difference between the costs of goods and the final retailing price, it is comparably easy for any individual to resell the goods online. Because these unauthorized individuals do not belong to formal distribution channels, they can set any retailing price to maximize their profits. These unauthorized online sellers usually sell goods cheaper than regular channels to create price advantage and attract online buyers. If the distribution channel is not in full control of the company, it might be difficult for manufacturers to find out from which sources these genuine goods flow out. Unauthorized online shops create not only negative influences on sales for manufacturers but also stir dissatisfaction among other authorized resellers.

JXSZZ is one of numerous enterprises troubled by these unrecognized online shops. These unauthorized online stores purchase goods from other wholesalers at discount prices similar to large supermarket chains and resell products online. Because these unofficial online shops do not need to cover fixed costs such as rents, shelving services and store decorations as normal physical stores do, unauthorized online resellers can sell more cheaply relative to official channels. Being a renowned brand, customers already recognize the brand and the quality of JXSZZ products. Once buyers have experienced the products and recognized the quality, they will not have quality concern while shopping online. Therefore, some customers purchase the products from unauthorized online shops for the lowest price. Unauthorized online stores cannibalize the sales of the official online shop. The company responds to this problem by emphasizing its freshness of products delivered directly from the factory rather than passing through complex wholesale channels.

Markfairwhale also encountered several cases when goods of the company are sold by unrecognized sellers on C2C online website. There are two sources for this problem. First situation happens when staffs of the company

buy inexpensively within the company under employee discounts and resell the goods to final customers. In this circumstance, Markfairwhale buys these unauthorized products and use serial numbers, product types, colors or transaction records to trace back where this item had been sold. Punishments will be given accordingly. Second situation arrives when goods (which might be defective and prohibited to be sold) flow secretly out of the factories of Markfairwhale's suppliers. In this case, the label of the clothes are cut in half or slightly destroyed and these products are usually much cheaper than usual. The exceptionally low price signals the forbidden behaviors. Markfairwhale buys these cheap items and find out the source. Once discovered, the suppliers will be punished by expensive fines according to the contract. The feedback from other physical stores can also be a way to discover unusual low priced items.

For Uniqlo, a company with wholly owned distribution channel, unauthorized price competition can be better controlled because the involving participants are simplified. For a manufacturer, it is important to note that online transactions are anonymous and price comparison is one characteristic in the online shopping market. Setting prohibitive rules on these incidents can help regulate distribution channels but cannot fully eliminate the risk.

4.3.   Logistics in the Online Shopping Market

Most manufacturers cooperate with local third party logistics providers for deliveries. The nation-owned postal service EMS covers 90% of areas in which online transactions on Taobao platform are taking place (EMS 2009). Nevertheless, postal service EMS is usually only used for areas where contractual logistic providers cannot deliver because its service is more expensive than other local expedited companies. Deliveries to rural areas might incur additional charges which should be paid by online sellers or buyers. The well established international carriers such as DHL and FedEx provide high quality services but are much more expensive than local players. Their services are normally not considered by cost conscious online buyers and sellers, except for extremely delicate goods like ceramics.

Two issues related to logistics are cost and quality:

• Delivery costs

Most online customers are highly price sensitive. Freights can account for a large percentage of the total cost which impedes buyers from purchasing online. If online total costs including delivery fees exceed offline purchases,

there is nearly zero incentive to shop online. Therefore, domestic logistic providers are considerably more popular than international logistic companies for the cost reason.

Some online stores cover delivery costs for customers in major cities as their sales promotions. Covering delivery costs is feasible for sellers of products with higher margins like clothing and cosmetics. In the case of JXSZZ, some online buyers also expect the seller to cover shipping costs as their discount offers. However, for JXSZZ, free shipping offers will result in losses because their low cost products are already sold at mediocre margins. To overcome this potential obstacle and encourage online purchases, it is crucial for online sellers to source reliable logistic providers at a reasonable price.

- Delivery quality of logistic providers

Online seller should consider delivery quality including speed, probability of damaged and missing goods, regional coverage, service, price, and complaint management (Taobao 2009a).

