

How Alibaba is improving welfare in parts of China

E-commerce is booming in China. And nowhere is it more obvious than in smaller and more remote cities, where the prevalence of online shopping is lowering barriers to entry and boosting economic output for those who need it most.



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E-commerce is transforming China. And China's e-commerce is leading the world. China alone accounted for more than 40 percent of all online sales worldwide, according to the McKinsey Global Institute. Chinese e-commerce transactions were worth more than the totals in the United States, the United Kingdom, Japan, Germany and France *combined*.

And in this vast — and growing — online-shopping market, there's a dominant player: Alibaba Inc., aka the Amazon of China. Journalists and academics talk about "the Alibaba effect" to describe the national impact of this tech giant, which offers a platform to connect sellers of any size to more than 600 million potential customers.

Using unique data from Alibaba, IESE's [Weiming Zhu](#), Jingting Fan, Lixin Tang and Ben Zou were able to better understand how e-commerce, as a new trade technology, is boosting business and consumers' purchasing power, even after accounting for the offline sales lost amid the digital disruption.

Open sesame

Here's the good news: Crunching the numbers, Zhu *et al.* found that e-commerce in China increased welfare — that is, the real wages, or, income expressed in terms of purchasing power — by 1.6 percent for the 320 cities studied. Drilling down, they found the welfare gains were unevenly distributed. For big cities — where incomes are higher and offline options proliferate — gains were nearly negligible. For medium-sized cities, the gains came to 1.2 percentage points. But for smaller and more remote cities, welfare gains were a significant 30 percent greater. That is to say, China's e-commerce is apparently helping to reduce inequality.

The study finds the denizens of smaller cities spend a larger fraction of their incomes online. These shoppers get a better selection and competitive prices via the internet. At the same time, smaller city e-tailers are saving on overhead and logistical costs and even mom-and-pop shops can find a potentially large market online. And this stokes local labor demands, which helps boost wages.

The research also notes that online shopping has already transformed the economic landscape in China. According to United Nations data, between 2008 and 2015, the nominal value of total online retail sales increased by more than 30 times. By 2015, online sales accounted for about 12.6 percent of total retail sales — and that number keeps growing. More recent data from Deloitte suggests that about a third of China's retail sales happen online, as the country's middle class keeps growing.

The co-authors call e-commerce "a powerful tool for improving welfare and reducing spatial inequality in living standards in the foreseeable future." They estimate that when online sales reach 24 percent of total retail sales, a typical Chinese city enjoys a 4.9 percent welfare gain from e-commerce. And since forecasts see more e-commerce growth ahead, that could boost

the living standards for millions.

For businesses, this research suggests it may be wise to skip the brick-and-mortar stores in remote and underpopulated cities in China and to shift more sales online. Unlike in the United States, with its more mature (and offline) retail environment, in China, online customers are ready and waiting.

Methodology, very briefly

This study is based on unique data from Alibaba Inc., the dominant online retail platform in China, covering 320 different Chinese prefecture cities. The co-authors also built a multi-region general equilibrium model and used econometrics to conduct their analysis.

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