Admart case study essay

This case is based primarily on interviews with key players conducted by the author in 2000 and 2001. Data from the interviews are supplemented by information extracted from media reports. Hong Kong-based businessman Jimmy Lai Chee-ying launched adMart in June 1999 to sell groceries over the Internet. This start-up was the cornerstone of an effort by Mr. Lai to once again demonstrate his entrepreneurial acumen by successfully diversifying into e-commerce.

Back in 1981, Jimmy Lai set up a garment factory and started to sell casual clothing in Hong Kong under the brand name of Giordano. He subsequently developed the Giordano brand into a multinational company that became one of Asia's most successful casual wear retailers. During the 1990s, Mr. Lai built a media empire by first starting Next Magazine and then challenging the crowded and conservative Chinese language newspaper market in Hong Kong with the launch of the Apply Daily tabloid. As the anchor tenant in an envisioned cybermall, adMart would be the latest venture to leverage Mr.

Lai's expertise in business development. Jimmy Lai versus the Establishment Mr. Lai was well known for being flamboyant, outspoken, and irreverent. Before and after the Tiananmen Square massacre, he had criticised Communism and taunted the Beijing government. Slogans on the t-shirts sold by his Giordano stores and editorials in his media outlets promoted democracy and ridiculed Chinese Communist Party officials. One particularly acute comment by Mr.

Lai about then Premier Li Peng had stymied Giordano's expansion plans in mainland China and eventually led Mr. Lai to sell his equity stake in the

clothing retailer. More recently, his Apple Daily newspaper was blacklisted by Chinese President Jiang Zemin. This was after it had taken on the Chinese language newspaper cartel in Hong Kong and emerged as the second best-selling daily publication in the territory. With adMart, Mr. Lai initiated another battle against the Hong Kong business establishment, including two of its biggest conglomerates.

Park'n Shop is part of the Hutchison Whampoa empire controlled by Hong Kong's leading business tycoon, Li Ka-shing. Meanwhile, Wellcome (as part of Dairy Farm International Holdings) was the grocery retailing arm of Jardine Matheson, the first and foremost British trading house in Hong Kong. Together these two chain stores accounted for nearly 70 per cent of retail grocery sales in Hong Kong. The remaining market share was held by convenience stores, primarily Seven-Eleven and Circle K, and a few niche vendors. Neither Park'n Shop or Wellcome were renowned for their wide production selection or attractive prices. In contrast to the freewheeling and competitive image of the Hong Kong economy, they were commonly perceived to be operating a cosy duopoly.

According to its first president, Wilson Chu Bun, adMart was to " change the way people buy groceries". It was also widely seen as another effort by Jimmy Lai to shake up the established order, initially in Hong Kong and perhaps subsequently in other parts of Greater China. The Rise of adMart Mr. Lai invested about US$ 50 million of his personal fortune to start up adMart.

By the end of 1999, the company had hired more than 1000 people, acquired more than 300 vehicles, and 1 operated 15 warehouses spread across Hong

Kong. Brisk sales and positive customer feedback suggested that adMart had a bright future. However, a year later it was out of business. Over the second half of 1999, adMart rapidly ramped up its business operations. It sacrificed operating margins in order to rapidly increase revenues and gain market share. Following a distribution model that was an emerging success in Japan, customers ordered their goods online and collected them at pickup points (often convenience stores operating 24 hours per day) near their homes.

This distribution model was abandoned after growing customer demand created bottlenecks and other logistics problems at the pickup points. Instead, adMart began to provide a free home delivery service for orders exceeding HK$ 100 (about US$ 13). The combination of attractive prices and free delivery services offered by adMart created a deluge of customer orders. It handled up to 12, 000 orders per day. Significantly though, the amount of the average order was less than half of the HK$ 750 that was needed to break-even on delivery costs.

As a result, adMart was losing money on almost every customer order and burning through its stockpile of cash. However, it was attracting the attention of customers, competitors, and the mass media. Rivals React adMart’s success in capturing market share also sparked strong reactions from Hong Kong’s two major grocery retailers. The two established retailers not only lowered their prices on competing products, but also curtailed their advertising in Mr. Lai’s publications.

(The Chinese name for adMart translates to Apple Delivery, and thus strengthens its literal connection to Jimmy Lai’s Apple Daily newspaper.)

They not only stepped up their advertising in local rivals to the Apple Daily, but also created alliances with them, such as the Shop-on-Post initiative between Park'n Shop, Fortress and the Oriental Daily News. At the height of the grocery retailing war in Hong Kong, Park'n Shop and Wellcome combined for more than 80 pages of advertising (costing HK$1 million or over US$ 120, 000) per week. The pair also enhanced their own online ordering capabilities and began to offer free delivery services for groceries ordered using the Internet.

Several Hong Kong media reports alleged that the established supermarkets also leveraged their bargaining power to not only reduce their own prices on fast-moving items like Coke, rice and noodles, but also to pressure many suppliers not to deal with adMart. One newspaper report suggested that IBM and Procter & Gamble were among the few top-tier suppliers to resist this pressure. If this allegation were true, adMart would have been forced to make use of grey market channels and/or to source lower-quality products. AdMart initially limited its product scope to 60 core items. Those included beer, cola and fruit juice, canned goods and rice, soap and laundry detergent, and baby products like disposable diapers. By selling bulk groceries instead of fresh produce, the company saved money on refrigerated storage even though it may have neglected certain high margin items.