Logistics in first tier cities can satisfy major delivery requirements. Most problems are caused in second, third tier cities and rural areas. Several reasons include natural geographic difficulties and overall development of logistic industry within the country. The mountainous landscape in China creates barricades in logistic development, particularly in rural regions in the west side of the country. In addition, many logistic companies deliver within the province in which they are based by themselves and outsource other-provinces-deliveries to other local companies to minimize costs. Because mutually recognized service standards among partners have not been unified, the control of delivery quality becomes difficult under collaboration. Customers in second and third tier cities generally have more complaints toward deliveries concerning damaged goods or unfriendly attitude of deliverymen. Although customers have transmitted their dissatisfaction, some logistic providers are still unable to solve the problem due to lack of direct control over partners.

The quality of logistic services pose a threat to the expansion of online business, especially for sophisticated, fragile and high priced products such as laptop, LCD and mobile phones. Even though the logistic industry has not matured, progress has been made in recent years, partly as a result of the growth of the online business. The government also highly emphasizes and invests in infrastructures to improve road and traffic conditions. Online platform

and online retailers also creates standardized selection criteria, like secret spontaneous control on logistic companies to provide better online experience for customers (Bendibao, March 30, 2009).

Furthermore, the service of delivery to neighboring convenience stores has been tested in certain cities. In the service areas, customers are able to pick up their parcels in nearby convenience stores. This provides more delivery choices and convenience to online customers. It is expected that the more delicate services will be offered and related logistic problem will be improved in the future.

Regarding deliveries of online services like Praxis, the e-learning firm, the main issues of content delivery lies in hardware compatibility, Internet connection and bandwidth. The company provides lessons compatible with PC, MP3, MP4 players and mobile devices such as IPhone, Android, Nokia Symbian and Blackberry. Besides, courses are offered in audio forms rather than videos, which help minimize the negative impact resulted from Internet download speed. Contents are provided in two formats, CD quality of audio files play at 128 kbps and radio quality files played at 64 kbps to further avoid slow downloading speed for Chinese users (EnglishPod 2009). Even the Internet penetration rate within China is 25.5%, the limited Internet accessibility does not cause concerns to Praxis because its target segments are white collars located in costal developed cities with stable Internet access. The sluggish Internet connection in rural villages does not create obstacles for the firm.

- Suggestions on logistic operations in the online business

In conclusion, online sellers need to assure the balance between cost and quality. It is crucial to cooperate with several logistic providers and reach a full coverage of target customer groups. Firms with larger delivery quantities, like Uniqlo, can set high partner selection standards and reach mutually agreed contracts with delivery companies. For online service providers with digitalized product, online connectivity and download speed need to be considered.

4.4.   Payments in the Online Shopping Market

Flow of capital is the second pillar supporting online shopping business. The improved online payment systems play a considerable role in the growth of Chinese online business industry. Chinese online retailers provide a number of flexible payment systems to customers, including third party payment tools, credit card, online banking, bank and post fund transfer, cash on delivery.

Certain retailers like 360Buy offer cash and carry service in several locations.

Established in China since 1999, local third party payment system is the most preferred payment mode relative to credit cards and online banking while shopping online. The service provided by local companies is similar to that of PayPal. This industry goes through a strong expansion by providing reliable payment transfers and ensuring transaction securities. Buyers' concern on how to obtain refunds can be fully addressed on the foundation of third party payment. For instance, if products are defective upon arrival, buyers can request third party payment providers to postpone or further return the funds. Without a third party payment system, fraudulent sellers may not fulfill the replacement responsibility on non-functioning items.

Another preferred payment mode among Chinese online customers is cash on delivery (COD). The particular choice can be partially explained by the fact that buyers perceive lower level of trust in online transactions; therefore, they are motivated to take the safest approach to protect themselves against online fraud (Xinhua, February 5, 2008). From customers' points of view, paying cash upon delivery provides the ability to confirm the arrival of the goods before payments to create more reassurance and convenience on online purchase.

From the perspective of online retailers, COD can result in increasing operational costs due to slow cash collections and risks of opportunistic behaviors of logistic partners. First, logistic companies take responsibility to collect payments when cash is paid upon deliveries. Online retailers will not receive payment directly after each collection. The payment will only be received until retailers settle accounts with logistic partners in each term, which leads to slow capital turnover rates. Second, online retailers bear the risk if logistic providers or delivery personnel steal the funds and disappear. These create higher operational costs for online retailers and offset a part of their comparable cost advantage relative to offline shops (Wang, September 12, 2007).

