CREDO WEALTH

The curious case of Jack Ma

In October 2020, days before the planned IPO of Ant Financial which is set to be the biggest in history, Jack Ma, co-founder of Alibaba and controlling shareholder of Ant, gave a speech at the Bund Summit in Shanghai. Despite the presence of the Vice President of the People's Bank of China, Ma took aim at China's financial system, or lack thereof, as he determined. He also targeted the regulatory system accusing it of stifling innovation and described Chinese banks as having a "pawnshop mentality". Then, in early November, Chinese regulators suspended the planned IPO, and in December announced an antitrust investigation into Alibaba in addition to the ongoing broader regulatory review. Jack Ma disappeared from public view. Since then, Alibaba's share price has undergone a sharp correction, and despite the re-appearance of Ma after nearly three months, sentiment has not fully recovered.

A former English teacher, Jack Ma founded Alibaba in 1999, with Softbank investing $20m just one year later. His rags to riches story has helped turn him into one of China's biggest celebrities and it is hard to overstate just how popular and influential Ma is. It is also difficult to find an accurate comparator in the Western World, the closest perhaps being Elon Musk. At an Alibaba annual party, he previously appeared on stage dressed as Michael Jackson sat astride a huge motorbike and performed a lengthy dance routine in front of 30,000 Alibaba employees. Videos online also show him singing on stage in packed stadiums and he has starred in his own Kung Fu movies. He is a Communist Party (CCP) member, who regularly appeared alongside China's top leaders and has also acted as some kind of unofficial ambassador, meeting with US President Trump in 2017. Since stepping back as Executive Chairman in 2019, Ma has focussed on philanthropy, with projects including promoting entrepreneurship in Africa, in keeping with China's Belt and Road initiative. And this reach perhaps goes some way to explain the apparent force of the crackdown by the CCP. Although it may be simplistic to place sole responsibility for events on Jack Ma's shoulders, indeed, there have been rumours that the crackdown on Ant may have been related to the ultimate benefactors of the IPO and their political standing; there is a broader correlation with a wider crackdown of dissenting opinion ongoing in China.

As is the case of any political event, it is important to assess what the ultimate impact may be on a company's business and its ability to operate. Whilst we recognise the risks, we also believe that the overall goal will not be to destroy the company which had been so celebrated as a success story of China. Alibaba's business fits in with the CCP's broader goal of transitioning the country towards a consumption and services led economy, which requires continued growth in household expenditure. In addition, the practices which the regulators have specifically taken issue with are not new. For some time, businesses have complained about a practice known as "1 of 2" where large platforms have leveraged their market power to force merchants to commit to not selling on competitor's platforms. In fact, there are a number of ongoing cases against most major internet platforms pertaining to exclusivity. ▶▶

On the 7th February 2021 the State Administration for Market Regulation released the official guideline for Anti-Monopoly Rules, which followed the published proposed revisions in November 2020. The rules seek to define things such as relevant markets and market dominance for the purpose of identifying monopolistic behaviour along with establishing the key metrics for identifying whether horizontal cooperation is taking place. Crucially, the law and regulation applies across all industries and appears to allow sufficient leeway for businesses to still be able to effectively compete, particularly on price. Alibaba's management have been cooperating and proactively communicating with the authorities and they expect the impact of the regulations to be manageable. Although the anti-trust investigation is ongoing, expectations are for a manageable impact on Alibaba's finances and operations. Management have explicitly stated that they have limited exclusivity agreements with some merchants, mainly around significant spending holidays.

Whilst we recognise that there are risks, we believe that at the current valuation we are being more than compensated. China continues to represent a highly attractive market with its middle-class cohort of 400 million consumers is expected to almost double over the next 10 years. Additionally, rising public wealth and disposable income will help to fuel continued growth. They say a rising tide lifts all boats and we see Alibaba's e-commerce operations continuing to benefit from this trend. With regards to the Cloud segment, which recently became profitable, we see additional positive optionality for the stock. China's Cloud market is still in its early stages, with spending on Cloud infrastructure representing around 3% of GDP, compared to ~6% in the US. Ultimately, we do not believe that the regulatory changes will impair Alibaba's business operations and outlook. Although in the short term, we may be exposed to some volatility, we believe that this remains a great business and therefore we see attractive reward versus risk trade-off at the present time. ■

Important notice