The decision to sell only a few products and making bulk purchases should have enabled adMart to keep down the costs of its goods sold. However, several key suppliers appeared reluctant to deal with adMart let alone to offer it preferential prices. At the beginning, adMart aimed to operate its own

warehouses and delivery systems. Despite its limited reliance on leading brand names, adMart made large investments in both its goods inventory and capital assets.

At one point, it had 48 outlets and/or warehouses while employing more than 1500 people – 150 to take orders and almost 1000 to handle logistics. The last CEO of adMart, Mr. Anton van Gorp, admitted that " We had excessive assets, we tried to provide a global choice for everything and invested too much in our distribution system. " 2 The Fall of adMart Within a year of its establishment, adMart dramatically repositioned itself. The biggest change was to broaden the product line beyond groceries.

Sales of office supplies, furniture, household appliances, and even travel services were expected to raise profit margins. The company also hired a manager with experience in sourcing low price, high quality products from vendors around the world, sought out strategic alliances, and tried to improve its relations with suppliers. As adMart adopted a new business model which required a different asset mix, other miscalculations came to light. The company had a long-term lease commitment for a lot of warehouse space that it no longer needed and it was using less than 100 of its 350 delivery vans.

Attempts to sell or lease spare delivery capacity were not very successful. Fortunately, 100 of adMart's vans had not yet been painted with the company logo, making them easier to resell. Meanwhile, a combination of grey channel sourcing and a streamlined organisational structure hurt adMart's reputation after it was discovered to be selling counterfeit Mouton

Cadet wine. Unfortunately, adMart did not have the operational resources to handle the problem or the public relations staff to limit the damage to its reputation.

As a result, adMart's bottom line suffered as even loyal customers became more selective in what they purchased online. In the early summer of 2000, adMart underwent a series of cost-cutting measures aimed at reducing its losses. The online retailer was able to narrow its losses from HK$ 51 million in May 2000 to HK$ 16. 3 million in October 2000. The cumulative losses from the business were nearly HK$ 1 billion or US$ 120 million.

Given that the firm's monthly turnover never exceeded HK$25 million, the prospects for profitability in the near term remained dim. According to Mr. Van Gorp, adMart's failure to lure shoppers to the Internet was a significant factor in the decision to close the business. AdMart offered a five percent discount for orders placed over the Internet.

Even so, the proportion of customers placing orders on the Web site peaked at 25 percent shortly before the shutdown. Most customers made purchases by telephone, often after finding the items they wanted in colour supplements slipped into newspapers. This method of sales robbed adMart of a significant advantage that comes from online retailing. The firm was forced to set up a call centre and hire telephone order-takers that created HK$ 20 million (about US$ 2. 5 million) in monthly operational expenses.

Jimmy Lai ssumed that adMart could entice huge numbers of consumers in Hong Kong away from brick-and-mortar stores. The migration towards online purchasing simply did not occur during the company's lifespan. The selective

purchasing behaviour of online customers resulted in unprofitable order sizes for adMart and undoubtedly contributed to its death spiral. Some media pundits also cited the lack of legislation in Hong Kong to restrict cartels and other forms of anti-competitive behaviour. In any event, the online B2C model remains unproven in Hong Kong even as high real estate prices restrict the rivalry among brick-and-mortar retailers. Revising the Vision During its corporate lifetime, adMart was able to improve both its sales levels and profit margins through fine tuning, cost cutting, and changing its product scope.

As a result, the retailer moved away from Mr. Lai's original vision. " Noodles and rice didn't sell, but the office supplies business kept growing," Mr. Lai said. " Business-to-business sales became our most interesting sector.

" According to him, sales revenue, driven by office furniture, was growing at such a rate that the company could have reached the break-even point in another year. After failing to produce a successful business on his own terms, Jimmy Lai first tried to sell the company. This effort was unsuccessful, and so he finally shut down adMart in December 2000 to focus on publishing. This was at least the third major retail failure in Hong Kong within two years. The GrandMart Warehouse Club was launched in 1992 and expanded to seven stores by 1996, but suspended operations in 1998. Meanwhile, the French-based supermarket chain, Carrefour, opened four huge stores starting in 1996, but closed them all in September 2000.

Mr. Lai also slashed the number of Web-related positions at his publications while starting to charge his online users a subscription fee. He wanted to

ensure a healthy balance between advertising and subscription revenues for the Apple Daily and Next Magazine. Reflecting on Failure Mr.

Jimmy Lai now admits that he was blinded by “ hyperbole about the Internet and my own arrogance. I was so rich that I didn’t have to borrow money or even stretch my resources. ” The market craze for Internet stocks reinforced Mr. Lai’s self-confidence.

At the time of the launch, he had little fear of running out of money since it appeared that the capital markets were ready to provide additional funds. With no oversight from bank loan officers or outside shareholders, adMart had little incentive to closely control either costs or quality. Unlike many other Internet entrepreneurs, Jimmy Lai had a record of succeeding against the odds. With adMart, the odds apparently caught up to him. Humbled but not embittered, Mr.

Lai suggested that his experience demonstrated that Internet-only businesses would not survive. He also expressed a belief that, “ China is the future, not the Internet”. 4