To satisfy customers' wishes for COD service, the online retailers with in house logistic departments gain more advantages in their direct controls over deliverymen. For instance, Amazon provides COD covering 600 cities (reaching third tier cities) in China. For online retailers who do not own logistic services, they need to cooperate with logistic providers and consider reliability issues and carrier thefts. Online platform Taobao has started to coordinate with three logistic companies by offering COD services and expect more

delivery companies will join. This measure reduces the entry barrier for non-online shoppers and encourage them to purchase online (Xin, August 21, 2009).

- Suggestions on payment operations in the online business

In conclusion, payment mode should provide convenience and be widely covered. Chinese customers have relatively low usage of credit cards and PayPal. Local third party payments, COD, online banking and offline fund transfers are widely used. Because of the large potential user bases that Alipay and Tenpay have, Ctrip, the largest online traveling platform in China, has adopted these two payment solutions in 2009 to facilitate online payments (Analysys International, June 9, 2009). Praxis, the online language courses provider will include Alipay to provide a more convenient online purchasing experience. These examples demonstrate the importance of complementary payment systems to provide convenience and wide coverage.

4.4. Problems of Counterfeit Products

Major counterfeit problems happen on C2C platform with individual sellers because of the low entry barrier to sell on C2C platform, this results in many unregulated online sellers. Meanwhile, online customers on C2C platform are highly price sensitive. The combination of low price preference from buyers and low entry barrier from sellers' side dramatically increases the number of fake goods on C2C marketplace. For online manufacturers, infringement of trademark does not happen often. However, the real problem bothering many online manufacturers is their designs are copied by other companies, especially for fashionable goods like bags and clothes. There is no effective method to fight against copy problem because designs cannot be patented.

The price competition is another phenomenon which comes along when original product designs are copied by lower cost manufacturers. These low cost manufacturers replicate designs quickly, use low-end materials to gain price advantages and sell online cheaply. Nearly identical photos of imitated products are posted on the low cost competitors' online stores. When potential buyers see these similar photos of products and large price differences between two online stores, customers usually go for the cheaper sellers and question the reason of the high prices charged by the original manufacturers. Some customers tend to suspect original sellers making unreasonable profits from customer ignorance. In fact, the reason behind the higher-priced products from original sellers is the higher quality materials and their efforts invested in product designs.

- Suggestions against counterfeit products

The problem mentioned above has been reported by several interview companies including two bag manufacturers (Gadozi, PGMall) and one clothing company (Markfairwhale). Any firm in this market should carefully consider this issue to minimize the negative effects. To fight against imitation, manufacturers can differentiate by creating brand recognition and emphasizing premium quality in products and services. The companies who copy designs can imitate styles but have limited capacity and efficiency. They may be able to copy 20-30 items but may be unable to imitate hundreds or thousands of items. If companies can create barriers by designing and producing a large variety at fast rate, imitators may not able to catch up. In a word, if a company wants to deal with single unauthorized individual or company in a legitimate way, it would take tremendous time and effort. Increasing overall competitiveness of the company to differentiate from imitators is a more practical way to the success.

5. Success Factors in the Chinese Online Shopping Market

5.1. Success Factors of Online Retailers

There are five key success factors for online retailers in the online shopping business. The central concept can be demonstrated into five dimensions: price, service, inventory management, delivery and web experience. These five areas are presented as below (Liu, May 15, 2009):

- Price

Price is the foremost core competence for a successful online retailer. The high competitive intensity in this market results from low entry barrier, low product differentiation among online retailers and moderately low switching costs for final customers going for alternatives. Given the intense competition, the rapid market growth still inspires new entrants and leads to continuously rising competition. Achieving scale economies for reductions in unit costs and providing lower price for price sensitive online buyers are determinants to the domination in the market (Liu, May 15, 2009).

- Customer service

Service quality is crucial for the success of online retailers. Buyers purchase online generally are different expectations from buying offline. Buyers in the brick-and-mortar world are aware of the trade-off relationship between price and quality and associate low price with low quality intuitively. Online buyers expect an equivalent service level from every online store and tend to judge both sophisticated and simple online stores by the same standards. Online customers demand fast delivery and immediate reply to every online store in the cyber world. That means even for online firms offering no frill products and operating in small scales, good customer service is still required in this market. Good customer service is indispensable for a successful online business (Liu, May 15, 2009).

