



# Taobao.com

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# Taobao.com – The Business of Online Shopping Platform

*(This case was written by Boyi Li, Lecturer in Entrepreneurship at the University of Exeter and based on his doctoral research)*

Taobao.com starts from a C2C platform for shopping. The company was established by Ma Yun (alias Jack Ma) and his team in Hangzhou city, China in 2003. Before Taobao, Ma Yun was already an icon of IT entrepreneur in China. He has been successfully running Alibaba.com since 1999<sup>1</sup>, helping domestic manufacturers find foreign procurement contracts and providing service for export industries. Taobao is among Ma's first attempts to find e-business opportunity in the market of domestic trade. Ma Yun and his Alibaba Group's strategic turn to the domestic market reflect his vision that the rise of Chinese domestic consumers in the next decades -- the urban middle class -- will reshape the growth model of Chinese economy.

The idea of Taobao.com was similar to eBay, which is creating a virtual market place and providing intermediary service connecting internet shoppers and sellers. In a fierce competition with eBay's Chinese subsidiary Eachnet, Taobao initially adopted free-service strategy, providing all free software tools for sellers and charging no commission fee on transactions. Taobao also differentiated itself from eBay by providing locally-customised tools to cater Chinese internet users' preferences <sup>2</sup>. Examples of such locally customised tools include the instant-message tools (Ali-Wang-Wang), virtual community (She Qu), credit-grade scheme (Xin-Yong-Ping-Ji), and an integrated escrow-based payment system (AliPay). Within a few years, Taobao quickly established itself

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<sup>1</sup> Alibaba.com has been list in Hong Kong Stock Exchange since 2007, with market capitalization about 1.5 billion USD. Alibaba.com is a member company of the Alibaba Group, which controls a number of major players in China's Internet business, such as the AliPay, Yahoo China, Ali-Cloud Service etc.

<sup>2</sup> The sudden success of Taobao in Chinese consumer market has raised serious concerns regarding the abuse of intellectual property by Taobao's individual sellers. It has been reported that some commodities that have been sold on Taobao platform either lack the legal authorization of distribution, or simply hold counterfeit trademarks. These concerns have not only been raised by Taobao's competitors, but also by the Chinese nati In our interview with Taobao, the senior executives of Taobao have relentlessly stressed that the company is committed to fighting with the abuse of intellectual property and counterfeit products, although some observers indicated that Taobao gained substantial initial advantage with its loose restrictions while eBay in China might be more strictly regulating the sellers.

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as the undisputed market leader in Chinese e-shopping sector<sup>3</sup>. In 2008, it is estimated that Taobao occupied 59 percent of Chinese C2C market. In 2010, the platform boasted over 170 million registered users, and an annual transaction volume of 400 billion RMB (roughly 40 billion GBP). The annual transaction volume (gross merchandise volume, GMV) exceeded 1 trillion yuan (roughly 100 billion GBP) for the year ended March 31 2013. According to the National Bureau of Statistics of China (NBSC), China's total retail scale of consumer goods in 2009 is 13,267.84 billion RMB, which means Taobao.com as a single marketplace is responsible for roughly 0.3 percent of China's total retailing market in 2009. Such a scale makes Taobao.com the dominant platform in China's internet shopping sector<sup>4</sup>. Such a scale makes Taobao the dominant platform in China's internet shopping sector.

### **Online Shopping Mall**

For general visitors, Taobao is a vibrant shopping community, the one-stop place where the experience of entertainment, fashion and bargain are mixed together. The platform imitates a physical shopping mall where lots of people not only do browsing and shopping, but also socialise in restaurants and coffee shops. In Taobao's virtual shopping mall, the scale is much larger -- millions of people actively visiting hundreds of thousands of shops 24 hours every day. Taobao catalogue lists twenty-four major market sections: virtual money and ticketing, consumer electronics, household appliance, women's fashion, men's fashion, children's fashion, women's shoes, men's shoes, underwear, luggage and bag, fashion accessories, jewellery and watch, cosmetics and beauty products, mother and baby, furniture and home decoration, household daily consumables, food and health, sport equipment, outdoor and camping, automobile and accessories, toys, stationary, hobbies pets and collection, local life service.

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<sup>3</sup> By saying e-shopping sector, I mean the Customer-to-Customer area (B2C) and Business-to-Customer (B2C) area. Taobao approached the e-shoppers by establishing C2C service first in 2004. However, many of the sellers on Taobao become so successful and quite-large business companies that since 2010, Taobao established a dedicated platform for B2C transactions - Taobao Mall (TMall). Sellers of TMall platform must be government-registered companies, instead of individuals, and held full legal/tax responsibilities for the product they sell.

