

ECONOMY

How e-commerce is making China's deflation even worse



No company embodies China's deflationary moment quite like Pinduoduo and shoppers flock to the app for its staggering discounts, the result of its unyielding push to lower prices. QILAI SHEN — THE NEW YORK TIMES

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When Lin Yunyun started selling diapers two years ago on Pinduoduo, China's fast-growing e-commerce site, she was not prepared for the relentless nagging about prices.

Pinduoduo, popular among Chinese consumers for its discounts, sent "reminders" whenever other sellers dropped their prices below hers. When Lin cut her prices, the site would temporarily promote her products — only to warn her a few days later that more reductions were needed for the site to continue driving customers to her goods.

"The platform keeps reminding me to lower prices," said Lin, 28, who lives in Zhangzhou, a city in southeastern China. "If I cut my price any more, I won't make any money."

No company embodies China's deflationary moment quite like Pinduoduo. Shoppers flock to the app for its staggering discounts, the result of its unyielding push to lower prices. As the country's second-largest online retailer, it is the shopping destination of choice for those who embrace so-called downgraded spending — a social-media fueled maxim of Chinese consumers' penny-pinching ways.

Rattled by a real estate crisis with no end in sight and a faltering labor market, Chinese consumers are spending less and saving more. Prices are falling, and profits are shrinking. Companies are hesitant to hire more workers or invest in the future, fueling even more concerns about the economy.

After a series of half-measures that have failed to reinvigorate the economy, Beijing has finally signaled that it is ready to take more aggressive action, although it's unclear how far it is willing to go. Late last month, the government announced interest rate cuts and other initiatives to revive the property market, as well as steps to prop up stock markets.

And despite hints of additional fiscal spending to put more money into the hands of Chinese consumers, the government has not revealed any specific plans. Rhodium Group, a research firm, said in a note that policymakers had demonstrated more willingness to act on the economy, but deflationary pressures were among several important issues that remained unresolved.

China's gross domestic product deflator, an economic indicator that measures prices broadly across the economy, has contracted for five straight quarters, the longest downturn in a quarter century. Ultimately, this means that the economy may not be growing as fast as the main GDP figure — targeted by Beijing to increase by about 5% this year — would suggest.

The government had directed most of its policy focus on supporting production and investment. While this has kept Chinese factories humming, it has left the country and its global trading partners awash in excess goods. An abundance of supply is helping to keep prices low.

And that's where Pinduoduo comes in. Because a growing portion of spending in China is happening online, price reductions by the app and other e-commerce platforms copying its success have contributed to a deflationary downturn. About 60% of the country's consumers buy through e-commerce, accounting for more than one-third of all retail spending, according to HSBC. *

"Pinduoduo is both the consequence and cause of deflation," said Donald Low, a professor of practice in public policy at the Hong Kong University of Science and Technology.

Founded in 2015, Pinduoduo has grown more quickly than its more established rivals, recently expanding abroad with its Temu brand. In its most recent quarter, Pinduoduo said revenue had risen 86%. It warned, however, that future profits might take a hit because it planned to invest heavily to support "high-quality" merchants.

Colin Huang, Pinduoduo's founder and one of China's richest men, has said that one of the company's core values is not to sell cheap products, but to offer goods that customers will feel are less expensive than they should be.

This year, Lin said Pinduoduo had enrolled her in an "automated price tracking system" to allow the company to lower the price of her diapers whenever it detected similar products available for less. A

few months after she opted out of the program, she discovered that the setting had been turned on again.

Pinduoduo, which did not respond to requests for comment for this article, has said that this feature helps to improve the "operating efficiency" of merchants, while providing customers with more competitively priced products.

Economists have studied the consequences of e-commerce on pricing for years.

In the mid-2010s, economists started citing something called the Amazon Effect, for the influence wielded by the dominant online retailer [Amazon.com](#) to drive down prices across the web and at brick-and-mortar stores. Almost all retailers, including Amazon, track each other's prices and then adjust their own using so-called dynamic pricing, when prices move according to market conditions. *

The conventional thinking was that the Amazon Effect helped to keep prices down. But Alberto Cavallo, a professor at Harvard Business School, argued in 2018 that e-commerce was making prices more sensitive to economic shocks, such as higher energy costs. He noted that prices could rise sharply if the shocks were inflationary.

Cavallo said China might be experiencing something similar but in the opposite direction. The economic shock of a slumping economy is applying downward pricing pressure, and the effect is being accelerated by e-commerce platforms.

Pinduoduo's success has prompted its two largest rivals, Alibaba and [JD.com](#), to join the low-price competition.

Last year, Alibaba's shopping site Taobao started a campaign to rate sellers based on how their prices compared to other e-commerce platforms, according to Chinese media. The sellers with better prices would receive more traffic and exposure for their products. [JD.com](#), once known for selling high-end electronics, has also created a series of low-price campaigns.

For its part, Chinese regulators established a new rule in May preventing online platforms from imposing "unreasonable restrictions" on merchants' prices, transaction rules and traffic.

Zhang Zhuo, a Chinese journalist, wrote a post titled "The Better Pinduoduo Is, the Worse the Times Are." In the article, which has been removed from WeChat, China's dominant messaging app, she said Pinduoduo has conditioned shoppers to ignore brands and look for the cheapest options.

Online merchants, Zhang wrote, "have only two choices, either lower price or sacrifice sales."

One shopper on Pinduoduo, Gao Ning, an office administrator in Beijing, said he had initially been wary of using the platform but found it to be a convenient way to buy groceries. Now, he also purchases toilet paper, garbage bags, trash cans, dish soap and cat food from the site.

"Pinduoduo is still a little cheaper," he said. He found that the same items were less expensive there than on other sites, because "everyone goes there expecting good value for money."