- Inventory management

Inventory management is highly relevant to online retailers' performance and is influential on buyers' satisfaction. An adequate inventory management can protect against stock out and improves cash-to-cash cycle time. Although online stores are characterized by unlimited shelf space, inventory capacity is

still bounded. Excessive stocks will increase inventory costs, require more spaces, result in risks of piling up unsold items and poor capital turnover. Insufficient inventory level can cause stock out and customer dissatisfaction. Optimizing inventory is a challenge for all enterprises and link to store results (Liu, May 15, 2009).

- Order fulfillment time

Order fulfillment time includes inquiry processing time and shipping time. Short lead time requires a precise inventory management. In physical stores, customers complete the purchases and collect goods at points of sales simultaneously. Transportation of goods to points of consumption is realized by buyers. In online retail business, the process of transportation becomes more sophisticated where sellers and logistic partners should jointly handle transportations from warehouses to consumers' places in small quantities, to spaced apart locations and at good timing. Each individual customer has distinct preference on delivery time and high expectation on e-tailers' delivery performance (Liu, May 15, 2009). Customers expect to be served faster and more efficiently in all aspects. The process of order fulfillment is a vital success factor in the industry.

- Web experience

Online purchasing experience is based on technical foundations. Key factors influencing customers' purchase decisions contain Internet speeds, usability, easiness to find online store while searching, layout, user interface, and store design. User interface is as important as the visual display in physical stores which can create pleasing or irritating shopping environment. Understanding customers' online experience and continuous website improvements are key drivers to serve the market (Liu, May 15, 2009).

The five elements above are of paramount importance in online retailing business and should be integrated to provide customers an overall enjoyable online shopping experience.

5.2. Success Factors of the Manufacturers with Online Sales

This part is devoted to demonstrate critical components in the online business operations. The key success factors brought by the interview companies are summarized in the next page. Lessons from their experience could be applied to other companies as general guidelines in this market.

- Product variety

Before market entry, product offers largely determine the future success. Products should be competitive and distinct in terms of features, pricing, brands or marketing. Once entering the market, the speed of new product development and the wide choices of selection are two main success factors.

In recent years, customers demand new merchandises more frequently; therefore, fast product release is important to attract the attention of customers. With great varieties and fast introduction of new products, competitors' imitations can be alleviated to some extent. Besides, more selections are provided to satisfy customers' various needs and prevents them turning towards alternatives. In the example of Praxis Language, its success can be attributed to quick updated contents based on current hot issues and wide topic selections, covering every useful situation including business, cultural and social events.

When considering extending product offers, firms should evaluate synergies and economies of scope generated from product diversification. Product varieties should be aligned with the companies' market positioning. Inventory costs and operating costs for increased product lines should also be evaluated.

- Marketing activities

Among all marketing measures, this section mainly focuses on online advertisements. Major online advertisement techniques include advertisement on search engine or portals, online news release, forums, blogs, use of public incident to create a fad, virus marketing and search engine optimization.

Search-engine marketing and online banners are two widely used approaches to increase brand exposure and boost sales revenues because web surfers can be guided to companies' websites through these two tools. First, search engines are entrances capturing a wide spectrum of people and direct them to web pages addressing to their interests. Combining precise keywords with accurate information introducing websites is substantial to attract traffic. Search engine optimization (SEO) is an important long-term process because it helps websites to obtain preferable search engine ranking. For newly established firms, keyword selection is a must in short term. In long run, SEO can be used for further improvement.

Second, web banners are another practical tools to attract traffics to websites.

Banner ads placed on portals provide users shortcuts to the websites in which users might be interested. Effective banners should be attractive with concise keywords. A short banner of 10 words still can create a massive impact if creativity is transmitted. The use of banners and search engine advertisements should follow consumers' web surfing habits and be customer centric.

After attracting customers to the websites through search engines or web banners, offering promotional activities can boost sales revenues. The sales promotions entail tactics like price reductions, buy one get one free and extra gifts. Free samples are useful promotional tools, particularly for experience goods whose quality can only be assessed upon consumption. For instance, Praxis launches a seven day free trial for its language courses to enable user experience. Online food retailers like Hadou and JXSZZ send out different kinds of small samples. It is more likely to acquire customers successfully after they have tried the samples and ascertained the product quality.

While designing marketing activities, the target customers and product types are two primary factors to consider. First, companies should gain abundant knowledge like demographic backgrounds, buying habits and information accessing points of their core audience for marketing campaigns. A firm without an understanding of its target customers will end up with inefficient spending and ineffective results. For example, some community websites or discussion boards gather users sharing their experience. Potential buyers tend to visit these categorical sites for purchasing advice. Advertisements in topic-related sites provide a closer approach to potential buyers.

