Retail consumption remains a key driver of economic growth in China, with an increasing number of consumers turning to their smartphones and apps to purchase goods and services. Digital payments are on the rise, with technology companies and other non-banks disrupting the retail industry by offering secure and easy-to-use e-wallets and payment solutions to their users.

In this article, we analyse how technology platforms and apps such as Alibaba’s Alipay and Tencent’s WeChat Pay are reshaping the payments landscape in China, and the subsequent impact this is having on banks and consumers. We also discuss whether other viable competitors to Alipay and WeChat Pay could emerge as challengers in the payments space.

The payments landscape in mainland China

While banks play a major role in payments in other jurisdictions – including as issuers of credit cards – rapid technological development in mainland China has seen the country leapfrog credit cards, with consumers shifting from cash directly to digital payments via e-wallets and mobile apps.

According to data from the People’s Bank of China (PBOC), the value of mobile payments in China hit RMB 277.4 trillion in 2018, an increase of 36.7 percent from the previous year and more than 12 times the total value recorded in 2014 (see Figure 1). Meanwhile, the transaction volume of mobile payments in China reached 60.5 billion in 2018, an increase of 61 percent from 2017 (see Figure 2). The volume of mobile payments growing faster than total value implies that consumers are using mobile payments for increasingly smaller transactions.

Data from the first quarter of 2019 also indicates that this upward trend is set to continue throughout the year. Total mobile payment transaction volume increased by 80 percent year on year to 19.7 billion in the first quarter of 2019, with the total value increasing by 22 percent year on year to RMB 86.6 trillion.

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Alipay and Tenpay (a combination of WeChat Pay and QQ Wallet) continue to be the dominant players in the market, with a combined market share of more than 90 percent in terms of transaction volume (see Figure 3). While other payment platforms such as 1Qianbao, Union Mobile Pay and JD Pay are also increasing their overall transaction volume, they still maintain only a small share of the overall retail payments market.

**Figure 3: Share of main players in China’s mobile payment market by transactions in 2018**

![Chart showing share of main players in China's mobile payment market by transactions in 2018.

Source: iResearch Global Group

With Alipay and Tenpay commanding the lion’s share of China’s retail payment market, could other players such as banks or other technology platforms compete in this space? One way to assess potential competitors could be to look at the businesses that have a sizeable and increasing number of users on their apps and platforms. WeChat for example, had 1.13 billion monthly active users as of the second quarter of 2019, while Alipay and its affiliated e-wallet partners have more than 1 billion annual active users worldwide.

Using active users as an indicator of success, Meituan Dianping could become a potential competitor if it was to actively focus on payments. The company’s diversified service categories and growing number of use cases – linking food delivery, restaurant booking and hotel booking – have helped it significantly increase its number of users, as well as their transaction volume and frequency.

Annual Transacting Users (users that paid for transactions of products and services on the platform in a given period) on Meituan in the last 12 months ended March 31, 2019 grew by 26.4 percent to 411.8 million from 325.8 million for the 12 months as at the end of March 2018.

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3. Meituan Dianping’s 2019 Q1 Results, http://is.aastocks.com/20190523/003507205-0-PDF
Ride-hailing services operator Didi Chuxing (DiDi) also stands as a potential competitor in the retail payments space. The company has grown its consumer base significantly in the last few years – including through its acquisition of Uber’s China business in 2016 – with its app serving 550 million users.1

<table>
<thead>
<tr>
<th>Platform</th>
<th>Number of users (million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alibaba*</td>
<td>&gt;1,000 (1)</td>
</tr>
<tr>
<td>Tencent**</td>
<td>1,130 (2)</td>
</tr>
<tr>
<td>Didi Chuxing</td>
<td>550</td>
</tr>
<tr>
<td>Meituan Dianping</td>
<td>411.8 (3)</td>
</tr>
<tr>
<td>JD</td>
<td>321.3 (4)</td>
</tr>
<tr>
<td>Baidu***</td>
<td>188 (5)</td>
</tr>
<tr>
<td>Toutiao</td>
<td>172 (6)</td>
</tr>
</tbody>
</table>

