

9th October 2023

Indonesia's e-commerce regulations: Good for GoTo and Shopee; not good for TikTok

On 26th September 2023, the Indonesian Ministry of Trade announced new regulations for e-commerce activities. These regulations included 1) prohibiting any e-commerce activity on social media platforms; 2) restricting the sale of imported goods by e-commerce companies; and 3) banning e-commerce companies from selling goods or services manufactured by themselves. A grace period of seven calendar days was provided to accommodate the transition.

After GoTo's IPO in April 2022, we published a report on the company and the headwinds it was facing. As a reminder, GoTo is an Indonesian company that provides e-commerce, ridesharing, and food delivery services. GoTo is the result of the merger of two household names in Indonesia, Gojek and Tokopedia. E-commerce represents approximately 50% of GoTo's revenues.

GoTo's e-commerce division grew immensely since its founding in 2009 and up until the Covid era: Their Gross Merchandise Value (GMV) grew at an annual rate greater than 50% during the Covid years. GMV refers to the dollar value of all the goods and services traded in e-commerce platforms. The platforms (also known as "third party" or "3P e-commerce" companies) charge merchants a take rate on the GMV to generate revenues. This is different from "first party" or "1P e-commerce" companies that own the inventory they sell. GoTo is a 3P e-commerce company.

Another large e-commerce player in Indonesia and across Southeast Asia is Shopee. Shopee is a Singapore-based e-commerce company that was first launched in 2015 in Indonesia, Singapore, Malaysia and Thailand. It is part of the SEA Group which also has businesses in gaming and fintech. Since its launch, Shopee took Indonesia by storm, growing spectacularly because of heavy and savvy advertising in what was at that time an underpenetrated e-commerce market. E-commerce penetration in Indonesia in 2015 was around one percent only. Shopee which had the backing of large investors including Tencent was perfectly positioned to succeed. In terms of market share, GoTo and Shopee today each has around 35% of the total GMV traded through Indonesian e-commerce

platforms. Shopee is popular for fashion and beauty shopping in Indonesia whereas GoTo's focus is on electronics.

However, as Covid started dissipating, e-commerce in Indonesia started suffering. The push by Shopee and GoTo increased the penetration of e-commerce in Indonesia to around 20% of total retail sales, on par with the UK. It meant that incremental growth was harder to come by, especially as people started going back to offline retail in a post Covid world. Profitability has always been an issue for these companies given the stiff competition as spending on ad costs and pressure on merchant take rates make it hard for these companies to be profitable. All these meant that post Covid, the high growth rates of the previous years could not be sustained, and incremental growth was coming at very low profitability. Investors were getting frustrated, and the stock prices of GoTo and SEA Limited came under significant pressure. At their peak, SEA and GoTo reached market capitalisations of \$200bn and \$33bn, respectively. Those capitalizations are now down to \$23bn and \$6bn, respectively.



Source: Bloomberg

In 2022, SEA Limited embarked in a cost-cutting spree, prioritizing profitability versus growth. SEA ceased operations in India and laid off 7,500 people globally. Business-class flights were banned, daily meal expenses and hotel stays were capped, and snacks disappeared from offices. The company even replaced local luxury tea brand TWG with the cheaper brand Lipton for tea provided in offices GoTo followed a similar path: The company laid off 1,300 people in late 2022 and 600 more in 2023.

Shopee and GoTo's grievances in Indonesia were magnified by the entry of TikTok into Indonesia. TikTok is the hugely popular social media app developed by China's ByteDance of China for use outside of China (it has another platform for mainland China – Douyin). TikTok quickly became a cultural phenomenon in Indonesia the same way it did around the world. Indonesia is today TikTok's second largest market with 125 million users.