<sup>4</sup> This is a rough calculation rather than a rigorous statistical analysis. We are fully aware that the 400 billion RMB annual transaction volume on Taobao platform could include a small proportion of sales occurring between business retailers, which are not counted as part of 'total retail scale of consumer goods' according to the definition of NBSC. In our interviews with Taobao company staff, we are informed that the Taobao platform does not encourage business-to-business sales and it does not seem reasonable for netpreneurs to buy and resale on the same Taobao platform, because the Alibaba Group has the another dedicated wholesale platform Alibaba.com to help netpreneurs find wholesalers and manufacturers with much lower price.

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Each market section is comprised of eight to ten sub-sections, which further contain increasing commodity categories. For example, the virtual money and ticketing section lists eight sub-sections: mobile-phone credits, online game credits, virtual game gadgets, flight ticket, QQ<sup>5</sup> special section, online game support, lottery, and travel package deals. Clicking each category leads to a list of shops offering the category of products. Buyers can filter the results by using various criteria such as credit grade, popularity, online seller, recent deals etc. The system may also suggest filters that are most popular at that time. Apart from regular catalogue and search, Taobao actively organises themed market sections -- such as the "Special Offer of the Day", "England Fashion Show", "Group Purchase Special", "Celebrity's Shops", "One Yuan Lucky Strike"<sup>6</sup> etc -- and advertise these themed-markets on its own homepage (ranked the world's 14th most popular website) or other major media spaces (television commercials, newspapers and magazines, outdoors, websites etc.). In short, Taobao visitors have multiple ways to access the shops, people, and products, either by searching, browsing, following advertisement or subscribing to themed activities.

Like other Web 2.0 platforms, Taobao platform is critically dependent on individual user's contribution of web content. The web content comes from both sides of sellers and buyers. On seller's side, Taobao provides software tools for building and maintaining online stores. Equipped with ready-made website builders (Wang Pu), sellers can select a few webpage models, styles and frameworks, and then supply updated and detailed information about the products or other information they want the buyers to know. Typical tasks of Taobao sellers include writing descriptions, uploading product pictures, setting prices for each product, and answering buyer's enquiries etc. To make their stores more attractive, sellers spend much time in 'decorating' their online pages, sometimes hiring professional website designers.

On buyer's side, users need to supply some personal information, such as postal address, ID number, payment information, product preferences and ratings etc. The platform provides search function and categories to help shoppers navigate in the system. The platform takes records of each registered user's browsing history, and

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<sup>5</sup> QQ is the largest online social interaction and game platform in China. The company that owns QQ is Tencent, listed in Hong Kong Stock Exchange. It starts from an instant messenger tool QQ and evolves into a comprehensive online virtual entertainment platform, covering games, virtual pets, gadgets, ringtone download etc. In 2012, QQ estimated that active members amount to 721 million.

<sup>6</sup> "One Yuan Lucky Strike", or in Chinese 一元秒杀 "Yi Yuan Miao Sha", is one of the most popular themes in Taobao. It is essentially an activity of "luck draw", in which a large number of buyers rush to buy a particular kind of commodity in a short period of time (in many cases, in seconds) and the system will determine that a few lucky buyers will get the commodity for one yuan. Taobao periodically advertise these themed activities in efforts to stimulate the shopping atmosphere in its community.

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makes recommendations based on user's accumulated viewing/buying history. Also buyers can keep and edit a personal list of stuff they like as they go around the shops, by clicking "adding to my album". These albums are categorised and themed by the buyers and can be made private or public. Those buyers who actively edit and publish their personal "albums" are generously rewarded with community-status-promotion (Fashion-Talent Badges or Chao Ren Xun Zhang) and shopping coupons<sup>7</sup>.

To encourage the sharing of shopping experience and information among buyers, Taobao's VIP Club has a set of rules to evaluate the contribution of buyers. The rating scheme of VIP status -- ranging from V1 to V6 -- takes into account not only historical shopping volumes, but also the contribution of "albums" in community. Highly ranked VIP members not only get discounts in Taobao stores, but also enjoy a number of other privileges, such as priority customer service, super-fast delivery or refund, and quick response from sellers as complaints from highly ranked VIPs are seriously handled by Taobao. When buyers browse online stores, they can chat with sellers (or the agents of sellers) using Ali-WangWang, make comments of each product or store, bookmark their favourite products, and subscribe to the stores they like. Both buyers and sellers keep a list of contacts in their Ali-Wangwang messenger, enabling them to chat whenever they would like to and develop long-term relationship. Taobao archives the chatting records generated by Ali-Wangwang, and claims a right to investigate these chatting content in cases that disputes occur between buyer and seller or fraud case is reported.