Second, product types also influence the way companies organize their marketing. For interactive goods or complex products in which certain level of knowledge is required, forums can facilitate communication between buyers and sellers. For example, one major challenge of Praxis Language is the lack of personal contacts compared to the offline classroom environment. The company builds an online forum to increase personal interactions between teachers and users. Learners can help each other whenever questions arise. Sophisticated products like PC and cars involve vast amounts of knowledge on product selection and technical problems. Online interactive tools can provide buyers information and assistance in time to increase overall service quality and purchase rate.

Last but not the least, online advertisements should be incorporated into a

complete set of marketing activities. For instance, if the exposure of advertisement is designed to reach all customers within the country, logistics distribution should be organized to cover rural areas. Moreover, the choice of key words, online portals and search engines require a multifaceted planning process to achieve the expected success.

- Customer service

Customer service is the foundation of the online success. In this competitive market with often undifferentiated retailers, customer service capabilities are decisive to rival those larger retailers. Chinese buyers usually consult sellers before their purchase via instant messengers. As a result, customer service personnel should understand customers' needs and have rich product knowledge. Polite attitude and timely answers are keys to turn visitors into customers. Potential customers will immediately turn to other competitors if their expectations are not fulfilled. In a word, professional knowledge and comprehensive customer support are factors in achieving customer satisfaction.

After sales service is another important element in the market, including delivery, products consultation, repair and return. Concerning delivery, companies can provide logistics partners' contacts to enable customers to track their deliveries. If any conflict arises between customers and logistic providers, sellers should respond as soon as it can.

In online shopping industry, seven days refund policy without condition is widely applied. Customers are allowed to replace products within 15 days if goods remain well packed. Online customers enjoy a better protection relative to offline transaction because purchases at physical stores can be return or refund only when products are defective (12315.net 2009)[3].

In general, disputing with dissatisfied customers is not a wise decision because disappointed customers will spread negative word of mouth at every opportunity in forums and blogs. Besides, negotiations with angry customers take hours or days. The cost can easily outweigh the cost of refund services. Providing good services not only benefits customers, but it can also create a win-win situation. The number of complaints will decrease and leads to

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[3] According to Chinese product quality law and the law of consumer protection, sellers are responsible to repair exchange or refund defective products. Customers have the right to refund, change or repair flawed goods within seven days. From the 8th to 15th days after the purchase date, buyers can choose to repair or replace broken products.

increase in productivity. In brief, good customer service leads to repeat purchase in the future and is a key to stand out from competitors.

- Technology

Severs, Internet connection and web experience are three main drivers behind the functionality of an online shop. Stable servers and Internet connection are the foundation for online shops. For foreign company intended to target Chinese audiences, severs hosted in China will provide a faster Internet access within the country. If severs are hosted in foreign countries, the download speeds might be slower. Customers might encounter difficulties to visit websites successfully or at a slow speed. Unsuccessful access experience influences not only sales revenues. Customers might doubt the existence of the store and will not come back again. Moreover, companies need to consider whether to rent virtual severs or to purchase dedicated ones. If sensitive data need to be stored, dedicated servers are suggested to avoid data loss or being stolen.

Online shopping experience affects users' purchases. Website appearance, store decoration, layout, functions, server installations, Internet stability and links to forum should be continuously improved to provide superior user experience.

- Payment

The choice of payment system should be aligned with the customers' using habits. Wide choices of practical online payment tools can provide convenience to buyers and leads to greater sales revenues. Collaborating with reliable third party payment companies can increase customer's confidence, offer convenient shopping experience and facilitate online transaction.

- Delivery

Delivery is another key element in the success of any online business. Customers are concerned with product damage during transit, especially for fragile and valuable products. Risks of product damage can largely impede online purchase. As a result, the quality of delivery cannot be overlooked.

Logistic providers are usually the only physical contact interface between online sellers and buyers. The moment when goods are delivered influences significantly customers' impression toward sellers. For a mid-sized enterprise without resources to deliver goods on its own, companies should cooperate with well-trained logistic services to avoid potential disputes in the future.