Notes:  
*Alipay and affiliated e-wallet partners  
**WeChat and Weixin  
***Baidu App  
(1) Annual Active Users (as of March 2019)  
(3) Annual Transacting Users (as of March 2019)  
(5) Daily Active Users (as of June 2019)  
(2) Monthly Active Users (as of June 2019)  
(4) Active customer accounts (as of June 2019)  
(6) Monthly Active Users (as of March 2017)

Source: Alibaba; Tencent; Meituan Dianping; JD; Baidu; Didi Chuxing; China Internet Watch

Competitive advantages for technology platforms

A key to Tencent and Alibaba’s continued success has been their ability to seamlessly integrate and immerse their platforms into a number of daily activities such as shopping, travel and hotel booking, ride hailing, food delivery and booking doctors’ appointments. Other platforms such as Meituan and DiDi have also been able to successfully create an ecosystem through their apps, offering a growing number of use cases for their users. Meituan’s 2018 annual report notes that the company was able to acquire users cost-effectively through cross-selling, for example by converting their food delivery and in-store dining transacting users to hotel booking and other lifestyle services.6

It is this ability to meet consumer demands for greater speed, flexibility and personalisation that is seeing these technology players filling the customer experience gap that traditional banks are not. KPMG analysis finds that in mainland China’s financial services sector, mobile payments platforms operated by fintech companies delivered the strongest customer experience, ahead of traditional banks.6 We believe that ‘super apps’ – which essentially serve as a single portal to a wide range of virtual products and services – or platforms are posing threats to traditional banks, disintermediating banks from their customers, using a vast wealth of data to deliver better services and building their brand reputations in financial services.7

This presents a challenge for banks, especially in mainland China where a recent KPMG report on customer insights finds that China’s consumers are more prepared to entrust their information to technology companies than any other group of consumers worldwide.8

Another competitive edge for Alipay, WeChat Pay and other new technology players over traditional banks in the retail payments space is their ability to easily tap into consumers in second and third-tier cities in China and get them connected to their apps and platforms. In fact, Alibaba noted in their fiscal year 2019 report that more than 70 percent of the increase in annual active consumers was from less developed cities.8 Similarly, Meituan noted in its annual report that lower-tier cities are a major growth driver and a key part of the company’s overall strategy for its service offerings.

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The payments landscape in Hong Kong

Hong Kong’s third party payment market is not as advanced as in mainland China, but transactions are expected to become increasingly digital over time as stored value facility operators expand their presence in the market and partner with more merchants and retailers. However, despite an increasing number of vendors and merchants now accepting payment options such as Alipay and WeChat Pay in Hong Kong, the market remains highly competitive due to the high penetration of the Octopus card and credit cards in the city.

In addition, the introduction of virtual banks in Hong Kong – with eight new players set to launch this year – is changing the competitive landscape and challenging the traditional banking model, including payments. In the initial stage following their launch in Hong Kong, we expect that virtual banks will likely focus primarily on attracting deposits and payments capabilities. Due to lower transaction costs, they will likely offer more competitive savings and fixed-term deposit rates than traditional banks.

Virtual banks could also seek to introduce new and innovative products for consumers. For example, we are starting to see ‘buy-now, pay-later’ platforms being introduced in other jurisdictions – such as Afterpay in Australia – where consumers can make a purchase and then repay via instalments, but with no interest or other additional charges. Instead, these new platforms charge the merchants a commission on the value of the transaction. This emerging model is starting to threaten the influence of credit cards and other forms of credit, where consumers traditionally have to pay additional fees.

Cross-border payments

The ability to offer seamless cross-border payments between mainland China and Hong Kong, as well as with the rest of the world is becoming increasingly important, especially given the proliferation of payments providers in the region. This is further underscored by national policy initiatives such as the Greater Bay Area (GBA) which promotes close cooperation between Hong Kong, Macau and nine cities in Guangdong Province to create a globally competitive, world-class city cluster. This is no small opportunity. In 2017, the total remittances mainland China received from other jurisdictions was USD 63.9 billion, of which USD 15.5 billion came from Hong Kong (see Figure 4).