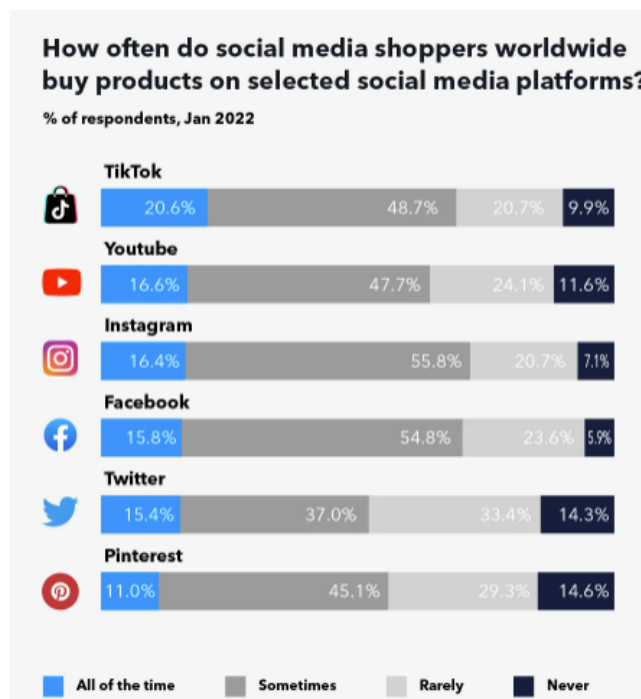


A TikTok influencer

TikTok introduced TikTok Shop in Indonesia in 2021. TikTok Shop is an immersive shopping feature within the TikTok app. It enables merchants, brands, and creators to showcase and sell products directly on TikTok's platform through various formats such as

in-feed videos and product showcase tabs. TikTok Shop has been growing immensely. It enabled ‘influencers’ – people with a big social media following – to promote brands to a large group of loyal customers. ByteDance, the company behind TikTok, does not publish its numbers. Despite this secrecy, it is clear that the company remains to this day in a high growth mode. It has adopted an aggressive stance in Indonesia by charging a two to three percent merchant take rate when GoTo and Shopee both charges upwards of five percent.

By 2022, TikTok had become a behemoth in the global online purchasing space:



Source: *Bazaarvoice*

Fast forward to September 2023, and the Indonesian government started floating plans to regulate e-commerce on social media. The reason given was to protect small businesses. The government narrative was that small “mom and pop” stores in Indonesia are suffering given TikTok’s low merchant take rates and predatory pricing. However, the Indonesian government failed to back up its narrative with any market analysis. No data was published, and no explanation was provided to support the government’s claims.

Many local brands were actually selling items through the TikTok Shop app. TikTok, which had announced last June that it would invest \$12.2m in Indonesia to help more than 120,000 small and medium enterprises transition their businesses online, was understandably angered but agreed to shut down its local e-commerce platform.

There is also a narrative that the new Indonesian regulation contained nationalistic undertones given the restrictions on the sale of imported goods through e-commerce platforms and given the Chinese origins of TikTok.

This news served as a temporary respite for Shopee and GoTo which badly needed it: The SEA results for the second quarter of 2023 dealt another blow to the company. While the company improved margins, GMV growth of 20% YoY was below analysts' expectations. The company also announced that going forward it would focus once again on growth at the expense of profitability at a time when the e-commerce sector in Indonesia saw its growth dwindle to less than 15% YoY.

Overall, we remain cautious about the e-commerce sector of Indonesia. Penetration is high, companies are in restructuring mode and their focus on growth for the sake of gaining market share is hitting margins once again. In addition, competition is heating up again: Pinduoduo, another major Chinese e-commerce platform, is considering entering Indonesia. There is also a possibility that TikTok will set up a standalone e-commerce entity to reenter the country and circumvent the recent regulations that prevent the company from using its social media platform as a conduit for e-commerce. As the latest set of government measures show, the sector is not immune to regulations, if not nationalism.

Sources: Bloomberg, Goldman Sachs, Tech in Asia, TechHQ, Channelengine, Bazaarvoice, Business Insider, CNBC Indonesia, The Jakarta Post

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