6. Conclusion

6.1. Trends in the Chinese Online Shopping Market

In this attractive online shopping market, more international enterprises are expected to be online, more online specialist stores will emerge, complementary services like logistics and payment will continue be improved. These trends are explained as below:

- More top international enterprises join the game

Online shopping market is getting more attentions. Enterprises such as Adidas, Procter & Gamble, Lenovo, Dell, Philips and Uniqlo are testing the waters. As more enterprises position their online channels as strategic elements, more investments are pouring in. The market is expected to expand further (IResearch, August 10, 2009). In addition to manufacturers, large retailers like Carrefour also open their online stores. Their presence will provide more choices to customers and have great impacts on online businesses.

- More pure-play online specialist retailers emerge

Many companies start to emphasize the development of their Internet channel. More Internet-based companies gain great attention from the public, like Vancl, a Chinese clothing retailer. Created in 2007, Vancl is the 5th largest online retailer in the market, holding 3.7% of the market share in 2009Q2 (IResearch, August 10, 2009). Financed by venture capitals, the company outsources its production and invests heavily in online advertisements to build brand and create demands. Nowadays, more and more categorical specialist platforms have emerged, like online shoes platform, food and cosmetics retailers.

Companies which were previously export-oriented are now shifting back their focus in the Chinese market due to the global economic crisis. These companies have started to establish online channels as their first step in the home market. One example is Gainreel, a Chinese underwear manufacturer selling on Taobao platform since 2008. Initially, the company was ODM, manufacturing high quality products for international brands. While selling in the local Chinese market, the company provides a good value for price and European design comparable to international brands; at the same time, products are modified to fit Asian body type (Gainreel 2009). More companies of this type are emerging and targeting the Chinese online channels. The level of competition will continuously increase in the market.

- Complementary service of online shopping will be more complete

Logistics and online payment are two core elements in the online shopping business. These complementary services have improved service level continuously. For example, Taobao created rating metrics of major third party logistic providers for quality comparison in 2009. Buyers and sellers can view a standardized evaluation and choose service providers accordingly. Concerning other major online retailers like 360Buy and Amazon, new fulfillment centers are expanded to fasten deliveries with wider coverage within control (Gao, March 5, 2009). The delivery of products to neighboring convenience stores and collection by customers are currently adapted in Guangzhou region. This indicates that the improvements are continuously made in the market.

Related to delivery is the payment service, as 35% of Chinese online customers pay cash upon delivery according to CNNIC (June 2008), this service has been extended to wider regions. In terms of online payment system, Other than market leaders Alipay and Tenpay, the number of online payment service providers has surged, including ChinaPay, the state-backed online payment company, which aims to unify online payment platforms covering all online payments like B2B payments, telephone banking, online banking, POS payment systems by cooperating with major banks for online transactions (ChinaPay 2009). Meanwhile, the dominant Alipay also extends its business outside of Taobao platform to other online retailers like Amazon and 360Buy. Alipay can be recharged in convenience stores and supports payments of electricity and water in some regions

Besides payment and delivery, other supporting services have been developed at a rapid pace, like engineers and consultants for online businesses, photographic professionals for online stores and online marketing firms. These newly-developed industries have been propelled by the growth of online business. These ameliorations will build solid foundation for the online shopping business.

- Declining growth for online C2C business in the long term

As online B2C shopping becomes popular, the growth of online C2C business will be gradually declined. The sales growth of online auctions is expected to decrease. This can be linked to the gradual change in online customers. The priority of online shopping will no longer be finding the cheapest price only. Besides price, customer will put more emphasize on convenience and

products quality. As more companies increase investments in the online market by enriching online product offers and providing more comprehensive services, online customers have greater choices available and are not confined by C2C individual sellers where stronger concerns on transaction security arise. In this general trend, online C2C sales growth will be decreased.

- Resource-sharing alliance among online B2C SMEs

To defend against large online competitors in their advantages of scale economies, a number of online SMEs form alliances and share online expertise, marketing techniques, lists of customers, and hold joint promotional activities periodically. Collaborative alliances among SMEs are formed on the basis of common customer groups. The goal of joint forces is to maximize sales at smallest expense by combining different types of online shops which do not involve direct competitions.

6.2. Advice for Foreign SMEs

6.2.1. Market Entry Evaluation

When a company considers going online to be an option, a cautious market evaluation is a must. The Chinese online market is highly potential but with high competitive intensity, especially after the entries of global enterprises in the market. Companies need to ascertain the competitiveness on core products and additional services. Firms without concrete advantages tailored to local market will eventually backfire.