Bargain is a common practice in Taobao market. Instead of clicking "buy it now" or "bid" directly, buyers usually use Ali-Wangwang to talk directly with sellers and negotiate a price and specific terms and conditions that both sides are satisfied with (special requirements include delivery time and means, package decorations or other personal preferences). When a negotiated price is agreed, the seller sends a dedicated webpage -- which is automatically generated by store management tools -- to the buyer, who then checks and confirms the agreement. The buyer then either clicks the "buy" button on this dedicated page and goes through the AliPay system to further the transactions, or saves the deal page and comes back later before the deal expires. The sellers are keen to chat and provide additional service for buyers because they want to get a positive feedback. When a deal is finished, both buyers and sellers leave comments on each other's trade history page. A long trade

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<sup>7</sup> The dedicated page for buyer-generated information is published in Love.taobao.com. The channel is similar to Youtube or Twitter, where each member has their own tube for publishing and sharing their own albums while they get recommended by the system to those with similar favorites. Buyers subscribe to the channels that fit their tastes. The system's recommendation of products and friends gets more precise as the buyers share more information about their tastes.

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history, with detailed feedbacks of good points and bad points by the trading party, is regarded as the most important “reputation asset” in Taobao platform.

Trust is the top priority concern in virtual market places. Taobao platform designs a set of schemes and rules to make transparency a principle of practice. For example, each user has a publicly-accessible profile page, which lists key information about this user (username, credit-grade, regions, business sector, recent trades etc.). The extent to which these personal information can be accessible depends on the roles (buyer or seller) and the user’s tolerance of being open. Seller’s profile page usually displays information such as username, business certificates, credit grade, location, business sector, and most importantly transaction record. Taobao platform makes it a default rule that each seller’s profile displays all transaction histories on the profile page<sup>8</sup>. The transaction history gives detailed information such as buyer’s username, purchased product, feedback texts, and transaction time and date. Clicking each buyer’s username leads to the profile page of the buyer, where most buyers show off their recent purchase with pictures and links, as well as their microblogs and social networks (friends, follows, fans, tubes etc). Most Sellers also leave comments on buyers’ profile page so that the general public can know how this particular buyer behaved in previous deals.

To measure credit and reputation, Taobao platform has a scheme to measure credit history of each seller (or buyer) -- Credit Grade (Xin Yong Deng Ji). The index is calculated based on a double-blind feedback rating scheme. When a transaction is finalised, Taobao system sends a questionnaire to both buyer and seller, asking them to give ratings (a scale from 1 to 5 star) to five questions. The feedback rating is mandatory, as the system sets a default answer of positive rating of 5-star to each question. Based on the answers, the system adjusts the general credit grade (Xin Yong Deng Ji) and the percent of positive feedback (Hao Ping Lv), which is displayed as the important sign of “reputation” on the top of each user profile page. It is the system’s rule that the raw results will not be seen by the subject individuals under evaluation. The credit grade and trade history subsystem is probably one of the fundamental schemes to ensure Taobao’s transparency principle. As the credit grade and trade history acts as the de facto “trademark” of sellers, Taobao platform has to deal with a large number of disputes and complaints regarding the authenticity of these user-generated information. The company employs

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<sup>8</sup> Since trading history is publicly accessible, the risk of online scams can be traced and therefore controlled. For example, one of the most popular scam is to inflate the Credit Grade in a short period of time -- Credit Inflation or *Shua Zhuan*. By creating fake transactions, the credit inflation scam gives the seller an opportunity to upgrade their credit grade level to the “Diamond” in a short period of time. However, this kind of ‘illegal’ business is easy to detect, because the transaction record is normally corresponding to the payment information collected by Alipay system, which means those deals without compatible Alipay records are suspicious and subject to Taobao’s further investigation.





thousands of customer service staff working 24/7 to ensure that these disputes and complaints are properly dealt with and the authenticity of these credit and history data is guaranteed.

