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The big sort

China's express-delivery sector needs consolidation and modernisation

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Claudio Munoz

"THE vultures all start circling, they're whispering, 'You're out of time'...but I still rise!" Those lyrics, from a song by Katy Perry, an American pop star, sounded often at Hillary Clinton's campaign rallies but will shortly ring out over a less serious event: a late-night party in Shenzhen to kick off "Singles' Day", an online shopping extravaganza that takes place in China on November 11th every year.

The event was not dreamt up by Alibaba, but the e-commerce giant dominates it. Shoppers spent $14.3bn through its portals during last year's event. That figure, a rise of 60% on a year earlier, was over double the sales racked up on America's two main retail dates, Black Friday and Cyber Monday, put together.

Chinese consumers are still confident, so sales on this Singles' Day should again break records.

It points to an intriguing question: how will all of those purchases get to consumers? Around 540m delivery orders were generated during the 24-hour spree last year. That is nearly ten times the average daily volume, but even a slow shopping day in China generates an enormous number. By the reckoning of the State Post Bureau, 21bn parcels were delivered during the first three quarters of this year.

The country's express-delivery sector, accordingly, is doing well. In spite of a cooling economy, revenues rose by 43% year on year in the first eight months of 2016, to 234bn yuan ($36bn). And although the state's grip on China's economy is tightening, the private sector's share of this market is actually growing. The state-run postal carrier once had a monopoly on all post and parcels. Now far more parcels are delivered than letters, and the share of the market that is commanded by the country's private express-delivery firms far exceeds that of Express Mail Service, the state-owned courier.

China's very biggest couriers have been rushing to go public on the back of the strong growth. Most of them started life as scrappy startups, and are privately held. But because of regulatory delays, which mean a big backlog of initial public offerings, many companies have resorted to other means. Last month, two of them, YTO Express and STO Express, used "reverse mergers", in which a private company goes public by combining with a listed shell company, to list on local exchanges. In what looks to be the largest public flotation in America so far this year, another, ZTO Express, raised $1.4bn in New York on October 27th. Yet another, SF Express, China's biggest courier, recently won approval to use a reverse merger too.

But investors could be in for a rocky ride. Shares in ZTO, for example, have plunged sharply since its flotation. That is because the breakneck growth of courier companies masks structural problems. For now, the industry is highly fragmented, with some 8,000 domestic competitors, and it is inefficient.

One reason is that regulation, inspired by a sort of regional protectionism, obliges delivery firms to maintain multiple local licences and offices. Cargoes are unpacked and repacked numerous times as they cross the country to satisfy local regulations. Firms therefore find it hard to build up national networks with scale and pricing power. All the competition has led to prices falling by over a third since 2011. The average freight rate for two-day ground delivery between distant cities in America is roughly $15 per kg, whereas in China it is a measly 60 cents, according to research by Peter Fuhrman of China First Capital, an advisory firm.

A handful of the biggest companies now aim to modernise the industry. Some are spending on advanced technology: SF Express's new package-handling hub in Shanghai is thought to have greatly increased efficiency by replacing labour with expensive European sorting equipment. A semi-automated warehouse in nearby Suzhou run by Alog, a smaller courier in which Alibaba has a stake, seems behind by comparison but in fact Alog is a partner in Alibaba's logistics coalition, which is known as Cainiao. The e-commerce firm has helped member companies to co-ordinate routes and to improve efficiency through big data.

Other investments are also under way. Yu Weijiao, the chairman of YTO, recalls visiting FedEx, a giant American courier, in Memphis at its so-called "aerotropolis" (an urban centre around an airport) in 2007. He was awed by the firm's embrace of advanced technology. He returned to China and sought advice from IBM on how his company could follow suit. YTO is using the proceeds of its recent reverse merger to expand its fleet of aircraft, buy automatic parcel-sorting kit and introduce heavy-logistics capabilities for packages over 50kg.

There is as yet little sign that China's regions will begin allowing packages to move freely, so regulation will remain a brake on the industry. More ominously, labour costs are rising. There are fewer migrant labourers today who are willing to work for a pittance delivering parcels. This week *China Daily*, a state-owned newspaper, reported that ahead of Singles' Day, courier firms were offering salaries on the level of university graduates.

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