Companies need to be aware of importation regulation on products prior to entry. For instance, the importation of foods and food-related products requires import licenses approved by the Chinese Ministry of Health. License applicants need to submit required information to the Ministry of Health. Within 60 days, The Ministry of Health will form expert groups from related fields and start to investigate product safety. The decision to grant a license will be determined by the findings of expert groups, national laws and regulations (Hogan & Hartson LLP, June 24, 2009). Concerning importation, the packaging should comply with the Chinese labeling and descriptions. Labeling contents and descriptions should follow the Chinese regulations. Information should include the addresses, names, contact information of local distributors and country of origin. Without complete packaging, products will not be allowed to be imported (State Food and Drug Administration, February 28, 2009). For

cosmetics, the State Food and Drug Administration will be responsible for the acceptance of the applications for hygiene licenses (State Food and Drug Administration, August 22, 2008). Detailed knowledge on local regulations should be extensively prepared.

6.2.2. Market Entry Strategies

After reaching a decision to sell online, a professional team with local expertise is necessary to understand local customer, to promote products and brands jointly with online retailers, to source suitable logistic partners and design a good customer service structure. Online retailers only deal with local companies to simplify their deliveries and financial operations. Therefore, foreign companies could set up their own representative offices or work with local agents, distributors or resellers for importations. Companies need to decide whether they would operate the online shop alone from scratch, cooperate with local partners or merge an existing company. Considerations of market entry mode are explained in Table 16 as below.

Table 16: Comparison of Market Entry Modes in the Chinese Online Shopping Market

	Advantage	Disadvantage
Go Alone	• Full control over operations • Obtain experience from the beginning	• Growth might be slow • Lack of market knowledge • Large investment from the beginning • No immediate cash inflow
Collaborate With Partners	• Access to partner's knowledge • Eliminate risk to a certain level	• Incompatibility of partners • No fully control on partner's Decision
Merger and Acquisition	• Cash inflow from beginning • Acquire existing customer base • Access to partner's knowledge • Fast expansion	• Risk of unsuccessful takeover • Integration of company cultures, business concepts, employees and distribution channels is needed • Capital intensive • Risk of overpay

As for a foreign SME who does not have business experience in China, it is suggested to collaborate with a well-established local partner in the beginning to exploit the local knowledge of partners. The preparation is not only an online store registration but also a complete planning covering logistics, marketing campaign, legal issues (e.g. import permit for certain products such cosmetics and foods, counterfeiting problem), market and customer analysis (e.g. buyer preference and purchasing habits). As many online retailers are eager to

source unique and exclusive products from foreign suppliers for their customers, foreign companies enthusiastic to take part in Chinese e-commerce market have great opportunities to find suitable distributors or resellers with good reputation.

6.2.3. Online Expansion Strategies

As an established online shop, companies face a question on how to grow further in the online market. This part is focused on the growth through web-based franchise model and online consignment system. With Internet-based franchise concept, manufacturers grant other independent franchisees the right to sell the products on franchisees' web shops and provide supports. Web-based franchisees typically have their own websites and purchase product inventories from franchisors. Under the concept of online consignment, consignors provide product photographs and product details to consignment stores. Consignees post product information on their own web shops and sell them without holding inventories. Once a purchase order is received, consignees then pass the order to the consignors, who will be responsible to ship goods to buyers. For small and medium sized manufacturers, establishing franchise and consignment over Internet takes less time and resource to expand than setting up wholly-owned online stores.

While companies further expand by cooperation with franchise or consignment partners, disciplinary pricing policies should also be formulated and executed to avoid vicious price competition among franchisees and consignees. The partners operate mainly for profits; therefore, the system design should enable mutually beneficial outcomes and avoid potential disputes which would damage brand images. Brand companies should select trustful partners who are determined to ensure service levels and implementations. Table 17 describes the advantages and disadvantages of three options for online expansion in the next page.