To ensure a high level of transparency, Taobao system actively collects user-generated data, compute and remix these data in various ways. The credit grade is a good example of using such user-generated data. Another example is that Taobao systems collects and analyses the business performance data of sellers (trade volumes, frequency of orders, price fluctuation, visitor popularity etc.) and makes sense of these data sector by sector. For instance, on each seller's profile page, three key performance index are required to be displayed publicly: Precision of Description (Miao Shu Xiang Fu), Service Attitudes (Fu Wu Tai Du), Speed of Delivery (Fa Huo Su Du). Each performance index (a scale of 1 to 5) is calculated based on customer feedback rating and real-time operation data recorded by Taobao system. Moreover, these index are displayed in a graphic scale featured with the position of the benchmark of industrial average (Yu Tong Hang Bi) -- another system-generated index. Similar schemes of data collection and analysis are also applied to the buyer's side.

Taobao employs an army of staff to provide "notarial" service for business accounts. Getting Taobao's official verification and certificates are important for sellers, because to promote sales they need to convince potential customers that they are trustable. Taobao provides various kinds of certificate service, ranging from ID verification, business license verification, credit card acceptance, to the third-party quality check. Once sellers get certified by Taobao (or its external partners), their profile pages will be featured with a particular badge, so that buyers will be informed as soon as they enter the shop. Moreover, Taobao system makes it possible that when buyers search specific products, they can always filter the results to those sellers who have particular Taobao certificates. Table 5.1 lists some examples of certification service that are popular on Taobao platform.

Name	Badge	Meaning
Golden Seller		1. Quality Assurance; 2. Highest Evaluation Credits; 3. Quick Service; 4. 7 Days No Reason Return
Consumer Protection Scheme (CPS)		1. 7 Days Guaranteed No Reason Return; 2. Less than 24 Hours Despatch; 3. No Counterfeit Guarantee; 4. 30 Days Free Repair Service; 5. The Third-Party Quality Check (Optional)

Name	Badge	Meaning
ID and Bank Account Verified		Personal ID checked, Bank Account verified, and Alipay registered
Quality Check Certificate		Product Quality Standard Guaranteed by a third-party.

**Table Error! No text of specified style in document.-1 A list of Certified Badges on Seller's Profile Page**

### Advertising: Commoditizing Connections and Flows

As a company, Taobao makes profits mainly by charging search-related advertising fees. With most of its service free of charge, the company has a search-advertising service available for store operators ('Zhi Tong Che', translated as the Express Train Service), providing customized web advertising opportunities for netpreneurs<sup>9</sup>. Imitating Google's strategy, Taobao has been trying to gather as much websites as possible under its Taobao Advertising Alliance (TAA), in efforts to maximize the range of web spaces that are available for Taobao ads. Taobao's ad service mechanism is very similar to Google's AdWords and AdSense. The Express Train Service (ETS) is Taobao's version of "AdWords", enabling netpreneurs and other business owners to buy key words in search results as well as featured ad spaces on web pages, with auctioned prices (pay-per-click, PPC). TAA is similar to Google's AdSense, providing an advertising market platform where ad space providers can customize the ad content and forms while those ad buyers (mainly netpreneurs) offer competitive commission rates to attract the best ad providers. In short, Taobao, aspiring to be not only a shopping mall but also a leading internet advertising company, has been ambitious and aggressive in developing the new media space in China, making itself a direct

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<sup>9</sup> Like Google, the keyword search results on taobao platform have two rankings for display, one is the paid-for-search result whose position is auctioned by bidders, the other is the organic page ranking calculated on several key measurements such as relevancy, page views, store reputation, transaction volume etc.



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competitor not only with eBay, but rather with search engines giants such as Google, Baidu, and Yahoo<sup>10</sup>, and those new media giants such as Facebook, Tweeter, and Youtube<sup>11</sup>.

### **Platform Strategy**

“Eventually, we become an utility company in e-commerce world, we specialize in supplying ‘water’, ‘electricity’, and ‘gas’ for e-commerce companies.”

-- Song Fei, Strategy Manager, Alibaba Group

Since 2009, Taobao company began to implement what it branded as “the big taobao” strategy (大淘宝战略), aiming to consolidate its current service architecture and make the system an “open” platform for external partners. A central task of this strategy is to publish a set of technology standards (programming language, API library, SDK etc.) and a centralised application market. The new Taobao technology standards enable external partners to quickly develop applications (apps) that are compatible with Taobao system. The centralised application market (“fuwu”, fuwu.taobao.com) is the place where external partners deploy apps and make them available for customers. Apps are stored and operated in Alibaba’s cloud (Ali-Cloud-Computing), and therefore are fully integrated into Taobao’s current service architecture.