Currently, Hong Kong users of payment providers such as Alipay and WeChat Pay are only permitted to make payments in mainland China if they have a bank account in the mainland. This opens up a potential significant first mover advantage for banks that are able to offer an effective platform for cross-border payments to their customers. Bank of China (Hong Kong) has been an early mover, launching its e-wallet BOC Pay app in December 2018 to enable its Hong Kong customers to make mobile payments in mainland China without the need to have a bank account there.

Figure 4: Total remittances mainland China received (USD bln) from other jurisdictions in 2017

Source: Financial Times
A challenging market for new payment service providers

While new technology platforms and apps continue to emerge in mainland China, they are likely to face additional challenges if they choose to compete in the retail payments arena. First, market players need to obtain a payment service licence from the PBOC to operate in mainland China. The PBOC has not approved any new payment service licences since 2016, maintaining strict control over new entrants. Meituan obtained a mainland China payment licence in late 2016 through the acquisition of third party payment company Qiandai.com. The PBOC has also taken steps to strengthen financial risk management and improve transparency of third party payment providers, which will increase regulatory scrutiny and costs not just for new and smaller players, but also for Alipay and WeChat Pay.

Furthermore, in January 2019 the PBOC introduced new measures requiring all third party payment providers to place their customers’ funds with the central bank. Under the new measures, the PBOC does not pay interest on the funds, thus eliminating the interest income that the third party payment companies previously used to earn from investing these funds. This is likely to have a downward impact on the margins of these companies, and could result in some of the smaller players exiting the payments market unless new sources of revenue are found. Whether these developments offset the advantages third party payment platforms have in the market over their traditional banking peers remains to be seen.

Third, customer stickiness is relatively high when it comes to the incumbent platforms and payment providers, which could make it difficult for new entrants to entice customers to switch to their apps and platforms on a large scale.

While we have highlighted some players that could potentially challenge Alipay and WeChat Pay in the payments market over time, the question also remains as to the extent that they have a desire to compete in this space, especially given the low margins on offer compared to other areas like lending. Instead, the easier route could be for emerging platforms and apps to partner with the leading providers. In fact, Meituan and DiDi both offer their services through the WeChat platform – while customers may use their platforms and apps on a daily basis, the end payment will be made through WeChat Pay. This allows these technology platforms to leverage the large user base of the likes of WeChat to sell their services without having to absorb high transition costs related to converting consumers over to their own payment channels.

What does this mean for banks?

It is clear that the trend is shifting from bank payments to non-bank payments – and from cash to non-cash transactions – not just in mainland China and Hong Kong, but also worldwide. In the payments ecosystem, banks typically generate revenue through handling and processing fees through the issuance of debit and credit cards, as well as by facilitating payments for merchants. However, the rise of new non-bank tech payment platforms is taking these sizeable revenues away from banks.

However, banks still maintain some advantages over their competition. First, many have longstanding relationships with their customers. While some may use other payment apps as a secondary option, many consumers may still prefer to park their savings and investments with their bank. In Hong Kong credit cards continue to be popular, with the total number of credit cards in circulation reaching 19.49 million by the end of the first quarter of 2019, representing a 0.2 percent increase from the previous quarter and a 2.6 percent increase from the previous year.¹¹

Banks continue to actively work with merchants and payment network providers to offer attractive loyalty programmes and credit card rewards, all for the benefit of the consumer. Given the popularity of credit cards in Hong Kong, it may take longer for consumers to shift completely – if at all – towards third party payment platforms.

With the proliferation of digital payments in China, both banks and technology companies continue to amass a wealth of customer data via their payments platforms and apps. We expect to see increasing competition in this space, with a key focus on the ability of these players to best leverage their data for the benefit of their customers.

Many technology companies have a comparative advantage of having built their services around their customers and designed digitally-enabled systems from scratch, while some traditional banks continue to struggle with legacy systems. However, banks also have a large amount of data from cardholders, as well as in-depth transactional and unstructured data as a result of their longstanding relationships with many of their clients. We believe that the organisations that are able to best leverage their customer data – including through the application of real-time predictive analytics – to provide compelling, personalised and seamless experiences and services for their customers will emerge as the long-term winners in the payments space.