Table 17: Advantages and Disadvantages of Three Expansion Modes over Internet

	How to Administer	Advantages	Disadvantages
Organic Growth	Establish own subsidiary websites	• Full control over online subsidiary sites • Opportunity to sell different product categories on sub-sites and increase sales	• Need to generate substantial traffic and guide visitors to sub-sites • Expansion might be slow
Collaboration With Partners	Engage Internet-based franchisees or consignees to sell products through partners' websites	• Access to partners' customer base and resources • Expansion may be faster • Wider customer coverage • Increase inventory turnover rate • Less pressure on overstock for manufacturers	• Partners may lack product knowledge • Partners' service level need to be standardized • Risk of price competition among franchisees • No control over partners' effort on brand promotion • Partners may not maintain brand image carefully • Risk of brand damage by ill-behaved partners • Web-based consignees do not have inventory and financial pressure and may lack of motivation
Merger and Acquisition	Purchase the ownership of other online stores	• Possibility to extend to other product categories • Cash inflow from the beginning • Access to partner's customer base and resources	• Risk of unsuccessful takeover • Capital intensive • Risk of brain drain

6.2.4. Operate the Chinese Way

• Understand the Market and Target Customers

Price/value is the main benefit Chinese online customers are particularly looking for. Offering good value for money and combining with a clear and touching marketing message are elements for the success.

Targeting middle class in urban areas can be a feasible option for foreign companies for two reasons. First, middle and upmarket consumer groups are fully covered by the Internet. Infrastructure bottleneck does not have negative effects on online purchase among this customer group. Second, foreign SMEs might not have competitive advantages to cope with local competitors for low priced market if local production resources have not been exploited. Focus on specialized niche products tailored to Chinese preferences, combining localized marketing to communicate brand and price quality can be a suitable entry strategy. Table 18 in the next page shows a SWOT analysis on foreign

companies in the Chinese online shopping market.

Table 18: SWOT Analysis for Foreign Firms in the Chinese Online Shopping Market

Strength	Weakness
• Branding knowledge • Marketing know-how • High service quality	• Localized brand promotion • Unfamiliar with local preference • Supply chain coordination
Opportunity	Threat
• Product uniqueness • Possibility of joint marketing • Chances to promote private labels or exclusive brands	• High price pressure • Intense competition • Governmental regulation

Source: eDynamics Inc. 2009, p.19

Meanwhile, companies should not underestimate the potential from customers in second tier cities, who will become the major driving forces for the future growth of online shopping market. Increasing low end product lines can be considered to tap into these segments.

• Provide convenient payment methods

Flexible, easy and comfortable payment methods should be provided for customers; for instance, fund transfer via post and banks, third party payment systems like Alipay and Tenpay, online banking, credit cards and further to cash on delivery. Chinese customers are less covered by credit cards and PayPal. A complete set of payment services should be prepared to enhance shopping convenience and increase sales.

• Careful selection of logistic providers

The quality of delivery has been improved in first tier cities; however, incidents such as product loss, stolen items can still happen, especially in rural areas. Companies need to choose reliable service providers at reasonable price. Choosing good logistic providers can help prevent customer dissatisfaction. The responsibility and compensation for loss or delay should be regulated before concluding the contract.

• Interactive communication via instant messengers

Instant communication between buyers and sellers is extremely essential for online shopping in China. Buyers normally contact sellers for product information or price negotiation before their purchases. Most used instant

messengers are Aliwanwan[4], QQ[5] and MSN messenger. Interactive chats facilitate information flow for new product release and product recommendations. The questions and requests obtained from customers can also be valuable for further improvements. In addition, email, telephone and cell phone numbers should remain available to provide quick responses in need.

- Be localized, flexible and innovative

The Chinese online shopping market has its distinctiveness and characterized by vigorous improvements, intensive competition, price war, and countless imitators springing up on all sides. Geographical diversity, customer preferences, shopping behaviors and competitive situations should be fully apprehended to make economic and effective decisions. The lesson from EBay's failure to Taobao is its neglect on the importance of customizing services to suit local market conditions (Tseng et al. 2007, p.6). Being responsive and acting fast and flexible are fundamentals, especially in the online world where fast-paced and want-it-now culture prevails. More importantly, companies should continuously enhance products and services and innovate to strengthen core competence. Constant increase in desirability and usability of products and services is a way to be recognized and embraced by customers. In conclusion, be localized to market, flexible to customers and innovative to competition are primary principals to run a success online business.

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[4] Aliwanwan is an instant communication system created by Alibaba group to enable immediate and direct communication between buyers and seller on Taobao platform. Aliwanwan allows buyers and sellers to confirm orders, stocks, and delivery issues to facilitate online transactions.
[5] QQ is an instant messaging tool created by Shenzhen-based Tencent group, controlling 77% of Chinese instant messaging market share in 2008Q1 according to Analysys International, a Chinese research firm (August 12, 2009).

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