With standardized technology interface, developers are able to combine Taobao’s sources codes and data with their own specialties, and deliver innovative service in a manner of SaaS (Software-As-A-Service). Following the open strategy of those internet platform giants like Google and Apple, Taobao aims to nurture a vibrant community of developers and the-third-party service providers, so that users have the capacity to enrich and customize their own experience in Taobao systems.

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<sup>10</sup> In a series of complex financial deals, Alibaba Group, Taobao’s parent company, has successfully acquired Yahoo China in 2008, at the cost of 40 percent of the Group shares controlled by Yahoo. For taobao, the acquisition of Yahoo’s cutting-edge search technology has critically strengthened its leading position in Chinese internet searching market, which forms the fundamental basis for the company’s advertising strategy.

<sup>11</sup> In China, due to the widely-known media regulation policies, these new media giants have their Chinese local copycats. For example, Renren.com and Kaixin.com are Chinese versions of Facebook, while Weibo.com is a counterpart of Tweeter, and Youku offers similar video-sharing service like Youtube. This situation is probably good for Taobao’s ambitious strategy, because comparing to those international giants, the whole Alibaba Group is in a better position with enough financial capacity to control these local media service providers, or make them to build collaborative relations with Taobao.

There are generally two categories of apps in Taobao's *fuwu* (meaning service) market: for buyers and for sellers. Apps for sellers provide enhanced functions for managing daily operations of online shops and analyzing customer's shopping behavior, while apps for buyers provide rich experience of shopping guide, credits and discounts or other service. Apps are also available for mobile devices. Service providers come from a wide range of background industries. Some are management or accounting software companies, while some others are specialized in e-business consulting or data analytics techniques. Still other developers come from the background of marketing & SEO consultants, web designers, voucher & discount dealers, specialized quality control agency (QC), and BPO (Business Process Outsourcing) providers etc. To ensure a high standard of service quality, Taobao company quarterly assesses the service quality of the third-party providers -- with specified standards customized to each market section -- and publish the assessment results to the public.

With such software service architecture, Taobao is set to become the infrastructure service provider for e-commerce companies, particularly SMEs. This strategic turn means that Taobao's service actually stretches outside the Taobao.com domain and becomes an open-end network of e-commerce process. To the extent that such network of processes could potentially dominate Chinese e-commerce industry and present a common industrial standard of e-commerce, Taobao is ambitious to be the maker of industrial standards. Jack Ma had a famous claim by paying tribute to the success of Intel: "I dream one day when every e-commerce company runs Taobao-Inside."

## Services on Taobao Platform

Taobao platform services	Description
Taobao Shop Management (Wang Pu)	SaaS tool that enables netrepreneurs to manage their shops, such as creating new product page, writing product descriptions, uploading pictures, setting prices.
Order Management	SaaS tool that handles customer orders, such as checking stock availability, sending order confirmation, producing delivery order and tracking order progress.

Taobao platform services	Description
eTao search engine	Search engine for comparing prices
Alipay	Third-party online payment service
Aliwang-wang	Instant-messenger tool
Express Train Service	Search word auction for advertisers, like Google's AdWord.
Taobao Advertising	Web-ad market where website owners and netpreneurs meet, negotiate and customize ad contents and prices, like Google's AdSense.
Credit Rating	The Taobao system automatically calculates each shop's level of credit based on the shop's accumulated behaviours such as the frequency of orders, customer satisfaction ratings, and compliance to online good conduct rules.
TrustPass (Cheng Xin Tong)	Alibaba certification of business enterprises. It requires some detailed government and professional qualifications, and is based on online business transaction records within Alibaba platforms.
Taobao Forum	Online community taking the form of discussion board, sharing life experience and entertainment information. Many local e-Business associations have their virtual webpage in this forum.
DataCubes	Subscription-based data analytics service producing market-transaction-based data mining.
Blogs and Magazines	Wiki-style of blog-writing. Taobao's industry-focused team routinely organize leading netpreneurs to publish their business stories, and to collectively edit shopper's guides and articles on new techniques among netpreneurs.
Circles and Groups (Quanzi, Bangpai)	Social-network-service similar to Facebook, which enables netpreneurs (and shoppers) to have personal pages displaying lists of friends.

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Taobao platform services	Description
Accounting and Management Software Service (Qian Zhang Gui, meaning MoneyManager)	SaaS tools free for netrepreneurs on Tabao platform. Taobao provides also a software market platform for third-party developers.